

STATE OF NEW MEXICO
COUNTY OF SANTA FE
FIRST JUDICIAL DISTRICT

FILED
FIRST JUDICIAL
DISTRICT COURT

2010 JAN -5 PM 3: 49



DONNA J. HILL,
On Behalf of Herself and All Others Similarly
Situated or, Alternatively, on Behalf of the New
Mexico Educational Retirement Fund and its
Members and Beneficiaries,

Plaintiff,

v.

Case No. *D101CV201000010*

VANDERBILT CAPITAL ADVISORS, LLC,
VANDERBILT FINANCIAL, LLC, VANDERBILT
FINANCIAL TRUST, PIONEER INVESTMENT
MANAGEMENT U.S.A., INC., BRUCE MALOTT,
GARY BLAND, VERONICA GARCIA, DOUGLAS
M. BROWN, PATRICK A. LIVNEY, OSBERT M.
HOOD, STEPHEN C. BERNHARDT, KURT W.
FLORIAN, JR., ANTHONY J. KOENIG, JR.,
MARK E. BRADLEY, RON D. KESSINGER,
ROBERT P. NAULT, JAMES R. STERN, NEW
ENGLAND PENSION CONSULTANTS, LLC,
ALDUS EQUITY, SAUL MEYER, JOHN DOE #1,
JOHN DOE #2, and DOES 3-100, inclusive,

Defendants,

and

THE NEW MEXICO EDUCATIONAL
RETIREMENT FUND,

Nominal Defendant.

COMPLAINT

THE NATURE OF THE CASE

Class Action Complaint for Breach of Fiduciary Duties

1. This is a class action or, alternatively, a derivative action, by plaintiff, a member and beneficiary of the New Mexico Educational Retirement Fund (the "Fund") on behalf of

IMAGED



herself and the other members and beneficiaries of the Fund (variously described herein as the “Class” or the “Beneficiaries”) against certain of the trustees (collectively, the “Trustees”) of the New Mexico Educational Retirement Board (the “ERB” or “Board”) and its investment advisors for breach of fiduciary duty (including waste of the Fund’s assets and breach of the duty of loyalty), breach of contract, and impairment of vested property rights and against certain third parties for aiding and abetting such wrongful conduct and fraud. This action also seeks injunctive relief to, *inter alia*, remove the defendant Trustees from the Board and to provide for standards of conduct so as to prevent the recurrence of conduct such as described herein.

2. This action arises out of “pay to play” schemes orchestrated by Vanderbilt Capital Advisors, LLC and its related entities (collectively, “Vanderbilt”), Saul Meyer and Aldus Equity, individuals with powerful political connections to New Mexico Governor Bill Richardson, and the Trustee defendants to cause the ERB to invest \$40 million in a highly speculative, risky, and leveraged investment (the “Vanderbilt investment”) and additional tens of millions of dollars in other inappropriate investments (the “Aldus investments”) for the political or financial gain of the perpetrators of the schemes and/or those involved in political fundraising for or on behalf of, *inter alia*, Governor Richardson.

3. Even if the Vanderbilt and Aldus investments had not been made for illicit purposes, they were wholly inappropriate for the Fund and contrary to the best interests of the Beneficiaries.

4. In approving the Vanderbilt investment, the Trustees and their investment advisor violated their constitutional, statutory, and fiduciary duties to the Fund and its Beneficiaries. Defendants Vanderbilt, John Doe #1, and John Doe #2 aided and abetted the Trustees’ violations of law and breaches of their fiduciary and contractual duties to the Fund and its members and beneficiaries. Further, Defendant Vanderbilt defrauded the Board and the Fund.

5. This action seeks to recover the damages caused to the Fund and its members and beneficiaries by the “pay to play” schemes involving the Vanderbilt and Aldus investments, including the \$40 million in lost principal, lost income, and fees and expenses associated with the Vanderbilt investment, to enjoin future “pay to play” schemes in New Mexico, to remove the culpable Trustees from their positions, and otherwise to obtain other appropriate remedial relief

for the Fund and its members and beneficiaries to protect them against similar wrongful conduct in the future.

JURISDICTION AND VENUE

6. This Court has jurisdiction of this action pursuant to Article VI, § 13 of the New Mexico Constitution and NMSA §§ 38-3-1.1 and 46A-2-203.

7. Venue is proper in this district because the plaintiff, most of the members of the Class herein, and many of the defendants reside in this district, and a substantial part of the events giving rise to the claims occurred in this district. All of the defendants have transacted substantial business, and committed unlawful acts, in this district.

THE PARTIES

8. Plaintiff Donna J. Hill is a Records Tech II at New Mexico State University and a member of the New Mexico Educational Retirement Fund.

9. Defendant Educational Retirement Fund provides retirement benefits to teachers, professors, and employees in New Mexico's public primary schools, colleges, and universities. The Board is charged with overseeing the Fund, which has approximately 63,700 active members and 31,200 retired members. The Board, as the Trustee of the Fund, should have taken the action asserted herein on behalf of the Fund and its members and beneficiaries, but it has failed to do so.

10. Defendant Vanderbilt Capital Advisors, LLC ("Vanderbilt Capital") manages and owns substantially all of the common membership interests of defendant Vanderbilt Financial, LLC ("Vanderbilt Financial") through defendant Vanderbilt Financial Trust ("Vanderbilt Trust"), a Delaware trust organized by Vanderbilt Capital.

11. Defendant Pioneer Investment Management U.S.A., Inc. ("Pioneer") is the corporate parent of Vanderbilt Capital and Vanderbilt Financial and, at all times relevant, directed and controlled their activities.

12. Defendant Bruce Malott ("Malott") has been the Chairman of the Board of Trustees of the Educational Retirement Board since August 2004, and has served on the Board since 1999. He also is the Chair of the Board's Investment Committee. Mr. Malott is a close political ally of Gov. Richardson and has served as the Governor's campaign treasurer in 2006

and as treasurer of the Governor's political action committee and charitable foundation. Gov. Richardson appointed defendant Malott to the ERB. In his position with the Board, defendant Malott owes fiduciary duties to the Board, the Fund, and the Fund's beneficiaries, the members of the Class defined below.

13. Defendant Gary Bland ("Bland") is a Board Trustee, having been appointed by Governor Bill Richardson, and the Board's Secretary. He also was New Mexico's State Investment Officer for the State Investment Council ("SIC") until his resignation in or about October 2009, having also been appointed to that position, in which he earns approximately \$300,000 per year, by Gov. Richardson. He also serves on the Board's Investment Committee. Defendant Bland owes fiduciary duties to the Board, the Fund, and the Fund's beneficiaries, the members of the Class defined below.

14. Defendant Veronica Garcia ("Garcia") is a Board Trustee, a position she holds as a result of being appointed as New Mexico's Secretary of Education by Gov. Richardson. Defendant Garcia owes fiduciary duties to the Board, the Fund, and the Fund's beneficiaries, the members of the Class defined below.

15. Defendant Douglas M. Brown ("Brown") is a former Board Trustee and custodian of the Fund. He served as a Trustee, a member of the Board's Investment Committee, and New Mexico's State Treasurer at the time the Vanderbilt investment was approved by the Board. Defendant Brown owed fiduciary duties to the Board, the Fund, and the Fund's beneficiaries, the members of the Class defined below.

16. Defendant Patrick A. Livney ("Livney") is the Chief Executive Officer and a director of Vanderbilt Financial. He also is the Senior Managing Partner of the Structured Finance Group of Vanderbilt Capital.

17. Defendant Osbert M. Hood ("Hood") is a director of Vanderbilt Financial and the President, Chief Executive Officer, and a director of Pioneer.

18. Defendant Stephen C. Bernhardt ("Bernhardt") is the Chief Investment Officer of Vanderbilt Financial and the Senior Portfolio Manager of the Structured Finance Group of Vanderbilt Capital. Along with Livney, Bernhardt headed the Vanderbilt investment project.

29. Defendant John Doe #1 was a longtime political aide to New Mexico Governor Bill Richardson. In 2002, John Doe #1 was Gov. Richardson's gubernatorial campaign manager and, in 2006, John Doe #1 was Gov. Richardson's presidential campaign manager. John Doe #1 also has served as Gov. Richardson's Chief of Staff.

30. Defendant John Doe #2 is a Santa Fe broker who has been a major political contributor to Governor Bill Richardson and his charity. Gov. Richardson appointed John Doe #2's wife as the state's first International Protocol Officer in 2004, a \$20,000 position. John Doe #2 also is the son of a long-time close friend and major political contributor and operative of Gov. Richardson's, whose support was instrumental in defendant Bland's being hired as the State Investment Officer. John Doe #2's father is a close friend of defendant Bland and served on a committee that recommended Bland for the State Investment Officer position to Gov. Richardson. John Doe #2's father also served as a director of a non-profit foundation that Gov. Richardson formed to do voter registration in preparation for the 2004 presidential election. John Doe #2 serves on the board of four Santa Fe non-profit organizations with defendant Bland. John Doe #2 has made at least \$11.5 million in fees by acting as a placement agent to secure private equity investments for his investment management firm clients from the defendant Board. These fees were paid by John Doe #2's investment management firm clients.

31. Plaintiff does not know the true names or capacities of the persons sued as Defendants Does 3 through 100, and therefore sues those defendants by fictitious names. Plaintiff believes that each of the Doe Defendants was in some manner legally responsible for the wrongdoing alleged in this Complaint. Plaintiff will amend this Complaint to set forth the true names and capacities of these defendants when they have been ascertained, along with appropriate additional allegations as may be required.

GENERAL ALLEGATIONS

A. The Trustees' Fiduciary and Contractual Duties to the Fund, its Members and Beneficiaries

1. Trustee Obligations Under New Mexico's Constitution and the Educational Retirement Act

32. Pursuant to the New Mexico Constitution and the Educational Retirement Act, the Fund is a trust fund. The members of the Board are the trustees of the Fund, charged with fiduciary duties and responsibilities for managing and investing the Fund – a portfolio of approximately \$8.5 billion – “for the sole and exclusive benefit of the members, retirees and other beneficiaries.” (Emphasis added).

33. All Board expenditures must be made solely for the benefit of the Fund’s members and beneficiaries and for expenses of administering the system and may not be used, diverted, loaned, assigned, pledged, invested, encumbered or appropriated for any other purpose. All investment costs must be appropriate and reasonable in relation to the purposes of the Fund.

34. The Trustees must comply with strict investment restrictions in managing the members’ retirement funds. For example, they must invest or reinvest the retirement funds in compliance with the Uniform Prudent Investor Act and the Prudent Investor Rule. Under the Prudent Investor Rule, the Trustees must invest and manage the retirement funds as a prudent investor would, by considering the purposes, terms, distribution requirements and other circumstances. In satisfying this standard, the trustees must exercise reasonable care, skill and caution. The Trustees also must manage and invest the Fund’s assets with loyalty and impartiality.

35. The Trustees’ investment and management decisions respecting individual assets must be evaluated as a part of an overall investment strategy having risk and return objectives reasonably suited to the trust. In investing and managing the members’ trust assets, the Trustees must consider, among other things, general economic conditions, the role that each investment plays within the overall trust portfolio, the expected total return from income and the appreciation of capital, and the needs for liquidity, regularity of income and preservation or appreciation of capital. Funds are to be used for investment, not for speculation.

36. The Trustees were and are required to make reasonable efforts to verify facts relevant to the investment and management of the Fund’s assets.

37. In delegating investment and management responsibilities, the Trustees must exercise reasonable care, skill and caution in selecting such agents, establishing the scope and

terms of the delegation consistent with the purposes of the Fund, and monitoring the agent's performance and compliance with the terms of the delegation.

38. The Board also must comply with strict restrictions on gifts, campaign contributions, and conflicts of interest. Except for small gifts of food or beverage, a Trustee may not receive or accept anything of value, directly or indirectly, from a person who has a current contract with the Board, is a potential contractor, or is authorized to invest Fund monies. A Trustee also may not have any interest, directly or indirectly, in the gains or profits of any Fund investments.

2. Trustee Obligations Under the Board's Policies

39. In February 2006, the Board adopted a set of investment policies entitled "New Mexico Educational Retirement Board Investment Goals, Objectives and Policies" (the "Investment Policy").

40. The Investment Policy includes a "Mission Statement" that states: "The New Mexico Educational Retirement Board is a statutory entity that provides secure retirement benefits for our active and retired members from school districts, higher education and educational agencies. We strive to make our members' retirement experience optimal by: Prudently managing the financial assets of the fund . . ." (Emphasis added). The document also states that one of its purposes is to "ensure prudence and care are maintained in the execution of the investment program."

41. The Investment Policy states that the Board is required to manage and invest the Fund's assets in compliance with the Prudent Investor Rule:

Under this standard, the Board shall discharge their duties with respect to the system:

(a) Solely in the interest of, and for the exclusive purposes of providing benefits to, participants and their beneficiaries and defraying reasonable expenses of administering the system.

(b) Investment of the fund shall be made with the exercise of that degree of judgment and care, under the circumstances then prevailing, which men of prudence, discretion and intelligence exercise in the management of their own affairs, not for

speculation but for investment, considering the probable safety of their capital as well as the probable income to be derived.

(c) Shall diversify the investments of the system so as to minimize the risk of loss and to maximize the rate of return, unless under the circumstances it is clearly prudent not to do so. (Emphasis added).

42. The Investment Policy states that the Board's investment goals are:

1. To invest the assets so they provide sufficient benefits to plan participants.

2. To develop an investment structure that minimizes risk and maximizes investment return, recognizing the theory of capital market pricing that maintains that over the long-term investment risk should be proportional to the investment return achieved.

3. To comply with existing and future state and federal statutes. (Emphasis added).

43. The Investment Policy states that the Board's investment philosophy is, among other things, to "incorporate effective risk controls."

44. Under the Board's specific "Private Equity Policy," the Trustees may only invest in a private equity investment if it is an "appropriate investment opportunity" that generally falls within the categories of buyout or corporate restructuring capital, venture capital, mezzanine financing, or "special situations" such as distressed securities, secondary funds, or "[o]ther investments as deemed appropriate." In addition, the private equity investment must: "[h]old[] out the prospects for capital appreciation . . . comparable to similar investments made by other professionally managed private equity funds"; "[h]a[ve] a minimum committed capital of fifty million dollars (\$50,000,000) exclusive of the investment with ERB"; "[a]ccept[] investments only from accredited investors, as that term is defined in Section 2 of the Federal Securities Act of 1933 . . ."; and "[h]a[ve] full-time management with at least five years of direct private equity experience."

45. The Private Equity Policy also provides that if the Board makes a private equity investment, "not more than fifteen percent (15%) of the amount authorized for investment in any

one year may be invested in any one private equity fund, and such investment shall not exceed twenty percent (20%) of the committed capital of that fund.”

46. The Private Equity Policy also requires that all private equity investments must first be approved by the Board’s Private Equity Investment Committee.

B. The Vanderbilt “Pay to Play” Scheme

47. Beginning in 2006, the Vanderbilt Defendants, John Doe #1, John Doe #2, NEPC, and the Trustees participated in a “pay to play” scheme intended to benefit Gov. Richardson and these defendants, to the detriment of the Fund and the members of the Class. This scheme was designed to misappropriate Fund assets to provide a lucrative business opportunity to Vanderbilt and John Doe #2 in exchange for political contributions to or for the benefit of Gov. Richardson.

48. Pursuant to this scheme, the Vanderbilt Defendants created the Vanderbilt investment as an offering specifically designed for, marketed to, and targeted at the ERB and the SIC. The ERB and the SIC were the only outside investors to which the Vanderbilt investment was sold.

49. John Doe #2, the son of a close friend and political supporter of Governor Richardson’s, acted as a “placement agent” for the Vanderbilt investment. John Doe #2 used his influence and close political ties with Gov. Richardson to obtain a Fund investment for Vanderbilt, for which John Doe #2 was paid a large sum by Vanderbilt. Vanderbilt paid John Doe #2 a \$2 million placement fee on a total \$90 million investment he secured for Vanderbilt from the State of New Mexico, \$40 million of which was from the Board.

50. John Doe #1 also used his influence and close political ties with Gov. Richardson to obtain a Fund investment for Vanderbilt to reward his campaign contributors and generate additional contributions.

51. Defendants Livney, Florian, and Bernhardt promoted the Vanderbilt investment to Board members, Board staff, and the Board’s investment advisors, and John Doe #1 and John Doe #2 exerted their influence and pressure on Board members, especially defendants Malott and Bland, to approve the investment.

52. Defendant Malott, in turn, pressured Board members and staff, including the Board’s Chief Investment Officer Frank Foy, to approve the Vanderbilt investment.

53. The Vanderbilt investment was a highly speculative, risky, and leveraged investment that was inappropriate for the Fund. Collateralized Debt Obligations (CDOs) investments are complicated investment vehicles that are only as good as their position, or tranche, and the quality of their underlying obligations. The Vanderbilt investment consisted of heavily leveraged positions in CDOs in which the Fund took the first loss position, or equity tranche (the riskiest position in a CDO, known as “toxic waste”) and/or in which a substantial portion of the underlying assets were subprime, Alt-A, and/or A-minus mortgages that had been provided to borrowers who provided little or no verification of their assets or ability to repay the loans or who did not meet minimal lending standards (certain of these loans are known as “liar’s loans” or “exceptional loans”). Many of the mortgagors lacked the means to repay these loans, especially with respect to the adjustable rate mortgages once the interest rate was adjusted. CDOs such as these played a major role in the collapse of the financial markets in recent years.

54. The Vanderbilt Defendants knew that a high default rate on a high percentage of the underlying loans was likely and that the Vanderbilt investment would never be able to sustain any income or value. They also knew that their interests conflicted with the interests of the Board and the Fund members; while they would profit from securitizing and selling defective mortgages, that were difficult to sell anywhere else, to the Fund, the Fund would suffer heavy losses.

55. The influence and pressure arising from John Doe #2 as a placement agent with close political ties to Gov. Richardson and from John Doe #1 as his top political aide and presidential campaign manager, created substantial conflicts of interest that prevented the Vanderbilt investment from being honestly, objectively, and diligently evaluated by the Trustees pursuant to the best interests of the retirement Fund and its members. The “pay to play” scheme contravened the purposes and requirements of the trust established by the New Mexico Constitution and the Educational Retirement Act.

56. Defendant Malott arranged to obtain approval of the Vanderbilt investment as quickly as possible. He scheduled a meeting of the Investment Committee to consider the Vanderbilt investment at 11:25 a.m. on May 12, 2006, to be followed immediately thereafter by a Special Meeting of the Board at 12:30 p.m. to approve the Investment Committee’s expected

recommendation of the investment. Neither the Investment Committee nor the Board held any other meeting on the Vanderbilt investment.

C. The Trustees' Abdication of Their Fiduciary and Contractual Duties and Vanderbilt's Aiding and Abetting and Fraud

57. On March 7, 2006, defendant Florian represented in an email to defendant Malott (which defendant Malott forwarded to defendant Bland and Mr. Foy) that "we are targeting an annual dividend yield of approximately 10%" for the Vanderbilt investment. This was knowingly or recklessly false and misleading, as there was no basis in fact for such a projection.

58. The Board's consideration of the Vanderbilt investment was woefully inadequate and intentionally rushed. The \$40 million investment was approved by both the committee and the Board in a little over one hour, with no advance background or explanatory materials, no briefing on the nature and risks of highly leveraged investments in CDOs or alternative investment vehicles, and almost no discussion.

59. On May 12, 2006, defendant Livney came to the Board's offices in Albuquerque to pitch the Vanderbilt investment to the Investment Committee. According to the Investment Committee's minutes, defendant Livney represented the investment "as a state of the art, 'top of the food chain' investment vehicle." This was knowingly or recklessly false and misleading. In fact, defendant Livney knew the investment consisted of toxic waste, liar's loans, and exceptional loans, and was highly speculative, risky, and leveraged, and virtually worthless.

60. At the Investment Committee meeting, defendant Livney stated that Citigroup was the lead placement agent for the Vanderbilt transaction and that Bear Stearns was a co-lead placement agent, but defendant Livney concealed the most important placement agent role of John Doe #2.

61. Defendant Livney also misrepresented that the Vanderbilt investment would be based on "fixed income" investments. When Board member Pauline Turner asked if the investment was "fixed income or private equity," defendant Livney responded "that it would be referencing all fixed income underlying assets" and that "Vanderbilt Financial Trust is a private company that ERB will own shares of, and the company itself will generate revenue from fixed income." Defendant Livney also touted the "underlying investment grade bonds," stating that

the CDOs were “a pool of assets/bonds that is financed by AAA, AA, and BBB rated bonds and they re-engineer cash flow.” Defendant Livney also provided the committee a document that referred to the CDO’s investment in “investment grade, high quality fixed income securities” and repeated the term “fixed income securities” two additional times. These representations also were false and misleading. There was no “fixed income” aspect to the Vanderbilt investment and the Fund never received any fixed income from it. The investment was backed by subprime loans that would not “re-engineer cash flow” like bonds. They were not “high quality,” but, rather, virtually worthless. Defendant Livney’s representation that the Fund would own shares of Vanderbilt Financial which itself would generate revenue from fixed income was misleading in that it gave the impression that the Fund would make profits from Vanderbilt Financial’s other ventures by which it would receive fixed income. This was false and misleading. The Fund’s profit (or loss) would be derived solely from the CDOs in which it invested, not from any of Vanderbilt Financial’s other investments.

62. Defendant Bland tried to reinforce the false impression that the CDOs were a fixed income investment. After trustee Turner had raised the question whether the investment was fixed income or private equity, defendant Bland stated that the SIC held the CDOs “under a separate asset class in fixed income.” The Board’s Chief Investment Officer, Frank Foy, responded by noting that although defendant Bland held the CDOs for the SIC in its fixed income portfolio, the investment would be allocated to private equity for the Fund. This exchange spurred by trustee Turner’s question should have raised a red flag to the Trustees, warranting further investigation of the true nature of the Vanderbilt investment. But it did not, or the red flag was simply ignored.

63. At this meeting, defendant Livney also stated that “we reunderwrite everything to our specs.” This was false and misleading.

64. Also at the May 12, 2006, meeting, defendant Livney provided the Investment Committee with a false and misleading “primer” on CDOs. According to this primer on how the Fund’s CDO investment would work, a \$15 million investment would be leveraged by a ratio of 20 to 1 by being combined with an additional \$285 million in loans with a 10-year term and investing the total of \$300 million in “investment grade, high quality fixed income securities”

also with a 10-year term. After collecting interest on the \$300 million CDO and paying the interest on the \$285 million in debt and fees, the “Expected Annual Return” was represented to be “10%-12%.” In addition, the Vanderbilt primer stated that, by the end of the 10-year term, “it is expected” that the “\$300 million fixed income securities will have matured,” that the “\$285 million debt [would be] repaid from proceeds,” and that the investor “will have received back the initial \$15 million invested.” Aside from the prospect of receiving any income or principal being little more than a pipe dream given the virtually worthless value of the underlying loans, the presentation was internally flawed. The interest on the \$285 million debt was represented to be .32% over LIBOR and the interest on the \$300 investment was represented to be .65% over LIBOR, resulting in a purported spread of 33 basis points. A spread of 33 basis points on \$285 million, or even \$300 million, would have resulted in approximately \$1 million before deducting fees. A gain of \$1 million on an initial \$15 million investment is far short of the “Expected Annual Return” of 10%-12%. Moreover, after deducting fees, which defendant Livney represented to be “1 3/4 of a point plus 25% over 9 1/2 dividend yield,” the actual return would be even further below the expected return. By Vanderbilt’s own analysis, the investment would not perform as represented. This should have raised another red flag to the Trustees, but they either failed to recognize the red flag or simply were indifferent to it given their desire to “play ball” with Gov. Richardson’s political team.

65. Defendant Livney also represented to the committee that “[t]here are 4 classes of holders, with the equity holder receiving the most return.” In fact, the equity position the Fund was to take was the highest risk position in the CDO, the “toxic waste.” Board member Pauline Turner again spoke up, catching defendant Livney’s misrepresentation on this point and questioning him on whether the Fund’s equity tranche actually would place the Fund in the lowest level position. Defendant Livney was forced to concede that this was true, raising yet another red flag calling for caution and further investigation.

66. Defendants Malott and Bland, however, quickly came to defendant Livney’s aid in an attempt to prevent the “railroad” approval process from getting off track, with Malott boasting that “ERB is getting a ‘manager’ of CDOs by investing with Vanderbilt Capital Advisors” and defendant Bland chiming in that the SIC also was investing in the Vanderbilt

CDOs (an investment it, too, entirely lost). Despite the concern raised by Ms. Turner and defendant Livney's response that conflicted with his own written and oral presentation, the Trustees approved the investment shortly afterward, with no further examination of the Fund's position in the CDO. This position ultimately resulted in no return for the Fund due to the unsound nature of the underlying loans.

67. In another attempt to smooth over any concerns with the investment, defendant Bland asked defendant Livney a "softball" question about the fee structure. Defendant Livney responded that the fee would be "1 3/4 of a point plus 25% over 9 1/2 dividend yield," but that "Citibank and Bear Stearns agreed not to charge a fee to 'friends and family' of Vanderbilt, which ERB would be considered under that umbrella." Even without the 25% bonus, a 1 3/4 point fee for Vanderbilt would be \$700,000, regardless of the performance of the investment. Yet the high fee was cushioned by fostering the impression that the Fund would be getting an especially good deal as "friends and family" of Vanderbilt. Defendant Livney's response was false and misleading. Citibank and Bear Stearns had not agreed to forego charging a fee to the Board to reward Vanderbilt's "friends and family." Upon information and belief, they did not charge a fee directly to the Board because John Doe #2, who had brought them into the transaction agreed to compensate his confederates in presently unknown amounts from the substantial profits he reaped from the deal. Defendant Livney did not disclose John Doe #2's role in bringing Citibank and Bear Stearns into the deal or how they would profit from it.

68. In tag team fashion, defendant Malott immediately followed up defendant Bland's "softball" question with a couple of his own, asking "how long the term of the deal will be" and what the annualized return would be. Defendant Livney was ready with his responses. To the first question, he answered: "1.3 years." He stated "you could own this for 1.3 years if you want and be out 100 percent if you want." To the second question, he answered: "12-15%." Both of these responses were different, and more favorable, than the corresponding information in the Vanderbilt "primer" document defendant Livney had provided to the committee. The document indicated a 10-year term by which the investor could expect to receive back its entire initial investment, during which time it could expect an annual return of 10-12%. This exchange among defendants Livney, Malott, and Bland and the differences between the written document

and defendant Livney's oral responses were concocted to foster the false impression that the Fund would receive an exceptional deal, far better than the CDO deal as reflected in the "primer." They were designed to impress the committee members that within a very short time, a little over a year, the Fund would receive back its full \$40 million investment, plus an annualized return of 12-15%. In even less time, under a year, the Fund would lose its entire investment.

69. When Board member Ms. Turner asked another pointed question as to how Vanderbilt came to the Board for this investment, defendant Livney responded that it was through prior investments with the SIC. This response served only to beg the additional, but unasked, question as to how it was that Vanderbilt came to the SIC for an investment, but more importantly concealed the truth regarding the "pay to play" arrangements with Gov. Richardson's political aides and the fact that the Vanderbilt investment had been specifically created and designed to obtain ERB and SIC funds. The Trustees failed to probe further on this issue because they knew the true answer and were aware of their complicity in the "pay to play" scheme.

70. In response to a question about "what could make this investment blow up," defendant Livney responded that a "default on [the] underlying bonds" could do so, but added that "historically the default rate of Vanderbilt since 1999 is zero." Defendant Livney knew that such a response was misleading (if not an outright lie), since the underlying investments in the particular deal being offered to the Board were exceptionally bad and a high default rate was inevitable. Defendant Livney also knew that his response would obfuscate the distinction between a default on the underlying bonds and defaults on the underlying mortgages or other loans underlying the bonds. None of the Trustees asked defendant Livney to explain his response or whether any of the past investments to which he was referring was anything like the current investment being offered to the Board.

71. Defendant Livney added that (apparently notwithstanding its perfect zero-default record) "[t]here is an assumption of recovery and default in every deal, [which] is priced in up front." Again, none of the Trustees asked defendant Livney to explain what was priced in up front or how it was priced in up front or otherwise what he meant by his statement. The

statement was misleading in that it implied that the risk of default or of the investment “blowing up” was somehow accounted for, mitigated, or offset up front when in fact that was not true. Allan Martin of NEPC, investment advisor to the ERB, asked: “If the defaults in [the] portfolio exceed [the] assumption, then [would there] be a negative return?” Defendant Livney was compelled to respond “Yes,” but hastened to add that Vanderbilt “will try to sell out of deals before they hit bottom.”

72. None of the Trustees asked any further questions or made any further comments. Defendant Malott moved to invest the maximum amount within the range recommended by the investment division – \$40 million – which was seconded by defendant Bland and passed.

73. The Special Meeting of the Board was called for May 12, necessitating the quick Investment Committee meeting immediately prior to the Special Meeting, purportedly because of a “deadline” of May 15 set by Vanderbilt for the Board’s decision to invest. In fact, there was no such deadline. When asked about the May 15 deadline at the May 12 Investment Committee meeting, defendant Livney responded “that the actual deadline was June 15, but he wanted to give ERB the opportunity to invest and give priority to ‘friends and family’.” Defendant Livney also stated: “what I wanted . . . is to give priority to our friends and family before Wall Street, Citi, and Bear oversubscribe this thing, which you’ll be shut out.” Defendant Livney’s altruistic and familial pretensions aside, Vanderbilt stood to profit handsomely from dumping \$40 million of worthless securities on a willing but unwitting buyer, for which the only urgency was to do so before the truth was discovered or the securities tanked. In addition, the purported deadline, desire to give “priority” to the ERB, and false threat of oversubscription was a sham in light of the fact that the Vanderbilt investment was created solely for the ERB and SIC and was not sold to any other outside investors.

74. At the same Investment Committee meeting, defendant Brown, then a Trustee of the Board, a member of the Board’s Investment Committee, and New Mexico’s State Treasurer, asked what a CDO is. Yet approximately forty-five minutes later, he voted to approve a \$40 million CDO investment for the ERB.

75. Handwritten notes on the Investment Committee's minutes of the May 12 meeting indicate that someone on or connected with the Board was not familiar with the basic financial acronym "ABS," which refers to asset-backed security.

76. Defendant Garcia arrived late to the Investment Committee meeting and missed approximately half of the presentation and discussion of the Vanderbilt investment.

77. Within approximately one half hour of the false and misleading "dog and pony show" orchestrated by defendants Livney, Malott, and Bland to favorably present the Vanderbilt investment to the Investment Committee, defendants Malott and Bland, along with defendant Brown (who did not know what a CDO was) and defendant Garcia (who had missed half the Investment Committee meeting), caused both the Investment Committee and Board of Trustees to approve the investment in back-to-back meetings.

78. The vote of the Board of Trustees approving the Vanderbilt investment was four to two, with the four members with political ties to Gov. Richardson in favor (defendants Malott, Bland, Brown, and Garcia) and the two members of the Board chosen by public school teachers opposed (Ms. Turner and Delman Shirley ("Shirley")). There was no discussion of the investment before the vote at this Special Board meeting called to evaluate the investment; the Board simply rubber-stamped the recommendation of the Investment Committee. The minutes of this meeting state: "Noting the detailed presentation made to the Investment Committee just prior to this meeting, defendant Malott asked the Board to take action on an equity investment in Vanderbilt Financial Trust." Defendant Bland then made the motion, defendant Brown seconded it, and the vote was taken within a matter of a couple of minutes.

79. Board member Turner stated her significant concerns with the investment in explanation of her vote in opposition. According to the Board minutes:

Dr. Turner cited three reasons for voting against the Investment Committee's recommendation: 1) she felt this investment instrument to be very complicated, and was concerned about what appeared to be a hasty decision; 2) the Board has not yet been educated on this investment instrument, and no written materials were provided for Board members to study in advance; and 3) the Board has not yet discussed policies and procedures with respect to alternative investment strategies.

Dr. Turner said she had no idea whether this was a good investment or not, and was concerned about what appeared to be unrealistic promises made by the Vanderbilt representative, Mr. Livney.

80. Board member Shirley also explained his opposition to the investment. He stated that “Dr. Turner had spoken to most of his concerns” and added that “he did not have enough information to make an informed decision, objected to the hastiness of this decision, and was not sure the Board was following its own policies and procedures.” He also stated that he was “not comfortable in using the SIC’s evaluations on any of these alternative investments because the SIC is not the fiduciary agent for the ERB.”

81. Board members Turner and Shirley correctly identified some of the breaches of fiduciary duty committed by the Trustees in ramming the Vanderbilt deal through for political purposes. The investment was complicated, the decision was hasty, the Board was not educated on the type of investment instrument or prepared to evaluate the particular investment being offered, and the Board had not yet discussed and did not follow its own policies and procedures for this type of investment. Yet even after these concerns were expressed by their fellow Board members, none of the Trustees asked for a reconsideration of the vote or any further discussion, deliberation, investigation, verification, evaluation, education, explanation, or clarification with respect to the investment.

82. In approving the Vanderbilt investment, the Trustees acted to further political goals, repay political favors, or accede to political pressures, but in any event abdicated their constitutional, statutory, and fiduciary responsibilities. NEPC’s recommendation or approval, or failure to oppose, the Vanderbilt investment also constituted a breach of its fiduciary responsibilities.

83. In the meetings on May 12, 2006, to consider the Vanderbilt investment, not one of the Trustees, nor NEPC, even asked about:

- a) the nature or quality of the loans underlying the CDOs;
- b) the past performance of similar investments;
- c) any objections from managers or staff members;

- d) whether the investment complied with the Board's own Investment Policy and Private Equity Policy;
- e) whether there were other outside investors;
- f) how it was that Citibank and Bear Stearns were brought into the deal or why they were not charging the Board for their services;
- g) the red flags raised by Board member Turner's questions about the fixed income or equity nature of the investment and the Fund's position in the CDOs;
- h) the red flag raised by Allan Martin's question about whether loan defaults could cause negative returns;
- i) the red flag raised by the conflicts and other flaws in Vanderbilt's presentation to the Investment Committee;
- j) the amount Vanderbilt principals stood to gain from the investment;
- k) the amount of the fees involved, any "pay to play" arrangements;
- l) the influence of persons with close political ties to Governor Richardson;
- m) political contributions;
- n) the use of placement agents; or
- o) any conflicts of interest.

84. Not one of the Trustees in these meetings, nor NEPC, questioned the amount of the Fund's investment in Vanderbilt, challenged Vanderbilt's analysis of the investment, sought more time to consider the investment, asked for additional documentation or information from or about Vanderbilt, or requested that the Board obtain an objective expert opinion or assistance. In a little over an hour, the Trustees caused the Board to invest (and ultimately lose) \$40 million in a worthless investment. In doing so, the Trustees and its investment advisor NEPC chose to stick their heads in the sand rather than stick up for ERB beneficiaries.

85. The Trustees voted for the Vanderbilt investment for political and personal reasons -- to curry political favor with Gov. Richardson and the Democratic party and to avoid adverse political repercussions if they did not go along. Defendant Malott's cooperation also was intended to generate business for his accounting firm.

86. Even if the Vanderbilt investment had not been made for political purposes, it was a wholly reckless and inappropriate investment of the fiduciary assets of the Fund. The Trustees and NEPC ignored or failed to apprehend that the investment consisted primarily of defective mortgages, that the Fund was likely to suffer a heavy if not a complete loss of its investment, and that the interests of the Vanderbilt Defendants, John Doe #1, and John Doe #2 were contrary to the interests of the Board and the Fund members.

87. After the Board approved the investment, the Vanderbilt Defendants continued to misrepresent the performance and prospects of the investment. These misrepresentations were designed to continue the deception and dissuade the Board from discovering the truth concerning the nature of the investment and pulling out of it.

88. For example, on June 2, 2006, defendant Livney told Mr. Foy that Vanderbilt wanted to register the securities in four months for purposes of an initial public offering. Defendant Livney also stated that within 14 days of closing, the securities would be listed on Euronext and thereafter on the New York Stock Exchange. According to defendant Livney, this meant that the Board's investment would have liquidity three to four months earlier than previously thought. On July 28, 2006, defendant Livney repeated his representation that the securities would be listed on a European stock exchange prior to listing in the United States, which would allow the securities to be publicly traded sooner rather than later and to earn a greater profit if the Board decided to liquidate its shares. All of these statements were false and misleading. As Vanderbilt knew, there was never any prospect of an initial public offering, registration, listing on a securities exchange, or liquidity with respect to the Vanderbilt investment.

89. By steering the Fund investment to Vanderbilt, John Doe #1 delivered on his part in the "pay to play" scheme, and the Vanderbilt principals held up their end of the bargain as well. Vanderbilt, its employees, and their families contributed more than \$15,000 to Gov. Richardson's presidential campaign, including the maximum contribution allowed by law from both defendant Livney and his wife.

90. The defendants' profit was the ERB beneficiaries' loss. The Vanderbilt investment was virtually worthless. In December 2006 and May 2007, the ERB

received small dividends. Other than those dividends, the Vanderbilt investment generated no other income, and the entire \$40 million principal investment was lost. Sometime after May 2007, Vanderbilt informed the Board that it should not expect any more money from its investment. In addition to losing its entire investment, the Fund lost the income it could have earned if the Vanderbilt investment had performed as represented or if the funds had been invested appropriately. The devastating loss from the Vanderbilt investment was a cause of the Board's decision to increase members' payroll contributions to the Fund by 1.5% of their salaries and to ask the Legislature to increase from 25 to 30 years the amount of time new employees must work to be entitled to full retirement benefits, further compounding the damages to Fund members.

91. By agreeing to the Vanderbilt investment, the Trustees breached their fiduciary duties to the Fund and its members. The Trustees failed to manage and invest the Fund solely in the best interests of the Fund members.

D. The Aldus "Pay to Play" Schemes

92. From approximately 2004 until February 2009, defendant Aldus served as a private equity consultant or advisor to the ERB. In this capacity, defendants Aldus and Meyer owed fiduciary and other duties to the ERB and the members of the Class, obligating them to provide objective investment advice, free from conflicts of interest and political and other improper pressures.

93. In October 2009, defendant Meyer pleaded guilty to securities fraud in New York arising from his conduct involving a public pension fund kickback scheme there. As he admitted in his allocution in the New York investigation led by New York Attorney General Andrew Cuomo, "[o]n numerous occasions, however, contrary to my fiduciary duty, I ensured that Aldus recommended certain proposed investments that were pushed on me by politically-connected individuals in New Mexico." Defendant Meyer's allocution continues as follows: "I did this knowing that these politically-connected individuals or their associates stood to benefit financially or politically from the investments and that the investments were not necessarily in the best economic interest of New Mexico."

94. Upon information and belief, John Doe #1 and John Doe #2 exerted their political influence on defendants Aldus and Meyer to recommend inappropriate investments for the ERB for the political and/or financial gain of John Doe #1, John Doe #2, Aldus, Meyer, and others. Upon information and belief, defendant Malott acted in concert with defendants Aldus and Meyer to cause the ERB to make the Aldus investments.

95. Defendant Meyer has admitted the following in his allocution: “From in or about January 2003 through in or about February 2009, acting in concert with others, I made false representations of material facts and concealed material information while engaged in inducing and promoting the exchange, sale, negotiation and purchase . . . [of] investment transactions involving . . . the New Mexico Educational Retirement Board in the State of New Mexico. As a result of this, I along with Hank Morris and others wrongfully obtained agreements and fees relating to these transactions.”

96. The Aldus investments were inappropriate for the ERB due to their highly speculative and risky nature, were inconsistent with the fiduciary and other duties of defendants Aldus and Meyer to protect public and the Class members’ money by safeguarding the integrity of the public pension fund investment process, were tainted by conflicts of interest and political pressures, and caused losses to the Fund and the members of the Class.

CLASS ACTION ALLEGATIONS

97. Plaintiff brings this case as a class action, under Rule 1-023 of the New Mexico District Court Rules of Civil Procedure, on behalf of herself and the other members of the New Mexico Educational Retirement System, defined as follows: All current members of the New Mexico Educational Retirement System.

98. The members of the Class are so numerous that joinder of all members is impracticable. There are approximately 95,000 Class members.

99. Common questions of law and fact affect the claims of all Class members and common relief by way of damages is sought for all Class members. The harm defendants have caused, are causing, and will cause is substantially uniform with respect to all Class members since there is one fund, the Educational Retirement Fund, from which all Class members’ retirement payments are made.

100. Common questions of law and fact that affect the Class members include, but are not limited to, the following:

- a) Whether the defendants engaged in a wrongful “pay to play” scheme involving the Vanderbilt investment, designed to use the Fund for political purposes at the expense of the Fund and the members of the Class;
- b) Whether the Trustees and NEPC breached their fiduciary duties owed to the Fund and the members of the Class in approving the Vanderbilt investment;
- c) Whether the Trustees and NEPC breached their contractual duties owed to the Fund and the members of the Class by approving the Vanderbilt investment;
- d) Whether the Trustees and NEPC impaired the vested property rights of members of the Class;
- e) Whether the Vanderbilt Defendants, John Doe #1, and John Doe #2 aided and abetted the Trustees’ breaches of fiduciary duties;
- f) Whether the Vanderbilt Defendants, John Doe #1, and John Doe #2 aided and abetted the Trustees’ breaches of contracts;
- g) Whether the Vanderbilt Defendants, John Doe #1, and John Doe #2 aided and abetted the Trustees’ impairment of vested property rights;
- h) Whether the Vanderbilt Defendants defrauded the Board and, indirectly, the members of the Class;
- i) Whether NEPC breached its fiduciary duties owed to the Fund and its Beneficiaries in recommending, approving, or failing to oppose the Vanderbilt investment;
- j) Whether defendants Aldus and Meyer breached their fiduciary duties in engaging in “pay to play” schemes involving the Aldus investments;

- k) Whether defendants Aldus and Meyer committed fraud in connection with recommending the Aldus investments to the ERB;
- l) Whether John Doe #1 and John Doe #2 aided and abetted defendants Aldus' and Meyer's breaches of fiduciary duties in connection with the Aldus investments;
- m) Whether John Doe #1 and John Doe #2 aided and abetted defendants Aldus' and Meyer's fraud in connection with the Aldus investments;
- n) Whether the Fund and the members of the Class have suffered damages as a result of defendants' wrongful conduct and, if so, the proper measure of such damages; and
- o) Whether defendants' wrongful conduct, including "pay to play" practices, should be enjoined.

101. These common questions of law and fact predominate over any individual questions that may exist or arise.

102. Plaintiff's claims are typical of absent Class members' claims. All claims arise from the same factual background and legal theories. Plaintiff and all members of the Class have suffered the same harm arising out of defendants' wrongful course of conduct. The harms suffered by plaintiff are typical of the harms suffered by the members of the Class, and plaintiff and the other members of the Class have a common interest in seeking redress for defendants' wrongful conduct and in preventing defendants from engaging in such activity in the future.

103. Plaintiff will fairly and adequately protect the interests of the Class. Plaintiff has retained counsel competent and experienced in class actions and has no conflict of interest with other Class members in the maintenance of this class action. Plaintiff has no relationship with defendants that would pose a conflict of interest with other Class members. Plaintiff will vigorously pursue the Class claims in the best interests of the Class.

104. A class action is superior to other available methods for the fair and efficient adjudication of this controversy because joinder of all members is impracticable. Furthermore, because the damages suffered by individual Class members may be relatively small, the expense

and burden of individual litigation makes it impracticable for the Class to individually seek redress for the wrongs done to them. Class members, to the extent they are aware of their rights against defendants herein, likely would be unable to secure counsel to litigate their claims on an individual basis because of the high cost of doing so and the relatively small nature of the individual damages. A class action is the only feasible means of recovery for the Class members. Individual actions also would present a substantial risk of inconsistent decisions, even though each Class member has an identical claim of right against defendants.

105. Plaintiff envisions no difficulty in the management of this action as a class action. The advantages of maintaining the action as a class action far outweigh the expense and waste of judicial effort that would result in hundreds or thousands of separate adjudications of these issues for each member of the Class or the injustice that would result if individual actions could not be brought due to lack of notice or resources. Class treatment further ensures uniformity and consistency in results and will provide optimum relief for members of the Class.

DEMAND EXCUSAL

106. For purposes of the derivative claims alleged herein against the defendants, no demand upon the Board is necessary.

107. For purposes of the derivative action alleged herein as an alternative to the direct action, pre-suit demand upon the Board is excused. A demand under the circumstances alleged herein would be futile because, among other things, this action alleges political corruption and other wrongful conduct committed by Trustees who constituted a majority of, and controlled, the Board and the Fund. Three of those Trustees continue to serve on the Board today, including the Chairman, defendant Malott, the State Investment Officer, defendant Bland, and the Secretary of Education, defendant Garcia. Even after numerous news articles exposing the corrupt “pay to play” schemes and disastrous Vanderbilt investment alleged herein and a “whistleblower” suit has been commenced, the Board has declined to take any action against any of the Vanderbilt entities or principals, John Doe #1, John Doe #2, defendants NEPC, Meyer, or Aldus, or any of the Trustees. They have intentionally failed to commence legal action against their friends, colleagues, and political confederates. Their failure to do so demonstrates their utter disregard of their obligations as fiduciaries. Further, none of the Trustees are disinterested or independent of

the “pay to play” schemes alleged herein and all owe their positions to Gov. Richardson and his close associates. None of the Trustees has admitted any wrongdoing. Not only has the Board failed to enforce rights that may be properly asserted by it on behalf of the Fund, it has, in fact, publicly defended the actions of the Trustees. None of the Trustees has been removed or resigned from the Board because of their role in approving the Vanderbilt or Aldus investments.

CAUSES OF ACTION

COUNT I:

BREACH OF FIDUCIARY DUTIES

(Against the Trustees and NEPC)

108. The allegations in paragraphs 107 are incorporated herein.

109. In approving the Vanderbilt investment, the Trustees failed to manage and invest the Fund solely in the best interests of the Fund and its members.

110. In recommending, approving, or failing to oppose the Vanderbilt investment, defendant NEPC failed to advise the ERB solely in the best interests of the Fund and its members.

111. The Vanderbilt investment was a highly speculative, risky, and leveraged investment that was inappropriate for the Fund, all of which was known or should have been known by each of the Trustees and defendant NEPC.

112. The Trustees caused the Board to invest and pay fees, investment costs, and other expenditures that were not solely for the benefit of the Fund’s members and that were not appropriate or reasonable in relation to the purposes of the Fund. Instead, the Trustees acted with other interests and purposes – political and personal interests and purposes – and diverted and misappropriated Fund assets for those interests and purposes.

113. The Trustees failed to comply with the Uniform Prudent Investor Act and the Prudent Investor Rule. Considering the purposes of the Fund to safeguard the retirement funds of public school teachers and college professors and other education employees and the circumstances of the highly speculative, risky, and leveraged Vanderbilt investment, the Trustees did not manage and invest the Fund as would a prudent investor.

114. The Trustees and defendant NEPC failed to appreciate, or ignored, the conflicts of interest presented by the placement agent and “pay to play” arrangements and kickbacks in the Vanderbilt deal and how such conflicts of interest prevented an honest, objective, fully-informed, and diligent evaluation of the investment in the best interests of the Fund and its members.

115. The Trustees and defendant NEPC acceded to political influence and pressure in approving the Vanderbilt investment and allowed Fund assets to be misappropriated for political purposes, contrary to the best interests of the Fund and its members. Defendants Malott and Bland went even further, in taking affirmative actions designed to further the “pay to play” scheme by influencing the other Trustees and otherwise ensuring the approval of the Vanderbilt investment.

116. The Trustees and defendant NEPC failed to exercise reasonable care, skill and caution.

117. The Trustees and defendant NEPC failed to properly investigate, discover, and consider the circumstances regarding the Vanderbilt investment that would have revealed that it was highly speculative, risky, and leveraged, virtually worthless, and not suitable for the Fund.

118. The Trustees and defendant NEPC failed to properly verify facts relevant to the Vanderbilt investment, including the reliability of the representations made by Vanderbilt.

119. The Trustees and defendant NEPC ignored a number of red flags with the Vanderbilt investment which, in the exercise of reasonable care, warranted further investigation. These red flags included unrealistic claims and inconsistencies concerning: the nature of the investment as being fixed income; the underlying assets as being of “high quality” and able to “re-engineer cash flow”; an internally incorrect “primer” on how the CDO investment would work; the length of the term of the deal; the expected return of principal; the expected annual return; how Vanderbilt came to the Board for an investment; how Citibank and Bear Stearns were brought into the deal and why they were not charging the Board a fee; the reasonableness of assumptions; the effect of defaults and how they purportedly would be mitigated and factored into the deal up front; the supposed “deadline” for the Board’s decision; and the points raised by Board members Dr. Turner and Mr. Shirley in opposing the investment.

120. The Trustees failed to obtain the financial knowledge necessary to evaluate the Vanderbilt investment in CDOs.

121. Defendant NEPC failed to properly inform itself of material facts, conduct a reasonable inquiry, and give the Board informed, objective, and reasonable investment advice with respect to the Vanderbilt investment consistent with its fiduciary duties.

122. All Board members were so unfamiliar with the Vanderbilt investment that was being considered that the Investment Committee had to receive a “primer” on CDOs in the same meeting held purportedly to evaluate the Vanderbilt investment. Defendant Brown, a Trustee and member of the Investment Committee, indicated that he did not even know what a CDO is. Defendant Garcia, another Trustee, missed half of the meeting. Yet within a little over an hour, the Investment Committee, including defendants Malott, Bland, and Brown, voted to approve the Vanderbilt investment, and all four Trustees voted to approve it at the Special Board meeting immediately following the Investment Committee meeting.

123. The Trustees and defendant NEPC failed to manage and invest the Fund with loyalty and impartiality. They placed their own political and personal interests above the Fund members’ interests.

124. The Trustees and defendant NEPC wasted the Fund’s assets.

125. The Trustees and defendant NEPC failed to follow the ERB’s own policies.

Among other things:

- a) The Vanderbilt investment, and the Trustees’ and defendant NEPC’s consideration of it, conflicted with the Trustees’ obligation to provide “secure” and “sufficient” retirement benefits. In fact, the losses suffered by the investment contributed to the subsequent decisions to increase employee contributions and propose an increase in the number of work years necessary to receive full retirement benefits.
- b) The Trustees and defendant NEPC also failed to “[p]rudently manag[e]” the Fund’s assets with “care” and consistent with the Prudent Investor Rule.
- c) The Trustees and defendant NEPC did not act “[s]olely in the interest of, and for the exclusive purposes of providing benefits to, participants and their

beneficiaries” or to defray reasonable expenses; instead, they acted with political and personal interests and purposes.

d) The Trustees and defendant NEPC impermissibly used the Fund for speculation with insufficient consideration of the probable safety of capital and income to be derived.

e) The Trustees and defendant NEPC failed to minimize the risk of loss, utilize “effective risk controls,” or exercise “prudence.”

f) The Trustees and defendant NEPC failed to comply with state statutes, such as the Educational Retirement Act and the Prudent Investor Act.

g) The Vanderbilt investment was not an “appropriate investment opportunity” for the Fund and did not fall within the permitted types of private equity investments set forth in the Board’s Private Equity Policy, nor was it deemed appropriate as a special exception to those permitted types.

h) The Vanderbilt investment also violated the Private Equity Policy because it did not “[h]old[] out the prospects for capital appreciation . . . comparable to similar investments made by other professionally managed private equity funds.”

i) The Trustees and NEPC failed to ascertain whether the investment had “a minimum committed capital of fifty million dollars (\$50,000,000) exclusive of the investment with ERB” or whether Vanderbilt had “full-time management with at least five years of direct private equity experience.”

j) The Trustees and defendant NEPC also failed to determine whether the amount of the Fund’s Vanderbilt investment exceeded the maximum allowable amount as set forth in the Private Equity Policy.

k) The Vanderbilt investment was not first approved by the Private Equity Investment Committee, as required by the Private Equity Policy.

126. The Trustees and defendant NEPC knew or should have known by the exercise of reasonable diligence that the Vanderbilt investment was part of a “pay to play” scheme involving political contributions, a placement agent, and conflicts of interest that would prevent an honest and objective evaluation of the investment and the firms and principals who promoted it.

127. Defendant Malott additionally breached his fiduciary duties by participating in the “pay to play” schemes with John Doe #1, John Doe #2, defendant Meyer, and defendant Aldus, in which he helped ensure that the ERB invested in the investments recommended by defendants Meyer and Aldus.

128. By the wrongful conduct alleged herein, the Trustees and defendant NEPC breached their fiduciary duties to the Fund and its members, which has caused and is causing substantial damages to them, including lost principal, lost income, fees and expenses, increased payroll contributions, and a looming increase in the number of years new employees must work to be entitled to full retirement benefits.

COUNT II:

BREACH OF CONTRACT

(Against the Trustees and Defendants NEPC, Aldus, and Meyer)

129. The allegations in paragraphs 107 are incorporated herein.

130. The constitutional and statutory obligations imposed upon the Trustees to act in a fiduciary capacity and solely in the best interests of the Fund and its members constitute an implied-in-fact contract between the Trustees and the Fund and its members, which was breached by the Trustees as alleged herein.

131. The Board’s written investment policies also constitute an implied-in-fact contract between the Trustees and the Fund and its members, which was breached by the Trustees as alleged herein.

132. Defendant NEPC’s contract with the ERB was breached by defendant NEPC as alleged herein.

133. Defendants Aldus’ and Meyer’s contract with the ERB was breached by defendants Aldus and Meyer as alleged herein.

134. The Trustees’ and defendants NEPC’s, Aldus’, and Meyer’s breaches of contracts have caused and are causing substantial damages to the Fund and its members, including lost principal, lost income, fees and expenses, increased payroll contributions, and a looming increase in the number of years new employees must work to be entitled to full retirement benefits.

COUNT III:

IMPAIRMENT OF VESTED PROPERTY RIGHTS

(Against the Trustees and NEPC)

135. The allegations in paragraphs 107 are incorporated herein.

136. Under the New Mexico Educational Retirement System, employees who have worked five years of qualified state employment have vested property rights in their retirement plan benefits.

137. Qualified employees' vested property rights are protected against impairment by the New Mexico Educational Retirement Act, the New Mexico Constitution, Article II, Sections 18 and 20, and Article XX, Section 22(D), and the United States Constitution, Amendment XIV, incorporating Amendment V.

138. By engaging in the conduct alleged herein, the Trustees and NEPC have impaired the vested property rights of plaintiff and members of the Class in violation of state statutes and the state and federal constitutions.

COUNT IV:

AIDING AND ABETTING BREACH OF FIDUCIARY DUTIES

(Against the Vanderbilt Defendants, NEPC, John Doe #1 and John Doe #2)

139. The allegations in paragraphs 107 are incorporated herein.

140. The Vanderbilt Defendants, defendant NEPC, John Doe #1, and John Doe #2 knowingly substantially assisted the Trustees in their breaches of fiduciary duties, as alleged herein.

141. The Vanderbilt Defendants', defendant NEPC's, John Doe #1's, and John Doe #2's wrongful conduct aiding and abetting the Trustees' breaches of fiduciary duties has caused and is causing substantial damages to the Fund and its members, including lost principal, lost income, fees and expenses, increased payroll contributions, and a looming increase in the number of years new employees must work to be entitled to full retirement benefits.

COUNT V:

AIDING AND ABETTING BREACH OF CONTRACT

(Against the Vanderbilt Defendants, NEPC, John Doe #1 and John Doe #2)

142. The allegations in paragraphs 107 are incorporated herein.

143. The Vanderbilt Defendants, defendant NEPC, John Doe #1, and John Doe #2 knowingly substantially assisted the Trustees in their breaches of contract, as alleged herein.

144. The Vanderbilt Defendants', defendant NEPC's, John Doe #1's, and John Doe #2's wrongful conduct aiding and abetting the Trustees' breaches of contract has caused and is causing substantial damages to the Fund and its members, including lost principal, lost income, fees and expenses, increased payroll contributions, and a looming increase in the number of years new employees must work to be entitled to full retirement benefits.

COUNT VI:

AIDING AND ABETTING IMPAIRMENT OF VESTED PROPERTY RIGHTS

(Against the Vanderbilt Defendants, NEPC, John Doe #1 and John Doe #2)

145. The allegations in paragraphs 107 are incorporated herein.

146. The Vanderbilt Defendants, defendant NEPC, John Doe #1, and John Doe #2 knowingly substantially assisted the Trustees in their impairment of the vested property rights of plaintiff and members of the Class, as alleged herein.

147. The Vanderbilt Defendants', defendant NEPC's, John Doe #1's, and John Doe #2's wrongful conduct aiding and abetting the Trustees' impairment of vested property rights has caused and is causing substantial damages to the Fund and members of the Class.

COUNT VII:

FRAUD

(Against the Vanderbilt Defendants)

148. The allegations in paragraphs 107 are incorporated herein.

149. The Vanderbilt Defendants knowingly or recklessly materially misrepresented the nature of the Vanderbilt investment to the Board, which relied on such misrepresentations, causing the Fund and its members to suffer damages as a result. The Vanderbilt Defendants knew the Board would rely on their material misrepresentations and omissions and intended such reliance.

150. The Vanderbilt Defendants' statement on March 7, 2006, that "we are targeting an annual dividend yield of approximately 10%" was false and misleading.

151. The Vanderbilt Defendants' false and misleading statements at the May 12, 2006, Investment Committee meeting included the following:

- a) That the Vanderbilt investment is "a state of the art, 'top of the food chain' investment vehicle."
- b) That Citigroup was the "lead placement agent" for the deal.
- c) That the Vanderbilt investment was based on "fixed income" investments and that the investment "would be referencing all fixed income underlying assets."
- d) That "Vanderbilt Financial Trust is a private company that ERB will own shares of, and the company itself will generate revenue from fixed income."
- e) That the investment was based on "underlying investment grade bonds."
- f) That the CDOs were "a pool of assets/bonds that is financed by AAA, AA, and BBB rated bonds and they re-engineer cash flow."
- g) That the CDOs were backed by "investment grade, high quality fixed income securities."
- h) That "we reunderwrite everything to our specs."
- i) That "[t]here are 4 classes of holders, with the equity holder receiving the most return."
- j) That the Fund was receiving an especially good deal because "Citibank and Bear Stearns agreed not to charge a fee to 'friends and family' of Vanderbilt, which ERB would be considered under that umbrella."
- k) That the term of the investment was 1.3 years.
- l) That the Fund could expect to receive back its entire principal investment by the end of the 1.3-year term.
- m) That the Fund could expect an annualized return of 12-15% on its investment.

- n) That Vanderbilt had come to the Board for an investment through its other investments with the SIC.
- o) That “historically the default rate of Vanderbilt since 1999 is zero.”
- p) That “[t]here is an assumption of recovery and default in every deal, [which] is priced in up front.”
- q) That a negative return as a result of defaults in the portfolio could be avoided because Vanderbilt “will try to sell out of deals before they hit bottom.”
- r) That there was a May 15, 2006, or June 15, 2006, “deadline” for the Board’s decision to invest or that Vanderbilt was extending any deadline in order to “give ERB the opportunity to invest and give priority to ‘friends and family.’”
- s) That Vanderbilt wanted to give priority to the Board “before Wall Street, Citi, and Bear oversubscribe this thing, which you’ll be shut out.”
- t) That the securities involved in the Vanderbilt investment would be listed on the New York Stock Exchange through an initial public offering and would be liquid soon after closing.

152. These statements were knowingly false and misleading. In fact, the Vanderbilt investment was highly speculative, risky, leveraged, virtually worthless, and targeted solely at the ERB and SIC. It was the vehicle of a “pay to play” scheme, orchestrated through the political influence of John Doe #1 and John Doe #2. It was not a “fixed income” investment. The Vanderbilt Defendants knew the CDOs’ underlying assets consisted mainly of subprime loans, including adjustable rate residential mortgages, toxic waste, liar’s loans, and exceptional loans that were likely to suffer a substantially high default rate. The investment was not backed by fixed income bonds that would “re-engineer cash flow.” They were not “high quality,” but, rather, virtually worthless. The Fund’s investment would not be protected by Vanderbilt Financial’s other business. The Fund’s equity tranche in the CDOs was “toxic waste” – the lowest position with the highest level of risk and least return. Citibank and Bear Stearns had not

agreed to forego a fee as a reward for being Vanderbilt's "friend" or "family." The Fund was not being offered an especially good deal due to the absence of a fee to Citibank or Bear Stearns or the purported short term and high return of the investment. The Vanderbilt Defendants knew the Board could not reasonably expect to receive back its entire principal investment plus an annualized return of 12-15% by the end of the 1.3-year term of the deal. The risk of default on the underlying loans was not mitigated, offset, or accounted for "up front." The Vanderbilt Defendants knew they would not realistically be able to sell out of the investment in the event of defaults in the portfolio in order to avoid a negative return. There was never any prospect of an initial public offering, listing on the New York Stock Exchange, or liquidity with respect to the Vanderbilt investment.

153. The Vanderbilt Defendants also omitted to state material facts it was obligated to disclose and that, under the circumstances, made its conduct false and misleading. These material omissions included:

- a) That the Vanderbilt investment was highly speculative and risky, excessively leveraged, and virtually worthless.
- b) That the underlying assets consisted mainly of subprime loans, including adjustable rate residential mortgages, toxic waste, liar's loans, and exceptional loans.
- c) That due to the nature of the underlying assets, a high default rate was probable.
- d) That Vanderbilt had come to the Board for an investment through the intervention of John Doe #1 and John Doe #2.
- e) That Vanderbilt had agreed to generate political contributions to the Richardson presidential campaign in exchange for a Fund investment.
- f) That Vanderbilt had paid John Doe #2 as a placement agent to exert his influence to obtain the Fund's investment.
- g) That John Doe #1 also was exerting his influence to obtain the Fund's investment.

- h) That John Doe #2 had brought Citibank and Bear Stearns into the deal.
- i) That the purported zero-default rate experienced by Vanderbilt was entirely irrelevant to the Vanderbilt investment being promoted to the Board.
- j) That the investment was created and targeted for the ERB and SIC and not sold to any other outside investors.

154. The Vanderbilt Defendants' fraud has caused and is causing substantial damages to the Fund and its members.

COUNT VIII:

BREACH OF FIDUCIARY DUTIES

(Against Defendants Meyer and Aldus)

155. The allegations in paragraphs 107 are incorporated herein.

156. Defendants Meyer and Aldus breached their fiduciary and other duties by recommending the Aldus investments to the ERB due to political pressures rather than on the basis of objective advice and the best interests of the Fund and its members. Defendants Meyer and Aldus did this knowing that the Aldus investments were inappropriate for the ERB and that politically-connected individuals would benefit politically or financially, and they would benefit financially, from them.

157. Defendants Meyer's and Aldus' breach of fiduciary duties has caused and is causing substantial damages to the Fund and the members of the Class.

COUNT IX:

FRAUD

(Against Defendants Meyer and Aldus)

158. The allegations in paragraphs 107 are incorporated herein.

159. Defendants Meyer and Aldus knowingly made material misrepresentations and omissions intending for the ERB to rely on them and designed to ensure that the ERB made the Aldus investments they recommended.

160. Defendants Meyer's and Aldus' fraud has caused and is causing substantial damages to the Fund and the members of the Class.

COUNT X:

AIDING AND ABETTING BREACH OF FIDUCIARY DUTIES

(Against John Doe #1 and John Doe #2)

161. The allegations in paragraphs 107 are incorporated herein.

162. John Doe #1 and John Doe #2 knowingly substantially assisted defendants Meyer, Aldus, and Malott in their breaches of fiduciary and other duties, as alleged herein.

163. John Doe #1's and John Doe #2's wrongful conduct aiding and abetting defendant Meyer's, Aldus', and Malott's breaches of fiduciary duties has caused and is causing substantial damages to the Fund and the members of the Class.

COUNT XI:

AIDING AND ABETTING FRAUD

(Against John Doe #1 and John Doe #2)

164. The allegations in paragraphs 107 are incorporated herein.

165. John Doe #1 and John Doe #2 knowingly substantially assisted defendants Meyer and Aldus in their fraud, as alleged herein.

166. John Doe #1's and John Doe #2's wrongful conduct aiding and abetting defendants Meyer's and Aldus' fraud has caused and is causing substantial damages to the Fund and the members of the Class.

PRAYER FOR RELIEF

WHEREFORE, plaintiffs pray for relief, including:

- A. An award of actual damages consisting of lost principal, lost income, and fees and expenses in an amount to be determined at trial;
- B. Pre- and post-judgment interest;
- C. An award of reasonable attorneys' fees and costs;
- D. Injunctive and other appropriate equitable relief prohibiting the wrongful conduct alleged herein, including "pay to play" practices and political contributions by

persons doing business with the Board, and removing the defendant Trustees from the Board; and

E. Such other relief as may be necessary or appropriate.

Respectfully submitted,

THE ROWE LAW FIRM

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