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and The Segregated Account of Ambac Assurance Corporation*

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

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AMBAC ASSURANCE CORPORATION and :
THE SEGREGATED ACCOUNT OF AMBAC : Index No. 600070/10
ASSURANCE CORPORATION, : Judge: The Hon. Shirley Werner
 : Kornreich
 :
 : Plaintiffs, :

- against - : **AMENDED COMPLAINT**

DLJ MORTGAGE CAPITAL, INC., and :
CREDIT SUISSE SECURITIES (USA) LLC, :
 :
 : Defendants. :

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Plaintiff Ambac Assurance Corporation (“Ambac”), by and through its attorneys, Patterson Belknap Webb & Tyler LLP, and plaintiff The Segregated Account of Ambac Assurance Corporation (the “Segregated Account”, collectively with Ambac, “Plaintiffs”), by and through its attorneys Patterson Belknap Webb & Tyler LLP and Foley & Lardner LLP, for their amended complaint against defendants DLJ Mortgage Capital, Inc. (“DLJ”) and its affiliate Credit Suisse Securities (USA) LLC, (“CS Securities”) (together, “Credit Suisse”), hereby allege upon personal knowledge as to themselves and as to their own conduct, and upon information and belief as to all other matters, as follows:

NATURE OF THE ACTION

1. Plaintiffs bring this action to seek redress for CS Securities' and DLJ's pervasive and material misrepresentations and breaches of the parties' agreement pertaining to a mortgage-backed securities transaction that DLJ sponsored, and Ambac insured, in 2007 (the Home Equity Mortgage Trust Series 2007-1 Transaction (the "Transaction")).

2. The Transaction consisted of DLJ, as the "sponsor," aggregating over two thousand residential mortgage loans into a loan "pool," which subsequently was transferred to a trust formed to issue securities that were to be paid down based on the cash flow from the pooled mortgage loans. CS Securities served as underwriter for the public offering, and thus marketed the securities to investors. To enhance the marketability of certain classes of the securities, CS Securities solicited and DLJ contracted with Ambac to issue a financial guaranty insurance policy guaranteeing payment on these securities.

3. CS Securities and DLJ, as affiliates under common control, acted in concert (a) to induce Ambac to enter into an insurance agreement and issue an insurance policy by making fraudulent statements and untrue contractual representations and warranties and, thereafter, (b) to conceal the misrepresentations and thwart the agreement's remedial protocol.

4. CS Securities fraudulently induced Ambac to participate in the Transaction by falsely representing (i) the attributes of the securitized loans, (ii) that Credit Suisse used certain strict underwriting guidelines to select the loans sold into the Transaction, when in truth far more lax guidelines had been applied, and (ii) that Credit Suisse conducted extensive due diligence on the securitized loans to ensure compliance with the strict guidelines, when in fact such diligence had not been undertaken. CS Securities also gave Ambac performance data pertaining to a prior Credit Suisse securitization that it offered as a model for the Transaction, but concealed that the prior securitization was replete with loans made to

borrowers who had little or no ability to repay their loans. After Ambac issued its insurance policy, moreover, CS Securities actively concealed its fraud by continuing to misrepresent which underwriting guidelines were used to select the loans for the Transaction.

5. DLJ induced Ambac to participate in the Transaction by making numerous untrue representations and warranties in the parties' insurance agreement and other operative transaction documents. DLJ made express representations and warranties regarding DLJ's mortgage loan conduit business as a whole (the "transaction-level warranties"), and relating to the attributes of the specific loans securitized in the Transaction (the "loan-level warranties"). The transaction-level and loan-level warranties both were critical to Ambac's assessment of the risk of insuring the Transaction.

6. The transaction-level warranties included, among other things, representations and warranties concerning the key attributes of the securitized HELOC pool as a whole, the accuracy and adequacy of DLJ's disclosures about its mortgage-loan acquisition and securitization practices, its financial statements, and its compliance with laws applicable to its business. These broad representations formed an important part of the foundation of the parties' bargain because the accuracy, or conversely the breach, of the representations necessarily would have a material effect on (1) DLJ's entire loan portfolio acquired for securitization, (2) its financial condition, (3) its ability to carry out its contractual obligations, and (4) its general suitability as a party to the contemplated securitizations.

7. The loan-level warranties concerned the attributes of the specific loans in the securitized pool. DLJ represented and warranted, among other things, that the critical attributes of each loan as supplied by Credit Suisse to Ambac were true, correct and complete, that each loan complied with the applicable loan originators' underwriting standards, and that

each loan conformed to the descriptions of the loans set forth in documentation provided by DLJ. If a loan failed to comply with the loan-level warranties, DLJ agreed to cure the breach, or repurchase or provide an adequate substitute for the non-conforming loan.

8. In making both the transaction-level and loan-level warranties, DLJ provided the assurance that systemic underwriting failures and origination abuses did not plague the loans it securitized, and assumed the risk in the event its representations were inaccurate. Ambac, in turn, assumed the market risk that loans that were originated pursuant to the represented practices and controls and bearing the represented attributes might not perform as expected. This fundamental allocation of risk was the heart of the parties' bargain.

9. Since the Transaction closed in March 2007, the securitized loans have defaulted at a remarkable rate. To date, loans representing over 33% of the original loan balance, or more than \$58 million, have defaulted, requiring Ambac to make over \$46 million in claim payments.

10. Once the losses began to mount, Ambac retained a third-party consultant to review loan origination files of 1,134 loans in the securitized loan pool, of which 390 were selected at random from the entire securitized pool. Incredibly, approximately 80% of all the loans reviewed, including those in the random sample, breached DLJ's representations and warranties based upon underwriting guidelines provided by Credit Suisse at the time of the Transaction. The review demonstrates that the HELOCs were made to numerous borrowers who were not eligible for the reduced documentation loan programs through which their loans were made and were originated in a manner that systematically ignored the borrowers' ability to repay the loans. Further, the review demonstrates that fraud by borrowers, brokers and/or originators was so rampant that Credit Suisse either knew or recklessly disregarded its prevalence.

11. Based on the review, Ambac provided DLJ with formal notice that loans with an aggregate initial principal balance of \$83 million breached DLJ's representations and warranties. In further breach of its contractual obligations, DLJ refused to repurchase a single one of the identified loans. Instead, DLJ for the first time took the remarkable position that the loans in the Transaction were not required to conform to the guidelines disclosed in advance of closing (and provided after closing in response to requests for governing guidelines), but rather were underwritten pursuant to guidelines that were far more lax and *never previously disclosed*. And in a final breach and bad-faith effort to circumvent its repurchase obligations, DLJ now contends that it did not retain the very guidelines that it asserts should apply.

12. Credit Suisse's myriad and cumulative endeavors to conceal its misrepresentations and to avoid its obligations merely underscore the gravity of its malfeasance and the harm it inflicted. For significant consideration, DLJ sold to the Transaction a pool replete with loans that did not comply with Credit Suisse's representations and warranties, and that were made to borrowers with little or no ability to repay their debt. CS Securities similarly profited from selling securities backed by these defective loans to investors whose payments were guaranteed by the policy it fraudulently obtained from Ambac. When the non-conforming loans began to default, Credit Suisse refused to comply with and instead frustrated its contractual repurchase obligations. As a result of Credit Suisse's wrongdoing, Ambac already has made claim payments on its policy in the amount of over \$46 million, and tens of millions of dollars in additional claims are expected in the future. Plaintiffs bring this action to recover for this harm.

THE PARTIES

13. The Segregated Account of Ambac Assurance Corporation is a segregated account that was established on March 24, 2010 pursuant to Wis. Stat. §611.24, with the

approval of the Office of the Commissioner of Insurance of the State of Wisconsin (the “Commissioner”).

14. Upon the Verified Petition of the Commissioner, the Circuit Court for Dane County, Wisconsin, placed the Segregated Account into statutory rehabilitation under Wis. Stat. §§ 645.31 and 645.32 on March 24, 2010. Pursuant to Wis. Stat. §611.24(3)(e), the Segregated Account is a separate Wisconsin insurer with the legal capacity and authority to sue in its own name and right. Ambac allocated the policies and claims at issue in this action to the Segregated Account pursuant to the Plan of Operation for the Segregated Account attached to the Commissioner’s Verified Petition (the “Plan of Operation”).

15. The Commissioner is the court-appointed Rehabilitator of the Segregated Account. In addition, the Wisconsin court appointed the Deputy Commissioner of Insurance as the Special Deputy Rehabilitator of the Segregated Account.

16. Ambac is a Wisconsin corporation with its principal place of business at One State Street Plaza, New York, New York 10004. Under the Plan of Operation, Ambac performs specified management services for the Segregated Account and retains the right to receive any cash recoveries relating to the policies and claims that were allocated to the Segregated Account, including the policies and claims at issue in this action.

17. Upon information and belief, DLJ is organized under the laws of the State of Delaware and maintains its principal place of business in New York, New York. Upon information and belief, DLJ is, or was at all relevant times herein, a wholly owned subsidiary of Credit Suisse Group.

18. Upon information and belief, CS Securities is organized under the laws of the State of Delaware and maintains its principal place of business in New York, New York.

Upon information and belief, CS Securities is, or was at all relevant times herein, a wholly owned subsidiary of Credit Suisse Group.

JURISDICTION AND VENUE

19. This Court has personal jurisdiction over DLJ and CS Securities pursuant to N.Y. C.P.L.R. §§ 301 and 311. Further, in the Insurance and Indemnity Agreement, dated as of March 9, 2007 (the “I&I Agreement”), DLJ irrevocably submitted to the jurisdiction of any court in the State of New York located in the City and County of New York.

20. Venue is proper in New York County pursuant to N.Y. C.P.L.R. §§ 503(a) and 503(c) because both DLJ and CS Securities have their principal offices within New York County and therefore are deemed to reside therein. Further, in the I&I Agreement, DLJ agreed to waive any defense of improper venue.

FACTUAL ALLEGATIONS

A. CS Securities Fraudulently Induces Ambac’s Participation in the Transaction

21. On November 30, 2006, Tim Kuo of CS Securities sent Ambac an email soliciting Ambac’s bid to provide financial guaranty insurance in a contemplated mortgage-backed securities transaction (*i.e.*, the Transaction). At the time, Mr. Kuo was a CS Securities Vice President, and the point person for Credit Suisse on the Transaction.¹

22. Credit Suisse affiliate DLJ had amassed for securitization a pool comprised of over two thousand home equity lines of credit (“HELOCs”) with an aggregate outstanding principal balance of approximately \$170 million. The contemplated Transaction involved the sale of the HELOCs to a trust formed to issue securities backed and to be paid down by the cash flow from the HELOCs. As the underwriter for the transaction, CS Securities would

¹ As noted below, Mr. Kuo was the signatory for DLJ on the agreements executed to effectuate the Transaction, including the Insurance and Indemnity Agreement between Ambac and DLJ.

market and sell the securities to investors. CS Securities solicited Ambac to issue a financial guaranty insurance policy guaranteeing payment on certain classes of these securities to enhance their marketability.

23. Ambac's decision whether to bid, and the premium to demand for its insurance policy, depended on its assessment of the likelihood that the HELOCs would generate sufficient cash flow to fund the amounts due to the securityholders. Unlike traditional first-lien mortgage loans used to finance the purchase of a home, the HELOCs were second-lien mortgage loans many of which were taken out in cash-out refinancing transactions that supplied borrowers with cash to draw down for any purpose they chose, whether to purchase a flat-screen television or to make the payments due on their HELOCs. Because the HELOCs were not secured by a priority lien on the underlying property, the likelihood that the holder of the HELOCs would recover the amounts due was highly dependent on the borrowers' ability to repay the loans in full (and less so on an expectation of recovery from foreclosure in the event of default).²

24. But the determination of borrowers' ability to repay takes time, and time was one thing that CS Securities did not allow. To the contrary, Mr. Kuo advised Ambac in his November 30, 2006 email that the deal was to close in December 2006. This meant that, in order to participate, Ambac had to provide its commitment in a matter of weeks - well in advance of closing. The short time-to-closing did not afford Ambac the opportunity, for example, to review the loan files created in connection with the loan origination to ensure the loans complied with appropriate underwriting guidelines. Moreover, as Credit Suisse was well aware, Ambac did not have access to the loan-origination files—or the infrastructure required to conduct loan-level re-underwriting and diligence—that Credit Suisse had as the aggregator of the HELOCs, in privity

² Moreover, insofar as the borrower could use the HELOC itself to finance initial loan payments, the short-term performance of the loans was not a good indicator of the borrowers' ability to repay.

with the HELOC originators. Credit Suisse knew and exploited that, consistent with industry practice, Ambac as a financial guarantor had to rely on Credit Suisse's due diligence and representations concerning the HELOCs securitized in the Transaction.³

25. Further, two aspects of the proposed Transaction gave Ambac pause. First, Ambac had not previously provided insurance for a Credit Suisse transaction. Second, CS Securities disclosed that a significant percentage of the loans in the proposed Transaction were originated by Secured Funding, a lender in whom Ambac had little confidence and whose loans it had refused to insure in the past.

26. In view of these constraints and concerns, Ambac required as a condition to providing its financial guaranty insurance strong assurances from Credit Suisse regarding, among other things, the borrowers' ability to repay their HELOCs. Credit Suisse provided these assurances via written and oral representations by CS Securities in advance of closing, and in express representations and warranties made by its affiliate DLJ in the parties' insurance agreement executed at closing.

27. From CS Securities, Ambac requested assurances regarding, among other things, the attributes of the pooled HELOCs, the underwriting guidelines used to evaluate the borrowers' ability to repay, and the due diligence undertaken to assess the HELOCs' compliance with such guidelines. In full recognition of Ambac's need for and reliance on such assurances, CS Securities made affirmative representations regarding these very matters.

³ In this regard, Ambac as a financial guarantor was situated markedly different than mortgage insurers, which earn significantly larger premiums to fund the infrastructure required to re-underwrite and diligence the loans they insure.

28. First, after adjourning the Transaction until February 2007,⁴ Tim Kuo of CS Securities sent Ambac an email dated February 7, 2007 which attached an Excel spreadsheet referred to as the “loan tape” that contained numerous fields of information pertaining to each of the HELOCs proposed for inclusion in the pool. The loan tape included critical metrics relating to each borrower’s ability to repay the loans and the value of the property as collateral, such as the borrower’s debt-to-income ratio (“DTI”), combined loan-to-value ratio (“CLTV”) and occupancy type. Mr. Kuo discussed those metrics at length with Ambac, representing that CS Securities analyzed and audited the disclosures during its purported thorough due diligence of the HELOCs.⁵ CS Securities intended Ambac to take the disclosures as true, accurate and complete in making its determination regarding whether to offer its insurance policy. Ambac did so, explicitly referencing the metrics supplied by Mr. Kuo in its internal memorandum authorizing the issuance of an insurance policy, dated February 21, 2007 (the “Credit Memo”).

29. Second, in response to Ambac’s requests for the guidelines that governed the pooled HELOCs, Tim Kuo sent Ambac an email dated February 14, 2007 that stated “Attached are our guides” and in fact attached Credit Suisse guidelines dated August 2006 (the “Credit Suisse Guidelines”).⁶ CS Securities knew that Ambac was interested in reviewing the

⁴ By email dated December 13, 2006, Mr. Kuo advised Ambac that it was postponing the Transaction. CS Securities revived the deal by email dated February 7, 2007, enclosing the loan tape, and the Transaction closed a month later, on March 9, 2007.

⁵ See, e.g., Email from Tim Kuo of CS Securities, dated February 20, 2007 (“Also, we review the related first lien note *during diligence* so we would have kicked the loan then. In cases where we allow loans with neg am lsts, we gross up the 1st lien balance and use the fully indexed rate when calculating *CLTV* and *DTI*. They all have to still be under 100% CLTV and 50% DTI. I believe we have 3 loans that have DTIs above 50% but less than 55%, but these loans were given exceptions b/c the related borrower has residual income of at least \$3000.”) (emphasis added).

⁶ Specifically, the attached guidelines included the Credit Suisse Correspondent Underwriting Guidelines Version 2.1, dated August 2006, the Credit Suisse HELOC Stand Alone Matrix, dated August 7, 2006, the Credit Suisse HELOC Piggyback and HELOC First Lien Matrix, dated August 7, 2006, and the Appendix of Underwriting Announcements, which was undated.

guidelines governing the HELOCs because this was the first transaction it insured for Credit Suisse. Credit Suisse also knew that Ambac would not participate in the Transaction unless the Credit Suisse Guidelines constituted the minimum underwriting standard applied to all loans because a significant percentage of the securitized pool was originated by Secured Funding, a lender that Ambac otherwise would not approve. In disclosing only the Credit Suisse Guidelines, CS Securities intended Ambac to believe—and Ambac reasonably believed—that the Credit Suisse Guidelines were the minimum guidelines that applied to all the HELOCs in the securitization, including the Secured Funding loans.

30. CS Securities' intent, and the reasonableness of Ambac's reliance, is evidenced not only by CS Securities' contemporaneous representations, but also by its post-closing conduct. As discussed below, Credit Suisse repeatedly disclosed only the Credit Suisse Guidelines in response to repeated requests made after closing for all the underwriting guidelines governing the loans in the Transaction.

31. Third, in response to Ambac's inquiry as to the due diligence conducted on the HELOC pool, Tim Kuo sent Ambac an email dated February 15, 2007, assuring Ambac that Credit Suisse had conducted due diligence on virtually 100% of the loans. Mr. Kuo presented a chart that specified the percentage of the pooled HELOCs that Credit Suisse obtained through each of its three origination channels: (i) the Loan-By-Loan ("LBL") channel, which accounted for 47.95% of the loans; (ii) the Mini-Bulk channel, which accounted for 42.89%; and (iii) the Bulk channel, through which just 9.16% were obtained. Mr. Kuo then explained that:

"As you can see, the majority of loans went through LBL and minibulk. we do 100% diligence on the LBL, and virtually 100% for the minibulk loans. For Secured Funding loans we do 100% diligence."

32. Mr. Kuo made explicit reference to the due diligence conducted on the Secured Funding loans to assure Ambac that those loans would be audited for compliance with

the stricter Credit Suisse Guidelines. In making these representations, CS Securities intended Ambac to rely—and Ambac did rely—on Credit Suisse to conduct the appropriate due diligence on virtually all the pooled HELOCs to ensure compliance with the Credit Suisse Guidelines and to ensure that the borrowers had the ability to repay their loans.⁷ Indeed, as noted, Credit Suisse knew that Ambac did not have the opportunity to undertake its own due diligence within the time frame allowed for the Transaction, and that it was the market practice for the insurer to rely on the sponsor’s due diligence, particularly a sponsor of the stature of Credit Suisse.

33. Moreover, to further assure Ambac regarding the quality of the due diligence conducted, by email dated February 22, 2007, Mr. Kuo transmitted to Ambac the due diligence results for a sample of 21 loans proposed for inclusion in the pool. The due diligence determined that the HELOCs complied with the governing underwriting guidelines, including the assessment that the borrowers’ stated income was reasonable and adequate to repay the loans. CS Securities intended that Ambac rely—and Ambac did rely—on the sample results disclosed as illustrative of the due diligence Credit Suisse purportedly conducted for virtually all the pooled HELOCs.

34. Fourth, CS Securities represented that the structure and collateral in the contemplated transaction mirrored that of a prior Credit Suisse securitization, which CS Securities represented was performing well. For example, by email dated December 11, 2006, Mr. Kuo forwarded to Ambac the Prospectus Supplement pertaining to its prior HELOC securitization—referred to as HEMT 2006-2—and represented that the “[s]tructure will be

⁷ Ambac’s reliance on CS Securities’ representation that Credit Suisse conducted due diligence of 100% or almost 100% of the loans is evidenced by Ambac’s recitation of that representation in its Credit Memo.

similar to that deal.”⁸ Moreover, by email dated February 15, 2007, Mr. Kuo sent to Ambac an Excel spreadsheet that showed relatively low delinquencies and losses on the HEMT 2006-2 transaction. Because the loans were HELOCs, and could be drawn down to pay their loans or refinanced in the rising market, these metrics masked what Credit Suisse knew, *i.e.*, the earlier deals was (just like the Transaction was about to become) replete with loans made to borrowers who did not have the ability to repay their loans when due. CS Securities intended Ambac to rely—and Ambac did rely—on the limited data disclosed pertaining to the HEMT 2006-2 transaction as a predictor for the performance of the contemplated Transaction.⁹

35. CS Securities made the foregoing representations in advance of Ambac’s execution of, and as an inducement for Ambac to issue, a financial guaranty insurance policy. Credit Suisse intended Ambac to rely on this information in evaluating the risk of issuing its policy, and Ambac reasonably did so in deciding to issue its policy. CS Securities’ motive for providing these representations is clear: CS Securities and its affiliates stood to profit handsomely from the Transaction and the sale of the mortgage-backed securities to investors.

36. As has recently come to light, CS Securities’ representations were false and misleading. First, as discussed further below, Ambac retained an expert third-party consultant that reviewed the files created during the origination of the HELOCs and determined, after great time and expense, that the disclosures on the loan tape concerning the key attributes of

⁸ Consistently, Credit Suisse’s deal lawyers Thacher Proffitt & Wood (“TPW”) forwarded drafts of the documents for the instant transaction that consisted of mark-ups of the HEMT 2006-2 deal documents. *See* March 4, 2007 email from Ady Adrefis of TPW to Ambac (“Attached please find an initial draft of the Prospectus Supplement for HEMT 2007-1, blacklined against HEMT 2006-2.”); March 6, 2007 email from Randi Taub of TPW to Ambac (enclosing the initial draft of the Loan Purchase Agreement black-lined against HEMT 2006-2 agreement).

⁹ By two emails dated February 7, 2007, Mr. Kuo sent Ambac shadow credit ratings, issued by the rating agencies, which were based on the same representations, warranties, and data provided to Ambac. Ambac detrimentally relied on the shadow credit ratings.

each HELOC were false and misleading. Having purported to audit the disclosures, CS Securities knew that its representations concerning the veracity and the integrity of the loan metrics were false, or at the very least CS Securities made the disclosure recklessly without knowing or caring whether they were true or false or without a genuine belief in their truth. Second, after years of obfuscation, Credit Suisse now concedes that its Credit Suisse Guidelines were not used to screen the majority of HELOCs sold into the Transaction, and instead that more lax guidelines were applied. Third, Ambac's third-party consultant's review and Credit Suisse's concessions affirm that the due diligence Credit Suisse conveyed to Ambac was not designed or conducted to assess the HELOCs' compliance with underwriting guidelines, including whether the borrowers' stated income was reasonable or adequate to repay the loan. Fourth, in making the limited disclosures concerning the performance of the prior Credit Suisse securitization, CS Securities' disclosure was incomplete and misleading because Credit Suisse failed to disclose the most salient fact relevant to Ambac's analysis, *i.e.*, that the earlier securitized loan pool was replete with loans that were made to borrowers that had little or no ability to repay their loans.

37. Ambac would not have agreed to participate in the Transaction had it known that CS Securities representations were false and/or omitted critical information that was required to make them not misleading. The misrepresentations ran to the core of the contemplated Transaction, directly contravening the assurances Ambac required as a condition to participating in the Transaction and materially increasing the risk of Ambac's insurance policy. As CS Securities knew full well, these representations were material to Ambac's assessment of its risk and decision to issue its policy. Ambac would not have agreed to insure the Transaction had it known that CS Securities disclosures concerning the HELOCs were false, that the Credit Suisse Guidelines did not represent the minimum standard required for inclusion of HELOCs in

the Transaction pool, that Credit Suisse had not conducted appropriate due diligence on 100% or nearly 100% of the loans to ensure compliance with the Credit Suisse Guidelines and borrowers' ability to pay, or that the disclosures concerning Credit Suisse's prior transactions were false and misleading. Had CS Securities made truthful disclosures, Ambac would have determined that the risk associated with the Transaction was too great for it to accept.

A. DLJ Makes Representations and Warranties to Induce Ambac to Issue its Policy

38. After CS Securities solicited Ambac's participation in the Transaction, its affiliate DLJ stepped in to provide contractual representations and warranties that Ambac required as a condition to issuing its insurance policy. The shift was seamless because Mr. Kuo of CS Securities also acted on behalf of, and was the authorized signatory for, DLJ with respect to two agreements that contained the representations and warranties: (1) the Insurance and Indemnity Agreement between DLJ and Ambac (the "I&I Agreement"), executed as of the closing date of March 9, 2007, which was just a month after CS Securities forward the loan tape to Ambac to renew its solicitation; and (2) the Loan Purchase Agreement ("LPA"), between DLJ and its affiliate Credit Suisse First Boston Mortgage Acceptance Corp. ("CSFBMAC"), also dated March 9, 2007. The two contracts were among the series of agreements DLJ caused to be executed to effectuate the Transaction.

39. First, DLJ as Seller sold and assigned its entire interest in the HELOC pool it had amassed to its affiliate CSFBMAC pursuant to the LPA. As of the Closing Date, the securitized pool was comprised of approximately 2,500 "Prime A" and "Alt A" second-lien HELOCs with an aggregate principal balance of almost \$170 million, with an additional approximately \$6 million in HELOCs to be subsequently transferred to the Trust. Under the LPA, DLJ made numerous detailed representations and warranties concerning the HELOCs, including, among other things, the standards to which the HELOCs were originated and the

completeness, truthfulness and correctness of the information set forth on a Loan Schedule that contained the key attributes of each HELOC, including its debt-to-income ratio, combined loan-to-value ratio and occupancy type.

40. CSFBMAC, in turn, sold its interest in the mortgage loans to the Home Equity Mortgage Trust 2007-1 (the “Trust”) pursuant to a Trust Agreement dated as of March 9, 2007. The Trust then issued mortgage-backed securities in the form of notes and certificates (the “Notes”) that were registered with the U.S. Securities and Exchange Commission (“SEC”) and marketed to investors by CS Securities by means of a March 1, 2007 Prospectus (“Prospectus”) and a March 8, 2007 Prospectus Supplement (“ProSup”).

41. Finally, pursuant to a Servicing Agreement, dated as of March 9, 2007 (the “Servicing Agreement”) among the Trust, the Trustee and PNC Bank, N.A. (“PNC”), PNC was engaged to act as servicer with respect to the loans.

42. With the underlying securitization agreements executed, DLJ and Ambac then entered into the I&I Agreement, which as discussed below, contains express representations and warranties and incorporates by reference representations and warranties in the LPA.

43. Relying on CS Securities’ representations made in connection with its solicitation of Ambac’s participation in the Transaction and DLJ’s representations, warranties, covenants and indemnities contained in and encompassed by the I&I Agreement, Ambac issued Certificate Guaranty Insurance Policy Number AB1064BE (the “Policy”). Under the Policy, Ambac agreed to insure certain payments of interest and principal due on the Class A-1 Notes and the Class G Certificates (the “Insured Securities”).

B. DLJ’s Representations and Warranties Allocate Risk of Loss

44. The representations and warranties DLJ made to and for the benefit of Ambac allocated certain risks of loss in the Transaction. As the “Sponsor” of the Transaction,

and the “Seller” of the HELOCs to the Transaction, DLJ assumed the risks associated with the origination, selection and description of the loans included in the Transaction. That is, DLJ accepted the risk that its disclosures pertaining to the loans and its practices were true, accurate and complete (*i.e.*, not false or misleading), regardless of its own (or Ambac’s) actual knowledge or diligence. Ambac, in turn, accepted the risk that the HELOCs *conforming to DLJ’s representations and warranties* would perform as expected.

45. This was a reasoned risk-allocation arrangement between sophisticated parties. Unlike Ambac, DLJ and its affiliates were in privity with the originators, and established the controls, protocols and criteria governing the selection of loans to acquire from the originators and securitize. DLJ also dictated to the lenders from whom it purchased loans for securitization the underwriting standards and protocols that must be followed in order for DLJ to accept loans from these lenders. DLJ thus had the ability to manage, and did in fact actively manage, the risk associated with the origination, selection and description of the HELOCs. In this regard, DLJ routinely obtained representations and warranties from the originators of the loans it purchased and had the ability to seek recourse for breaches of those provisions.¹⁰ Ambac, as an insurer, reasonably assumed only the market risk that the loans as represented would perform.

46. Conversely, as an insurer, Ambac was several steps removed from the process of vetting the borrowers to whom these HELOCs were made, and therefore was forced to rely on the information Credit Suisse conveyed to Ambac about the HELOCs and Credit Suisse’s due diligence of the HELOCs and the originators for the purpose of evaluating the risks of

¹⁰ Indeed, CS Securities represented in advance of closing that it had secured representations and warranties from the originators of the HELOCs. *See, e.g.*, Email from Tim Kuo of CS Securities dated February 20, 2007 (“when we bought those loans, *we got a rep* from the seller that no loans had no neg am firsts”) (emphasis added).

insuring the transaction. Accordingly, Ambac reasonably assumed only the market risk that the loans, *as represented by DLJ*, would perform.

47. DLJ made two types of representations and warranties to effectuate this risk sharing arrangement. The representations and warranties concerned, among other things, DLJ's mortgage-lending operations, practices and protocols, the key attributes of the securitized HELOC pool as a whole, and related disclosures (*i.e.*, transaction-level warranties), and each individual HELOC securitized in the Transaction (*i.e.*, loan-level warranties).

1. Transaction-Level Warranties

48. The transaction-level warranties were made in the I&I Agreement and include the following:

“Accuracy of Information. No information supplied by the Seller [DLJ] contained in the Company Documents to which it is a party nor other material information relating to the operations of the Seller or the financial condition of the Seller, as amended, supplemented or superseded, furnished to the Insurer [Ambac] in writing or in electronic format by the Seller contains any statement of material fact which was untrue or misleading in any material respect when made. The Seller does not have any knowledge of any circumstances that could reasonably be expected to cause a Material Adverse Change with respect to the Seller. Since the furnishing of the Company Documents, there has been no change nor any development or event involving a prospective change known to the Seller that would render any of the Company Documents untrue or misleading in any material respect.”¹¹

“Compliance with Securities Laws. . . . The Company Information¹² in the Offering Documents¹³ do not contain any untrue statement of a material fact and do not omit to state a material fact necessary to make the statements made therein, in

¹¹ *Id.* § 2.04(j).

¹² The I&I Agreement defines “Company Information” as “all information with respect to the Offering Documents other than the Insurer Information and the Underwriter Information.”

¹³ The I&I Agreement defines “Offering Documents” to include the March 8, 2007 Prospectus Supplement, the March 1, 2007 Prospectus, and any document with respect to the insured notes or certificates (as the case may be) that makes reference to the policy approved by Ambac.

light of the circumstances under which they were made, not misleading”¹⁴

49. As the foregoing provisions illustrate, the transaction-level warranties broadly attest that all the express information provided by DLJ concerning its operations (*e.g.*, its lending practices, underwriting guidelines and due diligence) or used to market the Notes (*e.g.*, the Prospectus or Prospectus Supplement), is true, accurate and complete. Any material misstatement or omission with respect to such disclosures therefore is a breach of these provisions, irrespective of whether or not DLJ knew of such misstatement or omission.

2. Loan-Level Warranties

50. The loan-level warranties were made in the LPA and explicitly incorporated by reference in the I&I Agreement. Specifically, the I&I Agreement provides as follows:

“Company Documents. The representations and warranties of the Seller [DLJ] contained in the Company Documents¹⁵ to which it is a party are true and correct in all material respects and the Seller [DLJ] hereby makes each such representation and warranty to, and for the benefit of, the Insurer [Ambac] as if the same were set forth in full herein.”¹⁶

The I&I Agreement defines “Company Documents” to include the LPA.

51. The I&I Agreement also provides that Ambac is a third-party beneficiary of the LPA, with all rights afforded thereunder, including the representations, warranties, and covenants that DLJ made therein:

“Third-Party Beneficiary. The Seller [DLJ] agrees that the Insurer [Ambac] shall have all rights of a third-party beneficiary in respect of the Company Documents and hereby incorporates and restates

¹⁴ I&I Agreement § 2.04(k).

¹⁵ The I&I Agreement defines “Company Documents” to include, among other things, the I&I, the LPA, and the SA.

¹⁶ I&I Agreement § 2.04(l).

its representations, warranties and covenants as set forth therein for the benefit of the Insurer.”¹⁷

52. In the LPA, DLJ makes numerous representations and warranties about the attributes of each HELOC in the Transaction, and thereby assumes the risk that those representations prove false, irrespective of DLJ’s knowledge of their falsity. These representations and warranties are found in Exhibit B to the LPA, and include, among others, the following with respect to each loan included in the Transaction:

“(b) Compliance with Laws. Any and all requirements of any federal, state or local law including, without limitation, anti-predatory or abusive lending, usury, truth-in-lending, real estate settlement procedures, consumer credit protection, equal credit opportunity or disclosure laws applicable to the Loan have been complied with in all material respects;”

“(d) Underwriting Standards. The Loan complies with all the terms, conditions and requirements of the related originator’s underwriting standards in effect at the time of origination of such Loan;”

“(e) Loan Schedule. The information set forth in the Loan Schedule is complete, true and correct in all material respects as of the related Cut-off Date;” and ¹⁸

“(i) No Defenses. The Loan is not subject to any right of rescission, set-off, counterclaim or defense, including, without limitation, the defense of usury, nor will the operation of any of the terms of the Loan, or the exercise of any right thereunder, render the Loan unenforceable, in whole or in part, or subject to any right of rescission, set-off, counterclaim or defense, including the defense of usury, and no such right of rescission, set-off, counterclaim or defense has been asserted with respect thereto.”

¹⁷ I&I Agreement § 2.05(j). Consistently, the LPA provides that Ambac is “an express third-party beneficiary” of the LPA and “shall have the right to enforce the provisions of the [LPA].” LPA § 9.

¹⁸ The Loan Schedule is Exhibit 7 to the LPA and contains key data concerning each HELOC that was included in the Transaction. Among many other things, the Loan Schedule contains the DTI ratio for each loan. Accordingly, any misrepresentation concerning the borrower’s income necessarily would render inaccurate DLJ’s representation as to the truthfulness and correctness of the debt-to-income ratio set forth on the Loan Schedule.

53. As the foregoing shows, the loan-level warranties are breached to the extent a HELOC in the Transaction fails to conform with the applicable originating guidelines, ¶(d), or does not bear the attributes disclosed on the Loan Schedule, ¶(e). Thus, the loan-level warranties are breached by, among other violations, HELOCs made to borrowers (i) with unreasonable stated incomes or that otherwise have no reasonable ability to repay the loan, which would contravene any originating guideline, and/or (ii) who falsely stated their income, which would render the information on the Loan Schedule untrue. As discussed below, the securitized HELOC pool is replete with such breaches and many others.

2. *The Repurchase Protocol*

54. DLJ agreed in the LPA that it would cure any breach of the loan-level warranties, or repurchase the breaching loan from the pool (the “Repurchase Protocol”).

Specifically, Section 2(d) of the LPA provides, in pertinent part, as follows:

“Upon discovery by [DLJ] or upon notice . . . of a breach of any representation or warranty set forth in Exhibit B attached hereto pursuant to Section 2(b) above with respect to any Loan that materially and adversely affects the interests of the [parties, including Ambac,] in such Loan . . . [DLJ] shall, within 90 days after the earlier of its discovery or receipt of notice thereof; either cure such breach in all material respects or either (i) repurchase such Loan from the Trust at the Repurchase Price, or (ii) substitute one or more Eligible Substitute Loans for such Loan, in each case in the manner and subject to the conditions set forth below.”

55. In consenting to the Repurchase Protocol as a fundamental component of the bargained-for agreement, DLJ was obligated to maintain and produce upon request all documents reasonably required to effectuate the Repurchase Protocol.¹⁹ Such documents include

¹⁹ Consistent with this obligation, the I&I Agreement explicitly states that DLJ “shall, upon request of the Insurer, from time to time, . . . deliver . . . within ten days of such request . . . such further

the originating guidelines explicitly referenced in the LPA, which if breached, give rise to DLJ's obligations to cure, repurchase or substitute.

56. As an express third-party beneficiary of the LPA, Ambac is entitled to enforce the Repurchase Protocol and seek redress for DLJ's failure to comply with its obligations to cure, repurchase or substitute breaching loans. But as noted below, the parties agreement expressly provides that the Repurchase Protocol is not an exclusive remedy, and that Ambac may seek whatever remedy it elects for DLJ's breaches of its obligations. *See* I&I Agreement §5.02.

3. Contractual Remedies

57. As befitting the significance of the representations and warranties to the parties' bargain, the I&I Agreement affords Ambac broad remedies to address breaches by DLJ of its loan-level and transaction-level warranties.

58. *All remedies at law and equity.* Section 5.02(a) of the I&I Agreement provides that Ambac "may take whatever action at law or in equity as may appear necessary or desirable in its judgment to the collect the amounts, if any, then due under this Insurance Agreement or the Indenture or to enforce performance and observance of any obligation, agreement or covenant of the . . . Seller under Company Documents." Moreover, Section 5.02(b) goes on to clarify that any and all remedies available may be asserted without exclusion, stating that "no remedy herein conferred or reserved is intended to be exclusive of any other available remedy, but each remedy shall be cumulative and shall be in addition to other remedies

instruments . . . as may be reasonably necessary to effectuate the intention, performance and provisions of the Company Documents . . ." *See* I&I Agreement § 2.05(g).

given under this Insurance Agreement, the Indenture, the other Company Documents or existing at law or in equity.”²⁰

59. *Payment and indemnification.* Pursuant to Section 3.04(a) of the I&I Agreement, DLJ also agreed to pay and indemnify Ambac for any and all losses, claims, demands, damages, costs, or expenses arising out of or relating to, among other things, any “negligence, bad faith, willful misconduct, misfeasance, malfeasance or theft committed by any director, officer, employee or agent of [DLJ] in connection with any Transaction arising from or relating to the Company Documents.” DLJ similarly agreed to pay and indemnify Ambac for any “breach by [DLJ] of any representation, warranty or covenant under any of the Company Documents” or “any untrue statement or alleged untrue statement of a material fact contained in any Offering Document or any omission or alleged omission to state therein a material fact required to be stated therein or necessary to make the statements therein, in light of the circumstances under which they were made, not misleading.”

60. *Reimbursement.* In Section 3.03(b) of the I&I Agreement, DLJ agreed to reimburse Ambac for “any and all charges, fees, costs and expenses that the Insurer [Ambac] may reasonably pay or incur, including reasonable attorneys’ and accountants’ fees and expenses (“Reimbursable Expenses”) in connection with . . . the enforcement, defense or preservation of any rights in respect of any of the Company Documents.”

²⁰ DLJ also agreed that upon the occurrence of an “Event of Default,” Ambac may “take whatever action at law or in equity as may appear necessary or desirable in its judgment to collect the amounts, if any, then due under this Insurance Agreement . . . or to enforce performance and observance of any obligation, agreement or covenant of . . . [DLJ] under Company Documents.” An “Event of Default” is defined under Section 5.01(a) of the I&I Agreement as occurring when, among other things, “[a]ny representation or warranty made by the Depositor, the Issuing Entity, the Servicer or the Seller hereunder or under the Company Documents, or in any certificate furnished hereunder or under the Company Documents, shall prove to be untrue or incomplete in any material respect.”

61. *Interest.* In Section 3.03(c) of the I&I Agreement, DLJ committed to pay Ambac interest on any reimbursement amounts due.

C. Credit Suisse Conceals its Misrepresentations

62. By December 2007, the HELOCs in the Transaction had defaulted at an inordinately high rate. Ambac thus advised CS Securities that Ambac intended to re-underwrite the defaulted loans to determine whether they conformed to DLJ's representations and warranties. To confirm that it was using the right guidelines, Ambac asked CS Securities to produce the guidelines governing the loans in the Transaction. With full knowledge of the reason for Ambac's request, by email dated December 11, 2007, Mr. Kuo of CS Securities forwarded to Ambac the same Credit Suisse Guidelines that he sent on February 14, 2007 to solicit Ambac's participation.

63. Thereafter, because Credit Suisse had not adequately responded to Ambac's informal requests to obtain the information Ambac needed (and had a contractual right to obtain) to determine whether DLJ breached its representations and warranties, by letter dated April 25, 2008, Ambac made a formal demand to DLJ as Sponsor and Seller for, among other things, "All applicable underwriting guidelines and product matrices relevant to loan underwriting and approval for each loan identified above." After repeated delays by Credit Suisse and subsequent demands by Ambac's counsel for the requested information, by email dated June 17, 2008, DLJ's counsel advised Ambac's counsel that it was forwarding the responsive guidelines, which were the same Credit Suisse Guidelines sent prior to closing and in February 2007. In making this formal response, DLJ knew that Ambac intended to use the guidelines to re-underwrite the HELOCs to assess their compliance with DLJ's representations and warranties, and as necessary, to invoke DLJ's obligations under the Repurchase Protocol.

64. As discussed below, Credit Suisse’s disclosures were deliberately false and misleading, and designed to conceal the fact that it had misrepresented the guidelines applied to the loans in the Transaction in advance of closing. At no point did Mr. Kuo or anyone else at Credit Suisse advise Ambac that Credit Suisse believed that other guidelines applied.²¹

D. Ambac Discovers Pervasive Breaches

65. After receiving Credit Suisse’s repeated confirmation that the Credit Suisse Guidelines governed the HELOCs, Ambac retained a third-party consultant to review the files created during the origination of the securitized loans for compliance with the guidelines.

66. From a sample of 744 loans in the Transaction, selected based upon certain identified characteristics, Ambac identified breaches of DLJ’s representations and warranties in a remarkable 593 loans—approximately 80%—with an aggregate principal balance of approximately \$54,583,218. Ambac also reviewed a sample of 390 randomly-selected loans from the Transaction. Of those, Ambac identified breaches of DLJ’s representations and warranties with respect to 311 loans—approximately 80% %—with an aggregate principal balance of \$27,404,954. The analysis demonstrates that breaches of representations and warranties are pervasive and exist in a comparable percentage of loans in the total securitized loan pool.

67. The breaching loans contained one or, in most cases, more than one defect that constituted a breach of one or more of DLJ’s numerous representations and warranties.

These defects include:

²¹ Credit Suisse similarly repeatedly refused to produce to Ambac the loan files pertaining to the HELOCs so that Ambac could audit those files for compliance with the governing guidelines. It was not until Ambac sent formal breach notice and threatened suit that Credit Suisse finally made the loan-file production. *See* Letter from Daniel Ruzumna, dated May 23, 2008 (providing formal notice of breach).

- pervasive violations of underwriting guidelines, including (i) qualifying borrowers under reduced documentation programs who were ineligible for those programs; (ii) systemic failure to conduct the required income-reasonableness analysis for stated income loans, resulting in the rampant origination of loans to borrowers who made unreasonable claims as to their income and (iii) lending to borrowers with debt-to-income and loan-to-value ratios above the allowed maximums;
- rampant fraud, primarily involving misrepresentation of the borrower's income, assets, employment, or intent to occupy the property as the borrower's residence (rather than as an investment), and subsequent failure to so occupy the property; and
- failure by the borrower to accurately disclose his or her liabilities, including multiple other mortgage loans taken out to purchase additional investment property.

68. The number and nature of the defects identified by Ambac's review indicate clearly that the HELOCs included in the Transaction were systematically originated with virtually no regard for the borrowers' ability or willingness to repay their obligations – the fundamental precept of mortgage lending. Rather, the review clearly indicates that borrowers were permitted or encouraged to take out loans they clearly could not afford to repay.

69. DLJ's breaches materially and adversely affected Ambac's interests in the identified loans. Loans that were not appropriately originated and underwritten, or with key attributes otherwise misrepresented, are markedly more risky and therefore less valuable than loans not suffering from such shortcomings.

70. Further, contrary to DLJ's representation in Section 2.04(k) of the I&I Agreement, the Prospectus and ProSupp that Credit Suisse prepared to market the Insured Securities (and the same documents that Credit Suisse filed with the SEC) did not adequately or accurately disclose the true attributes of the loans (*e.g.*, the weighted average combined loan-to-value ratio, occupancy status, or debt-to-income ratio), the level of fraud and underwriting

failings permeating the loan pool, the grossly deficient origination and underwriting practices of the originators of these loans, or DLJ's due-diligence practices.

71. The pervasive breaches in the securitized pool are borne out by the performance of the HELOCs since closing. As of April 2010, loans with an aggregate outstanding principal balance of over \$58 million (or over 33% of the original pool balance) have defaulted, resulting in the payment by Ambac of more than \$46 million in claims.

E. DLJ Frustrates the Repurchase Protocol

72. Having demonstrated DLJ's breaches of its loan-level representations, by letters dated October 24, 2008, November 10, 2008, and November 18, 2008, Ambac gave formal notice to DLJ of the breaches that Ambac had discovered with respect to approximately 534, 274, and 113 loans, respectively. Ambac demanded that DLJ comply with its obligations under the Repurchase Protocol and cure, repurchase, or provide substitute loans for the affected loans within 90 days.

73. DLJ did not cure, repurchase or substitute any loan within the requisite timeframe allowed under the Repurchase Protocol.

74. Then, on January 23, 2009, CS Securities Vice President Glenn Guskowski sent Ambac a letter in belated response to Ambac's first breach notice. Remarkably, in that letter CS Securities for the first time asserted that the Credit Suisse Guidelines did *not* apply to the majority of the loans in the Transaction. Rather, Mr. Guskowski inverted CS Securities' earlier representations and claimed that for "almost 60% of the loans at issue . . . Ambac was applying an inapplicable set of underwriting guidelines." This revelation, coming *after* Ambac was induced to participate in the Transaction and *after* it expended great cost and expense to re-underwrite a substantial number of the HELOCs, clearly confirms that CS Securities' repeated representations concerning the relevance of the Credit Suisse Guidelines

were made with the knowledge that they were false and the clear intent to deceive and mislead Ambac. Moreover, this belated admission is a patent and bad faith attempt by CS Securities to avoid the breach determinations in Ambac's formal notices.

75. But Credit Suisse did not stop there. When Ambac asked Credit Suisse to produce the guidelines that it now contends governed the majority of HELOCs, CS Securities asserted that it no longer had or could not locate the applicable guidelines. *See* Letters dated February 23 and April 8, 2009, from Glenn Guskowski of CS Securities to Ambac. According to Mr. Guskowski, "both the passage of time and extraordinary market dislocation have made the task of locating these documents more difficult." *See* Letter dated April 9, 2009. Credit Suisse takes the absurd position that the passage of time has made it difficult for it to locate the documentation, even though (i) the parties contemplated the Transaction would exist for years, (ii) Ambac demanded the guidelines for this very breach analysis in December 2007, just months after closing, and (iii) Ambac served the first breach notice in 2008, the year after the deal closed. Credit Suisse's purported failure to maintain the documentation required to assess its compliance with its representations and warranties and to effectuate the Repurchase Protocol constitutes a further breach of its obligations under the parties' agreements.

76. Credit Suisse's position now is, in effect, that the Repurchase Protocol cannot be enforced and is wholly frustrated for a significant percentage of the loans it securitized.

F. Credit Suisse Provides Piecemeal Disclosure of the “Correct” Guidelines

77. Credit Suisse did not make any disclosure of the guidelines it now contends govern the majority of the securitized HELOCs until February 2009, after Ambac was forced to threaten suit.²² And even then, Credit Suisse made only piecemeal disclosures.

78. Most significantly, with respect to Secured Funding, which originated almost 30% of the HELOCs in the Transaction, Credit Suisse provided only two short-form product matrices, *i.e.*, tables with objective underwriting criteria such as maximum debt-to-income ratios. Credit Suisse did not produce to Ambac the full underwriting guidelines or product manuals that dictate, among other things, the criteria for qualification of the programs pursuant to which the HELOCs purportedly were originated. The full underwriting guidelines were necessary for Credit Suisse to conduct meaningful due diligence of Secured Funding’s loans in advance of closing, and are necessary for Plaintiffs to assess the full extent of Credit Suisse’s breaches now. Credit Suisse’s failure to produce (or maintain) the Secure Funding guidelines is further evidence of its duplicity and bad faith.

79. Credit Suisse’s rationale for concealing the Secured Funding guidelines is apparent. The limited disclosures made suggest that the Secured Funding guidelines were less strict than the Credit Suisse Guidelines it disclosed with respect to, among other things, the level of debt-to-income the borrowers could bear and still qualify for a loan.

80. But even using the piecemeal provisions of the Secured Funding guidelines provided—which no doubt exclude parameters less favorable to Credit Suisse—the HELOC pool is replete with non-conforming loans. A third party re-review of the underwriting

²² See Letter From Glenn Guskowski of CS Securities, dated February 23, 2009 (“we now have gone back and, using our best efforts, provided to Ambac all of the underwriting guidelines we have been able to locate”); Email from Jason Nordyk dated April 17, 2009, with attachments.

files applying the newly-provided piecemeal provisions of the Secured Funding guidelines and other originator guidelines Credit Suisse now claims apply indicates that out of the sample of 744 loans in the Transaction selected based upon certain identified characteristics 552 loans – approximately 74% – with an aggregate principal balance of approximately \$51,213,014 contain breaches of DLJ’s representations and warranties. Out of the sample of 390 randomly selected loans from the Transaction, breaches of DLJ’s representations and warranties are observed with respect to 279 loans – approximately 72% – with an aggregate principal balance of \$25,338,865. No reasoned diligence by Credit Suisse of the HELOCs would have allowed these loans for inclusion in the Transaction, as that deal was described, marketed and sold. Rather, any reasoned diligence would have determined that the Secured Funding loans were not made to borrowers with sufficient income to repay the loans.

81. It is evident therefore that Credit Suisse did not undertake the due diligence it had represented it conducted, and that its representations that the Credit Suisse Guidelines governed this deal were made solely to convey a false assurance regarding Credit Suisse’s quality control and scrutiny of the HELOCs it securitized.

G. Credit Suisse Has Caused and Is Causing Plaintiffs Great Harm

82. Ambac would not have participated in the Transaction and issued its Policy had it known of CS Securities’ fraud *or* DLJ’s pervasive and material breaches of its representations and warranties. Credit Suisse’s pervasive misrepresentations and breaches pierce the very heart of the bargain struck by the parties. The portfolio of loans Credit Suisse sold into the Transaction did not have the attributes or bear any resemblance to what Credit Suisse represented and warranted would be transferred. Credit Suisse’s deliberate frustration of the Repurchase Protocol further compounds the harm from its breaches.

83. Despite repeated attempts by Ambac to address Credit Suisse's breaches, Credit Suisse continued to delay and obfuscate, without offering any meaningful resolution. As a result of Credit Suisse's malfeasance, Ambac incurred significant harm, including the payment of over \$46 million in claims payments to date, lost-opportunity costs on those amounts and the reserves Ambac has had to maintain relating to the future anticipated claims on the Transaction. With no alternative, Plaintiffs were forced to commence this suit.

FIRST CAUSE OF ACTION

(Fraudulent Inducement)

84. Plaintiffs reallege and incorporate by reference paragraphs 1 through 81 of this amended complaint.

85. As set forth above, CS Securities made materially false statements and omitted material facts in email communications with Ambac with the intent to defraud Ambac.

86. Ambac reasonably relied on CS Securities' statements and omissions when it entered into the I&I Agreement and issued the Policy.

87. As a result of CS Securities' statements and omissions, Ambac insured a pool of loans that had a risk profile far greater than CS Securities had led Ambac to believe.

88. As a result of CS Securities' false and misleading statements and omissions, Plaintiffs have suffered, and will continue to suffer, damages including claims payments under the Policy.

89. Because CS Securities committed these acts and omissions maliciously, wantonly, oppressively, and with the knowledge that they would affect the general public—which they have—Plaintiffs are entitled to punitive damages.

SECOND CAUSE OF ACTION

(Breach of Representations and Warranties)

90. Plaintiffs reallege and incorporate by reference paragraphs 1 through 87 of this amended complaint.

91. The I&I Agreement is a valid and binding agreement between Ambac and DLJ.

92. The LPA is a valid and binding agreement with respect to which Ambac is an express third-party beneficiary.

93. Ambac has performed all of its obligations under the I&I Agreement.

94. DLJ has materially breached its representations and warranties under Section 2.04 of the I&I Agreement and Section 2(b) of the LPA.

95. Plaintiffs have been damaged and will continue to be damaged in an amount to be determined at trial.

THIRD CAUSE OF ACTION

(Breach of Repurchase Obligation)

96. Plaintiffs reallege and incorporate by reference paragraphs 1 through 93 of this amended complaint.

97. DLJ has materially breached its obligations under Section 2(d) of the LPA by refusing to cure, repurchase, or provide substitutes for the loans that breached DLJ's representations and warranties and with respect to which notice of breach has been provided by Ambac to DLJ by letters dated October 24, 2008, November 10, 2008 and November 18, 2008.

98. DLJ has materially breached its obligations under Section 2(d) of the LPA by failing to maintain or produce the documents or instruments necessary to effectuate the Repurchase Protocol.

99. Plaintiffs have been damaged and will continue to be damaged in an amount to be determined at trial.

FOURTH CAUSE OF ACTION

(Breach of the Implied Duty of Good Faith and Fair Dealing)

100. Plaintiffs reallege and incorporate by reference paragraphs 1 through 97 of this amended complaint.

101. DLJ was obligated under the I&I Agreement and LPA to act in good faith to allow Ambac to receive the benefit of its bargain under those agreements, including the right to assess and seek recovery for breaches of DLJ's representations and warranties.

102. DLJ breached its duty of good faith and fair dealing by failing to maintain or produce the documents or instruments necessary to effectuate the Repurchase Protocol, and by actively concealing, individually and in concert with its affiliate CS Securities, the falsity of the representations and warranties made to induce Ambac to enter into I&I Agreement and issue its Policy.

103. Plaintiffs have been damaged and will continue to be damaged in an amount to be determined at trial.

FIFTH CAUSE OF ACTION

(Material Breach of the I&I Agreement)

104. Plaintiffs reallege and incorporate by reference paragraphs 1 through 101 of this amended complaint.

105. DLJ induced Ambac to enter into the I&I Agreement and to issue the Policy by making extensive representations and warranties concerning the loans that DLJ caused to be sold to the Trust, and by agreeing to broad remedies for breaches of those representations and warranties.

106. DLJ's representations and warranties were material to Ambac's decision to insure the Transaction, and Ambac was induced thereby to enter into the I&I Agreement and perform its obligations thereunder.

107. DLJ's pervasive and material breach of its representations and warranties, and its frustration of the loan-level repurchase remedy, constitutes a material breach of the I&I Agreement as a whole that has deprived Ambac of the very purpose of the parties' bargain.

108. Plaintiffs have been damaged and will continue to be damaged in an amount to be determined at trial.

SIXTH CAUSE OF ACTION

(Indemnification)

109. Plaintiffs reallege and incorporate by reference paragraphs 1 through 106 of this amended complaint.

110. Pursuant to Section 3.04(a) of the I&I Agreement, Ambac is entitled to be indemnified for any and all claims, losses, liabilities, demands, damages, costs, or expenses of any nature arising out of or relating to the transaction contemplated by the Company Documents by reason of, among other things, (i) any negligence, bad faith, willful misconduct, misfeasance, malfeasance or theft committed by any director, officer, employee or agent of DLJ and/or (ii) a breach by DLJ of any of the representations, warranties, or covenants contained in the Company Documents or any untrue statement or alleged untrue statement of a material fact contained in

any Offering Document or any omission or alleged omission to state therein a material fact required to be stated therein or necessary to make the statements therein, in light of the circumstances under which they were made, not misleading.

111. DLJ has breached numerous representations, warranties, and covenants and made material misstatements and/or omissions in the Offering Documents that have caused Ambac to pay claims and incur losses, costs, and expenses, and Plaintiffs will continue to incur losses, costs, and expenses as a result of DLJ's conduct.

SEVENTH CAUSE OF ACTION

(Fees, costs and expenses)

112. Plaintiffs reallege and incorporate by reference paragraphs 1 through 109 of this amended complaint.

113. Pursuant to Section 3.03(b) of the I&I Agreement, DLJ agreed to reimburse Ambac for any and all charges, fees, costs, and expenses paid or incurred in connection with, among other things, enforcing, defending, or preserving Ambac's rights under the Company Documents.

114. Pursuant to Section 3.03(c) of the I&I Agreement, DLJ agreed to pay Ambac interest on the amounts to be reimbursed under Section 3.03(b).

115. Plaintiffs have incurred numerous expenses, including attorneys' fees and expert fees, in order to enforce, defend, and preserve its rights under the relevant agreements.

PRAYER FOR RELIEF

WHEREFORE, Plaintiffs respectfully pray for the following relief:

- A. For an award of all legal, equitable and punitive damages, to be proven at trial, for CS Securities' fraudulent inducement of Ambac's participation in the Transaction and issuance of its Policy;

- B.** For an award of compensatory, consequential, and/or equitable damages, and any other damages to be proven at trial, for DLJ's pervasive and material breaches of its representations and warranties, and contractual repurchase obligation, constituting a material breach of the I&I Agreement and frustration of the parties' bargain;
- C.** For an order compelling DLJ to comply with its obligations under LPA § 2(d), to cure, repurchase, or substitute the loans that breach its representations and warranties;
- D.** For an order of indemnification for the claim payments and other losses and expenses Plaintiffs have paid or will pay in the future pursuant to I&I Agreement § 3.04(a);
- E.** For an order awarding reimbursement of Plaintiffs' attorneys' fees, and other costs and expenses incurred in enforcing, defending, or preserving its rights under the Operative Documents pursuant to I&I Agreement § 3.03(b), and interest thereon pursuant to § 3.03(c).
- F.** For an order of prejudgment interest; and,
- G.** For an Order awarding Plaintiffs such other and further relief as the Court deems just and proper.

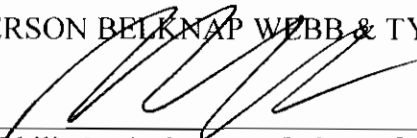
JURY DEMAND

Plaintiffs demand a trial by jury for all issues so triable as a matter of right.

Dated: New York, New York
May 14, 2010

Respectfully submitted,

PATTERSON BELKNAP WEBB & TYLER LLP



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