

**UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK**

U.S. SECURITIES AND EXCHANGE COMMISSION, Plaintiff, v. EDWARD S. STEFFELIN, Defendant.	COMPLAINT [Securities Fraud] 11-CV-_____ () ECF CASE Jury Trial Demanded
---	--

Plaintiff Securities and Exchange Commission (“Commission”) alleges as follows against the defendant Edward S. Steffelin:

SUMMARY

1. The Commission brings this securities fraud action relating to the structuring and marketing of a largely synthetic collateralized debt obligation (“CDO”) called Squared CDO 2007-1 (“Squared”). The investment portfolio for Squared consisted primarily of credit default swaps (“CDS”) referencing other CDO securities whose value was tied to the United States residential housing market. J.P. Morgan Securities LLC (f/k/a J.P. Morgan Securities Inc.) (“J.P. Morgan Securities”) structured and marketed to investors notes in this \$1.1 billion “CDO squared” in early 2007 when the housing market and the securities referencing it were beginning to show signs of distress. Synthetic CDOs like Squared contributed to the recent financial crisis by magnifying losses associated with the downturn in the housing market.

2. The marketing materials for Squared – including the pitch book, term sheet, and offering circular – all described the process by which GSCP (NJ) L.P. (“GSC”), a registered investment adviser with experience analyzing credit risk in CDOs, purportedly selected the investment portfolio of Squared. Undisclosed in the marketing materials and unbeknown to

investors or to the special purpose vehicles (“SPVs”) that issued the securities to investors in Squared, a large hedge fund, Magnetar Capital LLC (“Magnetar”), with economic interests adverse to investors in Squared, played a significant role in the portfolio selection process. While participating in the Squared portfolio selection, Magnetar shorted a substantial portion of the assets that it participated in selecting by entering into CDS to buy protection on them. The collateral Magnetar shorted had a notional value of approximately \$600 million, representing over half of the Squared investment portfolio. (Magnetar also invested \$8.9 million in Squared’s subordinated notes, or equity.)

3. Magnetar’s role in selecting and shorting assets in the Squared investment portfolio was undertaken with the knowledge and assistance of GSC. Edward S. Steffelin (“Steffelin”) was in charge of the team at GSC that implemented the process for purportedly selecting the investment portfolio for Squared. Steffelin executed the engagement letter and warehouse agreement with J.P. Morgan Securities, permitted Magnetar to participate in the selection of assets knowing it planned to short those assets, and reviewed and participated in the drafting of the pitch book and other marketing materials before they were provided to investors. In particular, Steffelin helped draft the portion of the pitch book addressing GSC’s CDO investment approach, *i.e.* the process for selecting the portfolio. The description of GSC’s CDO investment approach set forth in the pitch book made no mention of Magnetar’s involvement in the portfolio selection process. Steffelin knew, however, that Magnetar was directly involved in the portfolio selection process and had a substantial short interest in Squared. Also undisclosed in the marketing materials and unbeknown to investors and the SPVs, Steffelin was seeking employment with Magnetar during the relevant period.

4. J.P. Morgan Securities offered and sold approximately \$150 million of the so-called “mezzanine” tranches of Squared’s liabilities (“Notes”) – representing the riskiest notes of the deal after the equity – to a group of approximately 15 institutional investors (“Mezzanine Investors”). The Mezzanine Investors included a faith-based not-for-profit membership organization headquartered in Minneapolis, Minnesota (Thrivent Financial for Lutherans), a company that provides insurance and retirement products based in Topeka, Kansas (Security Benefit Corporation), and financial institutions located in East Asia (Tokyo Star Bank, Far Glory Life Insurance Company Ltd., Taiwan Life Insurance Company Ltd., and East Asia Asset Management Ltd.).

5. The Squared transaction priced on April 19, 2007, and closed on May 11, 2007. Steffelin, on behalf of GSC, executed the collateral manager agreement with the CDO when the deal closed. GSC was paid \$1.4 million in management fees, consisting of a \$350,000 up front fee at closing plus annual management fees. Steffelin was paid a \$250,000 base salary and a \$1 million bonus in 2007. A portion of Steffelin’s bonus was based on the profits of the structured products group he supervised at GSC, and a portion was based on the overall profits of GSC.

6. Squared declared an event of default on January 18, 2008. By January 29, 2008, 50 percent of the CDO securities in the investment portfolio had been downgraded and another 34 percent of the portfolio was on negative downgrade watch. The Mezzanine Investors lost most, if not all, of their principal.

7. By engaging in the conduct described in this complaint, Steffelin violated Sections 17(a)(2) and (3) of the Securities Act of 1933 [15 U.S.C. §77q(a)(2) and (3)] (“Securities Act”)

and Section 206(2) of the Investment Advisers Act of 1940 [15 U.S.C. §80b-6(2)] (“Advisers Act”). The Commission seeks injunctive relief, disgorgement of profits, prejudgment interest, civil penalties and other appropriate and necessary equitable relief from the defendant.

JURISDICTION AND VENUE

8. This Court has jurisdiction and venue over this action pursuant to Sections 20(b), 20(d) and 22(a) of the Securities Act [15 U.S.C. §§ 77t(b), 77t(d), 77v(a)] and Sections 209(d) and 214 of the Advisers Act [15 U.S.C. §§80b-9(d), 80b-14]. Steffelin engaged in acts and transactions in this judicial district constituting the violations and, directly or indirectly, made use of the means or instrumentalities of interstate commerce, or of the mails, or the facilities of a national securities exchange in connection with the transactions, acts, practices, and courses of business alleged herein.

DEFENDANT

9. **Edward S. Steffelin**, age 41, was a Managing Director at GSC and an unregistered investment adviser during the relevant period. Steffelin was in charge of the team that purportedly selected the collateral for Squared. Steffelin worked at GSC’s offices in New York City during the relevant period. He obtained his Series 7 and 63 licenses in March 2010 and is currently a registered representative with a broker-dealer based in Scottsdale, Arizona. Steffelin resides in New York, New York.

RELATED ENTITIES

10. **J.P. Morgan Securities** is and was the principal United States broker-dealer of J.P. Morgan Chase & Co., a global investment banking, securities, and investment management firm headquartered in New York City. J.P. Morgan Securities structured and marketed Squared.

11. **GSC** is and was a Delaware limited partnership and registered investment adviser headquartered in Florham Park, New Jersey. GSC served as collateral manager for a number of CDOs, including Squared. As of December 31, 2006, GSC had closed nine structured finance CDO transactions, had more than \$12.9 billion in structured finance assets under management, and over \$22 billion in total assets under management. GSC filed for Chapter 11 bankruptcy protection on August 31, 2010.

12. **Magnetar** is and was an asset manager headquartered in Evanston, Illinois. Magnetar hedge funds purchased the equity tranche of Squared and took the short counterparty position in over half of the assets in the Squared portfolio.

13. **Squared CDO 2007-1, Ltd. (“Squared CDO Caymans”)** was an SPV incorporated in the Cayman Islands on April 10, 2007. Squared CDO Caymans entered into a collateral management agreement with GSC, purchased the collateral of Squared at closing and issued Squared’s notes to investors.

14. **Squared CDO 2007-1, Inc. (“Squared CDO Delaware”)** was an SPV incorporated in Delaware on April 5, 2007, and served as co-issuer of Squared’s notes to investors. Squared CDO Delaware did not enter into the collateral management agreement with GSC or purchase any of Squared’s collateral.

FACTS

A. GSC’S PORTFOLIO SELECTION PROCESS FOR SQUARED

GSC Agrees to Select the Portfolio for Squared

15. On or about January 11, 2007, GSC and J.P. Morgan Securities executed an engagement letter pursuant to which J.P. Morgan Securities agreed to arrange and place a CDO

squared with an investment portfolio of primarily cash and synthetic investments in CDOs, and GSC agreed to select and manage that portfolio. Steffelin signed the engagement letter on behalf of GSC.

16. GSC was a registered investment adviser with knowledge of the domestic housing market and expertise in analyzing CDO securities. GSC promoted itself as relying upon proprietary research and modeling that included extensive quantitative and qualitative processes to select and manage CDO investment portfolios.

The Warehousing and Collateral Selection Process

17. A CDO squared is a complex, highly-leveraged structured product. Investors receive payments out of the interest and principal received on an investment portfolio of CDO securities or, where the CDO squared is synthetic, payments related to CDS referencing CDO securities (collectively, “CDO securities”). Squared was a synthetic CDO. The majority of Squared’s assets were CDS that referenced other CDOs.

18. The Squared CDO transaction followed a structure common to many CDOs sold during the relevant period. For this transaction, two SPVs (Squared CDO Caymans and Squared CDO Delaware) were created to issue notes entitling the holders to payments derived from the underlying assets held by one of the SPVs.

19. The cash flow necessary to make payments on the notes was to be generated primarily through a CDS contract referencing a pool of CDO securities that Squared CDO Caymans entered into on the closing date with a J.P. Morgan affiliate. The notes issued by the SPVs were securities with defined risk profiles determined by a hierarchical, tranching structure.

The cash flows from the investment portfolio of CDO securities were divided according to defined rights among the tranches of the CDO in a waterfall fashion.

20. The “super senior” AAA-rated tranche of Squared was at the top of the waterfall with the first right to receive principal and interest in the event of a shortfall. As a result, the super senior tranche had the highest credit quality, meaning the lowest likelihood of being affected by defaults or other credit events experienced by the underlying collateral. The lower “mezzanine” tranches were junior in priority and, therefore, carried more risk. Mezzanine investors were the first rated note holders to experience losses associated with a deterioration of the underlying collateral. Below the mezzanine tranches were the unrated subordinated notes, or equity, which were the unrated riskiest notes and the first to experience losses.

21. J.P. Morgan Securities acquired most of the CDO-related securities that would eventually form the Squared portfolio in the months prior to the closing date. The process of acquiring collateral is often referred to as “warehousing” or “ramping,” and the individual CDO-related securities or bonds are often referred to as “names.” This pre-closing process allowed CDO arrangers like J.P. Morgan Securities to acquire risk on behalf of the CDO investors that were expected to assume this risk on the closing date. During the warehousing period, J.P. Morgan Securities agreed to purchase collateral or enter into CDS contracts and to place these acquired CDO-related securities in a segregated account or “warehouse.” J.P. Morgan Securities bore the risk of loss on these assets prior to the closing date.

22. At the May 11, 2007, closing, J.P. Morgan Securities transferred the risk on the assets in the warehouse account to Squared CDO Caymans, through a CDS and through the sale

of assets. The SPVs, Squared CDO Caymans and Squared CDO Delaware, issued notes to CDO investors that were placed by J.P. Morgan Securities.

Squared Collateral Selection Process - Phase One

23. The collateral selection and warehousing processes for Squared began on or about January 12, 2007 – the day after J.P. Morgan Securities executed an engagement letter with GSC. The engagement letter provided that J.P. Morgan Securities would function as warehouse provider for Squared pursuant to a separate written agreement.

24. J.P. Morgan Securities entered into a warehouse agreement with GSC on or about February 14, 2007. Steffelin signed the warehouse agreement on behalf of GSC.

25. Between January 12 and February 7, 2007, GSC selected for the warehouse 27 names or CDO securities with a notional value of \$436.4 million. The collateral selected and placed in the J.P. Morgan Securities warehouse during this phase was selected by GSC with little or no input from Magnetar.

26. Magnetar bought protection on, or shorted, three of the selected CDO securities with a notional value of \$60 million. The short counterparties on the remaining 24 CDO securities were identified using a “bid wanted in competition” or “BWIC” process, in which lists of bonds were submitted to various brokers to solicit bids for protection on those bonds.

Steffelin’s Employment Negotiations With Magnetar

27. During the collateral selection process for Squared, from early January through late February 2007, Steffelin sought employment with Magnetar and, specifically, inquired about the possibility of starting a collateral management business for Magnetar.

28. On January 5, 2007, the employee at Magnetar primarily responsible for the firm's participation in the Squared transaction ("Magnetar Employee"), sent his supervisor an electronic mail message stating, "Steffelin wants to leave GSC and start a manager for us . . ." His supervisor replied, "Perfect," to which the Magnetar Employee responded, "I knew u'd like that!!"

29. On or about January 18, 2007, Magnetar prepared a 9-page Power Point presentation entitled "Manager of Managers." According to this presentation, Magnetar was considering establishing a network of CDO managers. The presentation represented in relevant part, "Identified potential first manager; based on: interest, apparent skill; [claimed] infrastructure."

30. On January 30, 2007, Steffelin sent an electronic mail message to the Magnetar Employee that read, "Feel[s] like times are right to start a company." Later that day, the Magnetar Employee responded to Steffelin via email, "Yes! . . . Partners committed to do it for sure . . . putting finishing touches on bus[iness] plan."

31. In early February 2007, Magnetar incorporated portions of the January 18 presentation into a 27-page power point entitled "Structured Credit Business Update."

32. On February 22, 2007, the Magnetar Employee sent his supervisor an electronic mail message with the subject line "Gsc blowing up" and the text "Ed [Steffelin] eager to get something going. We could get whole team and all deals." The Magnetar Employee's supervisor sent a reply electronic mail message asking, "Why are they blowing up?" and the Magnetar Employee explained "They've been having [a] big fight over comp[ensation]. Think

[the head of GSC's structured credit department] is going to split, rest of team not that happy at how they'll be treat[ed] if they stay. As u know, Ed [Steffelin] was already planning to leave."

33. On February 26, 2007, the Magnetar Employee sent his supervisor by electronic mail message another update, stating, "Just got off the phone w Ed [Steffelin] . . . Ed thinks whole team can be lifted, will be able to take along 5 deals currently in warehouse, makes it cash flow positive day 1."

34. Steffelin did not reach an employment agreement with Magnetar.

35. Steffelin did not disclose his employment interest in and inquiries to Magnetar to J.P. Morgan Securities, Squared CDO Caymans, or Squared CDO Delaware.

Squared Collateral Selection Process - Phase Two

36. On or about January 29, 2007, J.P. Morgan Securities executed a letter agreement with Magnetar obligating Magnetar to purchase the equity of Squared.

37. Although Magnetar committed to purchase the equity, Magnetar's short position was the motivating economic factor for Magnetar's involvement in the Squared transaction. For example, an internal January 29, 2007, Magnetar electronic mail message characterized Magnetar's equity position as "basically nothing" and explained its motivation for the equity purchase as "just doing it. . . to buy some protection."

38. By the time the deal closed in May 2007, Magnetar's \$600 million short position dwarfed its \$8.9 million equity (long) position and gave it an economic interest adverse to those of the Mezzanine Investors.

39. Shortly after executing the letter agreement, Magnetar began to play a significant role in the selection of the remaining collateral for Squared. From that point forward, Magnetar took the short positions on the vast majority of the synthetic CDO securities included in the investment portfolio.

40. Between February 8 and 23, 2007, GSC included 19 CDO securities with a notional value of \$365 million in the portfolio. Magnetar bought the protection on 18 of those CDO securities with a notional value of \$360 million. Electronic mail messages among Magnetar, GSC, and/or J.P. Morgan Securities establish Magnetar's significant involvement in the collateral selection process and Steffelin's knowledge of Magnetar's involvement and participation in that process.

41. On February 8, 2007, Magnetar informed Steffelin via an electronic mail message that "[it would] like to do a list of [securities] with [them]... if [they] have them ready." Steffelin responded by promising to "[g]et [Magnetar] ... a list shortly."

42. On February 9, 2007, Steffelin's subordinate sent Magnetar by electronic mail a list of 12 proposed CDO securities for the Squared portfolio. Steffelin was copied on this electronic mail message. Magnetar informed Steffelin that it wanted to short six of the 12 CDO securities.

43. On February 12, 2007, Steffelin asked J.P. Morgan Securities to include the six CDO securities selected by Magnetar in the warehouse for Squared. J.P. Morgan Securities approved all six trades on or about February 13, 2007. Magnetar was the short counterparty to all six CDO securities, adding \$120 million in notional value to the portfolio. The six CDO securities that Magnetar did not have an interest in shorting were neither included in the portfolio nor bid out to the market (using the customary BWIC process) to find other potential buyers.

44. On February 20, 2007, Magnetar took a short position on two more CDO securities added into the portfolio with a notional value of \$40 million; one CDO security was proposed by Magnetar, the other by GSC. J.P. Morgan Securities negotiated these trades with Magnetar rather than bidding the CDO securities out to the market.

45. Also on February 20, 2007, Steffelin's subordinate sent Magnetar by electronic mail a list of 12 additional proposed CDO securities for Squared and sought approval from J.P. Morgan Securities to include these CDO securities in the warehouse. Steffelin was copied on this electronic mail.

46. On February 23, 2007, Steffelin's subordinate informed Magnetar via electronic mail that J.P. Morgan Securities had granted warehouse approval for all 12 CDO securities listed in the February 20 message, and asked Magnetar to confirm which CDO securities it would like to take a short position on. Later that day, Magnetar replied by electronic mail and selected 10 of the 12 CDO securities. Steffelin was copied on these electronic mail messages.

47. Also on February 23, 2007, GSC included the 10 CDO securities that Magnetar selected, with a total notional value of \$200 million, into the portfolio for Squared. Magnetar was the short counterparty to all 10 of these CDO securities.

48. The two CDO securities that Magnetar did not have an interest in taking a short position on were not included in the portfolio or bid out to the market to find other potential buyers.

Squared Collateral Selection Process – Phase Three

49. On or about February 24, 2007, as a result of disruptions in the credit markets, J.P. Morgan Securities closed the warehouse for Squared, meaning it stopped acquiring collateral for the portfolio. On or about March 7, 2007, J.P. Morgan Securities' senior management requested an update on the Squared transaction. J.P. Morgan Securities' senior management received a summary of the transaction via electronic mail on or about March 8, 2007. According to that summary, the notional amount of the portfolio then being held in the warehouse was \$802 million, of which Magnetar had taken a short position on \$390 million. The summary also noted that J.P. Morgan Securities had already suffered a \$40 million mark-to-market accounting loss on the portfolio.

50. Senior management at J.P. Morgan Securities pressed the deal team responsible for the Squared CDO to avoid permanent losses on the transaction and continued to receive periodic briefings on Squared in March and April 2007. The deal team knew that the \$40 million mark-to-market accounting loss on the collateral in the warehouse could be reversed and other potentially significant losses avoided if they were able to sell the Notes and thereby transfer the collateral to an SPV at closing.

51. Magnetar continued to be significantly involved in the collateral selection process for Squared during April and early May 2007. J.P. Morgan Securities, GSC and/or Magnetar regularly exchanged lists of CDO securities for the investment portfolio and met to discuss ramping the balance of the portfolio for Squared.

52. On April 5, 2007, Steffelin's subordinate sent J.P. Morgan Securities via electronic mail a list of 31 CDO securities for warehouse approval. That list indicated that 10 of the 31

CDO securities had elicited “prelim[inary] interest from Magnetar” and four additional CDO securities were the subject of an “agreed trade with Magnetar.” Steffelin was copied on this electronic mail message.

53. On or about April 7, 2007, J.P. Morgan Securities sent Magnetar a list of 28 names for possible inclusion in the Squared portfolio. This list included at least 10 names on which Magnetar had previously decided that it did not want to take a short position. On April 7, 2007, Magnetar forwarded the list to Steffelin and noted that, “[J.P. Morgan Securities] sent us what the rest of the portfolio looks like, want to make sure you signed off on this. To be honest, I don’t love it, some recent deals I’d like to get in there are missing. Also, think they’re missing some of the trades to which we’ve already agreed. Lets discuss [sic].”

54. On April 8, 2007, in an internal electronic mail message, Magnetar characterized J.P. Morgan Securities’ list as “stupid” and explained that it needed to “use GSC to get some decent shorts off on the balance of the portfolio.” All 10 CDO securities that Magnetar had previously declined to take short positions on were excluded from the final portfolio.

55. On April 9, 2007, Steffelin and Magnetar discussed certain bonds to include in the balance of the portfolio. Later that day, Steffelin’s subordinate sent Magnetar via electronic mail a copy of a list of 30 names “discussed at our meeting this afternoon” and “highlighted the names which [Magnetar] had interest in shorting into the deal.” Steffelin was copied on this electronic mail message.

56. On April 10, 2007, J.P. Morgan Securities discussed with Magnetar certain CDO securities to include in the balance of the portfolio. Later that day, Magnetar sent J.P. Morgan Securities by electronic mail “a file that list[ed] proposed trades/backstops ... [that Magnetar

had] ... discussed with GSC which would finish out the portfolio” According to Magnetar, “[m]any of the bonds [were] still pending GSC’s internal approval. Assuming that Magnetar and GSC [were] more more-or-less on the same page, then [Magnetar] would be comfortable moving forward”

57. On April 20, 2007, Steffelin asked Magnetar via electronic mail “How was the me[e]ting with JPM.” Later that day, Magnetar replied to Steffelin via electronic mail that read in relevant part, “Fine, looks like we can price next week for sure . . . we need to finalize the portfolio.”

58. On April 17, 2007, J.P. Morgan Securities sent Steffelin a list of CDO securities, 12 of which Magnetar had agreed to take a short position on, and asked if all of the CDO securities on the list had been approved. That same day, Magnetar sent J.P. Morgan the CDO list and noted that it “looks like we [Magnetar] are shorting in \$168 million.”

59. Additional lists were exchanged between Magnetar and J.P. Morgan Securities on April 18, 2007, and an agreement was reached on the vast majority of the remaining CDO securities for the Squared portfolio. Late that afternoon, J.P. Morgan Securities sent Steffelin’s subordinate via electronic mail an updated portfolio and stated, “These are the names and levels agreed with Magnetar.” Steffelin was copied on this email. The deal priced on April 19, 2007.

60. On or about May 4, 2007, Magnetar informed Steffelin that it “need[ed] a few more bonds for Squared. [Magnetar] agreed to a few that JPM didn’t put in because they were saving room for swaps . . . Lets revive what you have approved and finish up [sic].” Steffelin responded to Magnetar via electronic mail, “Yes. I think we need one more to close a[t] 95 percent. Then we need to finalize the rest of the port[folio].”

61. In May 2007, Magnetar shorted 12 CDO securities into the portfolio with a notional value of \$183.9 million. None of these names were bid out to the market, as Magnetar was pre-identified as the buyer. The following chart summarizes the three phases of the warehousing and portfolio selection for Squared:

Phase	Total Notional Value (\$)	Total Number of Names	Magnetar Short Position (\$)	Number of Magnetar Names
I	436.4M	27	60M	3
II	365M	19	360M	18
III	293.9M	19	183.9M	12
Total	1.1B	65	603.9M	33

B. MARKETING EFFORTS FOR SQUARED FOCUSED ON GSC

62. J.P. Morgan Securities embarked upon a large scale effort to sell the mezzanine tranches of Squared in March and April 2007. Steffelin participated in these efforts by meeting with investors in person and talking with them over the phone.

63. Steffelin knew or should have known that the marketing of the Notes would be assisted if investors believed that GSC was selecting the portfolio. CDO investors and other market participants considered collateral managers to be important. The importance of the role played by collateral managers in the selection process is reflected by, among other things, reports issued by CDO analysts in early 2007.

64. A January 12, 2007, report by Morgan Stanley Fixed Income Research entitled, “CDO Market Insights, Manager Matters,” concluded that “the clear implication [of our analysis]

is that managers matter and are a major determinant of performance. Not surprisingly, manager choice is perhaps the most important decision that investors need to make.”

65. A UBS Global Fixed Income Research report, dated January 17, 2007, stated: “Painting every 2006 subprime bond the same shade of black is unfair; just as is condemning every single issue from a set of subprime issuers. Good managers may well be able to separate the good from the bad and ugly,” and “given all the signs pointing towards a rocky future in the subprime world, credit selection in and among CDOs is going to be even more important than it has been in the past couple of years.”

66. Steffelin also knew or should have known that it would have been difficult to place the Notes with investors if Magnetar’s role in the collateral selection process had been disclosed. CDO investors and other market participants considered the identity and motivation of those involved in the collateral selection process to be important factors. Standard & Poor’s, for example, on its website cautioned CDO investors to “consider who has selected the portfolio of assets and what their motivation was.”

67. J.P. Morgan Securities’ sales and marketing employees repeatedly emphasized to investors the advantages of having GSC select and manage the portfolio. The Risk Factor section of the offering circular for Squared provided in relevant part that, “the performance of the CDS Portfolio Assets and the Funded Portfolio Assets depends heavily on the Collateral Manager in analyzing, selecting and managing the CDS Portfolio Assets and the Funded Portfolio Assets. As a result, the Issuer will be highly dependent on the financial and managerial experience of the Collateral Manager and certain of its officers . . .”

68. The Mezzanine Investors were not informed that Magnetar participated actively and directly in the collateral selection process, engaging in back-and-forth negotiations with GSC, Steffelin, and J.P. Morgan Securities on names that would be included in the portfolio. Magnetar's involvement in the collateral selection process was material to investors and ultimately contributed to the negative performance of the Squared portfolio.

C. DISCLOSURES RELATING TO THE COLLATERAL SELECTION PROCESS

69. The marketing materials for Squared, including the pitch book, term sheet, and offering circular, described GSC's process for selecting the investment portfolio for Squared, but failed to disclose that Magnetar, a party with economic interests adverse to the Mezzanine investors, played a significant role in the collateral selection process.

Squared Pitch Book

70. J.P. Morgan Securities and GSC prepared the March 2007 pitch book for Squared. The pitch book was the primary marketing tool by which J.P. Morgan Securities offered to sell the Mezzanine tranches of the Squared CDO to institutional investors.

71. The pitch book stated in its "Executive Summary" that "[t]he portfolio [of the Squared CDO] will be selected and managed by GSC Group."

72. The pitch book also included an overview of GSC that described its senior management team, business strategy, expertise, credit selection process, and CDO investment approach. It also included a CDO report of a bond expected to be approved for the deal; a CDO report for a bond declined for inclusion in the deal; a summary of the performance of other portfolios managed by GSC; and background information on GSC's management team.

73. GSC prepared the portions of the pitch book relating to GSC's involvement in selecting and managing the collateral of Squared. GSC's portions of the pitch book were marked, "Source: GSC." Steffelin reviewed and edited GSC's portion of the pitch book and helped prepare certain of the GSC material including, but not limited to, a slide that described GSC's CDO investment process.

74. Steffelin knew or should have known that the pitch book would be and was used to market Squared to investors.

75. In mid-March 2007, J.P. Morgan Securities conducted an investor conference in Paris, France. Steffelin attended this conference.

76. On March 13, 2007, J.P. Morgan Securities informed Steffelin that it "would like to finalize the marketing book to generate momentum ahead of the Paris conference" and asked Steffelin to "[u]pdate GSC's [o]rganization [s]ection," "[u]pdate GSC's [t]ransaction [h]istory," "add an appendix with [statistics] on the current portfolio," and "[c]onsider adding slides that reflect on [GSC's] CDO investment/monitoring process."

77. On March 13, 2007, Steffelin's subordinate sent J.P. Morgan Securities "a recent version of [the] GSC Structured Finance Overview presentation, which [J.P. Morgan Securities] can use for the GSC section of the book." J.P. Morgan Securities then asked Steffelin's subordinate via electronic mail, "What's your view on putting together some slides on the investment process for CDOs?" Steffelin's subordinate replied, "Ed [Steffelin] and I are working on putting something together...." Steffelin was copied on these electronic mail messages.

78. On March 14, 2007, Steffelin's subordinate sent J.P. Morgan Securities several slides addressing GSC's CDO investment process, stating, "Here are the additional slides that Ed [Steffelin] and I have been working on." The subordinate further explained that she and Steffelin had contributed more information on the CDO process for the pitch book. Steffelin was copied on this electronic mail message.

79. The slides that Steffelin and his subordinate had been working on were a critical part of the pitch book relating to GSC's CDO investment approach. This portion of the pitch book discussed the model purportedly used to identify the underlying CDO assets, the CDO structure, the approval of credit, the relative value of the assets included in the portfolio, and the price discovery for the assets. Steffelin knew or should have known that the pitch book and, in particular, this portion of the pitch book, failed to disclose Magnetar's substantial involvement in the portfolio selection process.

80. Magnetar's involvement in the selection process was material information to Mezzanine Investors in the Notes.

81. Steffelin should have known that failing to disclose Magnetar's involvement in the selection process description contained in the pitch book and, in particular, GSC's portion of the document, rendered the pitch book materially misleading and operated as a fraud or deceit upon Mezzanine Investors in the Notes.

82. On March 15, 2007, Steffelin forwarded to J.P. Morgan Securities a lengthier presentation addressing GSC's methodology for selecting CDO securities, stating "[Here is a] DRAFT CDO investment write up... you may need to format a bit and if we have time to edit in the morning great."

83. On March 16, 2007, Steffelin asked J.P. Morgan Securities via electronic mail whether it was “able to use what we sent last night for [J.P. Morgan Securities’s] client.” J.P. Morgan Securities responded, “We weren’t able to use on the first meeting. We will work on it today and include [i]n the follow up material they requested.”

84. J.P. Morgan Securities provided copies of this presentation, entitled “GSC CDO Investment Process,” as a separate document to investors. Magnetar’s involvement in the process of selecting the Squared collateral was neither mentioned nor described in this document.

85. Steffelin should have known that failing to disclose Magnetar’s involvement in the selection process made the presentation materially misleading and operated as a fraud or deceit upon Mezzanine Investors in the Notes.

Squared Collateral Management Agreement

86. As was customary, two SPVs were formed to issue the Notes to the Squared investors. One SPV was based in the Cayman Islands, and a co-issuer was based in Delaware. These SPVs were GSC’s prospective clients throughout the asset selection process and were described as such in the engagement letter, warehousing agreement, and preliminary offering circular.

87. When the deal closed on May 11, 2007, Steffelin executed a collateral management agreement with the Squared CDO Caymans, pursuant to which GSC was appointed the Squared CDO Caymans’ investment advisor and agreed to select and manage the investment portfolio. (As CDO Squared Delaware did not purchase collateral, it was not a party to this agreement.) GSC agreed to perform its obligations as an investment adviser with reasonable care and in good faith.

88. GSC served as investment advisor to Squared CDO Caymans, which issued the Notes to the Squared CDO's Mezzanine Investors. GSC and Steffelin, as the head of the GSC team that purportedly selected the assets for the portfolio, owed a fiduciary duty to the SPVs that included an obligation to disclose all material facts fully and fairly. GSC and Steffelin had an affirmative obligation to act with reasonable care and in good faith to avoid misleading the SPVs about the process by which GSC selected the portfolio. They also had an affirmative obligation to inform the SPVs about Steffelin's employment interest in Magnetar, the undisclosed third party that played a substantial role in selecting the CDO portfolio.

89. GSC and Steffelin failed to disclose material facts concerning Magnetar's involvement in the collateral selection process and Steffelin's employment negotiations with Magnetar during the selection process either to Squared CDO Caymans or to Squared CDO Delaware, the SPVs that issued the Notes.

90. Steffelin knew or should have known that these material facts were not disclosed to either of the SPVs that issued the Notes.

91. GSC's and Steffelin's failure to disclose these material facts operated as a fraud or deceit upon their SPV clients and prospective clients.

D. OFFER AND SALE OF THE NOTES TO MEZZANINE INVESTORS

92. J.P. Morgan Securities offered the Notes to certain Mezzanine Investors from New York, New York.

93. J.P. Morgan Securities in New York, directly or indirectly, provided each Mezzanine Investor with marketing materials, including a term sheet, pitch book, and/or offering

circular, that represented that GSC selected Squared's investment portfolio. Those representations were materially misleading because, unbeknownst to the Mezzanine Investors, Magnetar, a party with economic interests adverse to investors, played a significant role in the selection of the investment portfolio.

94. Potential investors located in the United States received the pitch book and offering memorandum from J.P. Morgan Securities offices in the United States, either in New York or elsewhere in the country. Potential investors located overseas typically received the pitch book and offering memorandum from J.P. Morgan Securities offices located overseas.

95. The New York office of J.P. Morgan Securities led and coordinated the global sales effort for Squared. The New York office established pricing guidelines, provided analysis and follow-up information requested by potential investors, and monitored the progress of the sales effort.

96. J.P. Morgan Securities, which is based in New York, New York, served as the placement agent for the sale of the Notes. In that capacity, it agreed to place the Notes with the Mezzanine Investors on behalf of the SPVs. At the transaction closing, which was held on May 11, 2007, at the the law firm of Allen & Overy in New York, New York, J.P. Morgan Securities purchased the Notes from the SPVs. J.P. Morgan simultaneously made payment for the Notes to the trustee for the SPVs. The trustee was also based in New York, New York.

97. The sale of the Notes to certain Mezzanine Investors took place in New York, New York.

98. The delivery of the Notes from J.P. Morgan Securities to the Mezzanine Investors took place either the day of closing or within a few days afterward. In the case of 12 of the 15 Mezzanine Investors, the Notes were delivered directly from J.P. Morgan Securities in the United States to the investors. The delivery was made in book entry form through the Depository Trust Corporation in New York, New York. The confirmations on these 12 sales listed J.P. Morgan Securities as the selling party. The address listed for J.P. Morgan Securities on the confirmations was the firm's Confirmations Processing department at 500 Stanton Christiana Road, Newark, Delaware, 19713-2107.

99. The payment for the Notes from the Mezzanine Investors was made, directly or indirectly, to J.P. Morgan Securities in the United States.

E. SQUARED'S MEZZANINE INVESTORS

100. J.P. Morgan Securities sold Notes with a par value of \$150 million to the Mezzanine Investors, a group of approximately 15 institutional investors including seven located in the United States and eight located overseas. The Mezzanine Investors actually paid \$145.8 million after pricing discounts. The Mezzanine Investors lost most, if not all, their principal when their Notes became nearly worthless months after closing.

101. Mezzanine Investors would have considered it important to their investment decision to have known that the equity investor in Squared had shorted approximately half of the investment portfolio and played a significant role in the collateral selection process.

102. The seven United States Mezzanine Investors in Squared were Thrivent Financial for Lutherans, a Minneapolis, Minnesota.-based, not-for-profit life insurance organization (\$10 million notional); General Motors Asset Management, a New York City-based asset manager for

General Motors' pension plans (\$10 million notional); Security Benefit Corporation, a Topeka, Kansas-based provider of insurance and retirement products (\$12 million notional); Moneygram International Inc., a Minneapolis, Minnesota-based provider of global money transfer and bill payment services (\$15 million notional); Fifth Third Asset Management Inc., a Cincinnati, Ohio-based investment advisor and mutual fund company (\$4 million notional); Morgan Asset Management Inc., the Birmingham, Alabama-based asset management unit of broker-dealer Morgan & Keegan Co. (\$6 million notional); and Dillon Read Finance L.P., a New York City-based affiliate of a hedge fund unit within UBS known as Dillon Read Capital Management (\$20 million notional).

103. The eight overseas Mezzanine Investors were two Taiwanese life insurance companies, Far Glory Life Insurance Company Ltd. (\$5 million notional) and Taiwan Life Insurance Company Ltd. (\$3 million notional); three banks, Paris-based Caisse D'Epargne (\$20 million notional), Tokyo-based Tokyo Star Bank (\$8 million notional) and Singapore-based United Overseas Bank (\$13 million notional); two asset managers, Hong Kong-based East Asia Asset Management Ltd. (\$1 million notional) and Tel Aviv-based Leader Capital Markets Ltd. (\$2 million notional); and Sydney-based hedge fund, Basis Pac-Rim Opportunity Fund (\$10 million notional).

CLAIMS FOR RELIEF

FIRST CLAIM

Sections 17(a)(2) and (3) of the Securities Act

104. Paragraphs 1-103 are realleged and incorporated herein by reference.

105. As set forth above, Steffelin, in the offer or sale of securities or security-based swap agreements, by the use of the means or instruments of interstate commerce or by the mails, directly or indirectly, obtained money or property by means of untrue statements of material facts or omissions of material facts necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, and engaged in transactions, practices or courses of business which operated or would operate as a fraud or deceit upon purchasers of securities, in violation of Section 17(a)(2) and (3) of the Securities Act [15 U.S.C. § 77q(a)(2) & (3)].

SECOND CLAIM

Section 206(2) of the Advisers Act

106. Paragraphs 1-105 are realleged and incorporated herein by reference.

107. As set forth above, Steffelin, by use of the mails or means or instrumentalities of interstate commerce, directly or indirectly, engaged in a transaction, practice, or course of business which operated as a fraud or deceit upon any client or prospective client, in violation of Section 206(2) of the Advisers Act [15 U.S.C. §80b-6(2)].

PRAYER FOR RELIEF

WHEREFORE, the Commission respectfully requests that this Court enter a judgment:

A. Permanently restraining and enjoining Steffelin from violating Sections 17(a)(2) and (3) of the Securities Act of 1933 [15 U.S.C. §77q(a)(2) and (3)] and Section 206(2) of the Advisers Act [15 U.S.C. §80b-6(1) and (2)];

B. Ordering Steffelin to disgorge all profits that he obtained as a result of its conduct, acts, or courses of conduct described in this Complaint, and to pay prejudgment interest thereon;

C. Ordering Steffelin to pay civil monetary penalties pursuant to Section 20(d)(2) of the Securities Act [15 U.S.C. § 77t (d)(2)] and Section 209(d) of the Advisers Act [15 U.S.C. §80b-9(b)]; and

D. Granting such equitable relief as may be appropriate or necessary for the benefit of investors pursuant to Section 21(d)(5) of the Exchange Act [15 U.S.C. § 77u (d)(5)].

Dated: Washington, D.C.
June ____, 2011

Respectfully submitted,

	<p>Kenneth Lench Reid A. Muoio (RM-2274) Jason Anthony Carolyn Kurr Jeffrey Leasure Brent Mitchell</p> <p>Jan M. Folena Robert I. Dodge</p> <p>Attorneys for Plaintiff Securities and Exchange Commission 100 F St., NE Washington, D.C. 20549-4010 (202)551-4738 (Folena) folenaj@sec.gov (202) 551-4421 (Dodge) dodger@sec.gov</p>
--	--