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UNITED STATES DISTRICT COURT
DISTRICT OF NEVADA

█ Individually, and On
Behalf of All Others Similarly Situated,

Plaintiff,

v.

GOLDMAN SACHS GROUP, INC.,
GOLDMAN, SACHS & CO. and HENRY M.
PAULSON

Defendants.

Case No.

CLASS ACTION COMPLAINT—SECURITIES
FOR BREACH OF FIDUCIARY DUTY
AND VIOLATIONS OF FEDERAL
SECURITIES LAWS

JURY TRIAL DEMANDED

CV-S-03-0850-KJD-LRL

Plaintiff, by his attorneys, for his Class Action Complaint, alleges the following upon personal knowledge as to himself and his own acts, and upon information and belief based upon the investigation of plaintiff's attorneys as to all other matters. The investigation includes the thorough review and analysis of public statements, publicly-filed documents of defendants, press releases and news articles. Plaintiff believes that further substantial evidentiary support will exist for the allegations set forth below after a reasonable opportunity for discovery.

SUMMARY OF ACTION

1. This is a securities class action on behalf of public investors who purchased the common stock of Goldman Sachs Group Inc., during the period from July 1, 1999 through May 7, 2002 (the "Class Period"). Plaintiff complains of a fraudulent scheme and deceptive course of business that injured purchasers of Goldman Sachs stock during the Class Period.

2. During the Class Period, the Goldman Sachs Group, Inc., through its subsidiary, Goldman, Sachs & Co. (together, "Goldman Sachs") publicly touted its securities analysts as an objective and unbiased source of stock research. This illusion began to unravel in the spring of

2002 when New York State Attorney General Elliot Spitzer's (the "Attorney General") investigation turned up thousands of pages of incriminating documents and emails revealing widespread abuses involving analyst research at another investment banking firm, Merrill Lynch. The release of these documents fueled the worries of investors in each of the big Wall Street investment firms. These fears increased on April 10, 2002 when the Attorney General announced he would include Goldman Sachs in his investigation into conflicts of interests among Wall Street securities analysts. Two weeks later, investor confidence was further shaken when the Justice Department, SEC and a special task force created by the North American Securities Administration Association all announced they would conduct probes to examine fraud committed by investment firm securities analysts.

3. The rumors of wrongdoing at Goldman Sachs' securities research department that were circulating since the Merrill Lynch probe have been confirmed during a year long investigation by numerous government agencies. The evidence discovered by these regulatory probes include: pitchbooks that unabashedly market their research analyst's ability to praise the stock of investment banking clients, analyst self-evaluations that detail their involvement in investment banking deals, evaluations of analysts by investment bankers, emails in which analysts were told to alter their research, as well as other internal memos of an incriminating nature.

4. These regulatory investigations established that Goldman Sachs' own corporate policies subjected analysts to inappropriate influence from the firm's investment banking division during the July 1999 through June 2001 period. July 8, 2003. The SEC concludes in its complaint that Goldman Sachs failed to manage conflicts of interest between its research and investment banking divisions, ignored internal warnings that its research product had become

biased and misleading to investors, and in some cases actively initiated policies that encouraged analyst involvement in investment banking. Due to this corporate malfeasance, the Chinese wall separating investment banking from securities research had been breached, making it virtually impossible for analysts to deliver the honest and objective research reports Goldman Sachs had promised its customers.

5. The investigations launched against Goldman Sachs resulted in numerous charges by government agencies alleging violations of NASD and NYSE rules of conduct. On April 28, 2003, Goldman Sachs settled the claims brought against it by the SEC, NASD, NYSE, the New York Attorney General and other state regulators by paying \$110 million in penalties and restitution. As part of the settlement agreement, Goldman Sachs was required to comply with the provisions of the "Global Resolution" mandating that it along with the other Wall Street firms under investigation must, among other things: separate the company's securities research department from its investment banking division; base analysts' compensation on quantifiable measures of their research accuracy and not on investment banking revenue; prohibit analysts from soliciting IB (investment banking) business; and disclose any investment banking relationship it may have with the issuers its research reports cover. The misconduct uncovered by these government investigations spawned class actions suits by investors who had lost millions of dollars after buying stocks the Defendant's analysts had recommended.

6. Not surprisingly, the revelations of Goldman Sachs and its analysts' blatant misrepresentations, the ongoing governmental investigations, the specter of costly class action lawsuits and regulatory fines caused a substantial decline in the price of Goldman Sachs stock. As news of the conflicts of interest emerged, the price of Goldman Sachs stock declined significantly, falling from \$86.06 on April 8, 2002 when the Attorney General announced his

intention to expand his probe of Merrill Lynch to the whole industry, to \$81.24 on April 11, 2002, the day after the New York Attorney General first named Goldman Sachs as a target of his investigation. By May 6, 2002 the price had fallen to \$75.16 on news of a possible bond rating downgrade in response to the expanding scope of the investigations involving Goldman Sachs.

JURISDICTION AND VENUE

7. This Court has jurisdiction over this action pursuant to Section 27 of the Securities Exchange Act of 1934 (the "1934 Act"), 15 U.S.C. §78aa, as well as pursuant to 28 U.S.C. §§ 1331 and 1337. The claims asserted herein arise under Section 10(b) of the 1934 Act, 15 U.S.C. §§ 78j(b), and Rule 10b-5, 17 C.F.R. §240.10b-5, promulgated thereunder by the SEC.

8. Venue is proper in this District pursuant to Section 27 of the 1934 Act, 15 U.S.C. §78aa, and 28 U.S.C. §1391(b). At least one of the acts giving rise to the violations complained of herein, including the dissemination of false and misleading public statements, occurred in this District. In addition, on information and belief, many Goldman Sachs Group, Inc. purchasers are residents of this District.

9. In connection with the wrongs alleged herein, the defendants used the instrumentalities of interstate commerce, including the United States mails, interstate wire and telephone facilities, and the facilities of the national securities markets.

THE PARTIES

10. Plaintiff [REDACTED] purchased shares of Goldman Sachs Group, Inc. common stock during the Class Period as detailed in his certification filed herewith, and was damaged thereby.

11. Defendant Goldman Sachs Group, Inc., a Delaware company, through its wholly owned subsidiary Defendant Goldman, Sachs & Co., a New York company, both headquartered in New York, New York, provides investment banking and securities brokerage services to corporate and private retail clients. The brokerage services include the dissemination to clients of the ratings and recommendations issued by Goldman Sachs analysts with respect to the securities of publicly traded companies.

12. Defendant Henry M. Paulson, Jr. was Chairman and Chief Executive Officer of Goldman Sachs Group, Inc. during the Class Period.

CLASS ACTION ALLEGATIONS

13. Plaintiff brings this action as a class action pursuant to Rules 23(a) and 23(b)(3) of the Federal Rules of Civil Procedure, individually and on behalf of all other persons or entities who purchased or acquired Citigroup Inc. common stock during the Class Period and were damaged thereby, excluding the defendants herein, their affiliates and any officers or directors of the defendants or their affiliates, and any members of immediate families and their heirs, successors and assigns (the "Class").

14. The Class is so numerous that joinder of all the members of the Class is impracticable. Plaintiff believes there are thousands, if not tens of thousands, of record holders of the Company's common stock located throughout the United States.

15. Plaintiff's claims are typical of the claims of absent Class members. Members of the Class have sustained damages arising out of defendant's wrongful conduct in violation of the federal securities laws in the same way as the damages sustained by plaintiff from the unlawful conduct.

16. Plaintiff will fairly and adequately protect the interests of the Class. He has

retained counsel competent and experienced in class and securities litigation.

17. A class action is superior to other available methods for the fair and efficient adjudication of the controversy. The Class is numerous and geographically dispersed. It would be impracticable for each member of the Class to bring a separate action. The individual damages of any member of the Class may be relatively small when measured against the potential costs of bringing this action, and thus make the expense and burden of this litigation unjustifiable for individual actions. In this class action, the Court can determine the rights of all members of the Class with judicial economy. Plaintiff does not anticipate any difficulty in the management of this suit as a class action.

18. Common questions of law and fact exist as to all members of the Class and predominate over any questions affecting solely individual members of the Class. These questions include, but are not limited to, the following:

- a. whether defendants' conduct as alleged herein violated the federal securities laws;
- b. whether the press releases and statements disseminated to the investing public during the Class Period misrepresented Goldman Sachs Group's business, including but not limited to the true nature of its subsidiary Goldman, Sachs & Co.'s research analyst's opinions;
- c. whether defendants acted knowingly or recklessly in omitting and/or misrepresenting material facts;
- d. whether the market price of Goldman Sachs common stock during the Class Period was artificially inflated; and

- e. whether the members of the Class have been damaged, and if so, what is the proper measure of damages.

SUBSTANTIVE ALLEGATIONS

20. Goldman Sachs often touted the quality, honesty and integrity of its research analysts in public communications. During each year in the Class Period, Goldman Sachs issued an annual report to shareholders containing a list of business principles to which the company was committed. Four of the fourteen principles are excerpted below:

1. Our clients' interests always come first. Our experience shows that if we serve our clients well, our own success will follow.
2. ... We are dedicated to complying fully with the letter and spirit of the laws, rules and ethical principles that govern us. Our continued success depends upon unswerving adherence to this standard.
4. We take great pride in the professional quality of our work. We have an uncompromising determination to achieve excellence in everything we undertake...
14. Integrity and honesty are at the heart of our business. We expect our people to maintain high ethical standards in everything they do, both in their work for the firm and in their personal lives.

21. In Goldman Sachs' 1999 IPO prospectus the company observed that the quality of its research department was fundamental to its success:

We believe that investment research is a significant factor in our strong competitive position in debt and equity underwritings and in our generation of commission revenues.

Major investors worldwide recognize Goldman Sachs for its value-added research products, which are highly rated in client polls across the Americas, Europe and Asia. Our Research Department is the only one to rank in the top three in each of the last 15 calendar years in *Institutional Investor's* "All-America Research Team" survey. In December 1998, the Research Department also achieved top honors for global investment research from *Institutional Investor*. In Europe, based on the *Institutional Investor* "1999 All- Europe Research Team" survey, the Research Department ranked number one for coverage of pan-European sectors and number three in European Strategy and Economics.

22. These misrepresentations continued even after the governmental investigation that revealed the extent to which securities analysis at Goldman Sachs was riddled with conflicts of interest. In a June 5, 2003 speech before the National Press Club, Defendant CEO Henry Paulson said:

For an integrated investment bank such as Goldman Sachs, conflict management has always been a core competency because it is critical to our reputation and a key to our success...

Though he then qualified the statement:

“But, particularly in the context of the technology and telecom bubble of the late 1990s, we have not done as good a job as we might have in preserving and protecting the appearance of independence of our research analysts who play a vital role in the investing and capital allocation process.”

23. The disclaimers included in Goldman Sachs research reports during the Class Period failed to give an indication of the great extent to which individual conflicts of interest were biasing analyst opinions. A typical disclaimer contained in a February 5, 1998 report on AT&T Corp. read in part:

“An affiliate of Goldman Sachs & Co has acted as a dealer in the commercial paper of AT&T Corp and/or affiliates thereof within the past 12 months. Goldman Sachs, & Co. or an affiliate has acted as a dealer or co-managed a public offering of AT&T Corp securities in the past several years. Goldman, Sachs & Co. or affiliate has rendered significant corporate finance services to AT&T Corp. or affiliates thereof within the past twelve months. Goldman, Sachs & Co. or an affiliate may deal as principal in any of the securities mentioned.”

“This material is for your private information and we are not soliciting any action based upon it. This report is not to be construed as an offer to sell or the solicitation as the offer to buy any security in any jurisdiction where such an offer or solicitation would be illegal. The material is based upon information that we consider reliable, but we do not represent that it is accurate or complete, and it should not be relied upon as such. **Opinions expressed are our current opinions** as of the date appearing on this material only... We and our affiliates, officers, directors and employees, including persons involved in the preparation or issuance of this material may from time to time, have long or short positions in, and buy or sell, the securities, or derivatives (including options) thereof, of companies mentioned herein...” (emphasis added)

24. The above disclaimer failed to notify investors that Goldman Sachs' analysts may have been influenced by the conflicts of interest alleged below, that Goldman Sachs' own corporate practices had created.

25. Unbeknownst to the Class, Goldman Sachs' analysts did not furnish objective or independent ratings and reports. Instead, Goldman Sachs systematically created opportunities for analyst research to be influenced by investment banking concerns. As a result, ratings were frequently inflated and stocks were rarely disparaged even as they fell dramatically in value.

26. The Defendants' wrongdoing, which investors had begun to anticipate from the beginning of the Merrill Lynch investigation, was confirmed when the SEC with the support of the New York State Attorney General and other regulators filed a complaint against Goldman Sachs, on April 28, 2003, detailing the inappropriate commingling of investment banking and research activities at the firm. The plaintiff incorporates by reference into this complaint the entirety of the SEC's complaint against Goldman Sachs.

Goldman Sachs' Misconduct as Set Forth in the SEC's Complaint

27. The investment banking (IB) fees earned from underwriting IPOs, secondary offerings and other corporate transactions made up a large proportion of Goldman Sachs' business during the Class Period. In 2000, IB accounted for approximately \$5.37 billion or 32% of Goldman, Sachs & Co.'s total net revenue. By contrast, Goldman Sachs' research department was a cost center. Accordingly, Goldman Sachs pressured its research analysts to support the IB division's activities.

Goldman Sachs' Pressured Its Research Analysts to Support Investment Banking Through The Firms Compensation and Evaluation Policies

28. The level of compensation for research analysts at Goldman Sachs was

determined by numerous factors that included the level of participation in investment banking activities such as generating business for the IB division.

29. Analysts at Goldman Sachs were subject to annual performance evaluations that included self-evaluations, the development of business plans and a “360 degree review” in which fellow employees commented on the analysts performance. Goldman Sachs often asked investment bankers to offer their opinions of research analysts in these reviews. In a year 2000 presentation to research analysts it was stated that the review process included a, “Formal Investment Banking Division recognition of Research contribution to business we win and relationships we improve.”

30. Many of the comments contained in the 360 degree reviews illustrate the extent to which IB activities were considered important to an analyst’s performance. The following such comments, contained in the SEC complaint are a telling example:

- “One of my favorite analysts. A real traders analyst. Solid grasp of the industry; well liked by investors i.e. [sic] well informed as to their intentions, which translates to a ton of business...I’m sincere when I emphasize that many GS [Goldman Sachs] analysts can learn from his model insofar as a trading relationship goes. I realize that bringing in the banking bucks is primary to an analysts [sic] success and actually being able to pick a stock takes second, but I wouldn’t trade him for anyone...”
- “[needs to] make more of an effort to separate research views from banking views. Like many analysts, he has been known to be swayed by banking to support certain names”
- “he has been in the incredibly awkward position of having the investment bankers have a stronghold over his written work-STOR [StorageNetworks], LDCL [Loudcloud] to name a few embarrassments”
- “One gets the sense that he’s been held captive to the agenda of others within the Firm and that, were he allowed to exercise independent investment thesis, he would have had a decidedly different take of this group’s prospects”

Some of the analysts’ self evaluations confirm their own intentions to contribute to IB:

- “Need to get closure on some key wins. To monetize relationships for Goldman Sachs, both at the corporate and buyside level.”
- “has subordinated personal preferences on recommendations...for ‘commercial’ reasons.”

31. Analysts were asked to write up business plans that outlined their goals for the coming year. Questions from these business plans show that Goldman Sachs considered part of its analysts’ jobs to be supporting IB operations. As alleged in the SEC complaint these business plan questions included:

- How much of your time will be devoted to IBD [Investment Banking Division]? ...Are you using/managing IBD effectively? How can you work more effectively with IBD to exploit the opportunities available to the firm? What specific opportunities do you see? Do you have alignment-do you have counterparts in the IBD you work with to approach business in an integrated fashion? How can IBD help you in conferences, client meetings, etc.?
- What will be the three most important IBD transactions in your space not yet mandated (that can be identified now, of course)? How well placed are your IBD relationships with respect to winning this business? With which corporates can you use IBD’s relationship to enhance your own? For which corporates do you have a better relationship with senior management than IBD does? How will you use that to enhance GS business opportunities?

32. Analysts answered these questions by referring to their involvement in underwritings as well as the fees associated with the IB transactions they worked on. In the 1999 business plans, analyst estimates of the time they spent on IB activities ranged from 5% to 75% of their time not devoted to research.

33. When asked to list in his business plan his top three goals for 2000, one analyst wrote, “1. Get more investment banking revenue. 2. Get more investment banking revenue. 3. Get more investment banking revenue.”

**Goldman Sachs Used the Research Coverage of Its Analysts
as a Marketing Tool to Attract Investment Banking Clients**

34. One way in which the research department contributed to IB was through its decisions regarding the initiation and termination of their coverage of particular companies. While coverage decisions were also influenced by investor interest and a company's prominence in its industry, Goldman Sachs intentionally coordinated research coverage with its IB interests through a corporate initiative known as "Research Alignment" adopted in 1998-1999.

35. The practice of Research Alignment called for certain investment bankers, known as, "Sector Captains" to make requests for coverage, suggest coverage termination and priorities and relay them to the research division. The stated purpose of this policy was to, "insure a strategic alignment of [Goldman Sachs'] business – that the biggest opportunities for investment banking and equities were being covered, that [Goldman Sachs] had the right resources in the right places." (SEC para. 36) Implementation of the process was in recognition of the fact that the, "coverage provided by Global Investment Research helps drive the majority of the Firm's largest businesses, from winning financing deals and advisory business to obtaining orders in the secondary markets."

36. A Goldman Sachs memo, "Global Investment Research IBD Alignment Process" written in 2000, touted the success of the initiative, by reciting the following statistics:

- a. "Research analysts, on 429 different occasions, solicited 328 transactions in the first 5 ½ months of this fiscal year."
- b. "Research was involved in 82% of all, "won business' solicitations."
- c. "Research was involved in 49% of 'lost business' solicitations."
- d. "Only 4.3% of all IBD 'lost business' was attributed to lack of research coverage."

- e. “IR [Investment Research] was involved in 31 mergers amounting to \$56 billion. IR was involved in 209 financing transactions amounting to \$83 billion.”
- f. “In addition to financings, US IR was involved in a significant number of merger advisories, solicitations, and other transactions which have either not yet closed or were not captured [in the] database.”

The statistics show that the Goldman Sachs’ realignment process had measurably increased IB’s influence over research. A March 16, 2000 e-mail from an analyst to an investment banker provides an individual example of the policy’s effect,

“I wanted to harmonize with you strategically. [CEO at Ventro] suggested that there might be a banking opportunity for us, can we use a carrot and stick approach to win some economics here. I’ve been successful in the past using my research efforts to cement relationships where we previously had none.”

37. Having created a research department responsive to the needs of the investment banking department, Goldman Sachs then used this fact as a marketing tool to attract potential IB clients. Investment banking firms use what is known as a pitchbook as a means to present to clients the quality of the services they offer. Goldman Sachs would often discuss the benefits to the client of analyst coverage in its pitchbooks. The SEC complaint alleges that some of these pitchbooks implicitly suggest that research coverage by Goldman Sachs would be positive after they concluded the IB transaction. Pitchbooks would sometimes compare a particular analyst’s ratings to the changes in stock price of the covered company.

38. Some pitchbooks would include statistics detailing the number of IPO’s that Goldman Sachs lead-managed that are covered by research, the typical length of research reports and frequency of such reports.

39. The SEC complaint contains several quotes from Goldman Sachs’ pitchbooks:

“Goldman Sachs has placed Crown Castle on our Recommended List, our firm’s highest rating.” (July 2000 pitchbook for Crown Castle)

- “[the analyst] has sold more stock than any other sector.” (pitchbook for Willis Group)
- the, “[r]ole of investment research analyst,” is “creating the story...marketing the story...[and] following the story.” (October 2000 pitchbook for GeneProt)

40. Analysts worked with investment members to develop their pitch presentation and sometimes spoke at them, discussing their view of the client’s company. In the following quote from an email, a Goldman Sachs investment banker emphasizes the importance of an analyst, the head of telecom research, to pitching Crosswave Communications, “[the analyst] was fully involved in pitching this and thanks to him, we received a sole-book mandate with Joint Lead of MS.”

**Research Coverage By Goldman Sachs Securities Analysts
Was Influenced By Investment Bankers and Issuer Management**

41. Goldman Sachs, by communicating to its analysts their critical role in supporting IB and by soliciting their IB clients through an emphasis on their research, created a corporate environment in which it was all but inevitable that analysts be exposed to inappropriate pressure from IB and covered companies to alter the content of their research. This is exactly what happened. It went so far that some analysts would allow an IB client’s management to vet a draft research report before publishing.

42. The SEC’s complaint highlights numerous communications between analysts, investment bankers and the management of covered companies which evidence that the analyst was subjected to improper influence. A February 23, 2001 email from an analyst to investment bankers explains the difficulty of objectively writing an Internet Sector report without offending IB clients:

I have drafted a note that highlights our concerns yet does not translate into the lowering of numbers for specific companies. Considerations include: 1) we

believe that most of our cost back-end loaded 2001 numbers have to come down, 2) exds [Exodus] is a major offender of back-end loading, but to lower numbers right after selling equity @ \$18.50 could be a problem. It would also be a problem to cut other company's numbers for aforementioned reasons and not exds [Exodus] 3) we have a deal in the market and negative commentary could be a problem or used against us by Morgan Stanley. Based on these considerations this note is as far as I think we can go and even this might be too aggressive from a perception standpoint.

43. When this sector report was issued, Loudcloud, an IB client of Goldman Sachs reacted negatively in an email, "Are you trying to kill our offering? Or just issuing these reports blindly with no regard for the consequences?" The senior analyst on the report apologized directly to Loudcloud management:

I echo the [banker's] apology on not giving you a heads up on these calls. Wanted to reassure you on two fronts: 1) Both [the other analyst] and I continue to view the LDCL [Loudcloud] offering in these difficult markets our highest priority, and remain committed to doing everything we can to get us to a successful outcome over the coming days and beyond. 2) we continue to use every opportunity, including client discussions short and long-term differentiation against a lot of the public models. ...Again, I want to stress that both [the other analyst] and I remain committed to the short and long-term success of Loudcloud.

44. The SEC complaint recites the following communications between WebEx management and a Goldman Sachs analyst in January of 2001 regarding a draft research report sent for WebEx's approval:

- a. WebEx management virtually dictates the content of the upcoming report to the analyst: "As discussed, I want NO mention of any funding issues in this report. I told you if people called and asked you why your plan shows a need for modest funding, you can verbally tell them that management believes they have adequate funding and it is probably because management has a less conservative plan than you do." [Emphasis in the original.]
- b. The analyst gives in to management's concerns: "the webx [sic] funding issues is a key area of investor concern, as such will remove any mention from the top section of the note, but will address it in a manner this [sic] is consistent with your recommendation for verbal responses to client inquiries in a later section. To exclude it completely detracts from the intention of the note, which is to

address key investor concerns upfront and then give them a reason to buy the stock.”

- c. WebEx management responded: “Thank you. This is much better. The other note said the company has a funding problem, but we think it isn’t very big. This says that the company believes it has enough funds, but there could be a problem; and if there is it will be minor. Thanks against for the change.”

45. The following email cited in the SEC is another case in which an analyst sent a draft report to be vetted by an IB client. This time an analyst emails her supervising analyst, explaining that she had incorporated Global Crossing’s “extensive comments” into her report:

“...I also said we had slightly smoothed the negative edge (emphasis section up front and text) from when they say the report. I said we included throughout the piece technological cost benefit comments and in [sic] up front conclusion section. I also said we still think supply/demand balance is THE near term critical price determinant. I promised them I’d re-email the final report tonight so they could see our changes. Nonetheless, [Global Crossing official] still wants to talk to YOU life [sic] today if possible so that he knows his time was used well and so that ‘such an important industry report which is going to have profound implications will be to their liking--ALL YOURS” [emphasis in original]

46. As these communications illustrate analysts were subjected to pressure to alter their research from what would have been their honestly held beliefs. Thus, it is no surprise that Goldman Sachs published stock reports with exaggerated and unwarranted ratings and research for which there was no reasonable basis.

**Goldman Sachs Published Inaccurate Research
Contrary to the Authoring Analyst’s True Beliefs**

47. In furtherance of its quest to garner the good favor of potential clients, Goldman Sachs offered the investing public inaccurately optimistic stock ratings. During the Class Period, Goldman Sachs’ stock rating system consisted of five ratings listed below:

- RL: Recommended List – expected to provide price gains of at least 10 percentage points greater than the market over the next 6-18 months;

- MO: Market Outperformer – expected to provide price gains of at least 5-10 percent greater than the market over the next 6-18 months;
- MP: Market Performer – expected to provide price gains similar to the market over the next 6-118 months;
- MU: Market Underperformer – expected to provide price gains of at least 5 percentage points less than the market over the next 6-18 months;
- Trading Buy – expected to provide price gains of at least 20 percentage points sometime in the next 6-9 months.

48. Goldman Sachs analysts rated a large majority of issuers one of the top two ratings, RL and MO. The proportion of this majority ranged from in the first quarter of 1999 72% to 50% in the last quarter of 2001. Never during that time were more than 1.1% of covered issuers given an “Underperformer” rating.

49. Aside from stock ratings, the SEC complaint lists several examples of analysts publishing reports that were contrary to the authoring analyst’s truly held beliefs.

50. The head of European telecom research wrote the following to his U.S. counterpart in an August 2000 email about the egregiously high stock ratings for telecom stocks that have been, “tanking”: "In Europe, we have found that honour is preserved if we have a stock as an M[arket] O[utperformer] and the companies can't complain because its [sic] better than an M[arket] P[erformer]."

In his response, the Business Unit Leader for U.S. Telecommunications research agreed, saying:

"The plan we have in place now is that in early September we are going to re-rate most of the CLECs [competitive local exchange carriers], which is where the problem is the most egregious. The ratings were a residual from [a former research analyst], and I never changed them, not wanting to disrupt things too much. But it's ridiculous. I've already met with the bankers, and plan to move most of the companies down to M[arket] O[utperformer], from R[ecommended] L[ist] before [another analyst] takes over completely in September. For the other segments the situation is not as bad, and where there is a problem, investment banking considerations have prevented me from making a change (i.e. AT&T,

WCOM [WorldCom]). I don't think I would end up leaving only 7.5% as R[ecommended] L[ist], but the present 68% is ridiculous...."

51. In an April 27, 2001 e-mail a research analyst asked his supervisor whether he should downgrade a stock that was virtually worthless. The supervising analyst responded:

"Maybe the thing to do is to eliminate the price target. Maybe, put out a note that says, having a price target in this kind of situation is ludicrous...Changing the rating now is probably not a good idea, because from an outsider's perspective, who doesn't know anything, it may look like a belated ratings change. This happened last week to [an analyst], although he had been appropriately negative on WCII [Winstar Communications] all the way down, he belatedly dropped the rating from a M[arket] P[erformer] to an M[arket] U[nderperformer], and cnbc picked it up and made fun of him on the air."

52. In May 2001, the head of U.S. telecom research told his European counterpart that he, "would have loved to have cut ratings long ago. Unfortunately, we can't cut [AT&T], because we're essentially restricted there. And without cutting [AT&T], there is no consistency in cutting WCOM [WorldCom]." At the time, WorldCom had Goldman Sachs' highest rating, Recommended List.

53. Goldman Sachs maintained a Recommended List rating for WorldCom from July 1999 until July 2001 when it was downgraded to "Market Outperformer". When in April 2000 a hedge fund customer asked the head of U.S. telecom research whether it should buy, sell or hold WorldCom stock, he responded, "sell."

54. On June 21, 2001, Exodus was downgraded from the Recommended List to Market Outperformer. Shortly before this downgrade the analyst covering the company met with institutional investors. Emails from two of these investors make it clear that the analyst gave them a private opinion of the company contrary to the publicly issued ratings:

- a. An institutional investor wrote the analyst on June 21, 2001: "I wanted to write a quick email to you to THANK you for your candor when you came into our offices and gave me your teach-in on the company. You gave me the unbiased

view, told me the negatives I needed to know - - and basically gave me the ammo I needed to prevent my PM from buying the stock." [Emphasis in original.]

- b. Another institutional investor wrote the analyst the same day: "I really appreciate your straight forward comments on EXDS [Exodus] during our conversation last week. Looks like our worst concerns were realized yesterday. Fortunately, we were able to get out of our last piece at around \$5 and avoid the recent carnage in the shares. Still painful, but it could have been a lot worse. . . thanks."

55. A member of Goldman Sachs' sales force had this to say about the analyst

mentioned in the paragraph above, "his investment recommendations have been abysmal and while I understand he communicates what he really thinks to a select few, his public ratings have been an embarrassment to the firm."

56. Ostensibly, it is the role of a research analyst to produce objective research.

However, Goldman Sachs actively created an environment in which conflicts of interest were likely to arise. The conflicts resulted in misleading if not fraudulent research reports and ratings that while perhaps benefitting Goldman Sachs' investment banking clients, harmed the investing public that was not privy to the analysts' privately held, true beliefs.

Goldman Sachs Failed to Effectively Manage Conflicts of Interest Within the Firm

57. Having played a hand in the creation of this situation, in part through the implementation of the "Research Realignment" initiative, Goldman Sachs management was aware of the problems its analysts were facing in producing objective research.

58. Being aware of the problem, Goldman Sachs failed to adequately supervise its analysts in such a way as to minimize the risks presented by conflicts of interests within the firm. Corporate policy did not address analyst conflicts of interest sufficiently. Nor did Goldman

Sachs publicize the nature and extent of these conflicts to the investing public or to the stockholders of Goldman Sachs itself.

**Goldman Sachs Violated NYSE and NASD Rules
By Issuing Misleading Research Reports and Stock Ratings**

59. NASD Conduct Rule 2110 requires members to observe high standards of commercial honor and just and equitable principles of trade.

60. NYSE Rule 401 requires that member organizations adhere at all times to the principles of good business practice in the conduct of their business affairs.

61. NYSE Rule 476(a)(6) prohibits members from engaging in conduct or proceeding in a manner inconsistent with just and equitable principles of trade.

62. As the SEC charged in its complaint, the above alleged actions of Goldman Sachs, by creating a situation in which investment banking imposed conflicts of interest on research analysts violated NASD Conduct Rule 2110 as well as NYSE Rules 401 and 476(a)(6).

63. NASD Conduct Rule 2210(d)(1)(A) states:

All member communications with the public shall be based on principles of fair dealing and good faith and should provide a sound basis for evaluating the facts in regard to any particular security or securities or type of security, industry discussed, or service offered. No material fact or qualification may be omitted if the omission, in the light of the context of the material presented, would cause the communications to be misleading.

64. NASD Conduct Rule 2210(d)(1)(B) prohibits members from making

"[e]xaggerated, unwarranted or misleading statements or claims ... in all public communications" and from making "any public communication that the member knows or has reason to know contains any untrue statement of a material fact or is otherwise false or misleading."

65. NASD Conduct Rule 2210(d)(2)(B) requires, among other things, that members have a reasonable basis for all recommendations made in advertisements and sales literature.

66. NASD Conduct Rule 2210(d)(2)(C) prohibits members from making, among other things, "promises of specific results, exaggerated or unwarranted claims or unwarranted superlatives, opinions for which there is no reasonable basis, or forecasts of future events which are unwarranted" in communications with the public.

67. NYSE Rule 472 provides, among other things, that:

[n]o member or member organization shall utilize any communication which contains (i) any untrue statement or omission of a material fact or is otherwise false or misleading; or (ii) promises of specific results, exaggerated or unwarranted claims; or (iii) opinions for which there is no reasonable basis; or (iv) projections or forecasts of future events which are not clearly labeled as forecasts.

68. As the SEC charged in its complaint, the above alleged actions of Goldman

Sachs, by publishing research reports and ratings which constituted or contained exaggerated and unwarrantable claims, or opinions that had no reasonable basis violated NASD Conduct Rules 2110, 2110(d)(1) and 2210(d)(2) as well as NYSE Rules 401, 472 and 476(a)(6).

69. NASD Conduct Rule 3010(a) requires members, among other things, to "establish and maintain a system to supervise the activities of each registered representative and associated person that is reasonably designed to achieve compliance with applicable securities laws and regulations, and with NASD's own Rules.

70. NYSE Rule 342 requires members, among other things, to maintain "appropriate supervisory control" over all business activities to ensure compliance with securities laws and regulations, including providing a "separate system of follow-up and review to determine that the delegated authority and responsibility is being properly exercised."

71. As alleged in the SEC complaint, Goldman Sachs failed to establish and maintain adequate procedures over research analysts to prevent or manage conflicts of interest. Goldman Sachs therefore violated NASD Conduct Rule 3010 and NYSE Rule 342.

**Goldman Sachs' Practices Encouraged the Violation of the
Ethical Code Governing Investment Professionals and the Violation of the
Recently Developed Research Objectivity Standards**

72. The Association of Investment Management and Research (AIMR) is an international non-profit association of securities analysts and other investment specialists organized to maintain high levels of ethical conduct within their profession. The AIMR has adopted a Code of Ethics and Standard of Professional Conduct meant to promote integrity, competence, and dignity within the investment community worldwide.

73. Standard IV of the Code governs the relationship between investment professionals and their clients. Section A.2 (a) of Standard IV, entitled, "Research Reports" states: "Members shall...Use reasonable judgment regarding the inclusion or exclusion of relevant factors in research reports."

74. Section A.3 requires that: "Members shall use reasonable care and judgment to achieve and maintain independence and objectivity in making recommendations or taking investment action."

75. Goldman Sach's course of conduct during the Class Period acted to inhibit its

securities analysts' ability to comply with the AIMR's Code of Ethics and Standard of Professional Conduct.

76. In response to the scandals unearthed by the Attorney General's investigation of the big Wall Street investment firms, including Goldman Sachs, the AIMR has proposed a set of Research Objectivity Standards (ROS) that provides standards, implementation guidelines and recommended practices for investment firms to adopt to ensure the independence and integrity of their analysts' research.

77. Although the Research Objectivity Standards are still in the process of being drafted by the AIMR, the proposed Standards already proscribe many of the alleged practices attributed to Goldman Sachs during the Class Period.

78. Section 4.0 of the proposed ROS states: "Firms that engage in, or collaborate on, investment banking activities must":

- (a) Establish and implement effective policies and procedures that:
 - i. Segregate research analysts from the investment banking department; and
 - ii. Ensure that investment banking objectives or employees do not have the ability to influence or affect research or recommendations;

- (j) Implement reporting structures and review procedures that ensure that research analysts do not report to, and are not supervised or controlled by, investment banking or another department of the firm that could compromise the independence of the analyst; ...

79. As alleged in paragraph 29, Goldman Sachs' review process allowed investment bankers to review securities analysts, potentially breaching both Section 4.0(a) and (b). As alleged in paragraphs 34-36, Goldman Sachs developed the "Research Alignment" program through which analysts were encouraged to work closely with and to support Goldman Sachs' investment bankers. Both of these practices are inconsistent with the ethical principles underlying Section 4.0.

80. Section 4.3 of the proposed ROS recommends that “firms prohibit research analysts from participating in marketing activities, including “roadshows,” for IPOs and secondary offerings. As alleged in paragraph 40, Goldman Sachs allowed securities analysts to participate in roadshows and other IPO marketing activities. In fact, Goldman Sachs pitchbook for the GeneProt and Willis Group IPO’s touted its analysts’ value as marketers to investors.

81. Section 5.0 of the proposed ROS requires that firms do not link analyst “compensation to investment banking or other corporate activities on which the analyst collaborated...” As alleged in paragraph 28, participation in investment banking activities was one of the factors involved in the determination of the analyst’s compensation at Goldman Sachs.

82. Section 6.0 requires that firms must prohibit research analysts from:

- (a) Sharing with, or communicating to, a subject company, prior to publication, any section of a research report that might communicate the research analyst’s proposed recommendation, rating, or price target; and
- (b) Directly or indirectly promising a subject company or other corporate issuer a favorable report or a specific price target, or from threatening to change reports, recommendations or price targets.

83. As alleged in paragraphs 37-39, Goldman Sachs actively marketed their securities analysts’ ability to provide favorable research to potential IB clients. As alleged in paragraphs 44 and 45, analysts provided Global Crossing and WebX, with advanced copies of research reports, in direct contravention of Section 6.0’s prohibitions.

84. Section 10.0 of the proposed ROS requires that, “Firms must provide full and fair disclosure of all conflicts of interest to which the firm or its covered employees are subject.” As alleged in paragraphs 19-24, rather than disclosing analysts’ conflicts of interest, Goldman Sachs

consistently touted the objectivity and independence of their research.

85. Although Goldman Sachs' violation of the proposed ROS is not necessary to the Plaintiff's cause of action, the ROS stands as an exemplar of the sort honesty and integrity which investors should be able to expect from an established and prominent investment firm such as Goldman Sachs. Before the startling revelations produced by the Attorney General's investment banking probe, it was reasonable for the investing public to believe that such profound conflicts of interest were not as pervasive at Goldman Sachs as they eventually turned out to be.

86. Indeed, the public was unaware of the extent to which conflicting interests were tainting the objectivity of Goldman Sachs securities analysts. As alleged in paragraphs 19-24, Goldman Sachs had continuously represented to the public that its research provided honest and valuable guidance. It would take a year-long governmental investigation of immense proportions, involving both federal and state agencies to fully reveal the degree of Goldman Sachs' malfeasance.

The Fallout

87. On April 8, 2002 the Attorney General announced that he would expand his Merrill Lynch investigation to encompass the entire IB industry. Two days later, when the Attorney General named Goldman Sachs as one of the targets of the expanded probe, investor confidence in Goldman Sachs analysts was shaken. The negative investor reaction became more widespread with the announcement of Justice Department and SEC involvement on April 23 and April 25, 2002 respectively. News of the probe was not well received by Wall Street. On May 6th, bond raters threatened to lower their appraisal of the big investment firms in response to the expanding scope of the government's investigations. Stock prices fell correspondingly as each

of these developments were publicized. Between April 8 and May 7, 2002, Goldman Sachs stock price dropped from \$86.06 to \$74.85 per share, a drop of more than 13%.

88. On April 28, 2003 Goldman Sachs settled all of the charges brought against it by the government agencies involved in the investigation. The agreement obligated Goldman Sachs to carry out the structural reforms mandated by the global resolution governing all the firms. These reforms were meant to prevent the kinds of undue influence on analyst opinions that Goldman Sachs's past practices had previously fostered. Essentially, Goldman Sachs agreed to refrain from most of the activities alleged in this complaint. Research analysts may no longer solicit IB business or attend road shows. No amount of an analyst's compensation can be based on investment banking revenue, nor may investment bankers evaluate securities analysts.

89. In addition to these reforms Goldman Sachs was required to pay \$110 million in penalties, investor restitution and other fees.

**DEFENDANTS' MISREPRESENTATIONS PROXIMATELY CAUSED
PLAINTIFF'S DAMAGES THROUGH A FRAUD ON THE MARKET**

90. Goldman Sachs stock is listed and trades on the New York Stock Exchange, the largest stock exchange in the United States. At all relevant times, the market for Goldman Sachs securities was an efficient market that promptly digested current information with respect to the Company from all publicly-available sources and reflected such information in Goldman Sachs stock price.

91. Goldman Sachs stock was actively traded throughout the Class Period, with millions of shares trading on the average day.

92. Throughout the Class Period, Goldman Sachs filed periodic reports with the SEC, and filed registration statements on form S-3.

COUNT I

**BREACH OF FIDUCIARY DUTY
AGAINST ALL DEFENDANTS**

93. Plaintiff repeats and realleges each and every allegation contained above as if fully set forth herein.

94. Defendants owed a fiduciary duty to the Class, as purchasers and owners of Goldman Sachs stock.

95. Defendants, by means of their making the foregoing false and misleading statements, breached their fiduciary duty to the Class.

COUNT II

**VIOLATIONS OF SECTION 10(b) OF THE EXCHANGE ACT
AND RULE 10b-5 PROMULGATED THEREUNDER**

96. Plaintiff repeats and realleges each and every allegation contained in the foregoing paragraphs as if fully set forth herein.

97. At all relevant times, defendants, directly and indirectly, by the use and means of instrumentalities of interstate commerce and/or of the mails, engaged and participated in a continuous course of conduct whereby they recklessly made public representations and/or omitted material information regarding Goldman's Sachs research analysts. This continuous course of conduct resulted in the defendants publishing public statements which were knowingly or materially false and misleading, and did artificially inflate the market price of Goldman Sachs stock. This conduct operated as a fraud and deceit upon the market as a whole and upon Plaintiff and the members of the Class.

98. In ignorance of the adverse facts concerning Goldman Sachs' analyst operations, and in reliance on the integrity of the market, Plaintiff and members of the Class acquired Goldman Sachs common stock at artificially inflated prices and were damaged thereby.

99. Had Plaintiff and the Class known of the materially adverse information not disclosed by defendants, they would not have purchased Goldman Sachs common stock at all or not at the inflated prices paid.

100. By virtue of the foregoing, defendants have violated Section 10(b) of the 1934 Act and Rule 10b-5 promulgated thereunder.

COUNT III

VIOLATION OF SECTION 20(a) OF THE 1934 ACT ON BEHALF OF THE ENTIRE CLASS AGAINST THE DEFENDANT

101. Plaintiff repeats and realleges each and every allegation contained in the above paragraphs, as if fully set forth herein. This claim is asserted against defendant Henry M. Paulson.

102. Defendant Paulson acted as a controlling person of Goldman Sachs within the meaning of Section 20(a) of the 1934 Act, as alleged herein. By virtue of his executive position, Paulson had the power to influence and control and did influence and control, directly or indirectly, the decision-making of the Goldman Sachs, including the content and dissemination of the various statements which plaintiff contends are false and misleading. Defendant Paulson was provided with or had unlimited access to copies of the Company's internal reports, press releases, public filings, and other statements alleged by plaintiff to be misleading prior to and/or shortly after these statements were issued and had the ability to prevent the issuance of the statements or cause the statements to be corrected.

103. In particular, defendant Paulson had direct involvement in the day-to-day operations of Goldman Sachs and therefore, is presumed to have had the power to control or influence the particular transactions giving rise to the securities violations as alleged herein, especially by virtue of his senior position, and exercised the same.

104. As set forth above, defendant Paulson violated Section 10(b) and Rule 10b-5 by his acts and omissions as alleged herein. By virtue of his position as controlling person of Goldman Sachs, defendant Paulson is liable pursuant to Section 20(a) of the 1934 Act. As direct and proximate result of defendant Paulson wrongful conduct, plaintiff and the Class suffered damages.

JURY DEMAND

Plaintiff hereby demands trial by jury.

PRAYER FOR RELIEF

WHEREFORE, Plaintiff demands judgment:

1. Determining that the instant action is a proper class action maintainable under Rule 23 of the Federal Rules of Civil Procedure;
2. Awarding compensatory damages and/or rescission as appropriate against defendants, in favor of and all members of the Class for damages sustained as a result of defendants' wrongdoing;
3. Awarding Plaintiff and the Class the costs and disbursements of this suit, including reasonable attorneys', accountants' and experts' fees; and