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12	SUPERIOR COURT OF THE STATE OF CALIFORNIA		
13	COUNTY OF	SAN DIEGO	
14	CITY OF SAN DIEGO, a municipal corporation,) Case No.:	
15	Distractor) COMPLAINT FOR	
16	Plaintiff,	(1) PROFESSIONAL NEGLIGENCE	
17	VS.	(2) BREACH OF FIDICUARY DUTIES;	
18	ORRICK HERRINGTON & SUTCLIFFE, a California corporation CALDERON, JAHAM & OSBORN, a	(3) BREACH OF CONTRACT; (4) AND MONEY HAD AND	
19	California corporation; CAPORICCI & LARSON, an entity of) RECEIVED	
20	unknown qualification; WEBSTER & ANDERSON, an entity of) (EXEMPT FROM FILING FEES) PURSUANT TO GOVERNMENT CODE	
21	unknown qualification; and DOES 1 through 25, inclusive,	SECTION 6103)	
22	Defendants.	(GENERAL CIVIL CASE – DAMAGES	
23	2 of official to 1	EXCEED \$25,000)	
24		Jury Trial Requested	
25		,	
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27			
28			

Complaint

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	Complaint

1	Plaintiff, CITY OF SAN DIEGO ("the City"), alleges through its counsel of record as
2	follows:
3	I.
4	VENUE AND JURISDICTION
5	1. Venue is proper in this Court because the events and injuries complained of in
6	this Complaint occurred in the City and County of San Diego.
7	2. The amount in controversy under this Complaint exceeds the minimal
8	jurisdictional limit of this Court, and the claims asserted in this Complaint are within the
9	subject-matter jurisdiction of this Court.
10	II.
11	OVERVIEW
12	3. From 1996 to 2003, the City raised approximately one billion dollars on the
13	basis of bond offerings. To raise this money, the City hired outside professionals—high priced
14	lawyers and accountants who specialize in fulfilling municipal disclosure obligations—to
15	ensure that the City's financial condition was accurately disclosed to investors who bought the
16	City's bonds.
17	4. This Complaint explains how it is that the City's bond lawyer and outside
18	auditor caused the City to raise hundreds of millions of dollars on the basis of bond offerings
19	that contained false and inaccurate information regarding the City's municipal pension
20	system, San Diego City Employees' Retirement System ("SDCERS").
21	5. These same outside professionals approved the distribution to the investing
22	public annual financial reports for the City that similarly misrepresented the SDCERS funding
23	shortfall.
24	6. As will be explained, the City's disclosure since 1996 failed to provide
25	investors and other interested readers with adequate information to enable them to understand
26	clearly a variety of negative developments affecting SDCERS, which, in turn, left them with
27	insufficient information to evaluate fully the creditworthiness of the City. All of the
28	professionals named in this suit knew since 1996, but certainly not later than 2000, that the

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City was under funding SDCERS and knew, or should have known, that their own work products failed to admit it.

- 7. For seven straight years, the public disclosure documents these professionals approved and circulated—investment disclosures and annual statements—did not disclose the City's pension funding shortfall and even proclaimed that the law disallowed the very funding shortfalls that they knew to be occurring.
- 8. It was not until September 2003, that someone unconnected with the City's disclosure process discovered that a City fund raising document that was only days from hitting the municipal securities market contained erroneous and outdated (and significantly false) pension information. Reading a City document on her own time at her home, SDCERS Trustee Diann Shipione discovered that the City's investment documents scheduled to become public the next business day claimed falsely that the SDCERS actuary thought favorably, and hoped to gain government approval, of the City's method of avoiding actuarily required contributions. These statements were false, as the actuary had abandoned any hope that the method of reporting pension under funding as somehow acceptable would be approved. Ms. Shipione knew this, as would anyone familiar with the City's pension system.
- 9. As the Complaint will explain, Ms. Shipione set in motion a series of events on a Friday afternoon that exposed the false representations in the soon-to-be public offering (which was only one of the false statements in the offering, and many years' prior offerings). It was only then that the City's professionals finally acted to correct, and, then, to postpone, and, finally, to withdraw the offering that they were making on the City's behalf.
- 10. As will be explained, the professionals possessed for many years all the information one would need (certainly more than Ms. Shipione had at her home) to know that the disclosures regarding the status of the City's pension system were false. Yet, it was only after Ms. Shipione raised the serious misstatements in the investment documents that the professionals acted, and then in a self-serving way that suited their interests, not the City's.
- 11. In 2004, the same professionals who had for many years drafted and approved disclosures containing the same false claims crafted a mea culpa for the City to make, which it

did reluctantly. Specifically, in January 2004, and later in March 2004, the professionals prepared and then released "voluntary disclosures" in which the City acknowledged its history of under funding the pension system and the effect it would have on the City's future capacity to service its debt and repay the bonds.

- 12. As they were preparing the City's "voluntary disclosures," the professionals made no disclosures to the client or the public of their own failures. Aware as they were of cases holding lawyers and accountants liable for their role in drafting and circulating false and fraudulent securities offerings, the professionals acted in a manner that would ensure that the City would bear the brunt of the penalty for the years of disclosure errors.
- 13. Since then, the City has indeed paid a heavy price for the corrections it made in January 2004.
 - Nearly two years later, the City still cannot issue new debt securities and cannot refinance its current obligations to obtain market rates, as the City remains stranded without a credit rating (in the case of Standard & Poor's) or with a rating that is too low to gain access to capital markets. This means that the City is unable to undertake public debt to do the things that cities do: fix roads, replace sewers and build fire stations. The delay alone costs the city at least \$1 million a month in missed opportunities. For example, for every month that the city sits on the market sidelines it cannot refinance the rates on the ballpark bonds it had planned to rework at a savings of more than \$280,000 a month in debt payments.
 - The professionals' failure to explain and to account for their failures could have already done the City damage with the U.S. Securities and Exchange Commission ("SEC"), which is investigating the City's disclosures. The SEC uses an entity's cooperation level as a key benchmark in choosing the fines and sanctions it levies against entities. Precedent shows that those who follow the SEC's cooperation guidelines are spared and those who don't are fined heavily. Clearly, an explanation by the professionals that *they* failed to perform their professional duties in compliance with the standard of care would be of major assistance to the City with the SEC.
 - The City has paid at least \$18 million (in just the last 18 months) to teams of consultants and attorneys who have picked up where these professionals left off. KPMG, the City's new auditor, has charged the City more than \$2.6 million on its audit of the City's 2003 financial statements, and estimates that its work will cost the City another \$121,000 a month. One set of lawyers, Vinson & Elkins ("V&E"), billed the City \$6.2 million for work that was rejected both by the auditor and the

1	SEC. An audit committee, headed by former SEC chief Arthur Levitt of Kroll, Inc., bills the City \$800,000 a month to		
2	perform the independent investigation originally assigned to V&E for KPMG's use.		
3	Meanwhile, there remains an uncertain legal exposure to		
5	holders of bonds issued by the City, which, fortunately, continue to receive the principal and interest owed to them on their bonds.		
6	14. Meanwhile, as the City has been paying the heavy price for the errors in its		
7	disclosures, which includes making substantial remediation (see sections II(C)(3) and II(F)),		
8	the professionals who helped cause the problem have moved on. In the case of the law firm		
9	Orrick Herrington & Sutcliffe ("Orrick"), it has gone so far as to <i>refuse</i> to help the City by		
10	sharing the results of an Internal Investigation it commenced in February 2004. According to		
11	Orrick, the City's lawyer, the City cannot have the potentially exonerative information Orrick		
12	has uncovered because the information is <i>privileged</i> from disclosure to the City.		
13	III.		
14	BACKGROUND		
1.			
15 16	A. The Critical Role of the City's Outside Experts in Ensuring Truthful and Accurate Disclosures In The City's Bond Offerings And Public Disclosures		
16 17			
16	Accurate Disclosures In The City's Bond Offerings And Public Disclosures		
16 17	Accurate Disclosures In The City's Bond Offerings And Public Disclosures 15. A bond is a security that embodies a financial obligation between an issuer (in		
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1	1997 Disclosures	
2	Bond Offerings	
3	1. \$82,000,000 City of San Diego, California 1997-98 Tax	
4	Anticipation Notes Series A.	
5	Annual Reports	
6	Continuing Disclosure Certificate (Taxable Lease Revenue)	
7	Bonds, Series 1996A).	
8	2. Continuing Disclosure Certificate (Series 1996B Refunding	
9	Certificate of Participation).	
10	3. The City CAFR for FY 1996.	
11	1998 Disclosures	
12	Bond Offerings	
13	1. \$88,500,000 City of San Diego, California 1998-99 Tax	
14	Anticipation Notes Series A.	
15	2. \$205,000,000 Convention Center Expansion Facilities	
16	Authority Lease Revenue Bonds Series 1998A (City of San	
17	Diego, California, as Lessee).	
18	Annual Reports	
19	1. Continuing Disclosure Certificate (Series 1996B Refunding	
20	Certificates of Participation.	
21	2. Continuing Disclosure Certificate (Series 1996A Refunding	
22	Certificates of Participation.	
23	3. Continuing Disclosure Certificate Taxable Lease Revenue	
24	Bonds Series 1996A	
25	4. City CAFR for FY 1997.	
26		
27		

1	1999 Disclosures
2	Bond Offerings
3	1. \$99,500,000 City of San Diego, California 1999-00 Tax
4	Anticipation Notes Series A.
5	Annual Reports
6	1. Continuing Disclosure Certificate (Certificates of
7	Participation 1996A).
8	2. Continuing Disclosure Certificate (1996B Refunding
9	Certificates of Participation.
10	3. Continuing Disclosure Certificate (Taxable Lease Revenue
11	Bonds Series 1996A).
12	4. Convention Center Expansion Authority Lease Revenue
13	Bonds, Series 1998A.
14	5. City CAFR for FY 1998.
15	2000 Disclosures
16	Bond Offerings
17	1. \$53,000,000 City of San Diego, California 2000-01 Tax
18	Anticipation Notes Series A.
19	2. \$24,000,000 City of San Diego, California 2000-01 Tax
20	Anticipation Notes Series B.
21	Annual Reports
22	1. Continuing Disclosure Certificate (Certificate of
23	Participation Series 1996A).
24	2. Continuing Disclosure Certificate (Refunding Certificate of
25	Participation, Series 1996B).
26	3. Continuing Disclosure Certificate (Taxable Lease Revenue
27	Bonds, Series 1996A).
28	

1	4. Continuin	g Disclosure Certificate (Convention Center
2	Expansion	Financing Authority Lease Revenue Bonds,
3	Series 199	98A).
4	5. City CAF	R for FY 1999.
5	2001 Disclosures	
6	Bond Offerings	
7	1. \$73,000,0	00 City of San Diego, California 2001-02 Tax
8	Anticipati	on Notes Series A.
9	Annual Reports	
10	1. Continuin	g Disclosure Certificate (Certificate of
11	Participat	on Series 1996A).
12	2. Continuin	g Disclosure Certificate (Refunding Certificate of
13	Participat	on, Series 1996B).
14	3. Continuin	g Disclosure Certificate (Taxable Lease Revenue
15	Bonds, Se	ries 1996A).
16	4. City CAF	R for FY 2000.
17	2002 Disclosures	
18	Bond Offerings	
19	1. \$169,685,	000 Public Facilities Financing Authority of the
20	City of Sa	n Diego Lease Revenue Bonds Series 2002
21	(Ballpark)	
22	2. \$93,200,0	00 City of San Diego, California 2002-03 Tax
23	Anticipati	on Notes Series A.
24	3. \$25,070,0	00 Public Facilities Financing Authority of the
25	City of Sa	n Diego Lease Revenue Bonds Series 2002B
26	(Fire and	Safety Project).
27		

1	Annual Reports
2	Continuing Disclosure Certificate (Certificate of
3	Participation Series 1996A).
4	2. Continuing Disclosure Certificate (Refunding Certificate of
5	Participation, Series 1996B).
6	3. Continuing Disclosure Certificate (Taxable Lease Revenue
7	Bonds, Series 1996A).
8	4. City CAFR for FY 2001.
9	2003 Disclosures
10	Bond Offerings
11	1. \$15,255,000 San Diego Old Town Light Rail Transit
12	Extension Refunding Bonds
13	2. \$17,425,000 1993 Balboa Park/Mission Bay Park
14	Refunding Bonds
15	3. \$110,900,000 2003-2004 Tax and Revenue Anticipation
16	Notes.
17	All of these offering contained false and misleading information regarding
18	the City's pension system, and specifically the adverse developments which
19	reflected negatively on SDCERS' financial health.
20	2. The financial information that was part of the City's bond offerings and public disclosures from 1996 to 2003
21	unu public disclosures from 1770 to 2005
22	22. The City's financial information accompanying a bond offering is included in
23	an Official Statement. That Statement will contain a variety of appendices, including an
24	Appendix A, which covers many of the significant financial policies of the City, and an
25	Appendix B, which contains portions of the City's financial statements. The information
26	contained in these appendices should have contained all relevant information necessary for
27	investors to evaluate the City's financial health, including the City's general fund's financial
28	strength relative to the increasing pension and other costs.

1	31.	Readers of the 2003 SDCERS CAFR similarly found a description of the
2	modifications	s to City funding of SDCERS adopted by the City on November 18, 2002, as part
3	of what becan	me known as "Manager's Proposal 2" ("MP2").
4		b) The CJO-prepared <i>City</i> CAFR footnotes <i>did not</i> adequately disclose the City's pension funding shortfall
5		disclose the City's pension funding shortian
6	32.	At the same time it was disclosing the City's pension funding shortfalls in the
7	SDCERS CA	FRs, CJO failed to make comparable disclosures in the City's CAFRs. It its City
8	work product	t, CJO instead included inaccurate narrative descriptions of MP1 that distorted
9	and misrepres	sented its effect. As for MP2, CJO simply ignored it.
10		(1) 1997
11	32.	The City's 1997 CAFR described the funding of the City's pension obligations
12	as follows:	
13		SDCERS' funding policy provides for periodic employer
14		contributions at actuarially determined rates that, expressed as percentages of annual covered payroll, are designed to accumulate
15		sufficient assets to pay benefits when due. The normal cost and actuarial accrued liability are determined using the projected unit credit actuarial funding method. Unfunded actuarial accrued
16		liabilities are being amortized as a level percent of payroll over a
17		period of 30 years (25 years remaining) The City and the District contribute a portion of the employees' share and the
18		remaining amount necessary to fund the system based on an actuarial valuation at the end of the preceding year under the
19		projected unit credit method of actuarial valuation
20	33.	The CJO-prepared 1997 City CAFR footnotes contain at least the following
21	errors:	
22	1.	CJO failed to mention the significant changes to the funding policy resulting from MP1. ⁶
23	2	
24	2.	CJO described the City's SDCERS funding policy in terms that were inaccurate for that fiscal year. Specifically, that year the City
25	⁶ Appendix A	to the City's Official Statements also failed to disclose the effects of MP1,
26	_	d: "State legislation requires the City to contribute to SDCERS at rates y actuarial valuation." This statement is misleading, as it suggests falsely that
27	the City was	contributing at actuarially determined rates. This misstatement occurred in the al Statements until 2003.
28	City & Officia	ai Statements until 2003.

had ceased contributing to SDCERS on an actuarially determined basis, having substituted the agreed-to rates of MP1. Yet, CJO reported that "[t]here is no Net Pension Obligation at year end as Actuarially Required Contributions and Contributions Made have always been identical during [fiscal years 1995 through 1997]." This statement was false. At the time, the City's funding shortfall, called a net pension obligation (NPO) for that fiscal year of \$5.975 *million*.

3. CJO mischaracterized the amortization of the City's long-term liability to the retirement system (the UAAL). Although the City did, in fact, use a closed 30-year period to calculate the component of its annual contribution to SDCERS reflecting the UAAL amortization, it used a different and longer period for calculating UAAL for *reporting purposes*.

(2) 1998 – 2002

34. In 1998, CJO for the first time addressed the changes wrought by 1996's MP1. In the pension footnote in the 1998 CAFR, in language carried forward into many later disclosure documents, CJO reported:

In 1996 the City Council approved proposed changes to the [SDCERS], which included changes to retiree health insurance, plan benefits, employer contribution rates and system reserves. The proposal included a provision to assure the funding level of the system would not drop below a level the Board's actuary deems reasonable in order to protect the financial integrity of the SDCERS. A citizen required vote on the changes related to retiree health insurance passed overwhelmingly in 1996. In 1997 the active members of the SDCERS voted and approved the changes. Portions of the proposal requiring SDCERS Board approval (employer rates and reserves) were approved after review and approval by its independent fiduciary counsel and consultation with the actuary. The San Diego Municipal Code was then amended to reflect the changes.

The changes provide the employer contribution rates be "ramped up" to the actuarially recommended rate in .50 percent increments over a ten year period. At such time it was projected that the Projected Unit Credit (PUC) and Entry Age Normal (EAN) rates would be equal and the SDCERS would convert to EAN. The actuary calculated the present value of the difference between the employer contribution rate and actuarial rates over the ten-year period and this amount was funded in a reserve. This 'Corridor' funding method is unique to the SDCERS and therefore is not one of the six funding methods formally sanctioned . . . for expending purposes. As a result for June 30, 1998, the actuary rates are reported to be \$5,975,0000 more than paid by the City which, technically per GASB 27, effective for periods beginning after June 15, 1997, is to be reported as a [NPO] even though the shortfall is funded in a reserve. The actuary believes the Corridor funding method is an excellent method for the City and that it will

1 2		be superior to the PUC funding method. The actuary is in the process of requesting the GASB to adopt the Corridor funding method as an approved expending method, which would then
		eliminate any reported NPO. ⁷
3	25	
4	35.	The CJO-prepared 1998 City CAFR footnotes contain at least the following
5	errors:	
6	1.	CJO dismissed the pension funding shortfall as a technical accounting matter with no practical significance because it is
7		purportedly "funded in a reserve." This purported "reserve," however, was non-existent; there simply was no such fund.
8	2.	CJO failed to describe MP1 for what it was—a form of
9		contribution relief obtained by the City in exchange for various pension benefit enhancements, the cost of which would not be
10		reflected in the City's contribution rates for many years.
11	3.	CJO failed to disclose that SDCERS' earnings were being committed to a variety of uses not associated with supporting its
12		long-term financial strength. While it is conceivable a reader could glean that a funding shortfall is an expected result of this
13		agreement, but there is no disclosure that it was anticipated to be in excess of \$100 million over a ten-year period.
14	4.	• •
15	4.	CJO failed to discuss the factors that could cause the actuary's projections to be inaccurate and the implications for the soundness of the system should that prove the case.
16	5.	CJO reflected the funding shortfall as an accounting technicality,
17		likely to disappear once Government Accounting Standards Board ("GASB") recognized the utility of the "corridor funding method."
18 19		There was no basis for CJO to suggest that GASB was likely to adopt the actuary's "corridor funding" scheme, that would simply cause the funding shortfall to <i>disappear</i> . (Later, the actuary simply
20		gave up; GASB never approved the funding (really <i>under</i> funding) method.
21	6.	CJO recited the NPO balance as \$5.975 million. That was the NPO
22		balance for the <i>previous</i> fiscal year that CJO had incorrectly reported as non-existent. By June 30, 1998, as disclosed in the
23		1998 CAFR, the balance was approximately \$16 million.
24	As explained	below, the reliance on stale data would become a recurrent them in
25	CJO's work p	product.
26	7.	CJO described the trigger provision as if it were a benefit, rather than a risk. It referred to a "provision to assure the funding level
27		of the system would not drop below a level the Board's actuary
28	⁷ The last sen	ntence was omitted from the 2002 City CAFR.

1					
1	deems reasonable." This suggests that the trigger was a valuable				
2	new <i>safeguard</i> implemented at the actuary's request. In fact, it was an attempt to <i>limit</i> the additional risks to SDCERS' fiscal soundness resulting from MP1.				
3					
4		the trigger provision could result in an enormous lump-sum payment from the City to SDCERS. In short, the text of the			
5		footnote minimizes rather than fully discloses the risks inherent in MP1.			
6	9.	CJO described the amendment to the San Diego Municipal Code as			
7	<i>)</i> .	having occurred to reflect the changes in the City's relationship to SDCERS brought by MP1. The Municipal Code was indeed			
8		amended to reflect the new benefits granted at the time of MP1, as well as the new mechanism for funding the retiree healthcare			
9		benefit. However, the Municipal Code was never amended to permit a departure from actuarial funding, as CJO suggests. It is			
10		difficult to discern why CJO thought its suggestion might be correct, as Appendix A to the City's Official Statements			
11 12		unequivocally declared that "State legislation requires the City to contribute to SDCERS at rates determined by actuarial valuation." Nowhere did CIO account for what the decument elaimed the law			
13		Nowhere did CJO account for what the document <i>claimed</i> the law to be, or how MP1 supposedly complied with it.			
14	36.	CJO would blithely carry forward substantially all of these errors, and many			
15					
	others, into and through the City's 2002 CAFR.				
16 17		2. A Comedy of Errors: The Public Disclosures Defendants Drafted And Circulated from 1996 to 2003 Contained Other Material Misstatements and Omissions			
18	37.	It does appear that a reasonable investor would have wanted information about			
19	the benefit improvements contained in MP1. Yet, this was not the only error in Defendants'				
20	disclosures. Those who have investigated the issue (V&E and the City Attorney), have				
21	concluded that there were numerous additional failures. ⁸ As explained below, it was because				
22	of Defendants' negligence that the erroneous disclosures were drafted and circulated.				
23					
24	8 751				
25	⁸ Those reports differ considerably regarding the relative degrees of culpability of the Mayor, the City Council, and various City officials and employees. The V&E report is flawed in				
26	many respects, including its apparent lack of independence. Although the V&E report appears to be a work of advocacy—as is evidenced by its consistent indulgence of favorable inferences for those whom it was supposedly investigating—its conclusion that the disclosures in the City's disclosure documents were materially false is unassailable.				
27					
28	disclosures III	the City is discressive documents were materially raise is unassanable.			

as. In July 1998 the City's Employee's Retirement System was sued by four retirees ("the *Corbett* litigation") challenging the method by which their retirement pay was calculated. The matter was subsequently certified as a class action, joining all active and eligible retired City employees. The City entered into mediation with the class employees and a settlement was reached in May 2000. The results of the settlement committed surplus earnings to increase payments to retirees, as well as increasing benefits for future retirees thereby increasing the pension system's total liabilities. The Official Statements beginning with the issuance of the \$205,000,000 Convention Center Expansion Facilities Authority Lease Revenue Bonds Series 1998A to the April 5, 2000, Annual Reports do not mention the *Corbett* litigation or the exposure to the City if the *Corbett* litigation was determined adversely to the City. The *Corbett* litigation would have been relevant to investors in the City bonds as it would have indicated current and future additional costs with respect to the City's pension system, and the failure to include such information rendered the City's Official Statements over this period materially misleading.

- b) Various disclosures, including those made relative to the Ballpark financing, included stale information regarding the pension funding shortfall and decreasing funding ratios
- 39. On February 12, 2002, the SDCERS actuary issued its report for fiscal year 2001, which reflected an experience loss of \$193.2 million. The report indicated that half of the loss could be attributed to investment losses, and indicated that investment losses would be larger in subsequent years without significant improvements in investment earnings. Also the report indicated that the City's funding practices for the retirement system would foster additional declines in the funded ratio in the absence of healthier investment returns. Two days later, on February 14, 2002, the City issued \$169,685,000 Public Facilities Financing Authority of the City of San Diego Lease Revenue Bonds Series 2002 (Ballpark Bonds). On June 4, 2002, the City issued \$93,200,000 of its Tax and Revenue Anticipation Notes Series A (2002 TRANS). On June 12, 2002 the City issued \$25,070,000 Public Facilities Financing

Authority of the City of San Diego Lease Revenue Bonds Series 2002B (Fire and Safety Project).

- 40. In all of these offerings, the discussion of the financial condition of the pension system was substantially the same. In each case, the offering documents contained two year old information about the funding of the retirement system dated as of June 30, 2000, which showed a funded ratio of 97 percent. However a draft valuation report had been circulated within the City by no later than February 12, 2002, showing that the funded ratio had declined to approximately 89.9 percent. The failure to disclose this information rendered the City's public disclosures during Fiscal 2002 materially misleading.
- 41. Under the securities laws, issuers are required to provide the market information that, taken as a whole, represents a fair and accurate picture of the issuer's financial situation. The City's 2002 disclosure did not accurately disclose certain risks to the City's pension system that would be material to a reasonable investor. The SEC has previously taken the position that a municipal issuer is required to disclose information concerning material financial reversals, even if they cannot be estimated with precision. In the order relating to the Massachusetts Turnpike, the SEC stated:

At the time of these offerings, the project staff had projected cost increases exceeding \$1 billion, which should have been disclosed to the public, including bondholders, underwriters, and credit rating agencies in connection with the bond offerings. However, because the cost increases had not been fully quantified or confirmed, the Respondents deemed them to be speculative and did not disclose them. Instead, beginning in the spring of 1999, the Project staff embarked upon an effort to quantify and confirm the specific amount of any cost increases, including a "bottom-up" review of every Project contract . . . their failure to disclose such cost increases did not take into account their obligations under the federal securities laws. By their negligent conduct, the Turnpike Authority committed . . . violations of section 17(a)(2) and (3) of the Securities Act.

Massachusetts Turnpike Authority, Securities Act Rel. No. 8260 at 361.

27

Complaint

1	2. Orrick had a secret: It too could be liable—for both malpractice and securities fraud—for its role in the previous offerings			
2				
3	60. At this point, Orrick knew and understood that it had a major problem on its			
4	hands. It knew and understood the grave importance of the misstatements (which Orrick had			
5	circulated year after year in previous offerings). As "expert" municipal securities attorneys,			
6	Orrick knew that it faced securities fraud liability and malpractice liability according to at			
7	least the following principles:			
8	• Attorneys drafting offering documents face <i>direct liability</i> under			
9	section 10(b) for misstatements and omissions in the offering documents. Securities lawyers owe their clients duties of care			
10	and loyalty, just as any other lawyer owes his client. If the client becomes liable to investors for damages arising from			
11	misrepresentations or omissions made in connection with a securities offering, the attorney may be liable for failing to prevent			
12	the deficient disclosure. 11			
13	 Attorneys involved in the placement of securities are even charged with an independent duty to investigate the offering materials: 			
14	"An important duty of securities counsel is to make a 'reasonable, independent investigation to detect and correct false or misleading materials." ¹²			
15				
16	 Securities lawyers, like all attorneys, owe a duty of care to their clients to avoid malpractice.¹³ 			
17	61. Perhaps unknown to these Orrick lawyers, however, was the principle that a			
18	professional who conceals his mistakes from his client creates new problems for himself.			
19	First, concealment of a material fact by the fiduciary is a basis for actionable fraud. 14 Second,			
20	willful concealment prevents the statute of limitations from running, which commences only			
21	upon "discovery". 15 Whether they knew their duties or not, Orrick's lawyers <i>never</i> told the			
22				
23	See, e.g., Employers Ins. Of Wausau v. Musick, Peeler & Garrett (S.D. Cal. 1994) 871			
24	F.Supp. 381, 388-89. 11 See, e.g., FDIC v. O'Melveny & Meyers (9 th Cir. 1992) 969 F.2d 744, 748-50, reversed on			
25	other grounds (1994) 512 U.S. 79.			
26	FDIC v. O'Melveny & Meyers (9 th Cir. 1992) 969 F.2d at 748-50. Rutter Group, California Practice Guide, Professional Responsibility (2005) section 6:270			
27	at 6-53. Moe v. Transamerica Title Insurance Co. (1971) 21 Cal.App.3d 289, 306. Rutter Group, California Practice Guide, Professional Responsibility (2005) section 6:389			
28	01.6.75			

City that Orrick failed its responsibilities as bond counsel to ensure that seven years of bond offerings and public disclosures contained accurate information.

- 3. Orrick demands a confession: Orrick orchestrates the City's January 2004 "Voluntary Disclosure"
- 62. Once Ms. Shipione had spurred Orrick to action, Orrick doggedly led efforts that uncovered numerous additional errors going beyond pension issues, and eventually supervised the release of Voluntary Disclosure of January 27, 2004, detailing the results of the inquiry.
- 63. The MWWD offering was postponed pending resolution of the disclosure and financial statement issues. In fact, sufficient uncertainty about these issues has remained, despite the City's Voluntary Disclosure, that the City has never made the needed MWWD offering, nor any other debt security offering, since the summer of 2003.
- 64. By this time, Caporicci & Larson ("C&L") had acquired CJO and was a successor to all of CJO's rights and liabilities. As the City's (and SDCERS') Independent Auditors at that time, C&L joined in the error-correction effort. It produced *six pages* of corrections of the CJO-drafted 2002 footnotes alone. C&L declared *all* of the errors immaterial. (The City still does not know the materiality of CJO's auditing errors, as KPMG has yet to conclude its analysis of the City's 2002 financial statement. On information and belief, the City alleges that the errors were material.)
 - 4. The City Takes Its Medicine (Part One): It issues the Voluntary Disclosures Orrick and C&L Drafted
- 65. With Orrick's considerable pushing, the City made voluntary filings with the nationally recognized municipal securities information repositories on January 27, 2004, and again on March 12, 2004. The City had entered into various continuing disclosure agreements in order to assist compliance by underwriters with Rule 15c2-12 under the Securities Exchange Act of 1934, in which the City agreed to certain specified annual disclosures and to disclose certain specified events, if determined by the City to be material. The voluntary filings were not required pursuant to such continuing disclosure agreements. Such disclosures

of treatment is not alone sufficient to permit the inference of breach of duty").

72. Notwithstanding that it was Defendants who caused or contributed to the City's erroneous disclosures, it has been the City that has undertaken significant and unprecedented remedial measures in response to the deficiencies in its disclosure practices. In addition to the voluntary disclosures discussed above, the City has also done the following to mitigate its damages.

1. Investigative counsel

73. Upon learning of the disclosure concerns that resulted in the voluntary filings, the City hired Vinson and Elkins to conduct a thorough review of the City's disclosure practices from 1996 through 2004 relating principally to the pension system.

procedures.

2. Disclosure ordinance

74. The City, at the suggestion of V&E, adopted a disclosure ordinance (O-19320) on October 11, 2004 ("the Disclosure Ordinance"). The Disclosure Ordinance addresses the concerns raised by the First V&E Report. The Disclosure Ordinance is patterned after the reforms instituted by the Sarbanes-Oxley Act. The Disclosure Ordinance (1) establishes a Disclosure Practices Working Group, comprised of the City Attorney, the Deputy City Attorney for Finance and Disclosure, the City Auditor and Comptroller, the City Treasurer, the Deputy City Manager for Finance, the City's outside general disclosure counsel, and such other persons as such City officials appoint, to review "the form and content of all of the City's documents and materials prepared, issued, or distributed in connection with the City's disclosure obligations relating to its securities" and "disclosures provided by the City in connection with securities issued by the related entities"; (2) requires the City Manager and City Attorney to personally certify to the City Council regarding the accuracy of Official Statements; and (3) requires the Disclosure Practices Working Group to conduct a thorough

review of the City's disclosure practices and to recommend disclosure controls and

IV.

PARTIES

- 81. Plaintiff, City of San Diego, is a municipal entity established by charter pursuant to California Constitution Article XI section 3.
- 82. On information and belief, Defendant Orrick, Herrington & Sutcliffe is a California corporation which does business in the County of San Diego, State of California.
- 83. On information and belief, Defendant Calderon, Jaham & Osborn is a California corporation which does business in the County of San Diego, State of California.
- 84. On information and belief, Defendant Caporicci and Larson is an entity of unknown qualification, but claims to be a general partnership, which does business in the County of San Diego, State of California.
- 85. On information and belief, Defendant Webster and Anderson is an entity of unknown qualification that does business in the County of San Diego, State of California. It acted as bond "co-counsel" to Orrick for the offerings at issue. The City is not presently aware what Webster and Anderson did to assist Orrick, or to what extent it is responsible for the disclosure failures. Accordingly, the City has named Webster and Anderson, on the information and belief that it failed to uncover Orrick's failures as it reasonably should have as bond "co-counsel."
- 86. Plaintiff is currently unaware of the true names and capacities of the Defendants sued as Does 1 through 25, inclusive. Plaintiff is informed and believes that Does 1 through 25, in connection with the other defendants, legally caused the damages suffered by Plaintiff as alleged in this Complaint. Plaintiff will seek leave of Court or will otherwise amend this pleading to include the true names and capacities of Does 1 through 25 when they have been ascertained.
- 87. On information and belief, each Defendant is an agent and/or employee of each other Defendant, and at all relevant times was acting within the course and scope of such agency and/or employment, or the acts of each Defendant were approved or subsequently ratified by each other Defendant.

1 FIRST CAUSE OF ACTION 2 PROFESSIONAL NEGLIGENCE 3 (Against All Defendants) Plaintiff incorporates paragraphs 1-87 as if fully alleged here. 88. 4 5 89. At all relevant times, Defendants owed the City a duty of care and skill in 6 performing professional services on behalf of the City. Defendants also had an obligation to 7 comply with applicable professional standards, as promulgated from time to time. 8 90. Defendants breached their duty to exercise reasonable care and skill in 9 performing accounting services as set forth above. 10 91. As a proximate and legal result of Defendants negligence, the City has been 11 damaged in an amount to be proven at trial and in excess of this court's minimum jurisdiction, 12 but in a minimum amount of not less than \$100,000,000. 13 92. Defendants are not alleged to be, and were not in fact, tortfeasors claimed to be 14 liable for the same tort, within the meaning of Code of Civil Procedure section 877, 15 subdivision (a). Defendants' breaches violated different primary rights and caused distinct 16 and divisible injuries. 17 93. CJO continuously represented the City regarding the accounting matters herein 18 alleged until some time on or after April 2004. In addition, CJO has deprived the City of 19 knowledge of the facts and circumstances giving rise to this claim, such that the statute of 20 limitations was tolled during all periods up to and including the time of the filing of this case.18 21 22 94. Orrick has continuously represented the City, and its agencies, regarding bond 23 issues and disclosure obligations up to and including the present. In addition, Orrick deprived 24 the City of knowledge of the facts and circumstances giving rise to this claim, such that the 25 26 27

¹⁸ <u>See generally Electronic Equipment Express, Inc. v. Donald H. Seiler & Co.</u> (1981) 122 Cal.App.3d 834, 854-856 (discussing commencement of statute of limitations, including equitable tolling).

1	statute of limitations was tolled during all periods up to and including the time of the filing of				
2	this case. 19				
3	SECOND CAUSE OF ACTION				
4	BREACH OF FIDUCIARY DUTIES				
5	(Against All Defendants)				
6	95. Plaintiff incorporates paragraphs 1-94 as if fully alleged here.				
7	96. CJO has at all times relevant been an accountant for the City and actively				
8	assisted the City with its fundraising and accounting activities. In this context, and based on				
9	the facts alleged above, an accountant owes the City fiduciary duties.				
10	97. Orrick has at all times relevant been a lawyer for the City and actively assisted				
11	the City with its fundraising activities and disclosure obligations. In this context, and based				
12	on the facts alleged above, a lawyer owes the City fiduciary duties.				
13	98. Fulfillment of fiduciary duties requires more than the mere absence of bad				
14	faith or fraud. Representation of the financial interests of others imposes on a fiduciary an				
15	affirmative duty to protect those interests and to proceed with a critical eye in assessing				
16	information. ²⁰				
17	99. At no time were Defendants free to act in their own interests to the detriment				
18	of the City. As the City's fiduciaries, Defendants were required to disclose all information				
19	material to the City's interests; were required by law to put the City's interests above their				
20	own; and were required to exercise the greatest diligence in protecting the City				
21	100. The fiduciary duty of "disclosure" requires a fiduciary to disclose all germane				
22	information, which is defined as information material to evaluating a particular transaction—				
23	for example, financial information a reasonable seller of securities would consider important				
24	in deciding whether to make a voluntary disclosure. A fiduciary is not permitted to withhold				
25					
26	See generally Electronic Equipment Express, Inc. v. Donald H. Seiler & Co. (1981) 122 Cal. App.3d 834, 854-856 (discussing commencement of statute of limitations, including				
27	equitable tolling). 20 Smith v. Gorkom (Del. 1985) 488 A.2d 858, 872 (citing Lutz v. Boas (Del. Ch. 1961) 171				
28	A.2d 381 and Guth v. Loft (Del. Ch. 1939) 2 A.2d 225).				

²² Benenato v. McDougall (1913) 166 Cal. 405, 408

Benenato v. McDougall (1913) 166 Cal. 405, 408

1	PRAYER FOR RELIEF					
2	WHEREFORE, Plaintiff prays for judgment as follows:					
3	1.	. For general damages according to proof;				
4	2.	2. For punitive and exemplary damages in an amount to be set by the				
5		trier of fact;				
6	3.	For costs of suit incurred herein, and for such other and further				
7		relief as the Court deems just and proper.				
8	Dated: Dece	ember 1, 2005	STANFORD & ASSOCIATES			
9			BRYAN C. VESS APC			
10						
11		By:				
12		Dy.	Dan L. Stanford			
13			Attorneys for Plaintiff CITY OF SAN DIEGO			
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