SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK
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BEAR STEARNS HIGH-GRADE STRUCTURED CREDIT STRATEGIES ENHANCED LEVERAGE (OVERSEAS) LTD. AND BEAR STEARNS HIGH-GRADE STRUCTURED CREDIT STRATEGIES (OVERSEAS) LTD. (BOTH IN OFFICIAL LIQUIDATION),

Index No. 656378/2018

Plaintiffs,

COMPLAINT

-against-

REED SMITH LLP,

Defendant.

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Plaintiffs Bear Stearns High-Grade Structured Credit Strategies Enhanced Leverage (Overseas) Ltd. and Bear Stearns High-Grade Structured Credit Strategies (Overseas) Ltd. (Both in Official Liquidation) (collectively, the "**Bear Stearns Funds**"), acting through their Joint Official Liquidators Geoffrey Varga and Mark Longbottom (the "**Liquidators**"), hereby file this Complaint against Defendant Reed Smith LLP ("**Reed Smith**") for legal malpractice, breach of fiduciary duty, and breach of contract (under the law of the Cayman Islands), and allege as follows:

I. INTRODUCTION

1. Reed Smith's negligent failure to understand New York's statute of limitations cost the Bear Stearns Funds what Reed Smith identified as ***a billion-dollar claim*** against various rating agencies (collectively, the "**Rating Agencies**") for their well-

established RMBS-related fraud.[1] And, Reed Smith's further negligence in failing to inform its clients of potential claims against the underwriters of those RMBS, which Reed Smith identified internally well before limitations expired on those claims, cost its clients additional claims worth at least hundreds of millions of dollars. In total, Reed Smith's haphazard representation of the Bear Stearns Funds caused the funds to lose claims worth over a billion dollars—claims against defendants who unquestionably committed the fraud that gave rise to those claims and had the financial wherewithal to pay the full amount of the judgment the Bear Stearns Funds would have obtained.

2. Reed Smith's approach to its representation of the Bear Stearns Funds combined with its negligence doomed both the Rating Agencies case and the potential underwriter case before they even started. Reed Smith viewed its role as both lawyer and client. Reed Smith repeatedly made the legal and strategy decisions for the Bear Stearns Funds without advising or consulting its actual clients, only involving them when Reed Smith needed final approval of its pre-packaged strategy.

3. This misguided approach to the legal representation led to a disastrous result when Reed Smith failed to even raise the claim against the Rating Agencies with its clients until after limitations had run, even though the claims had been live when Reed Smith (unbeknownst to its clients) completed its initial, internal analysis nearly two years before.

[1] The Rating Agencies included: McGraw Hill Financial, Inc., Standard & Poor's Financial Services LLC, Moody's Corporation, Moody's Investors Service Inc., Moody's Investors Service Limited, Fitch Group, Inc., Fitch Ratings, Inc., and Fitch Ratings Limited.

4. In at least as early as 2011, Reed Smith identified potential claims against the Ratings Agencies and began analyzing those claims. As part of its analysis, in an October 11, 2011 internal memorandum, Reed Smith identified two important issues for the Rating Agencies case—limitations and standing. But, rather than correctly applying the law, informing its clients, and taking the necessary steps to protect what were then viable and extremely valuable claims, Reed Smith inexplicably told the clients nothing about the claims or the limitations and standing issues. Over the ensuing two years, as limitations ran on all of the claims, Reed Smith made mistake after mistake, which would eventually lead to dismissal of the Bear Stearns Funds' claims against the Rating Agencies on simple and well-founded limitations and standing grounds.

5. In the 2011 memorandum, Reed Smith correctly noted that New York's statute of limitations for fraud runs six years from accrual or two years from discovery of the fraud. Unfortunately, and inexplicably, for the following two years, Reed Smith confused the accrual and discovery aspects of the rule. Apparently, in contravention of its own memo and without any supporting New York authority, Reed Smith concluded that limitations ran six years from the date the Bear Stearns Funds discovered the Rating Agencies' fraud.

6. Ultimately, when Reed Smith argued what effectively amounted to a six-year discovery rule to the New York Supreme Court on behalf of the Bear Stearns Funds, the court rejected it, stating: "Plaintiffs have conflated the two-year discovery cases with the six year statutory cases" and "[t]his theory imbues the six-year statutory period with a degree of elasticity not reflected in any New York case law."

7. But, by the time Reed Smith made the six-year discovery argument to the court, it had long-since recognized its mistake internally. In fact, on May 16, 2013, just prior to finally notifying the Bear Stearns Funds about the potential claims against the Rating Agencies, Reed Smith recognized its mistake in an email that stated "***we need to address whether we have a good faith belief that the statute of limitations has not run on our fraud claims against the ratings agencies***" given that "the statute of limitations for fraud claims is six years from the date of the alleged misrepresentation, which in this case is the date the [Master Funds] became invested in a particular security" and "***the limitations will have run by the time we file this complaint in July 2013***." Notably, on May 16, 2013, there was still one security for which limitations had not run because it had been purchased on May 29, 2007. But, inexplicably, Reed Smith did not rush to file before May 29, 2013, which would have at least given the Bear Stearns Funds a claim based on one security that was not dead on limitations. Instead, the same email reflected Reed Smith's next approach: scrambling to come up with "tolling in order to claim that the SOL [statute of limitations] has not ran as of July 2013."[2]

8. Shockingly, although Reed Smith recognized limitations had run, it did not share that information with its clients. Instead, Reed Smith pivoted to arguing that the "continuing wrong doctrine" tolled the running of the six-year limitations clock. This argument would also be rejected out of hand by the New York Supreme Court as

[2] Although Reed Smith had not even discussed bringing these claims with their clients at this time, Reed Smith had already drafted a complaint, selected the relevant securities from the universe of securities owned by Bear Stearns, and identified the date they would file the case, which was well after limitations had already run.

"unpersuasive" and "inapposite" because the "cases relied on by Plaintiffs to support this theory do not implicate New York's six-year statute of limitations and can be otherwise differentiated."

9. Thus, by the time Reed Smith brought the Ratings Agencies claims to the Bear Stearns Funds' attention in June 2013, Reed Smith already knew that its six-year discovery rule argument was wrong, and knew or should have known that for its "continuing wrong doctrine" tolling theory to work, a court would have to apply that doctrine in a context where it had never been applied before.

10. But, rather than advising the Bear Stearns Funds that limitations had run and any attempt to extend limitations with a tolling doctrine would be an extreme longshot, Reed Smith, in early June 2013, merely told the Bear Stearns Funds that limitations was "burning." Reed Smith then advised the Bear Stearns Funds that if they filed by early July 2013, they would be fine. The Bear Stearns Funds filed their summons and notice on July 9, 2013, as instructed by Reed Smith. But, as Reed Smith knew or should have known, it was already too late.

11. Doubling down, and ignoring both its internal analysis and New York law, in September 2013, James McCarroll ("**McCarroll**"), the lead Reed Smith partner on the case, told the Bear Stearns Funds' Investment Advisory Committee ("**Advisory Committee**") that "the statute of limitations . . . ***is not a substantial concern***." Moreover, in a September 2013 affidavit submitted to the Cayman Islands court in support of the

Bear Stearns Funds' application for permission to file the Ratings Agencies complaint,[3] McCarroll incorrectly represented to the Cayman Court that the Bear Stearns Funds had a credible, well-supported argument that the six-year limitations period was "tolled" under the "continuing wrong" doctrine.

12. But, although Reed Smith tried to gloss over the massive limitations problems, those issues eventually came to light when the Bear Stearns Funds' claim was dismissed on limitations grounds, and that dismissal was upheld on appeal.

13. The second issue that Reed Smith spotted in 2011—when limitations was still live—was whether the Bear Stearns Funds, as feeder funds, or their master funds, Bear Stearns High-Grade Structured Credit Strategies Master Fund, Ltd. and Bear Stearns High-Grade Structured Credit Strategies Enhanced Leverage Master Fund, Ltd. (Both in Official Liquidation) (collectively, the "**Master Funds**"), had standing to bring the claims against the Rating Agencies. Reed Smith understood that as feeder funds, the Bear Stearns Funds suffered damages totaling hundreds of millions of dollars due to the Rating Agencies' fraud, but that because of the master–feeder structure, the Master Funds actually purchased the securities rated by the Rating Agencies.

14. Thus, Reed Smith correctly recognized that the Master Funds were the entities with direct standing to pursue the claim against the Rating Agencies, not the Bear Stearns Funds. To address that issue, Reed Smith concluded, in 2011, that the Bear Stearns Funds had a number of options available to bring the claims, including "buy[ing] the

[3] The Bear Stearns Funds filed only a summons and notice on July 9, 2013. They did not file their complaint until November 2013 after receiving sanction from the Cayman Islands court to do so.

claims from the Master Fund and asserting them thereafter" or "convinc[ing] a court to order the Master Fund liquidators to assert the claims or permit the [Bear Stearns Funds] to assert the claims." And, in fact, after Reed Smith filed the case and limitations had run, based on Reed Smith's tardy advice, the Bear Stearns Funds did receive an assignment of the claims from the Master Funds. But, by then it was far too late.[4] Again, Reed Smith never raised this standing issue with the Bear Stearns Funds in the nearly two years that it internally worked up the claim with no input from the Bear Stearns Funds.

15. If Reed Smith had informed the Bear Stearns Funds in 2011 about the potential claim against the Rating Agencies—as it had a fiduciary obligation to do—the Bear Stearns Funds would have taken the necessary actions to investigate and acquire the claim in early 2012, well before limitations expired. But, instead, Reed Smith wasted valuable time working up the claims on their own, under a mistaken and baseless belief that New York's statute of limitations for fraud would not run until July 10, 2013. And, even when it recognized its mistake, rather than admit the limitations problem, Reed Smith concocted a destined-to-fail tolling theory based on an inapplicable doctrine, and hid its malpractice from the Bear Stearns Funds, in breach of its fiduciary duties.

16. Reed Smith, on information and belief, was motivated to breach its fiduciary duties and conceal its malpractice from the Bear Stearns Funds for several

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[4] In addition, albeit also too late because Reed Smith had already blown limitations, in the Cayman Islands proceedings to get permission to file the complaint in New York, the Cayman Island court overseeing both the Bear Stearns Funds' and Master Funds' liquidations proposed directing the Master Fund to bring the claims as an option to address the standing issue, but Reed Smith inexplicably turned the court down.

reasons. First, Reed Smith had just resolved a prior case on behalf of the Bear Stearns Funds and was waiting to receive its large contingency fee for that case. Reed Smith, on information and belief, did not want to risk informing the Bear Stearns Funds that it had missed limitations on the claim against the Rating Agencies while its contingency fee was due to be paid.

17. Further, Reed Smith was billing the Bear Stearns Funds for millions of dollars in hourly fees, and the Rating Agencies litigation provided an opportunity to continue that billing. In fact, even at 50% hourly rates (the agreed-upon rate pursuant to the engagement letters), Reed Smith collected from the Bear Stearns Funds over $6 million in fees (meaning that Reed Smith billed around $12 million in time at 100% rates) to file the complaint against the Rating Agencies, brief and lose a motion to dismiss, and brief and lose a subsequent an appeal. The expenditure of this gargantuan sum of hourly fees was only made worse by the spectacularly bad—albeit predictable—result.

18. Reed Smith's failures were not only limited to the Rating Agencies litigation. In the same 46-page internal memorandum where Reed Smith identified the Rating Agencies claims and the pathway to pursuing those claims, Reed Smith also spent 20 pages discussing potential claims against the underwriters of the RMBS that the Rating Agencies rated. Reed Smith noted, "there have been countless lawsuits seeking to hold liable the parties that structured and sold the various products that plunged in value during the subprime meltdown," and also that "the case law does appear to support an action asserting common law claims against the underwriters." Reed Smith then went on to conclude: "We recommend pursuing a fact investigation to assess the viability of . . .

asserting claims for fraud, negligent misrepresentation, breach of contract, breach of fiduciary duty and aiding and abetting against the underwriters of each offering for which damages are sought."

19. Of course, Reed Smith never shared this conclusion with the Bear Stearns Funds, and so the Bear Stearns Funds were not even aware of the claims worth hundreds of millions of dollars they had against the underwriters. And, Reed Smith sat by and allowed the time to file those claims expire over the next two years without even raising the possibility of investigating the claims with the Bear Stearns Funds. So, as with the Rating Agencies claims, the Bear Stearns Funds lost staggeringly valuable claims, without even knowing they existed at a time when they were viable.

20. The Bear Stearns Funds, through their Liquidators, bring this action to recover at least hundreds of millions of dollars in damages and compel disgorgement of all fees paid to Reed Smith while it was breaching its fiduciary duties.

II. PARTIES

21. Plaintiff Bear Stearns High-Grade Structured Credit Strategies Enhanced Leverage (Overseas) Ltd. (In Official Liquidation) is a Cayman Islands exempted company, organized under the Companies Law of the Cayman Islands. It is in official liquidation proceedings before Cayman Court in the Cayman Islands.

22. Plaintiff Bear Stearns High-Grade Structured Credit Strategies (Overseas) Ltd. (In Official Liquidation) is a Cayman Islands exempted company, organized under the Companies Law of the Cayman Islands. It is in official liquidation proceedings before the Cayman Court.

23. The Bear Stearns Funds bring this action through their official Liquidators, Geoffrey Varga and Mark Longbottom.

24. Defendant Reed Smith is a Delaware partnership with partners that reside in and are citizens of New York. Defendant Reed Smith has a New York office at 599 Lexington Avenue, New York, NY, 10022.

III. FACTUAL ALLEGATIONS

A. The Bear Stearns Funds retained Reed Smith in 2008 to investigate and pursue claims against parties responsible for the Bear Stearns Funds' collapse.

25. The Bear Stearns companies and related funds collapsed in early 2008. In March 2008, the Bear Stearns Funds were placed into official liquidation in the Cayman Islands.

26. On March 1, 2008, Reed Smith and each of the Bear Stearns Funds entered into an engagement letter (collectively, the "**Engagement Letters**").[5] These Engagement Letters provided that Reed Smith would advise and represent the Bear Stearns Funds in connection with the "investigation and prosecution of claims" on behalf of the funds.

27. As stated above, the Reed Smith partner responsible for the representation was McCarroll, an attorney in Reed Smith's New York office. In the years 2008 to 2013 alone, McCarroll spent thousands of hours representing the Bear Stearns Funds pursuant to the Engagement Letters. Given the immense amount of work conducted by McCarroll, including his and Reed Smith's prior involvement with certain of the Bear Stearns Funds'

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[5] Each of the Bear Stearns Funds executed a separate engagement letter with Reed Smith, but the terms were identical.

investors in 2007 leading to the appointment of the Liquidators, he and Reed Smith should have understood the details concerning the Bear Stearns Funds' collapse, the parties responsible for the collapse, and the how the Liquidators could seek to recover the Bear Stearns Funds' losses. Indeed, McCarroll submitted to the Cayman Court that he was "very familiar with the Feeder Funds' position as part of the structure of the Bear Stearns hedge funds that suffered catastrophic losses in mid-2007."

28. Multiple other partners collectively spent thousands of hours on the Bear Stearns representation, including the litigation against the Rating Agencies. C. Neil Gray ("**Gray**"), a partner in Reed Smith's New York office, represented the Bear Stearns Funds in numerous actions and began billing time related to potential Rating Agencies litigation as far back as 2011. Jordan W. Siev ("**Siev**"), another partner in Reed Smith's New York office, also worked on multiple matters for the Bear Stearns Funds, including the litigation against the Rating Agencies.

29. Pursuant to the Engagement Letters, Reed Smith investigated multiple potential claims and, prior to 2013, pursued claims on behalf of the Bear Stearns Funds against, among others, JPMorgan, the successor-in-interest to Bear, Stearns & Co. Inc.

30. In 2013, in connection with the pursuit of claims against the Rating Agencies, Reed Smith and the Bear Stearns Funds agreed to amend the Engagement Letters to provide, among other things, that, in accordance with Cayman liquidation rules, the "ongoing engagement" was governed by Cayman law. Specifically, the amendment to the Engagement Letters was an acknowledgement that "the relevant provisions of the Grand Court of Cayman Islands' Companies Winding Up Rules,"

applied "to Reed Smith's ongoing engagements." By incorporating the relevant provisions of the Cayman rules—including Order 25, Rule 1, which governs engagements between attorneys and companies in liquidation—Reed Smith agreed that its Engagement Letters are governed by Cayman law.

B. Reed Smith negligently failed to inform the Bear Stearns Funds about the Rating Agencies claims prior to the expiration of the statute of limitations.

1. Reed Smith researched the potential claims in 2011, but never advised the Bear Stearns Funds about the Rating Agencies claims and how to acquire them.

31. Beginning in May 2011, if not earlier, Reed Smith began investigating potential claims against the Rating Agencies. In fact, from May 2011 to December 2011, Reed Smith attorneys spent a considerable amount of time analyzing the potential claims, billing the Bear Stearns Funds tens of thousands of dollars in the process.

32. Gray led the initial investigation into claims against the Rating Agencies. His analysis (and that of other Reed Smith attorneys) included: "review[ing] numerous cases re actions against rating agencies"; "research[ing] the law re statute of limitations and elements for various state law cause of action"; "research[ing] the law re lawsuits asserted against rating agencies"; and "research[ing] . . . duties and liabilities of rating agencies to third parties."

33. After conducting its preliminary analysis, Reed Smith prepared a memorandum to provide to the Bear Stearns Funds about the potential claims. But Reed Smith inexplicably never shared this memorandum or the underlying analysis with the Bear Stearns Funds.

34. In the memorandum, Reed Smith analyzed the potential fraud claim against the Rating Agencies and whether the Bear Stearns Funds had standing to pursue the claim. Reed Smith concluded that the Bear Stearns Funds lacked both direct and derivative standing. But, as explained below, Reed Smith recognized that the Bear Stearns Funds could seek to acquire the claims from the Master Funds, which also were in liquidation proceedings in the Cayman Islands.

35. With respect to whether the Bear Stearns Funds had direct standing to pursue the claims, Reed Smith concluded: "Based on our research, we believe the [Bear Stearns] Funds lack standing to assert direct actions against parties" such as the Rating Agencies and "[w]e have been unable to identify other potential bases for asserting claims directly against these entities." Because the Bear Stearns Funds lacked direct standing, Reed Smith then analyzed whether the funds had derivative standing as shareholders of the Master Funds.

36. Reed Smith, however, concluded that the Bear Stearns Funds also lacked derivative standing. Reed Smith stated in the draft memorandum:

> Unfortunately, the circumstances under Cayman law in which a minority shareholder may bring a derivative claim in his own name (but for the benefit of the company) are very limited. . . .
>
> Moreover, the ability of a shareholder in a Cayman company to pursue claims which belong to that Cayman company is even more limited where the company is in liquidation. ***Indeed, after a company goes into liquidation, it is no longer possible to bring a shareholder derivative claim because the right to bring a claim passes to the liquidator***.

37. Reed Smith, however, with the advice of Cayman counsel, identified a way around the standing issues. Reed Smith recognized that the Bear Stearns Funds could seek to "buy the claims from the Master Fund[s] and assert them thereafter."

38. Reed Smith—in 2011—concluded its 46-page internal memorandum (which it never shared with its clients) with the following advice: "We recommend pursuing a fact investigation to assess the viability of asserting claims for common law fraud, breach of contract, and aiding and abetting against the Rating Agencies." Reed Smith, however, did not advise the Bear Stearns Funds about the potential claims at the time.

39. Critically, had Reed Smith advised the Bear Stearns Funds about the potential claims, the Bear Stearns Funds would have requested that Reed Smith further analyze the claims and immediately start the process of requesting an assignment of the claims from the Master Funds.

40. Had Reed Smith continued its analysis in 2011 and 2012, it would have found more than ample evidence to draft a compelling fraud claim against the Rating Agencies. In fact, while Reed Smith stopped its research without even informing its clients of the potentially valuable claims, other parties were pursuing the Rating Agencies for hundreds of millions of dollars in damages on similar grounds.

41. Notably, as Reed Smith knew, certain plaintiffs filed a case against the Rating Agencies back in August 2008. That case, *Abu Dhabi Commercial Bank, et al. v. Morgan Stanley & Co. Inc., et al.*, had progressed to summary judgment by mid-2012. In response to a motion for summary judgment filed by the Rating Agencies, the plaintiffs

presented substantial evidence of the Rating Agencies' fraud. For instance, their opposition to the motion for summary judgment contained the following statement, supported by documentary evidence:

> Due to market pressures, the rating agencies engaged in an improper practice known as "grandfathering," which uses old, outdated models to rate new deals. In late 2005, Elwyn Wong, an S&P executive, responded to pressure from MS to grandfather existing deals by writing: **"Lord *help our f[***]ing scam* . . .** this has to be the stupidest place I have worked at." An S&P structured finance employee conceded: "[I]t could be structured by cows and we would rate it." Another S&P structured finance employee remarked: "Let's hope we are all wealthy and retired by the time this house of card[s] falters."

42. At bottom, Reed Smith knew back in 2011 that the Bear Stearns Funds, which suffered some of the most substantial losses of any victims of the financial collapse, had strong claims against the Rating Agencies and others as well. Reed Smith owed the Bear Stearns Funds a duty to advise them of these potential claims so that the Bear Stearns Funds could take appropriate actions to pursue the claims and recover their losses.

43. As explained below, had the Bear Stearns Funds been properly advised about the claims and the correct statute of limitations, they could and would have received an assignment from the Master Funds by early 2012 and filed the assigned claims shortly thereafter.

2. Reed Smith extensively researched the claim against the Rating Agencies again in early 2013—while a significant portion of the claim was still viable—but failed to timely advise Bear Stearns Funds.

44. On February 5, 2013, the Department of Justice ("**DOJ**") filed a detailed complaint against the Rating Agencies accusing them of fraud. Reed Smith almost immediately re-opened its analysis into claims against the Rating Agencies.

45. As part of this analysis, beginning on February 7, 2013, if not earlier, Reed Smith began researching the statute of limitations. This should have been a simple, straightforward assignment. Reed Smith, however, spent countless hours on the issue and still failed to understand the "clear" New York law on when a claim accrues for purposes of calculating the six-year limitations period.

46. Reed Smith's invoices reflect the fact that multiple attorneys, including partners Gray and Siev, and several associates, looked into the statute of limitations in early February 2013.

47. Below are just some of the pertinent entries from Reed Smith's February 2013 invoices:

Date	Attorney	Time Detail	Hours
2/5/13	Gray	Coordinate with [associate] regarding private rights of action under FIRREA; research the law re: same; email to J. McCarroll regarding preliminary results of research; pull main action against McGraw-Hill / S&P; research statutory bases for DOJ's action; confer with J. McCarroll regarding additional research.	2.00
2/7/13	[Associate]	Researched statute of limitations issues, including accrual and tolling issues, drafted email summarizing research.	4.15
2/8/13	Gray	Review cases supplied by [associate] in connection with research to identify civil claims against rating agencies.	.50
2/11/13	Gray	Review memorandum/chart setting out private civil claims asserted against rating agencies in connection with financial crisis; emails to [associate] and J. McCarroll re same; review revised memorandum/chart setting out civil claims asserted against rating agencies; email to J. McCarroll.	.30

2/11/13	[Associate]	Researched statute of limitations and accrual issues; began drafting memo on said issues.	1.15
2/12/13	[Associate]	Drafted memorandum on statute of limitations and accrual issues.	1.15
2/14/13	[Associate]	Research and review case law regarding tolling of statute of limitations in a derivative action; draft email regarding same to [associate].	2.40
2/16/13	[Associate]	Researched statute of limitations issue – when the statute of limitations accrues in a fraud action brought derivatively on behalf of an investment.	2.15
2/19/13	[Associate]	Legal research and analysis of case law re: statute of Limitations and in derivative fraud actions; telephone conference with [associate] re: same.	1.15
2/21/13	[Associate]	Review news articles search results; conduct research pertaining to statute of limitations and derivative claim issues.	1.05

48. Despite numerous hours spent on research of the statute of limitations, Reed Smith somehow overlooked the "clear" New York law on when a claim for fraud accrues for limitations purposes. In fact, not a single Reed Smith lawyer alerted the Bear Stearns Funds that, absent an unsupported argument for "tolling" the limitations period, the statute of limitations expired six years from the date of each investment made by the Master Funds.

49. The conclusions reached by Reed Smith attorneys concerning the operation of New York's statute of limitations evidence that Reed Smith simply had no clue what it was doing. For instance, on April 18, 2013, a Reed Smith attorney emailed Siev about the statute of limitations. As set forth in this email, the attorney confused the concept of accrual with the discovery rule, stating:

> Under New York law, a claim for common law fraud must be brought within six years from the time the cause of action accrued or within two years from the time the wrongdoing was or, with reasonable diligence, should have been discovered, whichever is longer. Under the six-year prong, the cause of action is deemed to have accrued on the date the fraud is committed. . . . Our conclusion is that this cause of action likely did not accrue until investors were aware that one or both of the Funds were certain to collapse, in or around mid-June 2007, as further explained below.

50. Siev then forwarded the email to Gray, stating that Reed Smith's analysis showed that the limitations would run on July 10, 2007: "Further to our discussion, yes, July 10th is the date the market became aware of S&P's intention to downgrade subprime securities and, thus, the date we have considered the absolute outside date for statute of limitations purposes." The analysis, however, was simply wrong.

51. As a result of Reed Smith's failure to grasp the legal principles, the statute of limitations continued to run on claims arising out of the Master Funds' purchases of securities from February 2013 through May 2013.

52. In early April 2013, Reed Smith started drafting a complaint against the Rating Agencies.

53. On April 15, 2013, Reed Smith prepared a memorandum to the "file." In this internal memorandum, which, like the 2011 memorandum, was not shared with the Bear Stearns Funds, Reed Smith reiterated that the Bear Stearns Funds "lack standing to assert a direct action against the rating agencies." Reed Smith then, as it did in 2011, stated that the Bear Stearns Funds should seek to "buy the claims from the Master Fund and assert them thereafter." Specifically, the memorandum concluded:

> [W]e will need to convince the Master Fund[s'] liquidators to assert the claims on behalf of the Master Fund[s] (which may require funding the liquidators' pursuits); convince a court to order the Master Fund[s'] liquidators to assert the claims or permit the [Bear Stearns Funds] Liquidators to assert the claims; or buy the claims from the Master Fund[s] and assert them thereafter.

54. Notwithstanding its opinion that the Bear Stearns Funds lacked standing to bring a direct claim, Reed Smith later advised the Bear Stearns Funds to file that exact claim with no warning that it was almost certainly a lost cause. And, despite its recognition that the Bear Stearns Funds should seek to "buy the claims from the Master Fund and assert them thereafter," Reed Smith inexplicably waited until limitations had expired to advise the Bear Stearns Funds of this course of action.

C. Reed Smith advised the Bear Stearns Funds to file the claim after limitations expired and without first acquiring the claim from the Master Funds.

55. Reed Smith determined sometime in May 2013, if not earlier, that it would advise the Bear Stearns Funds to file their claim in early July 2013. Eventually, some Reed Smith attorneys started questioning why Reed Smith was waiting until after limitations lapsed to file the lawsuit.

56. Notably, on May 15, 2013, a Reed Smith associate emailed other members of the Reed Smith team, including Siev and Gray, about the statute of limitations for the fraud claim against the Rating Agencies. The attorney questioned whether Reed Smith would have a "Rule 11" basis to knowingly bring the claims after limitations lapsed:

> I think we need to address whether we have a good faith belief that the statute of limitations has not run on our fraud claim against the rating agencies. . . .
>
> The statute of limitations for fraud is six years from the date of the alleged misrepresentation, which in this case, is the date the Overseas Funds became invested in a particular security that was mis-rated by one of the rating agencies (i.e., the date the security was sold to the Master Funds). ***Given that All of the securities purchased by the Master Funds were purchased prior to July 1, 2007, the six-year statute of limitations will have run (irrespective of the securities we choose to focus on) by the time we file this complaint in July 2013***.

57. Reed Smith ignored these concerns and waited until early June 2013 to, for the first time, advise the Bear Stearns Funds about the Rating Agencies claims.

58. Sometime in early June 2013, McCarroll advised Varga (one of the Liquidators) about what he described as the "burning limitations" issues and the need to immediately file an action to preserve limitations. But McCarroll did not advise that the limitations period had lapsed; rather, he wrongly (and repeatedly) advised that it would lapse on July 10, 2013.

59. Relying on McCarroll's and Reed Smith's advice, the Liquidators and the Bear Stearns Funds filed a summons with notice on July 9, 2013. The summons with notice was meant to serve as a placeholder for the Bear Stearns Funds to give the Liquidators time to seek approval from the Cayman Court to commence litigation on behalf of the Bear Stearns Funds.

60. Shortly after filing the summons with notice, McCarroll advised Varga that with respect to the statute of limitations, it was "clear[] that we came in under the wire." McCarroll knew or should have known that this representation was blatantly false.

D. Reed Smith negligently misled the Cayman Court and the Bear Stearns Funds, effectively concealing its malpractice in the process.

1. Reed Smith reassured the Liquidators and the Investment Advisory Committee that the statute of limitations was "not a substantial concern."

61. On September 26, 2013, the Liquidators convened a meeting of the Bear Stearns Funds' Advisory Committee to discuss, among other things, the proposed litigation against the Rating Agencies. McCarroll and Siev attended the meeting on behalf of Reed Smith.

62. After providing an overview of the proposed litigation and explaining that it would have to be brought in New York state court, McCarroll assured the Liquidators and the Advisory Committee that "Reed Smith [has] extensive experience of that Court and [is] confident of appropriate treatment of the case by the Judges there."

63. McCarroll provided further comfort that Reed Smith was "***highly optimistic***" that the Liquidators would be successful against a motion to dismiss. McCarroll and Siev noted the specificity requirement for pleading fraud claims but advised the Advisory Committee that they expected the evidence "will meet this requirement and be advantageous in any Motion to Dismiss hearing." McCarroll also touted the high damages involved in the litigation, noting damages figures ranging from $850 million to $1.1 billion.

64. With regard to the statute of limitations, McCarroll explained that the case was brought "very close to what is arguable [sic] the expiration of the limitation period." But McCarroll reassured the committee: "there is a possible argument that the statute of

limitations may have expired in some instances, ***however this is not a substantial concern***."

65. McCarroll and Siev did not raise the issue of the Bear Stearns Funds' standing to bring the claims or suggest that there was any risk in that regard.

66. Following Reed Smith's presentation, the Liquidators concluded that they had no concerns pursuing the litigation and incurring the necessary costs.

2. Reed Smith submitted an affidavit to the Cayman Court that failed to present an honest and reasonable assessment of the claims.

67. For the Liquidators to bring a claim on behalf of the Bear Stearns Funds, they must first receive the approval, or sanction, of the Cayman Court. To convince the Cayman Court to sanction the claim, the Liquidators had to present evidence that the claim had a reasonable prospect of success and that its pursuit would be in the interests of the Bear Stearns Funds and their stakeholders. The Liquidators, as is common practice and as generally required by the Cayman Court, requested that their attorneys submit an affidavit to the Cayman Court on the merits of the claim and its likelihood of success.

68. McCarroll represented to the Cayman Court that the statute of limitations was not a significant issue and that the Bear Stearns Funds only filed the summons with notice on July 9, 2013, "in an abundance of caution." McCarroll never advised the Cayman Court that Reed Smith's argument for tolling the statute of limitations was unsupported by a single case and, at the very least, novel. Rather, McCarroll, similar to his statement to the Advisory Committee, represented to the Cayman Court that limitations was not a substantial concern in the case.

69. McCarroll misconstrued or misinterpreted multiple New York cases in his affidavit to the Cayman Court. Notably, McCarroll stated that the Southern District of New York's opinion in *Abu Dhabi Commercial Bank v. Morgan Stanley & Co.* supported the argument that the continuing-wrong doctrine tolled the claims against the Rating Agencies. However, as McCarroll and Reed Smith knew, the *Abu Dhabi* case did not involve a statute-of-limitations dispute, much less the continuing-wrong doctrine. In fact, the case involved a lawsuit filed well within six years from the date of the alleged wrongful act and thus the limitations issue was never raised as a defense. Moreover, the tangential discussion in the court's opinion related to accrual of claims for purposes of determining the admissibility of evidence made it clear that accrual occurs, and thus limitations begins to run, on the date "which the plaintiffs purchased the [Note] allegedly in reliance on" the ratings issued by the Rating Agencies. In sum, Reed Smith's reliance on the *Abu Dhabi* case for the application of the continuing-wrong doctrine to toll a New York common-law fraud claim was completely misplaced and absolutely destined to fail. Thus, Reed Smith's representation to the Cayman Court that there was any basis whatsoever to make that argument was reckless at best.

70. In addition to being less than truthful regarding the prospects of overcoming a statute-of-limitations defense, McCarroll omitted material information concerning the issue of whether the Bear Stearns Funds had standing to pursue the claims. Despite internally concluding on at least two separate occasions that the Bear Stearns Funds lacked a basis to bring direct claims against the Rating Agencies, McCarroll told the Cayman Court that although the fraudulent ratings "arguably were made to the

Master Funds and not the [Bear Stearns Funds] directly also does not bar the Liquidators' fraud claim."

71. In reliance on McCarroll's affidavit, the Cayman Court sanctioned the litigation against the Rating Agencies on October 30, 2013.

72. Shortly thereafter, on November 11, 2013, the Bear Stearns Funds filed their complaint against the Rating Agencies in New York Supreme Court (the "**Trial Court**"). The complaint set forth a single cause of action for common law fraud and alleged damages of "not less than $1 billion."

E. Reed Smith advised the Bear Stearns Funds to obtain an assignment of the claim from the Master Funds after limitations lapsed.

73. On September 12, 2014, the Rating Agencies moved to dismiss the fraud claim, arguing to the Trial Court, among other things, that the statute of limitations had expired and that the Bear Stearns Funds lacked standing to bring the claim, both as a direct claim and as derivative claim.

74. In response to the arguments about their lack of derivative standing, the Bear Stearns Funds re-engaged with the liquidators of the Master Funds to discuss an assignment of the claims. Because Reed Smith did not inform the Bear Stearns Funds that the assignment was time-sensitive, the Bear Stearns Funds and the Master Funds negotiated an Assignment and Ratification Agreement (the "**Assignment**"), which the parties executed on May 11, 2015.

75. As part of the Assignment, the Bear Stearns Funds paid $500,000 (plus over $125,000 of ongoing costs) to the Master Funds.

76. Had Reed Smith advised the Bear Stearns Funds back in 2011 to receive an assignment of claims from the Master Funds, the Bear Stearns Funds could and would have negotiated the Assignment back in late 2011 or early 2012, well prior to the expiration of the statute of limitations.

F. The Trial Court dismissed the claim as untimely, and chided Reed Smith for its unsupported and unpersuasive arguments.

1. The Rating Agencies moved to dismiss based on, among other things, the statute of limitations and standing.

77. As stated above, on September 12, 2014, the Rating Agencies moved to dismiss the fraud claim on several grounds.

78. The Rating Agencies' statute-of-limitations defense was simple. Under New York law, the statute of limitations for a fraud claim is the greater of six years from the date the fraud claim accrued or two years from the date on which plaintiff could with reasonable diligence have discovered the fraud. The fraud claim was time-barred, they argued, because the Bear Stearns Funds commenced the action on July 9, 2013, (a) over six years after each of the dates on which the Master Funds purchased a security rated by the Rating Agencies, and (b) over two years after the Master Funds were on notice of the fraud, which occurred no later than mid-2008.

79. Reed Smith responded with an indisputably wrong interpretation of New York law.

80. First, Reed Smith argued that the claim did not accrue, and the six-year clock did not start, until the Bear Stearns Funds were on notice of the fraud—an odd position given that the statute explicitly establishes a *two-year* discovery rule. According

to Reed Smith, the Bear Stearns Funds could not have discovered the fraud until November 2007, when the Rating Agencies first downgraded securities that were at issue in the complaint. Therefore, the limitations period would not expire until November 2013.

81. Second, Reed Smith argued that the claim was timely under the "continuing wrong" doctrine, which provides that for certain ongoing wrongs, the statute of limitations will not run until the commission of the last wrongful act. Even though the last time the Bear Stearns Funds were fraudulently induced into buying the subprime securities was in May 2007, Reed Smith contended that the Rating Agencies engaged in a series of continuing misrepresentations and omissions through 2007 and into 2008.

82. The Rating Agencies also moved to dismiss on standing grounds. They argued that the Liquidators, as representatives of the Bear Stearns Funds' estates, could only assert claims that the Bear Stearns Funds could have brought prior to bankruptcy. Because the Master Funds purchased the securities that were knowingly mis-rated by the Rating Agencies, the Bear Stearns Funds only suffered harm derivatively as shareholders in the Master Funds. And Cayman law—which governed the issue of standing—prohibits shareholder derivative actions, subject to narrow exceptions that did not apply.

83. Reed Smith responded that the Bear Stearns Funds had direct standing because they indirectly relied on the credit ratings when they invested in the Master Funds, and alternatively, that the Bear Stearns Funds had standing to sue derivatively because they joined the Master Funds as nominal defendants. Of course, while Reed

Smith was responding to these arguments on standing, the Bear Stearns Funds were negotiating the Assignment.

2. The Trial Court granted the motion to dismiss, rebuking Reed Smith's misapplication of "clear" New York law.

84. On July 31, 2015, the Trial Court granted the Rating Agencies' motion to dismiss with prejudice. The Trial Court held that Bear Stearns Funds had sufficiently pleaded their fraud claim. However, in contrast to the advice Reed Smith provided to the Bear Stearns Funds, the Trial Court ruled that the claim was time-barred and that the Bear Stearns Funds lacked standing to sue directly or derivatively.

85. The Trial Court's opinion (the "**Dismissal Order**") illustrates that the law was clear and indisputable regarding limitations and standing, and that Reed Smith, by advising its client to pursue the fraud claim in June 2013, failed to exercise the degree of care, skill, and diligence commonly possessed and exercised by a member of the legal profession.

a. The Trial Court's opinion shows that Reed Smith's statute-of-limitations argument was blatantly wrong and to have worked, would have required a novel and expansive extension of existing law.

86. With respect to statute of limitations, the Trial Court stated: "***Clear authority*** expressly holds that the claim accrues on the date the plaintiff 'completed the act that the alleged fraudulent statements had induced'" (emphasis added). Because the Bear Stearns Funds acquired the securities at issue between February 7, 2006, and May 29, 2007, the July 9, 2013 complaint was "well outside" the six-year limitations window pursuant to unambiguous New York law.

87. The Dismissal Order shows that Reed Smith had no reasonable basis to advise or argue that the claim did not accrue until the plaintiffs were on notice of the fraud and could plead scienter. The Trial Court rejected that theory as no more than an "attempt to salvage [the] action" and observed that the "theory ***imbues the six-year statutory period with a degree of elasticity not reflected in any New York case law*** of which this court is aware. Plaintiffs have ***misapplied*** *Eisen* in an attempt to move the accrual of the statute of limitation beyond the date of the purchase of the securities" (emphasis added).

88. The Trial Court explained that the *Eisen* case Reed Smith cited to support its "discovery" trigger of the six-year statute of limitations, in fact, negated Reed Smith's argument. That case held that a fraud claim accrues from the date of injury, which, here, was when the Master Funds last purchased the securities. The Trial Court then cited additional appellate authority holding that a claim accrues at the time of purchase.

89. The Trial Court also pointed out that New York law explicitly provides for a *two-year* discovery rule, and that Reed Smith "conflated" that rule with the six-year statutory rule. The Trial Court stated what should have been obvious to Reed Smith or any other reasonably competent lawyer, that "questions about a plaintiff's knowledge or 'awareness' relate to the two-year prong of the statute of limitations, and not to the six-year statutory period." Indeed, the cases that Reed Smith cited to support its argument actually involved the application of the discovery rule, and thus the cases were germane to determining when the two-year—and not the six-year—clock began running. By Reed Smith's own admission, the Bear Stearns Funds could have truthfully alleged their claim

by October 2008; therefore, the fraud claim was still time-barred under the two-year discovery rule.

90. The Dismissal Order also shows that Reed Smith had no reasonable basis to advise or argue that the Rating Agencies' failure to update their ratings constituted a "continuing wrong" that tolled the limitations period for the fraud claim. The Trial Court referred to Reed Smith's argument as "***unpersuasive***" and called the doctrine "***inapposite*** in this case" (emphasis added).

91. The Trial Court called out Reed Smith for relying on cases that "do not implicate New York's six-year statute of limitations and can be otherwise differentiated from the instant action." Specifically, the court noted that the *Abu Dhabi* case cited by Reed Smith "[did] not advance Plaintiffs' position" because it did not involve a statute of limitations dispute, much less the continuing wrong doctrine, and involved a lawsuit filed well within six years from the date of the alleged wrongful act. Reed Smith's citation to *State v. 7040 Colonial Road Associates* was also misguided. Reed Smith "overlook[ed]" that the case concerned the New York Attorney General's exercise of a broad statutory mandate under the Martin Act—a concern that "[did] not comport with a private common-law fraud dispute."

92. The Trial Court further explained that the Rating Agencies' failure to update their ratings could only be considered a continuing wrong if the Rating Agencies owed the Bear Stearns Funds a duty, the necessary predicate for "omission" liability. Reed Smith did not allege that a duty was owed and thus the doctrine was "inapposite."

93. Moreover, the predicate of Reed Smith's continuing-wrong theory—that the Rating Agencies' inaction caused the Master Funds to hold, rather than sell, the securities—was fundamentally flawed. The Trial Court cited black-letter New York law stating that such "holder" claims are "not actionable" and are "too undeterminable and speculative to constitute a cognizable basis for damages." The Trial Court also noted that the claims were "belied by [Plaintiffs'] own arguments." The complaint did not allege that "inaction" caused the Bear Stearns Funds' losses; to the contrary, it alleged that their losses were caused by the Rating Agencies' issuance of high ratings, which were a substantial factor in the Master Funds' decisions to purchase the securities at issue.

b. The Dismissal Order shows that Reed Smith had no reasonable basis to assert its standing argument.

94. The issue of "standing" concerned whether the Bear Stearns Funds could bring claims against the Rating Agencies, given that the Master Funds (who had their own liquidators and were not plaintiffs to the action)—and not the Bear Stearns Funds—purchased the mis-rated securities. The Bear Stearns Funds were shareholders in the Master Funds, and the Master Funds invested in the securities.

95. The Trial Court ruled that the Bear Stearns Funds lacked standing to pursue the fraud claim.

96. First, the Trial Court rejected Reed Smith's argument that the Bear Stearns Funds had a direct claim—as opposed to a derivative claim—against the Rating Agencies. As an initial matter, Reed Smith neglected to realize that Cayman law applied to the question of whether the claim was direct or derivative. The Trial Court pointed out that,

under Cayman law, shareholders may not recover "reflective losses" that the company itself could recover if it chose to sue. Reed Smith did not even cite Cayman legal authority on the issue. The Trial Court did, however, including authority stating that "[w]here a company suffers loss caused by a breach of duty owed to it, only the company may sue in respect of that loss" and "[n]o action lies at the suit of a shareholder suing in that capacity."

97. Second, the Trial Court rejected Reed Smith's argument that the Bear Stearns Funds had standing to pursue a derivative action against the Rating Agencies. The court noted that Cayman law "prohibits shareholder derivative actions, subject to certain narrow exceptions not applicable here" (internal citations omitted). The Trial Court rejected Reed Smith's argument that the Master Funds, due to a cash shortfall, were "disabled" from bring the claim.

98. Notably, the Trial Court's reasoning mirrored the advice that Cayman counsel provided Reed Smith in 2011. Cayman counsel advised Reed Smith that, under Cayman law, shareholders did not have standing to bring direct claims to recover "reflective losses" that the company could recover if it pursued the action itself, and that shareholders generally lacked standing to assert derivative claims, subject to very narrow exceptions. Cayman counsel also advised that if a cash shortfall was preventing the Master Fund liquidators from pursuing the claim, then "one [could] explore funding the liquidators or 'buying' the claim."

99. Unfortunately for the Bear Stearns Funds, Reed Smith did not follow Cayman counsel's advice back in 2011. Instead, Reed Smith advised the Bear Stearns

Funds to pay millions of dollars pursuing litigation that was doomed from the start based on clear statute-of-limitations deficiencies.

c. The Dismissal Order shows that the fraud claim had merit apart from the limitations and standing problems

100. Although the Trial Court granted dismissal based on the statute of limitations and standing, its Dismissal Order nonetheless establishes that the claim would have been meritorious had it been timely brought with an assignment from the Master Funds.

101. The Trial Court rejected the arguments in the Rating Agencies' motion to dismiss relating to the substance of the fraud claim and found that the Bear Stearns Funds adequately pleaded falsity, scienter, reliance, and loss causation. Specifically, the Trial Court found that the Bear Stearns Funds sufficiently pleaded that: the Rating Agencies made "actionable misrepresentations"; the Rating Agencies' companywide abandonment of rating policies was sufficient to infer scienter; the Master Funds relied on the Rating Agencies' misrepresentations; and that the Rating Agencies' misrepresentations caused the Bear Stearns Funds' losses.

102. The Trial Court also rejected the Rating Agencies' additional defenses under the doctrines of judicial estoppel and *in pari delicto*.

3. Reed Smith advised the Bear Stearns Funds to continue pursuing their unsalvageable claim by filing a renewal motion.

103. Notwithstanding the predictable dismissal of the complaint based on established legal rules that should have been well known to Reed Smith, the firm advised

the Bear Stearns Funds to continue to fund the case by filing a Motion for Renewal and for Leave to File an Amended Complaint ("**Renewal Motion**").

104. On August 26, 2015, the Liquidators convened a meeting of the Bear Stearns Funds' Liquidation Committees (the successors to the Advisory Committee), so that Reed Smith could provide an update on the Rating Agencies litigation.

105. After explaining the Trial Court's holdings, McCarroll advised that the Liquidators file either a Renewal Motion or a motion for leave to file an amended complaint, based on "new facts" that arose after briefing the motion to dismiss. McCarroll further advised that the Renewal Motion would give the judge an "opportunity to re-consider his decision based on facts he may have previously failed to consider"—even though Renewal Motions are only permitted based on new facts or some other reasonable justification.

106. Despite noting that Renewal Motions are not routinely granted, McCarroll advised that "***Reed Smith remains positive about a favourable outcome***" because of its review of existing case law and its discovery of new facts. Reed Smith did not intend to change its theory regarding statute of limitations, but instead would "reiterate" its argument that the statutory clock restarted each time a credit rating was reaffirmed. In other words, Reed Smith advised the Bear Stearns Funds that it believed its theory—rejected once—would prevail a second time around.

107. The Bear Stearns Funds followed Reed Smith's advice and filed the Renewal Motion on September 9, 2015. The "new facts" regarding the statute of limitations consisted of evidence that, as late as February 28, 2008, the Rating Agencies

had expressly affirmed their prior ratings. Reed Smith used that evidence to reassert its "continuing wrong" theory by arguing that, but for these continued affirmative misrepresentations, the Bear Stearns Funds would have sold (*i.e.*, would not have "held") the securities. Reed Smith cited case law from the 1920s to support the validity of its theory.

108. At this point, there was no reasonable basis for Reed Smith to expect that the "new facts" would lead to a different result, given that Reed Smith was marshalling these facts in support of the identical theory that: (1) the Trial Court had already rejected, and (2) was not supported by clear New York law. Unsurprisingly, the Trial Court again ruled that such "holder" claims are "non-actionable" and "not recognized by New York Courts." The court denied the portion of the Renewal Motion seeking to amend the complaint based on the new facts as "***palpably insufficient and patently devoid of merit***."

109. With respect to standing, Reed Smith submitted new evidence that the Master Funds assigned their claims to the Liquidators in May 2015—after the Liquidators submitted their opposition to the motion to dismiss, but before the Trial Court issued its dismissal order.

110. Nonetheless, under established New York law, the assignment was futile because, as the Trial Court put it, "the Master Funds simply assigned a time barred claim." Even if the claim was tolled until February 2008, as Reed Smith unsuccessfully argued, the claim still would have been untimely in May 2015 when the Liquidators received the assignment. Reed Smith's actions put the Liquidators in a "catch 22," because "they did not have standing for the fraud claim prior to the assignment nor can the

assignment relate back to the commencement of this action to be timely." Accordingly, the Trial Court found Reed Smith's standing argument "***palpably insufficient and patently devoid of merit***."

111. In sum, the Renewal Motion lacked merit and was nothing more than a waste of time and resources. The Renewal Motion was frivolous because the "new facts" were clearly irrelevant to the Trial Court's statute-of-limitations analysis and prior holding that the claim was time-barred. Likewise, the May 2015 assignment of the Master Funds' claims was pointless because it occurred at a point in time when the statute of limitations had already expired.[6]

G. Reed Smith unsuccessfully appealed the Trial Court's rulings.

112. Although Reed Smith was clearly wrong on the law, it advised the Bear Stearns Funds to continue to pursue the action while racking up hundreds of thousands of dollars in additional fees litigating the appeal. Had Reed Smith advised the Bear Stearns Funds that an appeal had little to no chance of succeeding, the Bear Stearns Funds would not have expended further money on the case. Reed Smith, however, did not provide the Bear Stearns Funds with an honest assessment of the appeal's prospects.

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[6] Rather than amending the complaint to assert the assigned claim, Reed Smith should have moved to align the Master Funds as nominal plaintiffs in the action and/or filed a motion to substitute the Master Funds as plaintiffs. The Master Funds were the party-in-interest and New York courts have permitted corporations that are originally named as nominal defendants to take over derivative actions when there is no dispute that the corporations will faithfully prosecute them. In other words, had Reed Smith filed the summons and notice prior to expiration of the statute of limitations, there were steps that Bear Stearns Funds could have taken to keep the action timely even if the assignment of the claim occurred post-filing. The Cayman Court even inquired about similar options back in 2013, but Reed Smith negligently advised against these options.

113. Reed Smith filed a notice of appeal with the New York Appellate Division on February 11, 2016. Reed Smith then prepared a detailed memorandum to the "file" regarding the merits of the appeal. In this April 2016 memorandum, Reed Smith recognized that its prior arguments on limitations and standing were essentially meritless.

114. Specifically, in the memorandum, Reed Smith "analyze[d] whether to raise on appeal" the arguments "made in the trial court." Through a detailed analysis of case law, Reed Smith concluded that its prior arguments—including, notably, its argument that the statute of limitations was tolled under the continuing-wrong doctrine—were so meritless that Reed Smith would lose credibility with the appellate court if continued to advance them on appeal. Reed Smith thus concluded that the following arguments, among others, should *not* be made on appeal: (1) "Plaintiffs' claims are timely under the 'continuing wrong' doctrine"; and (2) the Bear Stearns Funds "have standing to assert a direct claim against the Rating Agencies."

115. Accordingly, on appeal, Reed Smith finally abandoned these arguments. With respect to limitations, instead of arguing tolling under the continuing-wrong doctrine, Reed Smith simply argued that the Bear Stearns Funds' claims did not accrue until they suffered their losses. Reed Smith claimed that the losses were suffered in July 2007 on the securities that the Master Funds still held at that time. This limitations argument was not only meritless, it significantly reduced the potential damages in the case because the Master Funds had sold the majority of the fraudulently rated securities prior to July 2007.

116. On May 31, 2016, Reed Smith filed its appellate brief on behalf of the Bear Stearns Funds.

117. On February 10, 2017, the appeals court unanimously affirmed the Trial Court's decision, holding that: the claims were time-barred because they were brought more than six years after the last purchase of the securities, which was when the Bear Stearns Funds sustained their injury; the Bear Stearns Funds' holder claims—to the extent they alleged any—were not actionable; and the Bear Stearns Funds lacked standing under Cayman law to sue derivatively.

118. Reed Smith made its last effort to resuscitate the claim by filing a motion for leave to appeal to the New York Court of Appeals on March 10, 2017. The Court of Appeals declined to accept the appeal on July 17, 2017.

H. While the Bear Stearns Funds suffered significant damages, Reed Smith enriched itself at their expense.

1. The Bear Stearns Funds lost a claim for at least hundreds of millions of dollars in damages.

119. The Master Funds suffered in excess of a billion dollars in losses on their investments in fraudulently-rated securities.

120. The Bear Stearns Funds, as assignees of the Master Funds' claim against the Rating Agencies, had a compelling case against the Rating Agencies.

121. Reed Smith, and McCarroll in particular, repeatedly emphasized the strength of the case to the Liquidators, the Advisory Committee / Liquidation Committees, and the Cayman Court. For instance, as described above, McCarroll told the Bear Stearns Funds that the value of the claim was between $850 million and $1.1 billion;

that Reed Smith was "highly optimistic" that the claim would defeat a motion to dismiss and result in extensive disclosure from the Rating Agencies; and that Reed Smith was "confident" of appropriate treatment of the case by the New York court. And McCarroll swore to the Cayman Court that the Bear Stearns Funds had "meritorious claims for fraud," which were "based upon compelling evidence of fraud and related misconduct by the rating agencies." According to McCarroll, Reed Smith believed that the recoveries from the Rating Agencies litigation would be "at least in the range of, and might well exceed" $250 million.

122. Notably, even prior to the filing of Bear Stearns Funds' complaint, courts had denied motions for summary judgment by the Rating Agencies in similar fraud cases. Specifically, in the *Abu Dhabi* case, the U.S. District Court for the Southern District of New York denied, in an August 17, 2012 opinion, motions for summary judgment filed by the Rating Agencies. The district court concluded that there was more than sufficient evidence of fraud for the case to proceed to trial. In doing so, the court rejected the same defenses that the Bear Stearns Funds would have faced if their claim had not been time-barred by ruling that: ratings "opinions" may serve as the basis for a fraud claim; plaintiffs offered sufficient evidence that the ratings were misleading and disbelieved by the Rating Agencies; and plaintiffs presented sufficient evidence of scienter, reliance, and loss causation. The Ratings Agencies subsequently settled with the plaintiffs in the *Abu Dhabi* case in 2013 for an undisclosed amount.

123. Other claims also proceeded to the summary-judgment stage. For instance, on November 13, 2014, the Federal Home Loan Bank of Pittsburgh, which timely filed a

complaint against the Rating Agencies, submitted an opposition to a motion to dismiss in its case. In its 141-page opposition, the Federal Home Loan Bank of Pittsburgh detailed the Rating Agencies' fraudulent representations and buttressed the evidence of fraud with expert analysis. Similar to the *Abu Dhabi* case, the Rating Agencies settled shortly after briefing was completed on the summary-judgment motions. Based on available information, the Ratings Agencies paid more than 10% of the alleged damages in that case to settle the action.

124. In another case, the California Public Employees' Retirement System ("**CalPERS**") filed a lawsuit in July 2009 against the Rating Agencies for over a billion dollars in losses. And, after CalPERS defeated an Anti-SLAPP-suit motion, which required that CalPERS marshal all of its evidence supporting its claims against the Rating Agencies, the Rating Agencies settled for $255 million.

125. In addition, in early 2015, the DOJ and other state agencies ultimately settled their claims against Standard & Poor's ("**S&P**") for over $1.3 billion. As part of its settlement with the DOJ, S&P admitted that its decisions on its rating models were affected by business concerns, and that it maintained and continued to issue positive ratings on securities despite a growing awareness of quality problems with those securities. Specifically, S&P admitted, among other things, that in early 2007 it failed to follow the recommendations of its RMBS Surveillance Group to place numerous tranches of securities under credit watch based on serious market concerns. Evidence showed that S&P executives prevented the Surveillance Group from downgrading subprime RMBS "because of concern that S&P's rating business would be negatively affected."

126. And, in early 2017, the DOJ and several states reached a settlement with Moody's. Moody's admitted as part of its settlement with the DOJ that: potential conflicts of interest existed in Moody's business model, which were passed on to its managing directors to solve; Moody's used tranching tools that it knew were not correct and resulted in faulty ratings; and Moody's did not follow its own targets in rating many tranches of CDOs thus allowing for more competitive ratings.

127. In their case against the Rating Agencies, the Bear Stearns Funds had substantial and compelling evidence of the Rating Agencies' fraud, which would have allowed them to succeed at trial but for Reed Smith's negligence. Even without completing discovery, the Bear Stearns Funds were able to present strong evidence of each element of their fraud claim: (i) a misrepresentation of material fact; (ii) falsity; (iii) scienter; (iv) reasonable reliance; and (v) injury resulting from the reliance.

128. The evidence cited in the Bear Stearns Funds' complaint and motion-to-dismiss briefing is incredible. For instance, the Bear Stearns Funds presented evidence in their 141-page Complaint that: an S&P analyst sent a text message to a co-worker that "it could be structured by cows and we would rate it" and that "[our] model def[initely] does not capture half of the ris[k]"; an S&P executive wrote "Lord help our f[***]ing scam . . . this has to be the stupidest place I have worked at" and expressed concern that he was "going to jail soon"; an S&P analytical manager wrote in an e-mail that the Rating Agencies continue to create an "even bigger monster—the CDO market. Let's hope we are all wealthy and retired by the time this house of cards falters"; a managing director of S&P's CDO group admitted "I knew it was wrong at the time" and "It was either that

or skip the business. That wasn't my mandate. My mandate was to find a way"; a Moody's employee admitted in an internal document that "we sold our soul to the devil for revenue"; Moody's co-director of CDO ratings warned "don't kill the golden goose"; and a former Moody's managing director of credit policy admitted that "[t]he recent failure of rating agencies to signal in a timely and accurate fashion the condition of many securities backed by subprime housing loans can be traced to weaknesses (or outright failures) in the protections against conflict of interest."

129. As described above, the Trial Court found that the Bear Stearns Funds sufficiently pleaded that the Rating Agencies made "actionable misrepresentations"; the Rating Agencies' abandonment of rating policies was sufficient to infer scienter; the Master Funds relied on the Rating Agencies' misrepresentations; and that the Rating Agencies' misrepresentations caused Funds' losses. Given the strength of the evidence supporting those allegations, the Bear Stearns Funds also would have succeeded against a motion for summary judgment and, ultimately, at trial.

130. Not only could and would have the Bear Stearns Funds obtained a substantial judgment on their claim against the Rating Agencies, the claim also had significant settlement value. As a practical matter, given the strength of the Bear Stearns Funds' claim, the Rating Agencies would have settled with the Bear Stearns Funds at some point prior to trial, just as they did in other similar, high-dollar cases against them. But because of Reed Smith's negligence, the Bear Stearns Funds lost the prospect of settlement and the settlement value of their claims, which, by Reed Smith's own

admission, was in the range of at least $250 million (had Reed Smith not blown limitations and failed to timely provide the correct advice with respect to the standing issues).

2. Reed Smith, while breaching its fiduciary duties, collected tens of millions of dollars in fees and even demanded that the Bear Stearns Funds pay an exorbitant late-payment penalty.

131. Reed Smith collected over $5 million (being over $10 million of time at full hourly rates) to litigate the case through the motion-to-dismiss hearing. Even after the Trial Court presented Reed Smith with clear legal authority that the claim was time-barred and lacked standing, Reed Smith continued to advise the Bear Stearns Funds to keep spending money to fight the issue. After the ruling, Reed Smith charged and collected roughly $1 million (or $2 million of time at full hourly rates), again, with no results. Specifically, Reed Smith charged and collected over $300,000 litigating the Renewal Motion, and nearly $600,000 litigating the appeal. In total, Reed Smith charged and collected from the Bear Stearns Funds $6,074,251.73 in legal fees (and billed twice that) to pursue the litigation. In other words, ***Reed Smith billed over $12 million simply to lose a motion to dismiss***.

132. Between July 2013 and July 2017, Reed Smith also received tens of millions of dollars in hourly and contingency fees in connection with its overall representation of the Bear Stearns Funds pursuant to the Engagement Letters.

133. Reed Smith collected these fees from the Bear Stearns Funds at the same time as it was breaching it fiduciary duties. As described above, after Reed Smith grossly miscalculated the statute of limitations on the fraud claim, it ultimately realized its mistake. But, rather than admitting to its error and providing the Bear Stearns Funds with

an honest assessment of the statute-of-limitations issues, Reed Smith concealed the truth from the Bear Stearns Funds. Reed Smith, among other things, represented to them that the statute of limitations was "not a substantial concern" when it had to have known otherwise. It further advised the Bear Stearns Funds to file an essentially frivolous Renewal Motion notwithstanding the clear law demonstrating that the claim was untimely.

134. Reed Smith owed the Bear Stearns Funds an absolute duty of loyalty, which included a duty of candor. Because Reed Smith breached its fiduciary duties and concealed its malpractice from the Bear Stearns Funds, it would be inequitable to permit Reed Smith to keep the tens of millions of dollars it received from the representation while it was breaching its fiduciary duties.

135. In fact, Reed Smith's inequitable conduct goes beyond its failure to disclose its malpractice and the related negligent, if not intentional, misrepresentations it made to its clients and the Cayman Court.

136. For instance, Reed Smith avoided addressing questions by the Bear Stearns Funds regarding a certain litigation target. Only after the Bear Stearns Funds pressed Reed Smith to pursue the claim did Reed Smith acknowledge that it was conflicted. The Bear Stearns Funds then retained separate counsel and settled the claim for a significant sum.

137. Despite Reed Smith raising its conflict as the reason why it could not pursue the action, McCarroll still insisted that the firm be paid its 12.5% contingency fee on the settlement even though Reed Smith had little to no involvement in the lawsuit.

Irrespective of whether Reed Smith had a technical, legal argument that it was entitled to a contingency fee on a case it did not work on, Reed Smith's conduct evinced an utter disregard for the fiduciary standards that the firm should have upheld.

138. Then, even more egregiously, Reed Smith demanded that the Bear Stearns Funds pay Reed Smith an exorbitant penalty of ***more than $10.3 million*** simply because the Bear Stearns Funds paid a few Reed Smith invoices a couple of weeks late.[7]

139. Specifically, during the unsuccessful Ratings Agencies case, the Bear Stearns Funds paid two sets of Reed Smith's invoices a few weeks late. Reed Smith, seeing an avenue to extract further money from the Bear Stearns Funds, claimed that those delayed payments on invoices totaling $479,424 entitled Reed Smith to a windfall interest payment of more than $10.3 million. Reed Smith arrived at this exorbitant interest sum through a convoluted, and legally indefensible, interpretation of the Engagement Letters.

140. The Bear Stearns Funds refused to pay Reed Smith any late-payment penalty, much less the $10.3 million demanded by Reed Smith. Reed Smith, nevertheless, persisted. Notwithstanding New York's Rules of Professional Conduct—including Rule 1.5, which provides, in pertinent part, that a "lawyer shall not make an agreement for, charge, or collect an excessive or illegal fee or expense"—McCarroll and Reed Smith sent

[7] Reed Smith even threatened to sue the Bear Stearns Funds in the Cayman Islands. Because Reed Smith, unlike the Bear Stearns Funds, agreed that the Cayman Islands had the exclusive jurisdiction to decide disputes concerning the representation, to the extent that Reed Smith still wants to pursue its frivolous claim, Reed Smith must file its claim in the Cayman Islands.

multiple emails to the Bear Stearns Funds demanding payment of the excessive fee.[8] Reed Smith's unconscionable demand that the Bear Stearns Funds pay an ***effective interest rate of over 2000%*** is but further evidence that Reed Smith had completely abandoned its fiduciary duties to its clients.

3. The Bear Stearns Funds also incurred millions of dollars in additional costs.

141. Reed Smith's advice to pursue a fraud claim against the Rating Agencies after the statute of limitations expired on May 27, 2013, came at a great price to the Bear Stearns Funds' estates.

142. In addition to Reed Smith's fees (described above), the pursuit of the stale fraud claim required substantial time and resources from the Liquidators and their staff, who had to spend hundreds of hours corresponding with their counsel, preparing documents for discovery, communicating with investors about the claims, and reviewing court documents, among other things. In total, the Liquidators' work related to the Rating Agencies litigation—which would not have been undertaken had they received competent advice from Reed Smith—cost the Bear Stearns Funds' estate $213,932.50.

143. Moreover, Reed Smith's negligent advice caused the Liquidators to hire experts and consultants to pursue the litigation, which came at an additional expense to the Bear Stearns Funds.

[8] Rule 1.5 applies not only to fees but also to interest and related charges. For instance, New York City Bar Opinion 2002-2 states: "Though interest is not part of the fee, but rather compensation for delay in payment of the fee, the rate of interest should be subject to the same reasonableness requirement."

144. In connection with the Renewal Motion, Reed Smith's advice to obtain an assignment of claims from the Master Funds also caused the Bear Stearns Funds to sustain substantial damages. The assignment was worthless, because the claim was already time-barred. But Reed Smith's advice caused the Bear Stearns Funds to purchase the assignment for $500,000 and incur a further $127,996 of additional costs in relation to the assignment.

145. In sum, Reed Smith never should have advised the Liquidators to pursue the claim, which under the applicable law, clearly and indisputably was time-barred. Beyond that, Reed Smith was wholly unreasonable in charging extraordinary amounts, billing hundreds of hours per month, and over $12 million in total, to do nothing more than lose a motion to dismiss.

146. Had the Bear Stearns Funds been advised by counsel that knew the law and exercised the degree of care, skill, and diligence commonly possessed by a member of the legal profession, they would not have pursued the litigation when they did, and they would not have wasted millions of dollars in unnecessary fees and costs.

I. Reed Smith negligently failed to advise the Bear Stearns Funds regarding claims against underwriter banks prior to the expiration of the statute of limitations.

147. Starting in 2011, Reed Smith began investigating potential claims that could be pursued against various parties involved with the sale of securities to the Bear Stearns Funds, including the underwriters of those securities ("**Underwriters**"). In fact, from May 2011 to December 2011, Reed Smith attorneys spent a considerable amount of time

analyzing potential Underwriter claims, billing the Bear Stearns Funds tens of thousands of dollars in the process.

148. Gray led the initial investigation into claims against the Underwriters. His analysis (and the analysis of other Reed Smith attorneys) included: "review[ing] recent press articles concerning lawsuits brought seeking damages in connection with mortgage-backed securities"; "research[ing] the law regarding actions asserted against banks, issuers, depositors, etc."; "research[ing] the law re lawsuits asserted against . . . issuers or underwriters"; and "research[ing] the law regarding cases alleging securities fraud in the context of credit crisis/subprime meltdown."

149. Reed Smith's preliminary analysis regarding claims against the Underwriters was ultimately included in the same 2011 memorandum that summarized claims against the Rating Agencies, described above. As with the claims against Rating Agencies, Reed Smith recognized that the Bear Stearns Funds could seek to buy the Underwriter claims from the Master Funds as a way around the standing issues identified in the memorandum. Reed Smith noted in its discussion of the investigation of the claims for the Bear Stearns Funds that "we will need to investigate—with respect to each security *owned by the Master Fund's* [sic] portfolio for which damages are sought."

150. Reed Smith concluded its 46-page internal memorandum by recommending a fact investigation to assess the viability of "asserting claims for fraud, negligent misrepresentation, breach of contract, breach of fiduciary duty, and aiding and abetting against the underwriters of each offering for which damages are sought." Again, Reed Smith inexplicably never shared this memorandum or the underlying analysis with

the Bear Stearns Funds and never advised the Bear Stearns Funds about the potential Underwriter claims.

151. Critically, had Reed Smith advised the Bear Stearns Funds about the potential Underwriter claims, the Bear Stearns Funds would have requested that Reed Smith further analyze the claims and immediately start the process of requesting an assignment of the claims from the Master Funds.

152. Had Reed Smith continued its analysis of Underwriter claims in 2011 and early 2012, it would have found more than ample evidence to draft compelling fraud claims against various Underwriters. As Reed Smith observed in its 2011 memorandum, "there have been countless lawsuits seeking to hold liable the parties that structured and sold the various products that plunged in value during the subprime meltdown and credit crisis." Had Reed Smith investigated the specific securities held by the Master Funds, it would have discovered that those holdings included some of the most egregiously toxic products unloaded onto the marketplace by Wall Street banks during the financial crisis.

153. For example, the Master Funds invested in a CDO-squared called Class V Funding III that was structured and marketed by Citigroup Global Markets Inc. ("**Citigroup**"). On October 19, 2011, the S.E.C. filed a complaint against Citigroup for its role, alleging that Citigroup has disseminated "materially misleading" marketing materials to investors in Class V Funding III that failed to disclose Citigroup's significant influence in selecting the underlying assets, or Citigroup's short position on those very same assets that enabled the bank to profit from their poor performance. As a result of

the S.E.C.'s action, Citigroup was ultimately ordered to pay $285 million in disgorgement, prejudgment interest, and penalties.

154. Similarly, the Master Funds invested in Octans II CDO, a deal arranged by Wachovia that was among the securities implicated in a fraudulent scheme—detailed at length in reports issued in early 2011 by the U.S. Senate and the Financial Crisis Inquiry Commission—that was engineered by Wall Street banks, the collateral manager Harding Advisory LLC ("**Harding**"), and a hedge fund called Magnetar Capital LLC ("**Magnetar**"). As described in a complaint filed by other Octans II investors in April 2012 against Wachovia's successor-in-interest Wells Fargo, Wachovia and Harding permitted Magnetar to "control structural features" of the security and exercise "veto power" over the assets selected for the CDO's collateral pool. This arrangement allowed Magnetar to profit from its massive short positions on those toxic assets. For its part in enabling this fraudulent scheme, Wachovia reaped millions in fees generated in connection with Octans II and other Magnetar-influenced deals. The Master Funds invested in another CDO deal for which Harding served as collateral manager called Lexington Capital Funding III, that was arranged by Merrill Lynch & Co. ("**Merrill**"). Merrill was implicated alongside Citigroup for participating in Magnetar's fraudulent scheme. Other investors have alleged that Harding was completely beholden to Merrill due to the substantial fees Harding received for managing Merrill's CDOs.

155. The Master Funds were also investors in a hybrid CDO called Timberwolf I that was structured and marketed by Goldman Sachs & Co. ("**Goldman**"). The particulars of the Timberwolf I transaction were described at length in the Senate's April

13, 2011 report on Wall Street and the financial crisis. The Timberwolf I CDO and similar deals engineered by Goldman in 2007 served dual purposes: first, to enable Goldman to offload the most toxic and risky assets held on its books, and second, to allow Goldman to profit from the substantial short positions it took on the very products it was peddling to investors like the Bear Stearns Funds. As quoted in the Senate report, a senior Goldman executive sent an email to the head of Goldman's mortgage department in June 2007 that described Timberwolf I as "one shitty deal." Goldman nonetheless continued to market the deal and offered massive incentives to its sales staff for unloading the security on unsuspecting investors. The assets backing Timberwolf I were so toxic that while Goldman slashed its internal marks reflecting their diminished value, its sales staff continued to sell Timberwolf I at much higher prices than Goldman knew it was worth. Goldman personnel were instructed not to provide any written information to investors regarding how Goldman was valuing or pricing Timberwolf I. Upon learning in September 2007 that Timberwolf I had already lost 80% of its value, Goldman's "deal captain" for Timberwolf I internally characterized the issuance of the security as "a day that will live in infamy." By June 2010, other investors in Timberwolf I filed a $1 billion suit against Goldman alleging fraud in connection with its role in structuring and marketing the security. Goldman resolved that lawsuit in June 2016 by agreeing to a confidential settlement.

156. At bottom, Reed Smith knew back in 2011 that the Master Funds had strong claims against the Underwriters. Reed Smith owed the Bear Stearns Funds a duty to advise them of these potential claims so that the Bear Stearns Funds could take

appropriate actions to pursue the claims and recover their losses that flowed directly from the losses suffered by the Master Funds. But, Reed Smith's disclosure failures did not end there. Reed Smith also did not disclose to the Bear Stearns Funds that it had actually defended the investment banks against the same types of RMBS claims the Bear Stearns Funds could have asserted, much less that Reed Smith was defending those banks ***at the same time*** Reed Smith was analyzing the Underwriter claims for the Bear Stearns Funds.

157. Had Reed Smith advised the Bear Stearns Funds back in 2011 regarding the existence of these claims against the Underwriters, the Bear Stearns Funds could and would have received an assignment from the Master Funds by early 2012 and filed the assigned claims shortly thereafter. Even if Reed Smith had been conflicted as a result of its defense of the investment banks in RMBS litigation, the Bear Stearns Funds could and would have found alternative counsel to bring those claims.

158. Reed Smith, however, failed to advise the Bear Stearns Funds of the Underwriter claims. As a result, the Bear Stearns Funds did not bring the claims, and limitations lapsed on those claims at the same time limitations lapsed on the Rating Agencies claims. Thus, Reed Smith's negligence caused the Bear Stearns Funds to lose hundreds of millions of dollars of claims against the Underwriters.

IV. CAUSES OF ACTION

Count I: Legal Malpractice / Professional Negligence

159. Plaintiffs repeat and re-allege the allegations set forth above.

160. Reed Smith had an attorney–client relationship with the Bear Stearns Funds.

161. As counsel to the Bear Stearns Funds, Reed Smith owed them a duty to exercise reasonable and professional care consistent with the standard of care that is expected to be exercised by a reasonably prudent attorney in providing legal services. Reed Smith, among other things, owed the Bear Stearns Funds a duty to keep them well informed and furnish them with all information material to the representation.

162. Reed Smith, however, failed to exercise reasonable and professional care in providing legal services to the Bear Stearns Funds.

163. Reed Smith negligently or willfully withheld information from the Bear Stearns Funds. Specifically, as further set forth above, in 2011, Reed Smith, among other things: (a) failed to advise the Bear Stearns Funds about the claims against the Rating Agencies; (b) failed to advise the Bear Stearns Funds about the claims against the Underwriters; and (c) failed to advise the Bear Stearns Funds how to acquire the Rating Agencies and Underwriter claims from the Master Funds through an assignment or otherwise to ensure that the Bear Stearns Funds had standing to bring the claims prior to the expiration of the statute of limitations.

164. Reed Smith also failed to understand New York's statute of limitations and, as such, did not correctly advise the Bear Stearns Funds as to when the statute of limitations expired on the claims against the Rating Agencies and Underwriters.

165. But for Reed Smith's negligence, the Bear Stearns Funds could and would have received an assignment of the claims back in early 2012 and filed an action against

the Rating Agencies and Underwriters well prior to the expiration of the statute of limitations.

166. But for Reed Smith's negligence, the Bear Stearns Funds could and would have succeeded on their claims against the Rating Agencies and Underwriters and received a substantial judgment for at least hundreds of millions of dollars.

167. Moreover, but for Reed Smith's negligent advice to pursue a time-barred claim, the Bear Stearns Funds would have saved millions of dollars in fees and costs.

168. Accordingly, as a direct and proximate result of Reed Smith's professional negligence, the Bear Stearns Funds suffered considerable damages in an exact amount to be proven at trial.

Count II: Breach of Fiduciary Duty

169. Plaintiffs repeats and re-allege the allegations set forth above.

170. The Bear Stearns Funds engaged Reed Smith as their counsel. As such, Reed Smith owed them the fiduciary duties of care, obedience, loyalty, candor, and communication.

171. Reed Smith breached its fiduciary duties by failing to advise the Bear Stearns Funds that, because of Reed Smith's mistakes, the lawsuit against the Rating Agencies was untimely. More specifically, Reed Smith never honestly communicated to the Bear Stearns Funds that absent a highly unlikely extension of existing law, the Bear Stearns Funds lacked an argument for the "tolling" of the statute of limitations.

172. In failing to provide its clients with an honest assessment of the case and, instead, affirmatively misleading them as to the merits of the claim, Reed Smith

subverted the attorney–client relationship in such a manner that the Bear Stearns Funds' interests were subordinated to those of Reed Smith.

173. Reed Smith further breached its fiduciary duties by charging the Bear Stearns Funds excessive fees by billing for unnecessary and repetitive work. Indeed, Reed Smith did nothing more than litigate the case through a motion to dismiss (which it lost), yet still managed to bill its client over $12 million (and collect 50% of that pursuant to the engagement terms). Reed Smith advised the Bear Stearns Funds to continue spending money on the claim, even after the Trial Court granted dismissal with prejudice, so that Reed Smith could continue to bill the funds and collect millions of dollars in the process.

174. In excessively billing its clients (and demanding that the Bear Stearns Funds pay an unconscionable fee of more than $10.3 million on a set of late invoices), Reed Smith subverted the attorney–client relationship in such a manner that the Bear Stearns Funds' interests were subordinated to those of Reed Smith.

175. As a result of Reed Smith's breaches of fiduciary duty and corresponding subversion of the attorney–client relationship in such a manner that the Bear Stearns Funds' interests were subordinated to those of Reed Smith, the Bear Stearns Funds are entitled to the remedy of fee forfeiture pursuant to which Reed Smith must disgorge all professional fees received from, or on behalf of, the Bear Stearns Funds during the period of disloyalty.

Count III: Breach of Contract
(Under the law of the Cayman Islands)

176. Plaintiffs repeat and re-allege the allegations set forth above.

177. The Bear Stearns Funds engaged Reed Smith pursuant to the Engagement Letters. On October 25, 2013, the parties amended the Engagement Letters to provide, among other things, that they are governed by the law of the Cayman Islands. Specifically, in a letter to the Liquidators, Reed Smith acknowledged the applicability of Order 25, Rule 1, of the Cayman Islands' Winding-Up Rules to its "ongoing engagement."

178. Reed Smith acknowledged the application of Order 25, Rule 1 of the Cayman Winding-Up Rules because this rule required contracts between liquidators and their counsel to be governed by Cayman law.

179. As set forth in the Engagement Letters, and pursuant to Cayman law, Reed Smith owed various contractual duties to the Bear Stearns Funds, including the implied duty to: (a) carry out the tasks which the Bear Stearns Funds instructed and Reed Smith agreed to undertake; (b) proffer advice to the Bear Stearns Funds that is reasonably incidental to the work being carried out; and (c) carry out its work with the skill and care which a normally competent practitioner would bring to it.

180. Furthermore, pursuant to the Engagement Letters and Cayman law, the standard of care that Reed Smith owed under its contractual duties was that of a reasonably competent attorney having regard to the standards normally adopted in the profession.

181. Reed Smith breached its contractual duties to the Bear Stearns Funds. Specifically, as further set forth herein, Reed Smith, among other things: (a) failed to advise the Bear Stearns Funds about the claims against the Rating Agencies prior the expiration of the statute of limitations; (b) failed to advise the Bear Stearns Funds about

the claims against the Underwriters; and (c) failed to advise the Bear Stearns Funds how to acquire the Rating Agencies and Underwriter claims from the Master Funds through an assignment or otherwise to ensure that the Bear Stearns Funds had standing to bring the claims prior to the expiration of the statute of limitations

182. The elements of a claim under Cayman law against an attorney for breach of his or her contractual duties are distinct from the elements of a professional-negligence claim under New York law. Specifically, the damages and causation elements of such a claim are different.

183. Under Cayman law, a client is entitled to recover damages on a "loss of chance" basis for the lost opportunity to recover in legal proceedings. A "loss of chance" damage measure includes the lost value of a claim based on the lost value of a reasonable settlement in the underlying lawsuit where settlement was more likely than the claim proceeding to a money judgment for damages following trial.

184. Reed Smith's negligence resulted in a situation in which the Bear Stearns Funds were not even able to negotiate a settlement of their claim—something that the Rating Agencies and Underwriters did in virtually all other similar cases filed against them. Had the Bear Stearns Funds, as assignees of the Master Funds' claim, filed a timely fraud case against the Rating Agencies and Underwriters, they could and would have had the opportunity to settle those claims for hundreds of millions of dollars. In fact, as Reed Smith even acknowledged, the lost settlement value on just the claim against the Rating Agencies was at least $250 million.

185. Reed Smith's breaches of the contractual duties it owed to the Bear Stearns Funds were the factual and legal cause of the Bear Stearns Funds not filing the timely claim they would have filed had they received competent advice and representation from Reed Smith, consistent with Reed Smith's contractual duties. As a result of Reed Smith's breaches, the Bear Stearns Funds lost the value of their claims against the Rating Agencies and Underwriters and suffered such damages in an amount to be proven at trial.

V. DEMAND FOR JURY

Plaintiffs demand a jury trial on all issues.

VI. RELIEF REQUESTED

WHEREFORE, Plaintiffs respectfully requests that a judgment be entered on Plaintiffs' behalf against Reed Smith for the following:

(a) actual, compensatory, consequential, and all other damages and equitable remedies in an amount to be determined at trial, but well in excess of $500 million;

(b) disgorgement of fees paid to Reed Smith;

(c) pre-judgment and post-judgment interest at the highest rates allowed by law;

(d) attorneys' fees; and

(e) any and all such further relief to which Plaintiffs are entitled at law and in equity.

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Index No. 656378/2018

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

BEAR STEARNS HIGH-GRADE STRUCTURED CREDIT STRATEGIES ENHANCED LEVERAGE (OVERSEAS) LTD. AND BEAR STEARNS HIGH-GRADE STRUCTURED CREDIT STRATEGIES (OVERSEAS) LTD. (BOTH IN OFFICIAL LIQUIDATION),

Plaintiffs,

-against-

REED SMITH LLP,

Defendant.

COMPLAINT

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