Annex 1

DEUTSCHE BANK

STATEMENT OF FACTS

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1. Deutsche Bank acknowledges the underlying conduct set forth in this Statement of Facts.

I. Introduction

2. Between 2006 and 2007, Deutsche Bank securitized over 400,000 subprime and Alt-A residential mortgages in residential mortgage-backed securities.[1] In all, Deutsche Bank issued or underwrote over $100 billion worth of RMBS to a wide range of investors, including charitable and religious organizations, pension plans, federal home loan banks, credit unions, government-sponsored entities such as Fannie Mae and Freddie Mac, and financial institutions, including many that were federally-insured.

3. Deutsche Bank made a concerted effort to expand its RMBS program during a period when it believed that mortgage lending standards were significantly declining. In the process, Deutsche Bank injected tens of billions of dollars into the housing market, which it knew[2] was on the verge of collapse from a severe excess of liquidity and housing price appreciation. By 2007, Deutsche Bank had grown from the ninth to the third-largest issuer of RMBS in the world.

A. Deutsche Bank's False Representations To Investors

4. Prior to issuing RMBS, Deutsche Bank conducted due diligence on samples of loan pools to be securitized. Deutsche Bank evaluated whether the loans were underwritten in

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1. "Subprime" mortgage loans are made to borrowers of lower credit quality and with lower credit ratings. Subprime mortgages typically result in higher interest rates as a result of a higher risk of default. "Alt-A" loans are mortgages made to borrowers with a risk profile in between prime and subprime. Borrowers of Alt-A mortgages typically have clean credit histories, but may have higher debt-to-income ratios or inadequate documentation of employment or income.

2. As used herein, "knew" and "understood" are intended to mean with actual knowledge or conscious disregard for the truth.

accordance with the mortgage loan originator's underwriting guidelines,[3] whether they complied with applicable federal, state and local laws and regulations, and whether they were underwritten to borrowers who had the ability to pay their mortgages, among other things. Deutsche Bank also conducted due diligence to verify originators' representations regarding the credit characteristics of the borrowers and the value of the mortgaged properties.

5. When issuing RMBS, Deutsche Bank made representations to investors and rating agencies about the characteristics of the mortgage loans it securitized in RMBS.

6. For each RMBS, Deutsche Bank made representations in publicly filed offering documents and other deal transaction documents, as well as in direct communications with investors. Deutsche Bank made representations in a Prospectus Supplement for each RMBS concerning the loans' compliance with loan origination underwriting guidelines, the borrowers' FICO scores, and the LTV or CLTV of the mortgage loans, among other representations.

7. Deutsche Bank made similar representations to rating agencies in order to obtain credit ratings for the RMBS securities, without which the RMBS could not have been marketed.

8. Throughout 2006 and 2007, Deutsche Bank intentionally made false representations and material omissions about key characteristics of mortgage loans that it securitized in certain RMBS.

9. For instance, Deutsche Bank represented to investors that loans securitized in its RMBS were originated generally in accordance with mortgage loan originators' underwriting

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3. Loan underwriting guidelines typically addressed a variety of key facts about the borrower, including: the borrower's overall debt level, annual income, debt-to-income ("DTI") ratio, amount of cash reserves or disposable savings, employment history and prospects for future employment, credit history, and credit score (a measure of a borrower's credit risk, also called a "FICO score"). Factors considered that concerned the property itself were: whether the property was owner-occupied or investor-owned, the nature of the property (*e.g.*, single family home, multi-family home), and the ratio of the mortgage loan amount to the property value, also known as the loan-to-value ("LTV") ratio. If other liens on the property were considered, such as second liens, it was the combined loan-to-value ("CLTV") ratio.

guidelines, which Deutsche Bank stated were primarily intended to assess whether a borrower had the ability to pay their loan. But Deutsche Bank knew, based on the results of due diligence, that significant numbers of loans did not meet those underwriting guidelines and were underwritten to borrowers who would not likely have the ability to pay their loans.

10. Deutsche Bank misrepresented to investors the value of the properties securing the loans securitized in its RMBS. Deutsche Bank concealed from investors that it knew that the value of the properties securing the loans was far below the value reflected by the originator's appraisal. In many cases, the properties were "underwater" at the time the security was issued, meaning that the value of the liens on the property exceeded the value of the property itself. Deutsche Bank also concealed from investors that significant numbers of borrowers had second liens on their properties, which underrepresented the combined value of the loans on the property.

11. Deutsche Bank represented borrowers' FICO scores, but concealed from investors that it knew many borrowers' FICO scores had already declined materially by the time of securitization. Deutsche Bank represented that borrowers with declining FICO scores were less likely to pay their mortgages.

12. By misrepresenting key characteristics of the loans that it securitized, Deutsche Bank concealed from investors and rating agencies the true risk of losses of its RMBS. In doing so, Deutsche Bank deprived investors of their right to make an informed decision about whether they should invest in those RMBS.

13. As a result of Deutsche Bank's misconduct, investors, including federally insured financial institutions, lost billions of dollars on their investments in Deutsche Bank RMBS.

B. Deutsche Bank's Securitization Process

14. From 2005 to 2007, Deutsche Bank purchased residential home loans for the purpose of securitizing the loans in RMBS. In such "principal" transactions, Deutsche Bank securitized and issued RMBS on several SEC shelf registrations,[4] including the "ACE" shelf and the "DBALT" shelf. Deutsche Bank securitized subprime loans in RMBS on the ACE shelf, and Alt-A loans in RMBS on the DBALT shelf, among others.

15. Deutsche Bank also underwrote RMBS issued on third parties' shelves, such as Countrywide Home Loans, Inc. ("Countrywide") and IndyMac Bank, F.S.B. ("IndyMac"). In such "third-party" or "agented" transactions, Deutsche Bank often structured the transaction and sold RMBS certificates to investors. In most third-party transactions, Deutsche Bank acted as the sole or lead underwriter. Occasionally, Deutsche Bank shared underwriting responsibilities in third-party transactions with other investment banks.

i. Principal Transactions

16. Deutsche Bank acquired newly-originated subprime and Alt-A mortgage loans for the purpose of securitizing them in principal transactions. Deutsche Bank purchased the majority of loans for principal transactions in pools from mortgage loan originators, such as Countrywide, New Century Mortgage Corporation ("New Century"), Ameriquest Mortgage Company ("Ameriquest"), Argent Mortgage Company LLC ("Argent") and American Home Mortgage Corp. ("AHM"), among many others.

17. Deutsche Bank also purchased loans from smaller originators on a loan-by-loan basis through an internal correspondent lending group. And in 2006 and 2007, Deutsche Bank

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[4] A "shelf registration" is an SEC-regulated procedure through which a corporation can register with the SEC a securities offering up to two years prior to the actual public offering. Upon establishing a shelf registration, a corporation can execute multiple issuances within the two-year period.

acquired two originators, Chapel, an originator of subprime mortgage loans, and MortgageIT, an originator of Alt-A loans, to increase the securitization of loans in Deutsche Bank RMBS.

18. Prior to purchasing a pool of loans from a mortgage loan originator, Deutsche Bank conducted due diligence on a sample of the loans in the pool. Deutsche Bank engaged third-party vendors to conduct due diligence on its loan samples, including The Clayton Group, Inc. ("Clayton").

19. Deutsche Bank often agreed with originators to limit the number of loans that Deutsche Bank could review in its diligence sample. Indeed, Deutsche Bank often agreed to further limit sample sizes when purchasing pools of loans from large originators, such as Countrywide. As a result, Deutsche Bank often did not review substantial portions of loan pools, regardless of the results of the Bank's due diligence on the loans reviewed in the sample.

20. Deutsche Bank's due diligence process consisted of a credit, compliance and valuation review.

21. During the credit review, Deutsche Bank evaluated whether the loan was underwritten in accordance with the originator's underwriting guidelines or otherwise had sufficient compensating factors to warrant a deviation from those guidelines. Deutsche Bank also evaluated whether the borrower had the ability to pay their loan based on an analysis of their credit profile, including their FICO score, income, and history of delinquencies, among other characteristics.

22. The compliance review evaluated whether the loan had been originated in compliance with federal, state and local laws and regulations.

23. The value review assessed whether the originator's appraisal of the mortgaged property was supported by the actual value of the home.

24. After Deutsche Bank completed due diligence on a sample of loans, Deutsche Bank's due diligence group, in conjunction with Deutsche Bank's mortgage trading desks, decided which loans to purchase and which loans to reject from the pool.

25. After Deutsche Bank compiled a final list of loans that it decided to reject from the pool, the Bank conducted a "tie-out" call with the originator selling the pool of loans. During a tie-out call, Deutsche Bank and the originator discussed the reasons Deutsche Bank had decided to reject certain loans from the pool. But Deutsche Bank often agreed to purchase loans that it had initially determined should be rejected. Indeed, throughout the diligence process, Deutsche Bank bowed to pressure from originators to purchase loans that the Bank's due diligence group had initially determined should be rejected.

26. Deutsche Bank's mortgage trading desks worked with the Bank's securitization group to determine which loans from which pools would be securitized in which RMBS. Some RMBS consisted of only one or two large loan pools, while others comprised loans from multiple loan pools.

ii. Third-Party Transactions

27. When Deutsche Bank underwrote RMBS for other issuers in third-party transactions, Deutsche Bank did not purchase the underlying loans, but instead marketed and sold most of the certificates of the RMBS to investors.

28. Deutsche Bank performed due diligence on a sample of the loans to be securitized in third-party transactions that was similar to the Bank's due diligence for principal transactions.

29. But Deutsche Bank was more lenient when conducting due diligence in third-party transactions. Indeed, Deutsche Bank conducted due diligence on even smaller samples of loans in third-party transactions. Deutsche Bank also "cleared" more loans to be securitized that it knew would not likely meet its representations to investors.

30. Moreover, in many third-party transactions, Deutsche Bank conducted no valuation diligence, despite its knowledge of rampant appraisal fraud throughout the mortgage industry.

C. Deutsche Bank's Representations To Investors

31. In both principal and third-party transactions, Deutsche Bank made a number of representations to investors regarding its diligence process and the credit, compliance and value characteristics of loans collateralizing its RMBS.

32. The Bank made these representations in publicly filed offering documents, such as Prospectus Supplements, as well as in marketing presentations to investors.

33. Among other things, Deutsche Bank represented in Prospectus Supplements for principal and third-party transactions that

- Loans in the securitized pools were originated generally in accordance with the loan originator's underwriting guidelines and that exceptions to those underwriting guidelines had been made when the originator identified "compensating factors" at the time of origination;
- Originators' underwriting guidelines were primarily intended to assess the ability and willingness of the mortgagor to repay the debt and to evaluate the adequacy of the property as collateral for the mortgage loan;
- Each loan had been originated in compliance with federal, state and local laws and regulations;
- No loan had a loan-to-value (LTV) or combined loan-to-value (CLTV) in excess of 100%; and
- No loan had a FICO score of less than a certain threshold, such as 500.

34. In addition, each Prospectus Supplement contained certain "stratification tables" that represented to investors particular characteristics of the loans, such as FICO scores or LTV or CLTV ratios, and how many loans in the securitization fell into specific ranges for each of those characteristics.

II. Deutsche Bank Intentionally Misrepresented That The Mortgage Loans Met Originators' Guidelines And That Originators' Guidelines Were Intended To Assess The Borrowers' Ability To Repay Their Mortgages

35. When Deutsche Bank conducted due diligence on a sample of loans, it determined which loans to sample from a "loan tape," which was a spreadsheet of the characteristics of each of the loans in the pool. Deutsche Bank usually selected the sample using an "adverse selection" process whereby a supervisor in Deutsche Bank's Due Diligence Department (hereinafter, "Diligence Supervisor") selected loans based on adverse credit characteristics such as a low FICO scores, high debt-to-income ratios, and prior foreclosures or delinquencies, among a number of other criteria. For some pools, the Diligence Supervisor selected a portion of the sample randomly.

36. Deutsche Bank then hired third-party vendors, such as Clayton, to assist Deutsche Bank in conducting credit and compliance due diligence on samples of loan pools. Clayton employed teams of trained underwriters to review the underlying loan files and assess the creditworthiness of the loans, including whether they complied with the originator's underwriting guidelines and federal, state and local laws and regulations, and whether they were underwritten to borrowers who had the ability to pay their loans.

37. Clayton underwriters graded each loan based on its compliance with the originator's underwriting guidelines and with federal, state and local laws and regulations.

38. Clayton graded a loan an Event Grade 1, or "EV1," when it complied with the originator's underwriting guidelines and all laws and regulations.

39. An Event Grade 2, or "EV2," did not comply with the originator's underwriting guidelines or laws and regulations but sufficient compensating factors offset the risk associated with the exceptions to the underwriting guidelines.

40. An Event Grade 3, or "EV3," did not comply with the originator's underwriting guidelines or laws and regulations and did not have sufficient compensating factors to offset the risks associated with those underwriting exceptions.

41. Clayton also graded a loan an EV3 when, based on additional criteria set by Deutsche Bank, often referred to as "overlays," it was evident that the borrower would not likely have the ability to pay their loan regardless of whether the loan generally complied with the originator's underwriting guidelines.

A. Deutsche Bank Identified High Percentages Of Loans That Did Not Meet Originators' Guidelines Or Were Underwritten To Borrowers Who Would Not Likely Have The Ability To Pay Their Mortgages

42. Deutsche Bank's final due diligence reports from 2006 to 2007 reflect the poor and fraudulent underwriting practices of mortgage loan originators. Those reports show that Deutsche Bank identified high percentages of loans graded EV3s in loan samples. Indeed, in many pools of loans, Clayton graded more than 50% of the loans in the sample as EV3s. (Appendix A shows the numbers and percentages of EV3s identified in samples of loan pools and securitized in a selection of RMBS sponsored or underwritten by Deutsche Bank in 2006 and 2007.)

43. Deutsche Bank identified high percentages of loans graded EV3s that were not underwritten in accordance with mortgage loan originators' underwriting guidelines and did not have sufficient compensating factors. The loans were graded EV3s because, for example, the borrower's credit was insufficient, they had unreasonable or fraudulent stated income, their debt-to-income or loan-to-value ratios were too high, or the loan was missing material documentation, among other reasons.

44. Deutsche Bank also identified significant numbers of loans graded EV3s in loan samples because they were underwritten to borrowers who, according to Deutsche Bank's own

overlays, would not likely have the ability to repay their loans even though the loans ostensibly met the originator's underwriting guidelines.

45. Mortgage loan underwriting guidelines were designed to assess whether a borrower would have the ability to repay their loan. Indeed, Deutsche Bank represented to investors in Prospectus Supplements that originators' guidelines were, for example, "primarily intended to assess the ability and willingness of the borrower to repay the debt . . . for the mortgage loan."

46. However, as early as 2005, Deutsche Bank knew that mortgage loan originators were expanding their underwriting guidelines to such an extent that they no longer sufficiently assessed the borrowers' ability to repay their loans.

47. In March 2005, the Diligence Supervisor reported to a senior member of Deutsche Bank's Mortgage Finance team, (hereinafter, the "Mortgage Finance MD"), that it was

> concerning that we're being sent proposed guidelines changes from Sellers every week. The larger firms (AMQ, NCEN, OOMC, and FMT) [Ameriquest, New Century, Option One, and Fremont] are putting significant pressure on the marketplace by expanding their guidelines. Very few Investors will push back on these large Sellers and it had made originating very difficult for lower tier competitors….It's definitely a Seller's market! (*Sic.*)

48. Indeed, in May 2006, the Diligence Supervisor warned a senior Trader on the Subprime Desk, a Managing Director (hereinafter, "Trader 1"), that Option One, a large mortgage loan originator, was making such "aggressive" revisions to its underwriting guidelines that it would underwrite a loan to anyone with "half a pulse":

> [T]his is almost becoming a weekly event with OOMC [Option One]. The revisions [ ] are very aggressive and I would not approve. Allowing a borrower with no credit history to be upgraded to an A with a 90% LTV is unbelievable. I once heard that OOMC will approve anyone with a pulse – I would move that to half a pulse.

49. The same month, the Diligence Supervisor admitted that Deutsche Bank, among other banks, "tolerate[d] misrepresentation" from mortgage loan originators with "misdirected lending practices." Those originators, for example, "marked out" borrowers' pay stubs in order to state, often fraudulently, that the borrowers had higher incomes:

> [T]he marked out paystub is just an example of how misdirected lending practices have become; we tolerate misrepresentation. What goes around will eventually come around; when performance (default) begins affecting profits and/or the investors who purchase the securities, only then will Wall St. take notice. For now, the buying continues. Put the postal worker on the Open Issues list for unreasonable income - we know the salary is not $100k or a paystub would have been provided - USPS 25+ years could be earning $70k-$90k. We may clear if the credit is very good, but at least it will send a temporary message.

50. In October 2006, the Diligence Supervisor reiterated to a senior Managing Director on Deutsche Bank's Subprime Trading team (hereinafter, "Subprime MD") that mortgage loan originators were "allowing exceptions [to their underwriting guidelines] and ignoring risk layering." He stated further that Deutsche Bank was "no longer" seeing loans with compensating factors:

> [I]t's the same trend we're seeing throughout the industry; Sellers are qualifying more borrowers by allowing exceptions and ignoring risk layering. We used to see compensating factors for borrower/loan weaknesses, that's no longer the case. I was interviewing an underwriter from Fremont who told me 'if the borrower has a pulse, we can make him the loan'; Fremont's not alone.

51. Moreover, the Diligence Supervisor remarked that one could "drive your truck through the guidelines" of certain originators from which Deutsche Bank was purchasing pools of loans. In February 2007, during a due diligence review of a pool of loans being purchased from First Horizon Home Loan Corporation, the Diligence Supervisor admitted that he was

"getting used to these 'Super Expanded', Super No Doc, etc. programs we've been seeing – it's the Alt-A version of Fremont (the 'original' drive your truck through the guidelines originator)."

52. Thus, from 2005 through 2007, Deutsche Bank created and applied additional criteria during due diligence primarily to identify borrowers who would not likely have the ability to pay their mortgages even if their loans were ostensibly underwritten in accordance with the originator's expansive underwriting guidelines. According to the Diligence Supervisor, identifying borrowers who would not likely have the ability to pay their loans was "the only way to control the abusive lending practices we've been seeing."

53. For example, Deutsche Bank directed Clayton to identify borrowers who would not likely have the ability to pay their loans with an overlay that it called "Ability to Repay," even if those loans were ostensibly underwritten in accordance with the originator's underwriting guidelines. The criteria for this overlay included, for example:

- Loans that were 60 or more days late at the time of origination of the new loan with stated income documentation;
- First time homebuyers with four or less trades, 100% CLTV and stated income documentation;
- Elderly (65+) borrowers on fixed income with stated income documentation and FICO scores of less than 600;
- Elderly (65+) borrowers on fixed income with stated documentation and any mortgage delinquency 30 or more days past due in the last 12 months; and
- Any loan with a grade of B, C, or D (or equivalent for lenders that did not use that grading system), where the prior mortgage was 60 days or more late in the last 12 months and stated income documentation.

54. Deutsche Bank also identified borrowers who would not likely have the ability to pay their mortgages by flagging loans with:

- FICO scores below 550;
- Lender credit grades of B or below;

- Payments that were 60 or more days late in the mortgage history;
- A prior loan taken out for less than 10 months;
- A prior loan that was refinanced 10 months or less before the subject loan was originated;
- Foreclosures in the last 4 years; and
- Bankruptcies in the last 3 years.

55. Over the course of 2006 and 2007, Deutsche Bank identified significant numbers of loans during due diligence that were underwritten to borrowers who would not likely have the ability to pay their loans, even though those loans were ostensibly underwritten in accordance with the originator's underwriting guidelines.

56. But Deutsche Bank did not disclose these findings to investors. Instead, Deutsche Bank misled investors by leading them to believe that the loans that the Bank securitized were underwritten to borrowers who could pay their mortgages because they met guidelines that were "primarily intended to assess the ability and willingness of the borrower to repay".

B. Deutsche Bank Knowingly Securitized Significant Numbers Of Loans That Did Not Meet Originators' Guidelines Or Were Underwritten To Borrowers Who Did Not Likely Have The Ability To Pay Their Mortgages

i. Deutsche Bank "Waived" Significant Numbers Of EV3s

57. Despite identifying such high percentages of loans graded EV3s that did not meet originators' guidelines or were underwritten to borrowers who would not likely have the ability to pay their loans, Deutsche Bank's due diligence group "waived" many of these defects, bowing to pressure from originators and Deutsche Bank mortgage traders to purchase more loans to securitize in RMBS.

58. Clayton labeled the loans that Deutsche Bank waived Event Grade "2Ws" as opposed to just "EV2s" to signify that Deutsche Bank—not Clayton—waived an EV3 that did

not meet the originator's underwriting guidelines or were underwritten to borrowers who would not likely have the ability to pay their loans.

59. In 2006 and 2007, Deutsche Bank securitized thousands of loans that Clayton graded EV3s and Deutsche Bank waived to EV2Ws. (*See* Appendix A.) Indeed, the Diligence Supervisor admitted that Deutsche Bank waived many EV3s for large originators because, for instance, "Fremont is one of our special Sellers and we want to provide addl. Flexibility." Thus Deutsche Bank knew that it was securitizing thousands of loans identified in loan samples that were not underwritten in accordance with originators' guidelines or were underwritten to borrowers who would not likely have the ability to pay their loans.

ACE 2006-CW1

60. For example, ACE 2006-CW1 comprised one pool of loans that Deutsche Bank purchased from Countrywide for $1 billion.[5] During due diligence, Deutsche Bank reviewed 1,601 loans for credit and compliance, constituting approximately 27.69% of the pool. Based on final due diligence reports, Clayton graded 786 loans as EV3s, representing 49.09%—or nearly half—of the sample. Clayton graded the loans EV3s because they were not underwritten in accordance with Countrywide's underwriting guidelines, contained missing documentation, or were underwritten to borrowers who would not likely have the ability to pay their mortgages.

61. However, after Clayton's due diligence review, the Diligence Supervisor assured Trader 1 and a Contract Finance Director in the RMBS department on a phone call that he would reduce the high reject rate of the loans in the pool despite their defects. The Diligence Supervisor stated on the call, "if you want to get to [a] 10 [percent rejection rate], I can get to 10," even though he said the pool "is a very adverse pool, we got [FICO] drifts in the 400s, I

5. Unless otherwise indicated, all numbers are approximate.

mean we've got a lot of shit in that pool trust me." By the end of the due diligence Review, the Diligence Supervisor reduced the rejection rate of the pool to 12%, and told Trader 1 that "[w]e provided a significant amount of flexibility just to get to these percentages . . . ."

62. The Diligence Supervisor waived 285—more than one-third—of the 786 EV3s to EV2Ws, which Deutsche Bank knew were not underwritten in accordance with Countrywide's underwriting guidelines, contained missing documentation, or were underwritten to borrowers who would not likely have the ability to pay their mortgages. Deutsche Bank subsequently securitized 254 of those EV2Ws in ACE 2006-CW1, representing 5.12% of the issuance by principal balance.

63. In significant part as a result of Deutsche Bank's misconduct, investors in ACE 2006-CW1 suffered considerable losses. The loans securitized in that deal have lost approximately $266 million, representing 31% of the collateral in the deal, and are projected to lose $317 million, representing 38% of the collateral in the deal.

ACE 2006-NC3

64. Similarly, ACE 2006-NC3 comprised two pools of loans that Deutsche Bank purchased from New Century—a pool purchased for $700 million in August 2006 and a pool purchased for $1 billion in October 2006.

65. In the pool for $700 million, Deutsche Bank sampled 896 out of 3,585 loans, constituting 25% of the pool. Clayton identified 368 out of 896 loans as EV3s, representing 41% of the sample. But the next day, a New Century employee asked Deutsche Bank's Diligence Supervisor to accept more loans because it "[l]ooks like our execution is lower than expected." Subsequently, the Diligence Supervisor cleared 195—over half—of those EV3s to EV2Ws, which had material exceptions to New Century's underwriting guidelines or were underwritten to

borrowers who would not likely have the ability to pay their loans. Deutsche Bank securitized 128 of those 195 loans in ACE 2006-NC3.

66. In significant part as a result of Deutsche Bank's misconduct, investors in ACE 2006-NC3 suffered considerable losses. The loans securitized in ACE 2006-NC3 have lost $616 million, representing 41% of the collateral in the deal, and are projected to lose $733 million, representing 49% of the collateral in the deal.

DBALT 2007-RAMP1

67. In January 2007, Deutsche Bank purchased a pool of loans from GMAC-RFC for $375 million, which was securitized in DBALT 2007-RAMP1.

68. Deutsche Bank sampled 269 out of 1,650 loans, constituting 16.30% of the pool. Clayton identified 158 loans as EV3s, representing 58.74% of the sample. At the conclusion of the review, Deutsche Bank's Diligence Supervisor informed a senior Hybrid ARMs[6] Alt-A Mortgage Loan Trader, a Managing Director (hereinafter, "Trader 2"), that

> [t]his Alt-A/Alt-B pool was the most adverse Alt pool I have seen in 4 years - many of the loans were defaulting on mortgages . . . and I believe RFC adversely selected this pool. I've been doing RFC securitization reviews for years and have never encountered anything like the loans found in this pool.

Yet Deutsche Bank waived 56 out of 158 EV3s—over one-third—to EV2Ws.

69. Despite the Diligence Supervisor's warning about the $375 million pool, in a subsequent transaction with GMAC-RFC, the Diligence Supervisor admitted to an employee at Clayton that he waived more EV3s because GMAC-RFC threatened to "pull the trade":

> [T]he first trade went very poorly. Within minutes of tying out I got a call from the trading desk. I was told there is a new bid out from RFC and they were not going to show it to us due to the results. I then heard they may pull the trade. I tried to provide

6. An ARM loan is an adjustable rate mortgage.

> flexibility on [this] pool as the loan composition was entirely different than the fixed piece.

70. In significant part as a result of Deutsche Bank's misconduct, investors in DBALT 2007-RAMP1 and subsequent deals suffered considerable losses. The loans securitized in DBALT 2007-RAMP1 have lost $63 million, representing 24% of the collateral in the deal, and are projected to lose $77 million, representing 29% of the collateral in the deal.

ii. Deutsche Bank Limited The Number Of Loans That It Rejected From Loan Pools

71. Deutsche Bank also knew that it was purchasing and securitizing significant numbers of loans that did not meet originators' guidelines or were underwritten to borrowers who would not likely have the ability to pay because Deutsche Bank traders directed the Due Diligence group to limit the number of loans that Deutsche Bank rejected from loan pools despite the results of due diligence.

72. For example, Deutsche Bank traders instructed the Diligence Supervisor to reject fewer loans from pools that it purchased from large mortgage loan originators. In November 2006, the Diligence Supervisor warned the Mortgage Finance MD that "limits on rejections" were hurting the performance of Deutsche Bank RMBS: "I was also coming off the OOMC [Option One] review where we had that discussion that I needed to keep rejection rates lower on large Sellers. Larger samples and no limits on rejections may curb some of the performance issues we are seeing, although, Fremont seems to stand out among other Sellers."

73. Indeed, Deutsche Bank traders agreed with mortgage loan originators to limit the percentage of loans it rejected from loan pools despite serious concerns about the quality of those originators' loans. For instance, Fremont's bid letters, which offered its terms for the sale of a pool of loans, stated that there was a "Minimum purchase requirement of 93% of the actual pool delivered to fill the commitment," or a 7% rejection limit. Despite Deutsche Bank's due

diligence results, which showed that loan samples from some of Fremont's pools contained nearly 32% EV3s, Deutsche Bank rejected less than 7% of the loans in six of the seven pools that Deutsche Bank purchased from Fremont and securitized in RMBS in 2006.

C. Deutsche Bank Intentionally Securitized Significant Numbers Of Un-Reviewed Loans That Did Not Meet Originators' Guidelines Or Were Underwritten To Borrowers Who Would Not Likely Have The Ability To Pay Their Mortgages

74. Deutsche Bank knew with a high probability that it was securitizing significant numbers of un-reviewed loans that did not meet originators' guidelines or were underwritten to borrowers who would not likely have the ability to pay their mortgages. Deutsche Bank knowingly disregarded substantial evidence that significant numbers of un-reviewed loans would not comply with its representations to investors.

i. Deutsche Bank Knew That The Size And Composition Of Its Samples Failed To Capture Loans That Did Not Meet Guidelines Or Have The Ability To Pay

75. Deutsche Bank knew that the size and composition of its loan samples frequently failed to capture loans that were not underwritten in accordance with originators' underwriting guidelines or were underwritten to borrowers who would not likely have the ability to pay their loans.

76. In November 2006, the Mortgage Finance MD told the Diligence Supervisor to "[n]ote the fc [foreclosure] rate on [this] pool already!", referring to a pool that Deutsche Bank purchased and securitized in a 2006 ACE RMBS. The Diligence Supervisor responded that the Bank's sample sizes in the pools purchased were too small to capture a large number of defective loans: "[O]ur sample[s]…were only 25% on both pools – to allow 75% of the pool through without review is a large number."

77. Indeed, Deutsche Bank routinely represented to investors in marketing materials that it conducted either a "100% review or a judgmental sample of adversely selected mortgage loans – approximately 25-50%." However, for certain large originators, Deutsche Bank often limited its sample sizes to smaller percentages, such as 5-13%. In order to meet these percentages, Deutsche Bank loosened its adverse selection parameters by, for example, increasing its threshold for purchasing loans with higher LTV and DTI ratios and lower FICO scores.

ii. Deutsche Bank Routinely Did Not Increase Its Samples After It Identified High Percentages Of EV3s

78. Moreover, Deutsche Bank routinely did not increase the size of its loan samples when it identified high percentages of loans in those samples that did not meet originators' underwriting guidelines or were underwritten to borrowers who would not likely have the ability to pay their loans.

79. For example, in June 2005, Deutsche Bank identified a significant number of loans with fraudulent income documentation in a pool of loans that it was purchasing from Argent, a subsidiary of Ameriquest, for $150 million. The Diligence Supervisor explained to a Contract Finance Director in the RMBS Department that:

> Approximately 30-40% of the Credit Rejections had either Unreasonable Income (Stated Documentation) and/or Signatures that did not match… To find such a large number of loans with Income misrepresentation leads me to believe that Argent is accepting Stated Income from borrowers without concern to the reasonableness of that income… There were several loans (at least a dozen) rejected due to the signatures on the Stated Income Letter being different than the borrower's signature.

80. Despite these findings, Deutsche Bank did not increase its sample to identify loans in the un-reviewed portion of the pool that it knew with a high probability had either

fraudulent or unreasonable stated income documentation.[7] Indeed, in 2006 and 2007, Deutsche Bank's Diligence Supervisor believed that "most (if not all) Stated Wage Earner loans have inflated incomes," and the Subprime MD commented that "borrower or broker fraud is rampant on these" types of loans. Nevertheless, Deutsche Bank did not implement a practice of reviewing all stated income loans in pools of loans that it purchased. Thus Deutsche Bank knew that it was securitizing loans with a high risk of income misrepresentation or fraud.

81. As another example, in January 2007, the Diligence Supervisor recommended to a senior Fixed-Rate Alt-A Mortgage Loan Trader, a Managing Director (hereinafter, "Trader 3"), to increase a 15% sample for a GMAC-RFC $375 million pool. The Diligence Supervisor stated that he had identified "some of the most adverse loans I have seen in any Alt-A pool," which "may be indicative of the pools overall risk":

> These loans were some of the most adverse loans I have seen in any Alt-A pool. The majority of these loans have current past due mortgages - from 30 days to foreclosure - and the FICO scores have drifted from 68 points to 260 points (there were 1 or 2 where the borrowers had defaulted on all consumer trades)…. There were a large number of loans where the borrowers were past due on consumer trades or had very thin credit files that are not included on this list - I will be selecting those loans in my due diligence sample. I would recommend upsizing the sample on this pool from 15% as these loans may be indicative of the pools overall risk.

82. Despite the Diligence Supervisor's recommendation, Trader 3 did not increase the sample. As a result, Deutsche Bank did not review 85% of a pool of loans that the Diligence Supervisor described as "some of the most adverse loans [he] ha[d] seen in any Alt-A pool" by January 2007.

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7. A "stated documentation, "stated doc," or "stated income" loan is a loan as to which the originator relies on the borrower's declaration of his annual income on the loan application without supporting documentation.

iii. Deutsche Bank Often Allowed Large Originators To Add Significant Numbers Of Loans To Its Pools After It Completed Due Diligence

83. After it completed due diligence, Deutsche Bank often allowed large originators, such as Countrywide, to add or substitute significant numbers of loans to the pool, many of which Deutsche Bank knew would not meet its representations to investors.

84. For example, in May 2006, Deutsche Bank purchased a pool of loans from Countrywide for $1 billion to securitize in ACE 2006-CW1. After completing due diligence on a sample of loans in the pool, Deutsche Bank allowed Countrywide to "substitute" approximately 293 loans for loans that Deutsche Bank had rejected during due diligence. The Diligence Supervisor subsequently "found a number of very adverse loans from both a Credit (refreshed credit scores) and Value (ran through AVM model) perspective" in the substitute pool. In particular, he explained that "[a]pproximately 30% of the upsize were loans that had a 60 days late or greater (90+, 120+) on the mortgage in the last 12 months or have a FICO score less than 550. This is a very large percentage of adverse loans for a subprime pool."

85. But Deutsche Bank still purchased 270 out of 293 of the substitute loans without reviewing their loan files to determine if they met Countrywide's guidelines, were underwritten to borrowers who could pay, and complied with laws and regulations.

86. In July 2007, a mid-level Trader on the Hybrid ARMs Mortgage Loan Trading Desk, a Director (hereinafter, "Trader 4"), allowed Countrywide to replace the loans that the Diligence Supervisor rejected from three Countrywide pools despite the Diligence Supervisor's warning that "there is no guarantee the replacements are not increasing the risk in the pool":

> I understand why we are allowing [Countrywide] to replace the deleted loans in the 3 trades. However, I'm hopeful [Countrywide] does not adversely select the population of replacements. While I will be reficoing the loans, that by itself cannot identify all adverse loans and there is no guarantee the replacements are not increasing the risk in the pool.

87. Thus, in 2006 and 2007, Deutsche Bank knew with a high probability that significant numbers of loans added to its pools after the completion of due diligence would not meet its representations to investors.

iv. Deutsche Bank Rejected Significantly More Loans When It Sampled Larger Percentages Of Loan Pools

88. Deutsche Bank also knew with a high probability that it was purchasing and securitizing significant numbers of un-reviewed loans that did not meet originators' guidelines because, when Deutsche Bank reviewed larger percentages of loan pools, it found and rejected substantially more loans.

89. For example, in October 2006, Deutsche Bank purchased a pool of loans for $25 million from Sebring, an originator of subprime loans. Deutsche Bank conducted due diligence on 100% of the loan pool and rejected 16.49% of the loans in the pool. In response, the Subprime MD commented that, "[i]n general, [Sebring's] fallout seems high," and asked, "[w]hy is this? How would you characterize them as a borrower?" The Diligence Supervisor answered that "we are sampling 100% of their production. Inevitably, that leads to much higher rejection rates as 'the more you sample the more you reject.'" The Diligence Supervisor also confirmed that the quality of loans originated by Sebring were consistent with other subprime loans in the market at that time: "While the percentages would indicate Sebring's loans are more adverse, I don't believe they are that much different than other subprime Sellers we purchase loans from."

90. On rare occasion, Deutsche Bank increased—or "upsized"—the percentage of loans it reviewed from the loan pool. When it did, Deutsche Bank rejected substantially more loans from the pool. In April 2007, Deutsche Bank purchased a pool of loans for $89 million from Opteum. After completing the due diligence review, the Diligence Supervisor explained to Trader 4 that, "[w]e initially had sampled 50% of the pool and found a large number of issues -

we then upsized the sample to 100%. The upsize easily increased the number of rejected loans substantially."

D. Deutsche Bank Intentionally Securitized Loans In Third-Party Transactions That Did Not Comply With Its Representations To Investors

i. Deutsche Bank Conducted Less Stringent Due Diligence In Third-Party Transactions When It Was Not "On the Risk"

91. Deutsche Bank knew that it was securitizing significant numbers of loans that did not meet its representations to investors in third-party, as well as principal, transactions.

92. Throughout 2006 and 2007, Deutsche Bank identified high percentages of loans that did not meet originators' guidelines and did not have sufficient compensating factors, or were underwritten to borrowers who would not likely have the ability to pay their loans in third-party transactions.

93. But when Deutsche Bank conducted due diligence in most third-party transactions, Deutsche Bank "typically clear[ed] most of the Credit Issues" that it identified in loan samples because it did not consider itself "on the risk" for the deal. Deutsche Bank considered itself "on the risk" when, as the underwriter, it was responsible for marketing and reselling all of the bonds to investors, including the subordinate bonds that carried greater credit risk in the transaction. Deutsche Bank did not consider itself "on the risk" when it was responsible for marketing and reselling to investors only the issuer's AAA-rated bonds, which carried less credit risk.

94. In other words, Deutsche Bank waived and securitized even more loans with material credit and compliance defects when it was not responsible for selling the subordinate bonds with greater credit risk in the deal. As Trader 2 explained, "[the Diligence Supervisor] upstairs will approve anything on a third-party transaction where we don't have risk."

95. Moreover, in third-party transactions, Deutsche Bank selected part or all of its loan samples randomly, as well as adversely. Thus, Deutsche Bank knew that similar high percentages of EV3s identified in its loan samples were likely present in the un-reviewed portions of the pools that it was securitizing.

CWALT 2006-19CB

96. For example, Deutsche Bank was the co-lead underwriter for CWALT 2006-19CB, which closed on or about June 29, 2006.

97. In CWALT 2006-19CB, like other Countrywide securitizations, Deutsche Bank and Countrywide agreed to conduct due diligence on only a 5% sample of the loans in the transaction.

98. Deutsche Bank and Countrywide also agreed which loans could be reviewed. Countrywide provided only a partial loan tape of 3,545 loans from which to sample, constituting 60% of the total loan count for the deal. Moreover, Deutsche Bank agreed with Countrywide that it would only review those loans that were flagged by a particular designation. Out of 3,545 loans, Countrywide made available only 2,017 with this designation to be sampled.

99. According to the final due diligence report for CWALT 2006-19CB, Clayton determined that 215 out of 360 loans, or 59.70% of the sample, did not meet Countrywide's guidelines and did not have sufficient compensating factors, or were underwritten to borrowers who would not likely have the ability to pay their loans.

100. But Deutsche Bank disregarded the majority of Clayton's determinations in CWALT 2006-19CB because it was not "on the risk" for the deal. Deutsche Bank "clear[ed] most of the Credit Issues" for 166 out of 215 loans identified as EV3s, all of which were securitized in CWALT 2006-19CB.

101. Moreover, based on Clayton's findings that nearly 60% of the loans in the sample were EV3s—most of which were selected randomly—Deutsche Bank also knew with a high probability that a similar percentage of the loans that it did not review in the pool had similar defects.

102. But Deutsche Bank decided not to confirm whether any of the un-reviewed loans from the 3,545-loan tape, constituting 90% of the deal, had similar defects because it did not increase the sample. Moreover, Deutsche Bank did not review, or even request, the loan files for the 2,433 additional loans that were securitized in CWALT 2006-19CB.

103. In significant part as a result of Deutsche Bank's misconduct, investors in CWALT 2006-19CB suffered considerable losses. The loans securitized in CWALT 2006-19CB have lost $197 million, representing 13% of the collateral in the deal, and are projected to lose $230 million, representing 15% of the collateral in the deal.

ii. Deutsche Bank Agreed With Originators To Review Only Partial Loan Tapes

104. Deutsche Bank knew that reviewing partial loan tapes in third-party transactions would allow large originators, such as Countrywide, to securitize even more loans that would not meet Deutsche Bank's representations to investors in the deal. Nevertheless, Deutsche Bank often did not sample from complete loan tapes.

Countrywide

105. For example, in September 2006, before selecting a credit and compliance sample for CWALT 2006-31CB, a third-party transaction sponsored by Countrywide, Deutsche Bank's Diligence Supervisor admitted that "[Countrywide] has the ability to provide tapes with only 50-60% of the files available for review. I don't believe there are many other Sellers out there that

can get away with that. I suppose as long as there deals perform to expectations, they will continue dictating terms!" (*Sic*.)

106. But Countrywide's CWALT securitizations did not perform to expectations. The loans securitized in CWALT 2006-31CB, for example, have lost $118 million, representing 14% of the collateral in the deal, and are projected to lose $154 million, representing 18% of the collateral in the deal.

107. In January 2007, the Diligence Supervisor stated, concerning CWALT 2007-2CB, "I would like to point out after I filter (per Countrywides' instructions - "Select only when 'Credit File Received is Y' and 'Slim Pack Loan File Flag is N'") many of the loans with Data Issues are not available for review (ex. CLTV > 100%). It's not surprising; when I filter, only 453 out of 1,050 loans are available for review! Leave it Countrywide." (*Sic*.)

108. And in July 2007, after Countrywide provided to Deutsche Bank a 40%-funded tape from which to conduct due diligence on CWALT 2007-HY8C, the Trader 2 acknowledged to the Diligence Supervisor that "it seems to me if we did due dili[gence] on just the 40pct [percent] sample there would be a big opportunity for cwide [Countrywide] to slip things under the rug when they deliver the remaining 60." The Diligence Supervisor agreed, stating that "I'm fine with selecting 10% on the initial tape and 10% on the remaining 60% - I agree it would not be prudent to sample only the first tape."

Other Originators

109. Even though Deutsche Bank identified high percentages of loans that did not meet originators' guidelines and did not have sufficient compensating factors in third-party transactions issued by other originators, Deutsche Bank decided not to sample from complete loan tapes in many of those transactions, either.

110. For example, Deutsche Bank was the sole underwriter for AHMAT 2006-5, which was sponsored by AHM and closed on or about September 22, 2006. Deutsche Bank traders limited due diligence to a 10% sample from a 70%, partially-funded loan tape (7.2% of the fully-funded pool). After conducting credit and compliance due diligence, Clayton determined that 104 loans—or 36.11% of the sample—were EV3s. Nevertheless, Deutsche Bank waived material credit and compliance exceptions for 51—nearly half of those loans—all of which were securitized.

111. Even though Deutsche Bank knew that 36.11%—more than one-third of the loan sample for AHMAT 2006-5—had material credit or compliance defects, Deutsche Bank did not increase its sample or review loans from the remaining 30% of the loan tape.

112. In significant part a result of Deutsche Bank's misconduct, investors in AHMAT 2006-5 suffered considerable losses. The loans securitized in AHMAT 2006-5 have lost $495 million, representing 32% of the collateral in the deal, and are projected to lose $553 million, representing 36% of the collateral in the deal.

113. Deutsche Bank was the sole underwriter for RALI 2007-QO2, which was sponsored by Residential Funding Company, LLC ("RFC") and closed on or about February 26, 2007. Deutsche Bank conducted a 10% sample from a 77%, partially-funded loan tape. After conducting credit and compliance due diligence, Clayton determined that 95 loans—or 64.19% of the sample—were EV3s. Yet Deutsche Bank waived 64 out of 95 of those loans, most of which were securitized.

114. Even though Deutsche Bank knew that over two-thirds of the sample had material credit or compliance defects, Deutsche Bank did not increase its sample or review loans from the remaining 23% of the loan tape.

115. In significant part as a result of Deutsche Bank's misconduct, investors in RALI 2007-QO2 suffered considerable losses. The loans securitized in RALI 2007-QO2 have lost $198 million, representing 37% of the collateral in the deal, and are projected to lose $224 million, representing 42% of the collateral in the deal.

116. Deutsche Bank was the sole underwriter for INDA 2007-AR9, which was sponsored by IndyMac Bank and closed on or about December 27, 2007. Deutsche Bank conducted a 17.62% sample from an 83%, partially-funded tape. After conducting credit and compliance due diligence, Clayton determined that 17 loans—or 23% of the sample—were EV3s. Indeed, when emailing the results to Trader 4, the Diligence Supervisor admitted that "[t]he sample was randomly selected - I would expect the entire pool has similar percentages of issues." Yet Deutsche Bank did not increase its sample or review loans from the remaining 17% of the loan tape.

117. In significant part as a result of Deutsche Bank's misconduct, investors in INDA 2007-AR9 suffered considerable losses. The loans securitized in INDA 2007-AR9 have lost $64 million, representing 17% of the collateral in the deal, and are projected to lose $70 million, representing 18% of the collateral in the deal.

III. Deutsche Bank Intentionally Misrepresented The Loan To Value Ratios Of The Mortgage Loans

118. In determining whether to purchase and securitize a loan, Deutsche Bank placed particular importance on the mortgaged property's value. Deutsche Bank knew that the mortgaged property value of a home was an important metric associated with mortgage

origination that impacted not only the likelihood that the borrower would default, but also the severity of the loss on the loan if the borrower defaulted.[8]

119. The value of the mortgaged property was used to calculate LTV or CLTV ratios, which Deutsche Bank represented to investors in offering documents.

120. For example, a loan to a borrower who takes out a mortgage for 80% of the value of a property, but does not take out a second mortgage on that property, has an LTV and CLTV ratio of 80%. But if that borrower also takes out a second mortgage on the same property for the remaining 20% of the property's value, then the LTV for the first lien of the property is 80% and the CLTV for the property is 100%.

121. A high LTV or CLTV ratio meant that a borrower was more likely to default on the loan.[9]

122. Despite the impact of LTV and CLTV ratios on the borrowers' likelihood of default, Deutsche Bank intentionally misrepresented to investors the value of the mortgage loan properties it securitized. Deutsche Bank also concealed from some investors the existence and impact of second liens on those properties, which affected CLTV ratios.

A. Deutsche Bank Intentionally Securitized Loans With Inflated Appraisal Values

123. Nearly every loan purchased and securitized by Deutsche Bank, or securitized in a RMBS underwritten by Deutsche Bank, included an originator-obtained appraisal of the value of

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8. In the case of a borrower's default, "loss severity" is the difference between the amount borrowed and the amount recovered through foreclosure on the mortgaged property. For instance, if a borrower obtained a $100,000 mortgage and defaulted on that mortgage, and the originator (or whoever owned the loan) recovered $80,000 through foreclosure, the loss severity would be $20,000.

9. A high LTV or CLTV ratio also meant that, if the borrower defaulted, the lender was less likely to recover the amount lent.

the mortgaged property. During the origination process, the appraisal was used by the originator to determine a loan's LTV and CLTV ratios.[10]

124. Deutsche Bank believed that appraisal fraud was rampant in the mortgage industry. Specifically, Deutsche Bank believed that it was "common knowledge" that appraisers were under "intense pressure from lenders" to provide appraisals that would justify originating the loan, that there was a "lot of bias in the industry at the time," and that "brokers [were] 'giving' appraisers the value they want[ed]" and expecting appraisals to meet that value, regardless of the actual value of the property. Indeed, the Diligence Supervisor, a member of the Appraisers Association of America himself, went so far as to state that he believed that fraud was taking place in the appraisal industry.

125. In principal transactions, Deutsche Bank conducted due diligence on the valuation of mortgaged properties in order to determine whether the originator's appraisal accurately reflected the property's value and whether the originator's LTV and CLTV ratios were accurate. Deutsche Bank conducted valuation diligence so that it could, among other things, determine for itself whether the loan in question presented a risk profile acceptable for the Bank's purchase.

126. Even if Deutsche Bank determined that the true value of a mortgaged property was lower than the amount reflected in the originator's appraisal, Deutsche Bank nevertheless often decided that other factors militated in favor of purchasing the loan. In these instances, when Deutsche Bank decided to purchase loans that it knew were originated based on inflated

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10. For purposes of Deutsche Bank's valuation diligence, an LTV ratio was the ratio of the principal balance of a mortgage loan at the time of origination to the lesser of the sale price of the mortgaged property or its appraised value at the time of sale. A CLTV ratio was the ratio of all liens on the property, including second liens, to the lesser of the first-lien sale price of the mortgaged property or its appraised value at the time of the first-lien sale.

appraisals, it often made adjustments to the loss severity model it used to assess the risk of holding the loans on its own books, prior to their securitization.[11]

127. Thus, Deutsche Bank used its diligence in order to protect itself from the risks inherent in purchasing subprime mortgages. Although it knew that investors in its RMBS were taking the same or similar risks in their investments, Deutsche Bank nevertheless decided to withhold from those investors the information they would need to adequately assess their own risk.

128. Deutsche Bank's valuation diligence also provided the Bank with the knowledge necessary to make accurate representations to rating agencies and the Bank's investors regarding LTV and CLTV ratios of the loans securitized in a particular RMBS issuance.

129. Despite Deutsche Bank's knowledge of pervasive appraisal fraud in the mortgage industry, Deutsche Bank generally conducted no valuation diligence whatsoever for RMBS when it did not retain any risk of its own, as with RMBS issuances where Deutsche Bank acted only as underwriter for a third-party transaction. Instead, Deutsche Bank performed valuation diligence on only a small handful of third-party transactions in which Deutsche Bank did retain some level of risk in the issuance, such as purchasing a portion of the issuance's subordinated bonds.

130. Further, Deutsche Bank routinely securitized loans for which its valuation diligence exposed that the originator's appraisal significantly overstated the value of the mortgaged property. Yet when it disclosed to investors and rating agencies the property values, and LTV ratios and CLTV ratios based on those values, it without fail reported figures based on

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[11.] For pools of loans that Deutsche Bank purchased, it utilized a model to predict the expected losses on those loans prior to their securitization. Because high LTV and CLTV ratios negatively impact loss severity, when Deutsche Bank purchased loans with higher ratios than represented by the originator, it had to adjust the model accordingly. However, rating agencies generated the loss severity model used to model expected losses for Deutsche Bank's RMBS. Because Deutsche Bank misrepresented LTV and CLTV ratios to rating agencies, the loss severity models for Deutsche Bank's RMBS did not have the benefit of this adjustment.

the inflated originator appraisals, with no disclosure of the results of the Bank's valuation diligence. In other words, Deutsche Bank assessed its own risk tolerance based on accurate valuation data, but did not afford its investors the same courtesy.

i. Deutsche Bank's Valuation Diligence In Principal Transactions

131. Upon receiving the initial loan tape from the originator, Deutsche Bank would order an automated valuation model ("AVM") from a third-party provider for each loan on the tape. An AVM is a statistically based computer model that uses a variety of neighborhood and property specific data to generate an objective market value for the property in question. On completion of the AVM, Deutsche Bank would review the vendor's "AVM Analysis", which provided for each loan, among other things, the property value generated by the AVM, the variance between the AVM property value and the originator-appraised value (the "AVM Variance"), and an overall score, based on a variety of factors,[12] indicating the risk of default of the loan.

132. After reviewing the AVM Analysis, Deutsche Bank determined which loans would receive additional valuation diligence (the "Collateral Sample"). The factors Deutsche Bank used to determine the Collateral Sample varied over time, but the most prominent factor was an AVM Variance in excess of -15% (*i.e.*, Deutsche Bank's "official" value risk tolerance). Indeed, in response to a Standard & Poor's questionnaire in late 2007, Deutsche Bank admitted that it believed that a variance of -10% was an "inhibitor of salability" and that a variance of -15% was "considered potential fraud."

133. Moreover, Deutsche Bank often falsely represented to potential investors that if "the variance [between the AVM and appraised values] is greater than 15%" or if "no [AVM]

[12.] In addition to the AVM Variance, risk factors could include whether the property was located in an area with a high incidence of foreclosures, a low FICO score, or high debt to income level.

value is returned," an additional more detailed valuation . . . is obtained." Additional factors that merited further diligence included revised LTV or CLTV ratio over 100%, properties located in regions with high default rates, or borrowers that otherwise reflected substantial credit risk.

134. The "more detailed" valuation diligence performed on the Collateral Sample consisted of broker price opinions ("BPOs"). A BPO involved a licensed real estate broker visiting a mortgaged property and examining the exterior property, as well as the neighborhood in which the property resides, and reviewing the details of the property, *e.g.*, square footage, number of bedrooms and bathrooms, etc. The real estate broker would also take pictures of the property. The real estate broker then compared the mortgaged property to recent comparable sales and existing listings in the same geographic market—inspecting those properties as well—to arrive at a high and low supportable market value range for the mortgaged property.

135. Deutsche Bank made this representation because it knew that if the Bank did not perform additional diligence on loans for which the AVM Variance exceeded -15%, it would invariably be securitizing loans with unsupported appraisals, thus rendering false its LTV and CLTV representations. Indeed, in May 2006, Trader 1 requested valuation diligence results for an Ameriquest third-party transaction, the Diligence Supervisor informed him that

> We ran the credit sample through our AVM model and the variance percentage returned was the highest I had seen - 36% of the loans in the pool had a variance greater than -15%. We ordered only 80 BPOs, due to cost constraints, and rejected 34 loans or 32% of the collateral sample - you can imagine if a full review was conducted, what the rejection percentage would have been.

136. Upon completion of the BPOs for the Collateral Sample, Deutsche Bank engaged Clayton to conduct a "reconciliation analysis" in order to reconcile the originator's appraisal with the BPO value, if those values differed. The reconciliation analysis included a licensed appraiser obtaining the original appraisal and supporting documents, the AVM, and the BPO and

supporting documents. The third-party appraiser then reviewed all of the materials and arrived at a preliminary reconciled market value. The data collected by the third-party appraiser, as well as a detailed factual basis supporting the preliminary reconciled market value, was documented in an Excel spreadsheet referred to generally as the Open Value Issues Report.

137. The Open Value Issues Report was then provided to the originator in order to afford the originator with the chance to rebut the preliminary reconciled market value with additional comparable homes sales, existing listings, market information, or other data the originator believed relevant. If the originator provided a rebuttal, Clayton would consider the rebuttal and supporting evidence and arrive at a final reconciled market value.[13] The originator's rebuttal and the final reconciled market value would then be recorded in the Open Value Issues Report, along with the variance between the originator's appraisal and the final reconciled market value (the "Final Variance") as well as revised LTV and CLTV figures, based on the final reconciled market value, if appropriate. This document was titled the Final Open Value Issues Report.

138. Deutsche Bank trusted in and relied on the accuracy of the reconciliation analysis. Indeed, Deutsche Bank often used the Final Open Value Issues Report to determine which loans to purchase and which loans to reject, as well as to model for expected losses while it held the loans on its books.

139. The Final Open Value Issues Report, incorporating all of the above data, was available to any employee in Deutsche Bank's due diligence, mortgage trading and securitization desks, including the Diligence Supervisor, the Subprime MD, Trader 2, Trader 3 and a Director in the Securitization Group (hereinafter, the "Securitization Director"), among others, and was

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13. If the originator did not provide a rebuttal, the preliminary reconciled market value would stand as the final reconciled market value.

used by the due diligence and mortgage trading desks, in conjunction, to determine which loans to purchase for future RMBS.

140. Deutsche Bank represented to its investors that "if the new valuation is significantly above 90% [LTV], it will be automatically rejected," and that the "value of the property must be supported and the value must be greater than the loan amount or the loan is rejected."

141. Deutsche Bank's representations were false. If the Final Variance did not exceed -15%, Deutsche Bank as a matter of course purchased and securitized such loans regardless whether the LTV or CLTV ratios were "significantly above 90%," were "under water," *i.e.*, the LTV or CLTV exceeded 100%, or whether the originator appraisals were "supported". In fact, Deutsche Bank "typically" purchased loans with a Final Variance of as much as -20% (and higher) if the loans had a CLTV under 100%, the property was in "good condition," and the "borrower's credit profile [was] an acceptable risk," and in many instances even when these mitigating factors did not exist.

142. In addition, Deutsche Bank routinely purchased and securitized loans with LTV or CLTV ratios in excess of 100%, despite the Bank's frequent representation that it did not purchase or securitize loans for which the "value [was not] greater than the loan amount[.]" Indeed, as the Diligence Supervisor admitted to the Subprime MD on February 22, 2007, Deutsche Bank's Due Diligence Department, in order to get value rejections down, had been sending "[v]alue rejections to the Alt-A [trading] desk for review" and that there were "loans with revised BPO LTV ratios out of tolerance that the desk has been willing to accept[.]"

143. Similarly, only a few months earlier, the Diligence Supervisor informed the Subprime MD that, after completing valuation diligence on a $1 billion pool of New Century

loans and rejecting what loans they could, Deutsche Bank was "left with loans where the value is less than the loan amount." The Subprime MD replied that he was troubled that the Bank was "buying loans where it seems the BPO value is less than the loan amount." Despite the Subprime MD being "troubled," Deutsche Bank purchased out of this pool hundreds of New Century loans for which the revised LTV and CLTV ratios exceeded 100%. Deutsche Bank securitized those loans a short time later in ACE 2006-NC3.

144. Although Deutsche Bank frequently decided to purchase loans that were originated based on inflated appraisals, it also purchased loans that it determined, based on valuation diligence, did not present an acceptable risk profile. Deutsche Bank did so as a result of significant pressure from originators to purchase loans with inflated appraisals. Deutsche Bank complied with originators' demands—despite believing that inflated appraisals rendered the loans unacceptably risky—because it believed that if it did not comply, originators would cut off the flow of loans to the Bank. Deutsche Bank also frequently obtained discounts on risky loans that it accepted.

145. Because Deutsche Bank understood the true value of the properties securing the loans it purchased, it was able to make a full and informed decision as to whether a loan presented an acceptable risk. It did not afford investors the same opportunity.

ii. Deutsche Bank's Valuation Diligence In Third-Party Transactions

146. Deutsche Bank performed valuation diligence on only 11 out 71 third-party transactions it underwrote, and only when Deutsche Bank itself took on some risk associated with the transaction. It neglected any valuation review for 60 securitizations despite the fact that the Bank believed that it was "common knowledge" that appraisers were under "intense pressure from lenders" to provide appraisals that would justify originating the loan, that there was a "lot of bias in the industry at the time," and that "brokers [were] 'giving' appraisers the value they

want[ed]." Indeed, Deutsche Bank's Diligence Supervisor affirmatively believed that fraud was taking place in the appraisal industry.

147. For the limited number of third-party securitizations on which Deutsche Bank performed valuation diligence, the mechanics of that diligence—AVMs followed by BPOs on a subset of loans followed by a reconciliation review—were mostly the same as for Deutsche Bank's own principal transactions. There were, however, two substantial differences.

148. First, although Deutsche Bank generally ran AVMs for the entire tape of loans to be securitized,[14] it ordered BPOs on only a small fraction of those AVMs that reflected an AVM Variance of in excess of -15% from the originator's appraisal, and frequently declined to order BPOs even when the AVM Variance was much greater than -15%. In one instance, the Bank ordered BPOs only on refinances and only when a refinance was coupled with a greater than -30% variance.

149. Deutsche Bank decided not to order additional BPOs even when a significant percentage of the BPOs it ordered confirmed the accuracy of the large variances in the AVM Analysis. In other words, despite substantial evidence that hundreds of loans in a given securitization were originated based on substantially inflated appraisals, Deutsche Bank refused to perform further diligence.

150. By refusing to perform further diligence, it decided not to confirm appraisal fraud in the loans for which Deutsche Bank knew fraudulent appraisals were indicated. Deutsche Bank actively decided not to run BPOs on loans it normally would have, if it were purchasing and securitizing the loans, partly in order to save money.

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14. In fact, in order to keep its costs down, Deutsche Bank did not always order AVMs on the entire loan tape.

151. More importantly, Deutsche Bank understood that it could not securitize loans with defects that violated representations made in the Prospectus Supplements, (such as that no loan was originated with a LTV or CLTV ratio in excess of 100%), though Deutsche Bank frequently did so. Indeed, as the Diligence Supervisor informed the Subprime MD with regard to other key issues such as compliance, "Keep[] in mind [that] whatever compliance issues we find [in the loans], we may not be able to put in a securitization . . . ." For this reason, the Diligence Supervisor suggested that Deutsche Bank intentionally limit what it learned about the loans it was considering for securitization, by limiting "our sample sizes to less than 300 loans."

152. The second substantial difference in valuation diligence was that, even for the loans on which Deutsche Bank performed full valuation diligence, it exercised far greater lenience in allowing loans to be securitized. For instance, Deutsche Bank had no set risk tolerance with regard to variances between origination appraisals and values reflected by AVMs/BPOs/reconciliation analyses, routinely "clearing loans with variances greater than -15% as long as the LTV/CLTV d[id] not exceed 100%." Indeed, Deutsche Bank cleared loans with variances greater than -15% even if the LTV/CLTV exceeded 100%. As the Diligence Supervisor instructed his team after a value review on a third-party transaction, the securitizing entity was "expecting [Deutsche Bank] to clear the majority of value issues (if not all) and to provide the 'standard' flexibility we typically use on securitization tie outs."

153. Deutsche Bank's practice was to conduct little to no valuation diligence on third-party transactions despite its knowledge of a high probability that many loans in those securitizations were based on inflated appraisals. This practice, in conjunction with the lenience that Deutsche Bank exercised in the instances in which it did conduct valuation diligence, resulted in severely understated LTV and CLTV ratios being represented to investors.

iii. Deutsche Bank's Knowledge Of The Importance To Investors Of LTV And CLTV Ratios

154. Deutsche Bank knew that LTV and CLTV ratios were of significant importance to its investors.

155. For example, in several deals, including, for example, MHL 2007-1, investors pulled out of or declined to subscribe to an issuance after finding that the LTV/CLTV ratios were higher than expected or desired.

156. In another instance, INDX 2005-AR13, after an investor suffered unusually high loss severities on a bond underwritten by Deutsche Bank, it complained to the Bank about appraisal fraud and demanded that a loan with clear appraisal fraud be put back to the originator.

157. Investors routinely requested information regarding second liens, which impacted substantially a loan's CLTV. And as the Diligence Supervisor observed in discussing Deutsche Bank's risk tolerance for loan purchases, "[i]t makes a big difference when you have a variance on a Purchase at 80% LTV/CLTV than one with 80% LTV/100% CLTV."

158. Thus, Deutsche Bank understood that LTV and CLTV ratios were material to investors' decisions to purchase RMBS securitized or underwritten by the Bank.

iv. Deutsche Bank Knowingly Misrepresented Its Valuation Diligence Process And The LTV And CLTV Ratios Of Loans It Purchased And Securitized

159. Deutsche Bank, in its attempt to convince investors and rating agencies of the soundness of its value related representations, portrayed its valuation diligence process as far more comprehensive, and its standard for rejecting a loan based on unsupported value as far more rigorous, than they were. Thus, Deutsche Bank instilled in investors and rating agencies a false sense of trust regarding the Bank's representations regarding LTV and CLTV ratios.

160. In a significant number of Deutsche Bank-sponsored RMBS, the Bank made consistent and material misrepresentations concerning the LTV or CLTV ratios of the loans collateralizing the RMBS. The result of these significant and wide-ranging misrepresentations was not only a higher probability of default, but also a greater likelihood of loan-level losses when those defaults occurred.

161. The specific deals referenced below are illustrative only. Deutsche Bank's misconduct and misrepresentations with regard to property valuations were consistent across a significant number of securitizations.

ACE 2006-HE2

162. The closing date for ACE 2006-HE2, a $917 million issuance comprised of 5,198 loans, was April 28, 2006. The primary originators of loans securitized in ACE 2006-HE2 were Argent, Chapel, and CIT Group, Inc. ("CIT"), which originators were responsible for over 50% of the loans securitized in the deal.

163. In addition to Deutsche Bank's knowledge of appraisal fraud in the mortgage market generally, and that appraisers were often providing originators with whatever appraisal was necessary for a borrower to obtain a loan, Deutsche Bank knew of especially serious problems at originators that provided loans for ACE 2006-HE2.

164. Specifically, on January 16, 2006, the Diligence Supervisor observed in a discussion with Clayton that "Chapel's valuation process has serious issues" and that "appraised values are very distorted."

165. In a later January conversation with Clayton, the Diligence Supervisor more pointedly stated that Chapel's "appraisers are trying to mislead us as often as they can" and that

"Chapel purposely put loans that were rejected by another investor due to inflated values into [the] pool" from which loans were taken to securitize into ACE 2006-HE2.

166. Similarly, with regard to CIT loans purchased to securitize in ACE 2006-HE2, the Diligence Supervisor characterized the "AVM results [as] undoubtedly the most surprising I've seen," as a result of the large number of loans with significant AVM Variances.

167. Despite overwhelming knowledge, both general and specific, regarding the epidemic of inflated appraisals, Deutsche Bank decided not to conduct full valuation diligence on ACE 2006-HE2 loans that either preliminarily indicated appraisal fraud or for which Deutsche Bank was unable to get an initial AVM value.

168. Of the 11,578 loans, from multiple originators, that comprised the loan pools from which Deutsche Bank selected in order to issue ACE 2006-HE2, 2,055 loans had an AVM Variance in excess of -15%. And despite Deutsche Bank's representation that if "the variance [between the AVM and appraised values] is greater than -15%" "an additional more detailed valuation . . . is obtained," the Bank determined not to conduct further diligence on 224 of those loans. Of those 224 loans for which the AVM indicated potential appraisal fraud, Deutsche Bank securitized 96, representing $16.17 million by principal balance of the issuance.

169. Similarly—and again contrary to Deutsche Bank's representation that it conducted further diligence on loans for which "no [AVM] value is returned"—Deutsche Bank decided not to conduct further diligence on 62 of the 261 loans that came back with no AVM value. Thirteen of these loans were securitized.

170. Of the ACE 2006-HE2 loans for which Deutsche Bank conducted full valuation diligence, Deutsche Bank securitized hundreds for which the final reconciled market value reflected a substantially inflated appraisal, the revised CLTV was in excess of 100%, or both.

The securitized loans included over 100 loans purportedly out of Deutsche Bank's tolerance due to a Final Variance in excess of -15%.

171. Specifically, Deutsche Bank securitized 142 loans, representing a principal balance of $23.54 million, for which the Final Variance exceeded -15%, *i.e.*, loans that were purportedly outside of Deutsche Bank's risk tolerance. A substantial portion of these "out of tolerance" loans also had LTV and CLTV ratios above 100%. Nevertheless, Deutsche Bank represented for these loans CLTV ratios based on the originators' appraisals.

172. Deutsche Bank securitized an additional 286 loans, representing $47.34 million, for which the revised CLTV based on the final reconciled market value exceeded 100%. Nevertheless, Deutsche Bank represented in the Prospectus Supplement that no securitized loan had a CLTV in excess of 100%.

173. Deutsche Bank securitized an additional 131 loans, representing $23.32 million, for which the final reconciled market value indicated a Final Variance between -10% and -15%. Nevertheless, Deutsche Bank represented for these loans CLTV ratios based on the originator's appraisal.

174. Deutsche Bank purchased loans for ACE 2006-HE2 with substantially inflated appraisals at least in part as a result of originator pressure. In other words, after the Bank determined that a property's true value rendered the loan an unacceptable risk, it was nevertheless coerced by the originator into purchasing the loan.

175. Specifically, for example, in January 2006, Deutsche Bank purchased from Town & Country for inclusion in ACE 2006-HE2 a $77 million pool of loans. After Deutsche Bank concluded its diligence and made final decisions as to which loans would be rejected on the basis of unsupported valuations, Town & Country was upset with the value rejection percentage. In

order to pressure Deutsche Bank into purchasing loans it had decided posed an unacceptable valuation risk, a Town & Country executive officer personally reached out to the Subprime MD to persuade him to purchase 20 loans that had been rejected for value issues.

176. Deutsche Bank capitulated. As the Diligence Supervisor instructed certain of his colleagues, "[the Subprime MD] has been in discussions for 2 days with . . . [an executive officer at] Town and Country. We have gone back 3 times and have cleared additional loans as [he] was very upset with the rejection percentage."

177. Deutsche Bank similarly capitulated to demands by Argent, agreeing to purchase previously rejected loans, including a loan with a final reconciled market value 38% below the appraised value resulting in a revised LTV of 145%.

178. In total, for $94 million of loans in ACE 2006-HE2—representing 10% of the issuance by principal balance—Deutsche Bank knowingly misrepresented the CLTV ratio and/or that the loans' CLTV ratio did not exceed 100%. For an additional 1.75% of the loans in ACE 2006-HE2, Deutsche Bank disregarded an AVM Variance that indicated appraisal fraud and decided not to conduct further diligence on the loans.

179. In significant part as a result of Deutsche Bank's misconduct, investors in ACE 2006-HE2 suffered considerable losses. The loans securitized in ACE 2006-HE2 have lost $295 million, representing 31% of the collateral in the deal, and are projected to lose $310 million, representing 33% of the collateral in the deal.

DBALT 2006-AB4

180. The closing date for DBALT 2006-AB4, a $1.1 billion issuance comprised of 5,422 loans, was September 29, 2006. The primary originator of loans securitized in DBALT 2006-AB4 was AHM, which originated nearly 40% of the loans in the issuance. In addition,

MortgageIT, later acquired by Deutsche Bank, originated approximately 5% of the loans in the issuance.

181. Deutsche Bank was aware that AHM and MortgageIT routinely originated loans based on substantially inflated and fraudulent appraisals.

182. In March 2006, the Diligence Supervisor informed a mortgage trader that “Value Issues in Alt-A pools [had been] increasing significantly in the last 5-6 months.” Indeed, the value issues with AHM and MortgageIT had become so pervasive that the Diligence Supervisor began doing his own quality control checks of the value reconciliation analysis. These checks confirmed the accuracy of reconciliation process. As the Diligence Supervisor informed the mortgage trader, “I have been looking very closely at these variances . . . and am convinced our values are truly supported.”

183. Additionally, in January 2007, the Diligence Supervisor informed the Deutsche Bank relationship manager for AHM that, since Deutsche Bank began purchasing loans from AHM, “the Company’s variances on our AVM analyses are some of the highest of all Sellers[.]”

184. Indeed, on an AHM pool of loans purchased shortly after DBALT 2006-AB4 closed, the Diligence Supervisor stated that he had noticed that for loans being refinanced only 5-7 months after the borrower initially purchased the property, “AHM had increased the value between 10-40% for the refinance.” He stated further that “there were several [loans] I felt went beyond misrepresentation into the fraudulent area.”

185. In other words, Deutsche Bank knew that it was securitizing loans that were originated based on unsupported and fraudulent appraisals.

186. Nevertheless, Deutsche Bank again decided not to conduct full valuation diligence on DBALT 2006-AB4 loans that either preliminarily indicated appraisal fraud or for which Deutsche Bank was unable to get an initial AVM value.

187. Of the 15,946 loans, from multiple originators, that comprised the loan pools from which Deutsche Bank selected in order to issue DBALT 2006-AB4, 3,189 loans had an AVM Variance in excess of -15%. And despite Deutsche Bank's representation that if "the variance [between the AVM and appraised values] is greater than 15%," then "an additional more detailed valuation . . . is obtained," the Bank determined not to conduct further diligence on 673 of those loans. Of those 673 loans, Deutsche Bank securitized in DBALT 2006-AB4 143 loans for which the AVM indicated appraisal fraud, representing $30 million by principal balance of the issuance.

188. Similarly—and again contrary to Deutsche Bank's representation that it conducted further diligence on loans for which "no [AVM] value is returned"—763 loans came back with no AVM Value. Of those 763, Deutsche Bank decided not to conduct further diligence on 501, 135 of which were securitized.

189. In addition to Deutsche Bank's knowledge of substantial appraisal problems generally at AHM and other originators whose loans were securitized in DBALT 2006-AB4, Deutsche Bank's due diligence team, after completing valuation diligence on a $118 million pool of AHM loans to be securitized in part in DBALT 2006-AB4, alerted Trader 3 of significant value problems within the pool.

190. Specifically, on June 25, 2006, an Associate in the Due Diligence group raised with the Diligence Supervisor the fact that the valuation diligence process for the $118 million pool had resulted in an unusually high "value kick rate." He then informed the Diligence

Supervisor that there were 10 loans with revised LTV ratios between 90-100% and 23 loans with revised LTV ratios in excess of 100%. With only one exception, the diligence for all 33 loans reflected a Final Variance in excess of -18%.

191. With respect to the unusually high value kick rate, the Diligence Supervisor stated that "AHM has large variances with it AVMs and BPOs and ultimately Value rejections." (*Sic.*) He instructed his associate to "[s]end [Trader 3] the list," although the Diligence Supervisor suspected "[Trader 3] may elect to reject all." The Diligence Supervisor was incorrect.

192. After the Final Open Value Issues Report for the 33 loans was sent to Trader 3, Deutsche Bank cleared for purchase 7 of the 33 loans. All seven loans had Final Variances in excess of -15% and three of the loans had Final Variances in excess of -20%. Two of the purchased loans had revised LTV ratios in excess of 100% and 6 of the purchased loans had revised CLTV ratios in excess of 100%. Five of these purchased loans were securitized in DBALT 2006-AB4.

193. Overall, Deutsche Bank securitized hundreds of loans for which it knew that the final reconciled market value reflected a substantially inflated appraisal, the revised LTV was in excess of 100%, or both.

194. Specifically, Deutsche Bank securitized 90 loans, representing a principal balance of $22.25 million, with a Final Variance in excess of -15%. A substantial portion of these "out of tolerance" loans also had LTV and CLTV ratios above 100%. Nevertheless, Deutsche Bank represented for these loans LTV ratios based on the originator's appraisal.[15] These securitized loans included, for instance, an AHM originated loan with a -22% variance, 102% LTV, and 124% CLTV.

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[15] For Deutsche Bank's "ACE" deals, it represented the CLTV ratios of the securitized loans. For Deutsche Bank's "DBALT" deals it represented the LTV ratios.

195. Deutsche Bank securitized an additional 72 loans, representing $11.04 million, for which the revised LTV based on the final reconciled market value exceeded 100%. Nevertheless, Deutsche Bank represented in the Prospectus Supplements that no securitized loan had an LTV in excess of 100%.

196. Deutsche Bank securitized an additional 109 loans representing $21.23 million—or 1.9% of the issuance—for which the final reconciled market value indicated a Final Variance between -10% and -15%. Nevertheless, Deutsche Bank represented for these loans LTV ratios based on the originator's appraisal.

197. In total, Deutsche Bank knowingly misrepresented the LTV ratios and/or that the loans' LTV ratios did not exceed 100%, for $54.52 million of loans in DBALT 2006-AB4—representing nearly 5% of the issuance. For an additional 2.9% of the loans in DBALT 2006-AB4, Deutsche Bank disregarded an AVM Variance that indicated appraisal fraud and decided not to conduct further diligence on the loans.

198. In significant part as a result of Deutsche Bank's misconduct, investors in DBALT 2006-AB4 suffered considerable losses. The loans securitized in DBALT 2006-AB4 have lost $311 million, representing 28% of the collateral in the deal, and are projected to lose $365 million, representing 33% of the collateral in the deal.

2007

199. In 2007, Deutsche Bank purchased and securitized thousands of additional loans with inflated appraisals, continuing intentionally to represent LTV and CLTV ratios based on those appraisals.

200. Deutsche Bank's conduct in 2007 was even more objectionable given the trends that it observed at that time.

201. Namely, by early 2007, Deutsche Bank knew that the already existing problem with inflated and fraudulent appraisals was being exacerbated by a tightening credit market and decelerating or depreciating home values.

202. For example, in May 2007, the Diligence Supervisor informed the Subprime MD, the Mortgage Finance MD, Trader 2, Trader 4 and others that:

> In reviewing the AVM analysis on a large number of 2007 Alt-A pools across all Sellers (Countrywide, AHM, IndyMac, Greenpoint, Wachovia), the percentage of loans with variances is steadily climbing. . . . Brokers/Lenders will continue to exert pressure on appraisers to meet value expectations and with home prices experiencing rapid deceleration/depreciation, I expect values to continue deteriorating through 2007.

203. However, rather than tighten its valuation diligence and processes and restrict the loans it was purchasing—or, at a minimum, begin to disclose to investors the true LTV and CLTV ratios—Deutsche Bank in fact loosened its valuation standards in order to appease originators.

204. As the Diligence Supervisor stated to Trader 2 and the Mortgage Finance MD in May 2007 after describing the trend of increasing valuation problems, "[w]e are finding ourselves going back quite often and clearing large numbers of loans [with inflated appraisals] to bring down the deletion percentages. I expect this trend to continue through the year."

205. But Trader 2 was well aware that Deutsche Bank was expanding its risk tolerance in order to keep originators happy and thereby keep production of loans flowing. For example, despite the Diligence Supervisor's belief that AHM appraisals went "beyond misrepresentation into the fraudulent area," in late 2006 and early 2007, Trader 2 instructed the Diligence Supervisor to expand the Bank's variance tolerance from -15% to -20% with regard to AHM loans (which numbered in the hundreds of millions of dollars in the first quarter of 2007) so that AHM would continue doing business with the Bank.

206. In Trader 2's words, he was "willing to take a calculated risk and accept a 20 pct [percent] variance threshold if you think that could be the tipping point in keeping the AHM DB relationship at a point where they'll continue to sell us loans." Trader 2 accounted for this "calculated risk" on Deutsche Bank's books by "proportionally increase[ing] [the] loss severities" that he was modeling for. Deutsche Bank did not provide its investors with the opportunity to account for the calculated risk Trader 2 decided to take.

207. Deutsche Bank's determination to expand its risk tolerance with regard to loans with inflated and fraudulent appraisals was based, in addition to Deutsche Bank's need to appease originators, on Deutsche Bank receiving favorable prices on the fraudulent loans, including on loans from Countrywide.

208. For instance, in February 2007, after describing for the Subprime MD certain originator's "frustration" with "value rejections," the Diligence Supervisor informed the Subprime MD that:

> We have begun sending our Value rejections to the Alt-A desk for review – there have been loans with revised BPO LTV ratios outside of tolerance that the desk has been willing to accept – some with a price adjustment. Sellers have viewed this as a positive step in providing relief from the large percentages of Value deletions.

209. In May 2007, when discussing with Clayton the valuation diligence for over a billion dollars in Countrywide loans, the Diligence Supervisor instructed an employee at Clayton that "I would like to point out we purchased these 3 [Countrywide] pools at a very competitive price so we were able to provide addl. flexibility w/clears. We just purchased 3 more today; however, I was told we paid more and will be taking a more conservative approach."

210. In other words, as originators increased their incidence of appraisal fraud, Deutsche Bank enriched itself by paying reduced prices for risky loans while representing to investors LTV and CLTV ratios based on appraisals the Bank knew to be inflated.

211. Deutsche Bank's expanded tolerance for appraisal fraud, even in the face of an acknowledged increase in the problem, was reflected in its 2007 RMBS issuances.

v. Deutsche Bank Consciously Disregarded The Falsity Of The LTV And CLTV Ratios In Third-Party Deals

212. Despite Deutsche Bank's knowledge of pervasive and consistent appraisal inflation and fraud throughout the origination industry—including specifically and most pervasively at many of the originators for which Deutsche Bank underwrote RMBS securitizations—the Bank decided to perform valuation diligence on only a small portion of the loans in these issuances, and then only when Deutsche Bank retained some risk on the issuance.

213. For example, in each of the following third-party deals, Deutsche Bank, in order to save money and to appease the sponsor—which uniformly was an originator that also sold loans to the Bank to securitize on its own shelves—disregarded substantial initial evidence of inflated appraisals and consciously determined not to perform additional diligence, *i.e.*, a full reconciliation analysis, to confirm that initial indication of fraud.

ARSI 2006-M1

214. The closing date for ARSI 2006-M1, a $3 billion issuance comprised of 14,828 loans, was June 28, 2006.[16] ARSI 2006-M1 securitized loans from two affiliated originators—Argent and Ameriquest Mortgage Company ("AMQ").

215. Deutsche Bank believed that AMQ engaged in among the worst and most pervasive appraisal fraud in the mortgage industry.

216. In May 2005, when discussing loss severities on past AMQ loans purchased by the Bank, the Diligence Supervisor stated to Trader 1:

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[16] Only approximately 12,300 loans were included in the securitization upon the initial closing date. However, less than two weeks after closing an additional, pre-funded approximately 2600 loans were added to the securitization. No diligence was performed on the subsequently added loans.

> We should never buy AMQ loans[.] AMQ appears to have very little control on its valuation process. The variances I see when doing their Securitization reviews [*i.e.*, when Deutsche Bank acted only as underwriter] is the highest (35-40+% >-15%) of all Sellers. I recently had the opportunity to talk with a former employee of AMQ . . .; he had some frightening stories of what they are doing to skew values. I believe the lack of controls at the Company comes from senior management on down and many of the abuses we are reading in the newspapers are more widespread then most people realize. (*Sic.*)

217. Despite its knowledge of AMQ's extreme appraisal fraud, Deutsche Bank did not conduct additional valuation diligence. To the contrary, the Bank conducted less.

218. Deutsche Bank co-underwrote ARSI 2006-M1 primarily with Merrill Lynch, Pierce, Fenner & Smith Inc. ("Merrill") and Credit Suisse Securities LLC ("CS") (the "Syndicate"). Lehman Brothers Inc. and Greenwich Capital Markets, Inc., collectively, underwrote 10% of the issuance. The Syndicate was responsible for diligence on the issuance.

219. When the time came for valuation diligence, an associate at Deutsche Bank circulated a budget that provided for AVMs on the entire loan pool, but BPOs on only approximately 5% of the pool. In response, an employee at CS stated that it "typically [did] BPOs on loans that don't get AVM hits or on loans whose AVM value falls outside a particular variance," and that "[t]his generally ends up being significantly higher than 5% of the pool." The Deutsche Bank associate agreed, stating that the "more AVMs we do, the more BPOs we will have to do." He therefore suggested that, in order to circumvent Deutsche Bank's and CS's valuation diligence practices, the group might consider refraining from performing AVMs on the entire pool.

220. Notwithstanding Deutsche Bank's recommendation, the Syndicate did run AVMs on the entire initial loan tape. Of the approximately 12,300 loans for which an AVM was

obtained, 2423 loans representing $489 million—or nearly 20% by principal balance—reflected an AVM variance in excess of -15%. An additional 140 loans returned no AVM hit.

221. Despite Deutsche Bank's and CS's acknowledgement of the Syndicate members' practices of ordering BPOs for all out-of-tolerance AVMs and any loan for which the AVM did not return a value, the Syndicate, in order to keep their own costs below $350,000, chose only 580 loans for which to order BPOs, representing only 16% by principal balance of the loans with an AVM Variance in excess of -15%.

222. Of the 580 loans for which the Syndicate ordered BPOs, 133 loans were confirmed by the reconciliation analysis to have a Final Variance in excess of -15%. In other words, for the loans on which the Syndicate performed full valuation diligence, the AVM's initial indication of appraisal fraud was confirmed for nearly 25% of the loans.

223. Of the 2132 loans for which the AVM initially indicated a fraudulent appraisal, but for which the Syndicate disregarded this indication, 130 loans representing $33.5 million had an AVM Variance in excess of -50%; for an additional 416 loans representing $80 million the AVM Variance was between -30% and -50%; for an additional 799 loans representing $164.2 million—or approximately 5.5% by principal balance of the issuance—the AVM Variance was between -20% and -30%; and for the remaining 787 loans representing $159 million—or approximately 5.3% by principal balance of the issuance—the AVM Variance was between -15% and -20%.

224. For 14.5% of the loans securitized in ARSI 2006-M1, the AVM Variance exceeded -15%, and yet Deutsche Bank determined to conduct no additional diligence. Deutsche Bank made this determination despite the Diligence Supervisor's knowledge of pervasive

appraisal fraud at AMQ and despite the fact that for the loans on which the Bank did conduct full valuation diligence, the AVM's initial indication of fraud was confirmed nearly 25% of the time.

225. In other words, Deutsche Bank decided not to confirm the high probability, if not certainty, that a substantial number of loans securitized in ARSI 2006-M1 were originated based on inflated appraisals, and that the representations in the ARSI 2006-M1 Prospectus Supplement regarding LTV and CLTV ratios were false.

226. In significant part as a result of Deutsche Bank's misconduct, investors in ARSI 2006-M1 suffered considerable losses. The loans securitized in ARSI 2006-M1 have lost $963 million, representing 32% of the collateral in the deal, and are projected to lose $1.1 billion, representing 35% of the collateral in the deal.

vi. RMBS Issuances Affected By Valuation Misrepresentations

227. Deutsche Bank securitized thousands of loans for which it made one or more of the above misrepresentations. Appendix B shows the percentage by principal balance of loans securitized in violation of such representations in a selection of Deutsche Bank RMBS.

B. Deutsche Bank Knowingly Misrepresented Combined Loan To Value Ratios By Concealing Second Liens

228. Deutsche Bank also knowingly misrepresented CLTV ratios by concealing the existence and impact of second liens in RMBS issued on its ACE shelf.

229. In 2006 and 2007, the Prospectus Supplements for Deutsche Bank's ACE RMBS represented in stratification tables the CLTV of the underlying mortgages, as well as summary CLTV and weighted CLTV averages for the underlying mortgage pools in the security.

230. The underlying collateral securitized in the majority of Deutsche Bank's ACE RMBS offerings included a combination of both first and second liens. It was not uncommon for Deutsche Bank to securitize both the first and second liens on the same property in the same

RMBS. Often, however, only the first lien, but not the second lien, was securitized in a single RMBS. Alternatively, sometimes only the second lien, but not the first lien of the same property, was securitized.

231. Deutsche Bank knew, based on the loan tapes of pools that it purchased from originators, that a vast number of the loans securitized in in its ACE RMBS contained multiple liens on the same property.

232. But Deutsche Bank concealed from investors the existence and impact of second liens on the CLTV ratios of the first lien loans that it securitized, and thus misrepresented the CLTV ratios in 27 ACE deals between 2006 and 2007. Deutsche Bank knowingly represented the LTV ratios of the first liens that it securitized as CLTV ratios for those loans, even though Deutsche Bank knew that there were second liens on the same properties.

233. For example, in the Prospectus Supplement for ACE 2006-HE1, Deutsche Bank represented that 4,925 loans had CLTV ratios between 75 and 80%. However, Deutsche Bank knew that 3,873 of those loans had a second lien on the same property, and that the actual CLTV of those loans was close to or 100%. Thus, if Deutsche Bank had accurately represented the CLTV for the loans in ACE 2006-HE1, the number of loans with CLTVs of 75-80% would be only 1,142, but the number of loans with CLTVs between 95 and 100% would have more than doubled from 2,913 to 6,786.

234. Appendix C shows that Deutsche Bank knowingly underrepresented the number of loans with CLTV ratios of 95-100% in ACE RMBS between 2006 and 2007 by 5.18% to 59.24% of the entire security.

235. Deutsche Bank knew that the CLTV of the mortgage loans, and the impact of second liens on that ratio, were important to investors.

236. In February 2005, Deutsche Bank's research group explained to investors that, when issuing RMBS, the "issuer specifically chooses to disclose" the existence of "silent" second liens in the security:

> Often the LTV ratio on the first lien loan is 80%, and the LTV ratio on the second lien loan is 15% or even 20%, making the combined LTV 95% or 100%. Because the second lien loans are not included with the first lien mortgages being securitized, ordinary pool statistics relating to the first lien mortgages often do not reflect the existence of the second lien loans, unless the issuer specifically chooses to disclose their existence. (These loans are often thus referred to as "silent".)

237. But Deutsche Bank did not warn investors that, as an issuer of RMBS, it chose not to disclose the impact of second liens on CLTV ratios.

238. For example, in June 2005, an investor requested from Deutsche Bank the percentage of silent second liens in ACE 2005-HE4. In response to the request, Trader 1 directed his team to "[t]ell them verbally its 32.4 I think . . . But don't put in [the] prospectus."

239. Indeed, while Deutsche Bank knowingly misrepresented CLTV ratios to investors by not disclosing second liens in Prospectus Supplements, Deutsche Bank simultaneously expected mortgage loan originators to accurately disclose them to Deutsche Bank. Trader 2 stated that, when he bid on pools of loans to purchase from originators, he expected originators to provide accurate CLTV ratios with silent second liens. Similarly, when the Diligence Supervisor identified loans in due diligence samples with CLTV ratios that did not accurately account for silent second liens, he raised those concerns with the originator.

240. Although investors expected Deutsche Bank to disclose full and accurate CLTV ratios—including second liens—Deutsche Bank disclosed second liens to investors only when investors specifically asked for that information.

241. Thus Deutsche Bank knowingly misrepresented to investors accurate CLTV ratios of the mortgage loans in Prospectus Supplements that were necessary for them to be able to make an informed economic decision about investing in Deutsche Bank's ACE RMBS.

IV. Deutsche Bank Intentionally Misrepresented Borrowers' FICO Scores

242. In 2006 and 2007, Deutsche Bank represented to investors in Prospectus Supplements for both principal and third-party transactions the FICO scores of the borrowers whose mortgage loans backed its RMBS.

243. Specifically, Deutsche Bank represented borrowers' FICO scores "as of the cut-off date" of the security. The "cut-off" date was typically the first day of the month that the security closed.

244. But the FICO scores that Deutsche Bank represented to investors were not FICO scores "as of the cut-off date" of the RMBS. Instead, Deutsche Bank knowingly represented borrowers' FICO scores as of the time of the origination of their loans. Deutsche Bank knew, by "refreshing" borrowers' FICO scores during due diligence, that borrowers' FICO scores at the time of origination had often declined materially by the cut-off date.

245. Additionally, in principal transactions, Deutsche Bank represented to investors that it "does not make any representations or warranties as to the actual performance of any Mortgage Loan or that a particular FICO Score will not change over time." But Deutsche Bank already knew that FICO scores had often declined and concealed that information from investors.

246. Deutsche Bank knew that FICO scores predicted a borrower's risk of default on a mortgage loan. Deutsche Bank routinely stated to investors, in both offering documents and marketing presentations, that FICO scores are a statistical method used to predict the default risk posed by potential borrowers, and that a borrower with a higher FICO score is statistically

expected to be less likely to default in payment of their loan than a borrower with a lower FICO score.

247. For that reason, beginning in 2005, the Diligence Supervisor began "refreshing" borrowers' FICO scores for all of the loans that the Bank was purchasing from mortgage loan originators. Based on the results, the Diligence Supervisor stated that "I'm amazed at how quickly some of these borrowers' credit deteriorates so soon after the loan is originated. I've seen bankruptcies, foreclosures and even found a borrower that had passed away since origination!"

248. In 2006 and 2007, Deutsche Bank rejected loans from pools purchased from mortgage loan originators solely because the borrowers' FICO scores declined materially, which Deutsche knew was a strong indicator that the borrower would not have the ability to pay their loan. Additionally, Deutsche Bank priced the loans that it purchased from mortgage loan originators differently depending on the FICO scores of the borrowers.

249. Indeed, in April 2006, the Diligence Supervisor warned his Due Diligence team that refreshing FICO scores "is vital for preventing the purchase of adverse loans that could become EPDs [Early Payment Defaults]."

250. Moreover, rating agencies often requested from Deutsche Bank refreshed FICO scores for borrowers with loans seasoned six months or more. FICO scores affected rating agencies' calculations of loss coverage levels for Deutsche Bank's RMBS.

251. Despite the importance of refreshed FICO scores to Deutsche Bank, Deutsche Bank knowingly concealed from investors the refreshed FICO scores that had declined materially.

252. For example, when Trader 3 was asked by another Deutsche Bank employee whether the Bank should withhold securitizing from DBALT 2006-AR5 a number of loans with FICO scores that Trader 3 knew had dropped below 600, Trader 3 declined, directing the employee to "leave them in. We should rep[resent] original ficos anyway into the deal."

253. The FICO scores of the mortgage loans that Deutsche Bank represented to investors in Prospectus Supplements would have changed materially if Deutsche Bank disclosed the refreshed FICO scores that it knew had already declined. In particular, the lower FICO ranges of the "Tabular Characteristics" of each Prospectus Supplement would have increased materially if Deutsche Bank disclosed borrowers' refreshed FICO scores.

254. Deutsche Bank knew that FICO drift in lower FICO ranges had a greater effect on a borrower's credit than the same amount of drift in higher FICO ranges. Trader 4 explained to a salesperson that, "[y]ou should also keep in mind that in the 700s, a 8 point move in FICO has a very incremental effect on credit. It would be more pronounced in the low to mid 600 range." (*Sic.*)

255. Additionally, Deutsche Bank knew that the refreshed FICO scores for significant numbers of loans securitized in RMBS sponsored and underwritten by Deutsche Bank dropped below the minimum threshold represented in the Prospectus Supplements for those deals.

256. For example, the refreshed FICO scores of the borrowers with loans securitized in ACE 2006-NC3 dropped dramatically, but Deutsche Bank did not represent those scores to investors. If Deutsche Bank had disclosed the refreshed FICO scores that it knew had declined in that deal, the number and percentage of loans represented in the lower ranges of the FICO tables in the Prospectus Supplement would have increased significantly and the minimum FICO score represented would have plummeted.

257. For instance, Deutsche Bank represented that no loans were securitized in ACE 2006-NC3 to borrowers with refreshed FICO scores of less than 500. However, Deutsche Bank learned that the FICO scores for 569 borrowers with loans securitized in ACE 2006-NC3 dropped below 500, representing approximately 5.56% of the entire security by aggregate principal balance outstanding as of the cut-off date.

258. Additionally, the percentage of loans by aggregate principal balance securitized in ACE 2006-NC3 with refreshed FICO scores that dropped below 550 nearly doubled from 11.23% to 22.22%. Indeed, Deutsche Bank knew, according to the Diligence Supervisor, that "there are no true compensating factors to mitigate the risk of the borrowers with" FICO scores less than 550.

259. Similarly, for example, the refreshed FICO scores of the borrowers with loans securitized in DBALT 2006-AR2 dropped materially, but Deutsche Bank concealed those scores from investors. As in ACE 2006-NC3, if Deutsche Bank had disclosed the refreshed FICO scores that it knew had declined in DBALT 2006-AR2, the number and percentage of loans represented in the lower ranges of the FICO tables in the Prospectus Supplement would have increased significantly and the minimum FICO score represented in the deal would have plummeted.

260. For instance, Deutsche Bank represented that only six loans were securitized to borrowers with FICO scores of less than 600 in DBALT 2006-AR2. However, after refreshing borrowers' FICO scores, Deutsche Bank learned that the scores for 56 loans securitized in DBALT 2006-AR2 dropped below 600, representing approximately 2.65% of the entire security by aggregate principal balance outstanding as of the cut-off date. Moreover, Deutsche Bank

learned that the FICO scores for 126 Alt-A loans in the deal—6.33%—dropped below 620, which was even lower than the FICO average of approximately 625 for subprime loans in 2006.

261. Deutsche Bank also knew that it misrepresented the borrowers' FICO scores in third-party RMBS that it underwrote.

262. For example, Deutsche Bank represented that no loans to borrowers with FICO scores less than 600 were securitized in RAST 2006-A7CB, a third-party transaction. However, after refreshing borrowers' FICO scores, Deutsche Bank learned that the scores for 120 loans dropped below 600, representing approximately 4.95% of the entire security by aggregate principal balance outstanding as of the cut-off date. Moreover, Deutsche Bank learned that the refreshed FICO scores for 218 loans—8.62%—dropped below 620.

263. In many cases, the sponsors of third-party transactions underwritten by Deutsche Bank, such as Countrywide, did not provide Deutsche Bank with the social security numbers for all of the loans to be securitized in the RMBS. Thus Deutsche Bank was unable to refresh the FICO scores for all of the loans in those RMBS. Despite knowing that borrowers' FICO scores "deteriorate[d] . . . so soon after the loan is originated" in 2006 and 2007, Deutsche Bank, as the underwriter, did not compel certain sponsors of third-party RMBS—particularly Countrywide—to provide the borrowers' social security numbers before securitization.

264. In 2006 and 2007, Deutsche Bank knowingly misrepresented borrowers' FICO scores in numerous RMBS. (Appendix D shows examples of Deutsche Bank's misrepresentations of FICO scores in ACE 2006-NC3, DBALT 2006-AR2 and RAST 2006-A7CB, among others.)

V. Deutsche Bank Intentionally Securitized Loans Originated By Chapel And MortgageIT That Did Not Meet Its Representations To Investors

265. In order to further drive the production of RMBS in 2006 and 2007, in September 2006, Deutsche Bank acquired Chapel, an originator of primarily subprime loans, and in January 2007, acquired MortgageIT, an originator of primarily Alt-A loans. Deutsche Bank knew that it was securitizing significant numbers of loans originated by Chapel and MortgageIT that did not meet its representations to investors.

A. Chapel

266. On September 12, 2006, Deutsche Bank acquired Chapel. Prior to the acquisition, however, Deutsche Bank knew from purchasing pools of loans from Chapel in 2005 and 2006 that Chapel originated loans with inflated appraisals and to borrowers with unreasonable stated incomes who did not likely have the ability to pay their loans.

267. In January 2006, for example, the Diligence Supervisor noted that Chapel's valuation process had "serious issues" because "Chapel is refinancing properties within a few months of purchase or the last refinance - appraised values are very distorted." The Diligence Supervisor also warned the Mortgage Finance MD that Chapel had "higher than average percentage[s]" of loans with delinquencies, unreasonable stated incomes, multiple refinancings, limited tradelines and high debt to income ratios.

268. Indeed, on January 20, 2006, the Mortgage Finance MD told the Subprime MD that Deutsche Bank's rejection rates of pools of loans purchased from Chapel "[m]ore than double[d]" over the course of Deutsche Bank's last four trades with Chapel. She explained that Chapel loans were underwritten to borrowers who had "unreasonable stated income [and] multiple refinances in a year with no proven ability to repay."

269. Deutsche Bank continued to notice the declining quality of Chapel's loans in 2006. Nonetheless, beginning on April 5, 2006, Deutsche Bank began purchasing all of the loans that Chapel originated on a daily basis in order to increase its own production of subprime loans for securitization.

270. Deutsche Bank did not subject loans originated by Chapel to its standard due diligence process. Instead, Deutsche Bank performed quality control reviews on a random sample of Chapel's monthly productions. But the negative results of these reviews did not stop Deutsche Bank from securitizing Chapel loans, including those that Deutsche Bank knew would not likely meet its representations to investors.

271. For example, in July 2006, Deutsche Bank learned from the results of a quality control review of Chapel loans originated in April 2006 that 46% of the loans in the sample had "serious" issues. Chapel misrepresented borrowers' occupancies and incomes, permitted multiple borrowers to use the same social security numbers, and originated new loans to borrowers who were simultaneously refinancing other loans with Chapel. Because the sample was selected randomly, Deutsche Bank knew that a similar percentage of the un-reviewed loans from Chapel's April production likely had similar defects.

272. Deutsche Bank noticed similar results throughout 2006 and into 2007. In March 2007, after reviewing a sample of loans originated by Chapel in October 2006, the Diligence Supervisor complained that:

> I have had concerns about the credit policy at Chapel since we began conducting reviews; especially when I found senior management attempting to remove questionable documents from the loan files prior to my review. I continue to have those same concerns - it's unfortunate that I cannot trust the management at Chapel to control the credit, regulatory and reputational risk of the Bank.

The Diligence Supervisor further noted that loans originated by Chapel in October 2006, which were graded EV3s but securitized anyway by Deutsche Bank, were already defaulting by March 2007.

273. Based on the results of Deutsche Bank's quality control reviews of Chapel loans, Deutsche Bank knew with a high probability that significant numbers of Chapel loans that it did not review had similar defects. For example, Chapel loans comprised 55% of ACE 2007-HE4. On July 12, 2007, less than three months after the deal closed, Trader 1 complained that the results of ACE 2007-HE4 were "fucking horrible" and that "the guys at Chapel should be arrested." Trader 1 admitted that he knew that Chapel had "cleaned" up loan files that Deutsche Bank had selected randomly for review before giving them to Deutsche Bank's due diligence team. Indeed, Trader 1 laughed over the phone when discussing the poor quality of the Chapel loans in the security.

274. Despite Deutsche Bank's knowledge of Chapel's poor, often fraudulent, origination practices, Deutsche Bank decided not to confirm whether it was securitizing loans originated by Chapel that did not meet its representations to investors. Indeed, in 2006, the Diligence Supervisor instructed Clayton not to prepare the "Exhibit 1s" that summarized Chapel's diligence results because Deutsche Bank "owned all the loans and were not 'rejecting' loans with exceptions. If we disclose we reviewed loans, we would have no 'results' and if asked, would have to disclose all loans with issues were purchased."

275. Between 2006 and 2007, Deutsche Bank securitized loans originated by Chapel in approximately 20 ACE and DBALT RMBS.

B. MortgageIT

276. In January 2007, Deutsche Bank acquired MortgageIT, an originator of primarily Alt-A loans. Both prior to and following the acquisition of MortgageIT, Deutsche Bank knew

that it was securitizing loans originated by MortgageIT that did not meet its representations to investors.

277. In 2006, Deutsche Bank regularly purchased pools of loans from MortgageIT. Based on the results of Deutsche Bank's due diligence on MortgageIT pools that year, the Diligence Supervisor warned the Mortgage Finance MD and the Subprime MD that MortgageIT lacked adequate controls to manage the increasing volume of loans that it was originating in 2006. Indeed, an internal memorandum about Deutsche Bank's potential acquisition of MortgageIT confirmed that MortgageIT had "sloppy" predatory lending controls, weak processes for determining whether the loan actually benefitted the borrower and layered risk for option ARM and stated documentation loans.

278. Over the course of 2006, Deutsche Bank rejected increasing percentages of loans from MortgageIT pools. According to the Diligence Supervisor, MortgageIT loans were often underwritten to borrowers with unreasonable stated incomes who did not have the ability to pay their mortgages.

279. Despite these warnings, in mid-2006, Deutsche Bank announced its decision to acquire MortgageIT in order to increase its production of Alt-A loans for securitization.

280. Moreover, in December 2006, before formally acquiring the company the following month, Deutsche Bank ceased conducting credit, compliance and valuation due diligence on loans originated by and purchased from MortgageIT. Deutsche Bank's rationale for not conducting due diligence on loans originated by MortgageIT was that once Deutsche Bank formally acquired the company, it would own all of the loans originated by MortgageIT, including those loans that it would have otherwise rejected purchasing before acquiring the company.

281. Deutsche Bank concealed from investors that it ceased conducting due diligence on MortgageIT loans as of December 2006.

282. On December 5, 2006, Trader 2 and a Trader at MortgageIT (hereinafter, the "MortgageIT Trader") presented a "roadshow" to market to investors Deutsche Bank's upcoming acquisition of the company. At that roadshow, Trader 2 and the MortgageIT Trader delivered a presentation, which touted to investors that "[f]eedback from Due Diligence required MortgageIT to adopt 'best in class' loan review processes," and that, "[b]y selling 'whole loans' on a best execution basis to virtually all major investors, MortgageIT adopted policies to ensure loans would meet any investor's toughest due-diligence requirements."

283. But contrary to their statements in the roadshow, beginning in December 2006, loans originated by MortgageIT no longer had to "meet any investors' . . . due-diligence requirements" because Deutsche Bank owned all of MortgageIT's loan production and decided not to conduct due diligence on them. Trader 2 and the MortgageIT Trader knowingly omitted from these statements that Deutsche Bank had ceased conducting due diligence entirely on loans originated by MortgageIT and would instead securitize those loans that it would otherwise have rejected purchasing from the company before the acquisition.

284. Indeed, on December 6, 2006, the evening after the roadshow, Trader 2 admitted to a senior Managing Director on Deutsche Bank's RMBS Team that investors would "notice the weak points" in Deutsche Bank's and MortgageIT's "integrated . . . processes." Trader 2 confirmed that there was no "due diligence process" to prevent loans that were typically rejected from MortgageIT before acquisition from being securitized after the acquisition:

> [I]t's impossible to have a presentation like this and not have investors notice the weak points in the integrated company's processes. Case in point – the second investor question asked – "what are your current kickout percentages on average?" The

> answer is 7%. The next question is, "what happens to that 7% of kickouts after change of control?" And the answer is, that 7% goes into our deal because there's no due diligence process. If there's a high incidence of defaults after the fact, than we can identify the problem, but that's no consolation for the investors who bought subs prior to us identifying a problem.

285. Trader 2 also acknowledged to a senior Managing Director on the RMBS Team that Deutsche Bank's "goal is to drive production," and warned that "we should be ready for investors—and the salesforce—identifying the weak points in the revised origination process."

286. Trader 2 repeated his concerns to a salesperson that Deutsche Bank was not accurately disclosing to investors that loans originated by MortgageIT would not be subject to due diligence before being securitized:

> I've expressed my concern up the chain of command, as well as pointed out the potential problems of having a stand-alone MiT shelf with a high incidence of delinquencies. Happy to give more color in person – I spend the majority of my customer meetings pitching the DBALT shelf (with and without [the Diligence Supervisor]) and our value proposition is 180 degrees from the story we're telling with MiT. When I meet with credit customers, I stress the mandate that [the Diligence Supervisor] and company have to aggressively farm out pools and discuss examples of what our processes turn up (refico'ing pools and the examples of credit migration, valuations and our kick percentages, etc.). This presentation – and business process – is the opposite because of the lack of a due diligence gatekeeper.

287. From December 6, 2006 through February 6, 2007, the Subprime MD, Trader 2 and the MortgageIT Trader repeated these misrepresentations to investors by disseminating the MortgageIT roadshow presentation to them.

288. On January 3, 2007, Deutsche Bank formally acquired MortgageIT.

289. Contrary to Trader 2 and the MortgageIT Trader's statements during the roadshow that MortgageIT had adopted strict origination guidelines, Trader 2 loosened MortgageIT's guidelines to further increase production volume. For example, on February 12,

2007, Trader 2 emailed the MortgageIT Trader, copying a senior Managing Director on Deutsche Bank's RMBS Team, that "we are fine extending the neg[ative]-am[ortization] limit to 125%, like American Home." But Trader 2 warned the MortgageIT Trader that if MortgageIT "continue[d] to pursue what's really an Alt-B borrower, this is not going to make for a successful program. To reiterate – we are OK copying AmHome's guide[line]s as long as you originate to the same type of borrower as AmHome – not MiT's current mix."

290. On July 16, 2007, in an email to the Subprime MD and a senior Managing Director on Deutsche Bank's RMBS Team, Trader 2 made recommendations for solving "serious issues with MiT." Trader 2 explained that MortgageIT had "made money by overaggressive lending that got bailed out by positive HPA [Home Price Appreciation]," but that "the downward turn in HPA blows this strategy apart." Consequently, "EPDs [Early Payment Defaults] are high and result in serious losses. Risk is not easily distributable because of the poor credit and origination processes."

291. Trader 2 complained further that the "design of [MortgageIT's] business model does not create accountability" because "account executives are paid for origination, not performance." "This type of attitude," he explained, "creates an atmosphere where the riskiest loans are pushed through the system." Trader 2 admitted that, "[i]n a time of strong HPA this is fine because they end up in someone else's hands but now they end up in ours."

292. Based on Trader 2's concerns about MortgageIT, on July 12, 2007, Trader 2 asked the Diligence Supervisor to conduct credit, compliance and valuation due diligence on "a pool of [MortgageIT] loans we have for this month." "The end goal," Trader 2 explained, "is to create a list of loans that would be rejected if this were a pool from an external seller," a process that was not implemented when Deutsche Bank acquired MortgageIT seven months earlier.

Trader 2 stressed that, "in this stage of the credit cycle it is crucial to make sure that the loans coming through the [MortgageIT] process are at least comparable to bulk [pool purchases], especially since we are not able to distribute risk at the bottom of the capital structure."

293. On August 23, 2007, the Diligence Supervisor completed the credit and compliance portion of his due diligence review of MortgageIT loans and emailed the results to Trader 2 and the Mortgage Finance MD, among others. For his review, the Diligence Supervisor "selected 200 loans randomly in order to get a representative look at the entire portfolio." He "rejected" 31 out of 200 loans, representing 15.5% of the random sample by loan count. The Diligence Supervisor identified loans that did not meet MortgageIT's guidelines or were underwritten to borrowers who would not likely have the ability to pay due to unreasonable income, excessive refinancing, FICO drift, "[n]on arms[-]length misrepresentation of purchase of home," and missing documentation, among other reasons.

294. According to the Diligence Supervisor, the main "areas of concern from [his credit] review [were] reasonableness of income, value and seasoning." He emphasized that it was "very apparent" that MortgageIT was underwriting loans to borrowers with inflated incomes:

> Regarding the income, that's an issue we've been discussing with MIT for some time. This is a judgement call by the underwriters and it's very apparent, when reviewing many of these rejections, they are allowing inflated incomes to pass through. I understand that all Sellers purchase a percentage of adverse/marginal loans, it's keeping the percentage to a minimum that's critical.

295. The Diligence Supervisor also reported "seasoning issues from all Alt-A Sellers," including MortgageIT, where "borrowers are refinancing out of recent loans to eliminate 2nd liens and/or avoid paying mortgage insurance." He explained that "[s]easoning ties into value – when you're financing borrowers within a 12 month period, the value must increase in a short

timeframe." According to the Diligence Supervisor, MortgageIT was refinancing borrowers with inflated appraisals even when, as he explained, "[i]n the current environment, values are not increasing – in most cases there has been either little or no appreciation or value declines." The Diligence Supervisor provided an example of a borrower who refinanced with MortgageIT within 10 months of his original mortgage and MortgageIT appraised the borrower's property with an inexplicable 29.5% increase in value.

296. Finally, the Diligence Supervisor warned that MortgageIT underwriters and credit managers were "very reluctant to reject loans within guidelines" even where those loans were underwritten to borrowers who would not have the ability to pay their loans. He stated that MortgageIT was underwriting loans to borrowers with "excessive revolving debt on stated loans, excessive refinancing within a short timeframe, unusual transfers prior to the refinance, elderly fixed income borrowers on reduced doc. programs, limited tradelines which are not representative of the FICO score, etc."

297. On August 24, 2007, the Mortgage Finance MD forwarded the results of the Diligence Supervisor's due diligence review to the Subprime MD. In her email, the Mortgage Finance MD added that she had been told at a MortgageIT conference that MortgageIT underwriters were "afraid to turn down a loan," and that it "[d]oesn't seem like they are changing from underwriters reporting to sales."

298. Based on the results of the Diligence Supervisor's random sample showing a 15.5% rejection rate, the Subprime MD, Trader 2 and the Mortgage Finance MD, among others, knew with a high probability that a similar percentage of the un-reviewed MortgageIT loans in Deutsche Bank's portfolio at that time did not meet MortgageIT's guidelines or were underwritten to borrowers who did not have the ability to pay. But they knowingly disregarded

these results and decided not to conduct any additional credit or compliance due diligence on the un-reviewed MortgageIT loans in Deutsche Bank's portfolio.

299. On August 29, 2007, the Diligence Supervisor completed the valuation portion of his due diligence review of MortgageIT loans and emailed a summary of the results to Trader 2 and the Mortgage Finance MD. For his review, the Diligence Supervisor ran 4,355 MortgageIT loans through an AVM. Then, he ordered BPOs on 344 of those loans for which the AVM results showed the highest confidence factors and variances of more than 20% from the appraisal value, even though he normally ran BPOs on loans that showed a lesser AVM variance of 15%. Clayton then determined the Final Variance for the loans.

300. According to the results of the Diligence Supervisor's valuation review, the property values for 211 MortgageIT loans were inflated by greater than 10%, and the property values for 178 MortgageIT loans were inflated by greater than 15%. The Diligence Supervisor stated that MortgageIT was underwriting loans to borrowers with inflated property appraisals even though, one week earlier, he informed Trader 2 and the Mortgage Finance MD that "values are not increasing - in most cases there has been either little or no appreciation or value declines." He reported that:

> I mentioned that I saw a trend when reviewing these values that was tied into seasoning – similar to what we found in the [MortgageIT] credit review. We were seeing borrowers that had purchased the home 6 months ago taking out an 80/20 – MIT refinanced the property 6 months later and now the LTV/CLTV is 80/80. I told them these appraisals are being inflated in order for the borrower to pay off the high interest rate 2nd lien and avoid paying [Mortgage Insurance].

301. Nevertheless, Trader 2 and the Mortgage Finance MD consciously disregarded the due diligence results that identified hundreds of MortgageIT loans with materially inflated appraisals. Many of the MortgageIT loans that the Diligence Supervisor identified with property

values that were inflated by more than 10% were securitized in principal transactions that the Trader 2 brought to market, such as MHL 2007-2, DBALT 2007-2 and DBALT 2007-3. Neither Trader 2 nor the Mortgage Finance MD took any action to prevent these loans from being securitized.

302. Worse, Trader 2 touted the average LTV for some of these deals knowing that he was securitizing hundreds of MortgageIT loans with inflated appraisals. On August 30, 2007, in an email to a Director in the Securitized Product Group, Trader 2 stated that "[the average LTV of 73% for DBALT 2007-3]. . . is a 'well supported' LTV because the collateral is newly originated which means the values take into account current real estate markets."

303. Indeed, Trader 2 securitized the remainder of Deutsche Bank's entire portfolio of MortgageIT loans within six weeks after receiving the results of the Diligence Supervisor's credit, compliance and value reviews. By the end of September 2007, Trader 2 securitized 1,500 MortgageIT loans in MHL 2007-2, 1,200 in DBALT 2007-2, and over 2,000 in DBALT 2007-3—hundreds of which he knew with a high probability did not meet MortgageIT's guidelines, were underwritten to borrowers who did not likely have the ability to pay, or had inflated appraisals. Deutsche Bank sold certificates from MHL 2007-2 and DBALT 2007-2 to investors, but was unable to sell the bonds from DBALT 2007-3 due to the rapidly deteriorating market for RMBS in the fall of 2007.

304. Between 2006 and 2007, Deutsche Bank securitized thousands of loans originated by MortgageIT in at least 32 ACE, DBALT, and MHL RMBS.