UNITED STATES DISTRICT COURT
FOR THE WESTERN DISTRICT OF PENNSYLVANIA

IN RE PNC FINANCIAL SERVICES GROUP, INC. SECURITIES LITIGATION.	:	**Case No. 02-CV-271**
	:	**JUDGE CERCONE**
THIS DOCUMENT RELATES TO ALL ACTIONS	:	**JURY TRIAL DEMANDED**

SECOND CONSOLIDATED AND AMENDED CLASS ACTION COMPLAINT

Plaintiffs, by their undersigned attorneys, on behalf of themselves and the Class they seek to represent, for their Second Amended Consolidated Class Action Complaint (the "SAC"), make the following allegations based upon the investigation conducted by and under the supervision of Plaintiffs' counsel, which included reviewing and analyzing information relating to the relevant time period obtained from numerous public and proprietary sources (such as LEXIS-NEXIS, Dow Jones, Bloomberg, and First Call reports), including, among other things, Securities and Exchange Commission ("SEC") filings, a Cease and Desist Order issued by the SEC against PNC Financial Services Group ("PNC" or the "Company"), a Deferred Prosecution Agreement (the "PNC DPA") entered into between a subsidiary of PNC and the United States Department of Justice (the "DOJ"), an SEC complaint filed against American International Group, Inc. ("AIG"), a Deferred Prosecution Agreement (the "AIG-FP DPA") between AIG-FP PAGIC Equity Holdings Corp. ("AIG-FP PAGIC"), a subsidiary of AIG Financial Products, Inc. ("AIG-FP"), and the DOJ, publicly available press releases, published interviews, news articles and other media reports (including those disseminated in print and by electronic media), reports of securities analysts and investor advisory services, and internal documents and deposition testimony provided to government regulators by PNC or AIG-FP in the context of the government investigations into the allegations complained of herein.

In conjunction with the filing of the SAC, Plaintiffs are also submitting a motion for preliminary approval of a settlement with PNC and certain of its officers and/or directors (defined below as the "Individual Defendants" and collectively with PNC as "PNC Defendants"), AIG-FP, as well as Arnold & Porter, LLP ("AP") and Buchanan Ingersoll, P.C. ("BI"), two law firms which served as counsel to PNC during the Class Period, for total consideration of $36.6 million in cash, plus the assignment by PNC and its subsidiaries of all

claims these entities may have had against its former outside auditor, defendant Ernst &Young, LLP ("E&Y"). Hereinafter, the aforementioned settlement will be referred to as the "Partial Settlement." If approved, the Partial Settlement will release all claims of the Class brought against PNC, the Individual Defendants, and AIG-FP. PNC and the Individual Defendants will be collectively referred to hereinafter as the "Settling Defendants" unless otherwise indicated. If approved, the Partial Settlement will also release and dismiss any and all claims they may have against AP and BI, including, and subject to the approval of PNC, any potential claims against AP and BI assigned to Plaintiffs and the Class by PNC and its subsidiaries, as part of the terms of the Partial Settlement.

Claims being brought by the Class in this action include: (i) claims brought as Count I for material misrepresentation and omission pursuant to Section 10(b) of the Securities and Exchange Act of 1934, [15 U.S.C. § 78j(b)] (the "Exchange Act"), as well as Rule 10b-5, [17 C.F.R. § 240.10b-5] promulgated by the SEC, against the PNC Defendants and E&Y (collectively, with respect to these allegations, the PNC Defendants and E&Y will be referred to herein as the "Misrepresentation Defendants"); (ii) claims brought as Count II for engaging in a deceptive scheme pursuant to Section 10(b) of the Exchange Act and Rule 10b-5 promulgated by the SEC, against: the PNC Defendants who entered into the PAGIC transactions; and E&Y who created, marketed, and opined on the SPE type structure for AIG-FP with respect to marketing the structure, and opined on the structure for PNC as its "independent auditor" (collectively, with respect to these allegations, the PNC Defendants and E&Y will be referred to herein as the "PAGIC Defendants"); (iii) claims brought as Count III for control person liability pursuant to Section 20(a) of the Exchange Act of 1934 against the Individual Defendants (defined below); and (iv) claims brought as Counts IV-VI pursuant to the laws of the Commonwealth of

Pennsylvania against E&Y for malpractice, breach of contract and negligent misrepresentation, which claims were assigned to the Class by PNC and its subsidiaries in connection with the Partial Settlement, against E&Y. Collectively, the Settling Defendants and E&Y will be referred to as the "Defendants" unless otherwise indicated.

NATURE OF THE ACTION

1. This is a class action brought on behalf of a Class (further defined below) of investors consisting primarily of all persons who purchased PNC common stock, who purchased call options on PNC common stock, or who wrote (sold) put options on PNC common stock from July 19, 2001 through July 18, 2002, inclusive (the "Class Period"), and the PNC Incentive Savings Plan on behalf of its present and former participants and beneficiaries who purchased or otherwise acquired PNC common stock during the Class Period through the PNC Incentive Savings Plan.

2. During the Class Period, the PAGIC Defendants participated in a deceptive scheme pursuant to which, over the course of three consecutive quarters, these Defendants secretly created three separate special purpose entities (sometimes referred to herein as "SPEs" or "PAGIC" entities) in order to remove certain volatile, troubled, and non-performing loans and venture capital investments from PNC's financial statements without disclosing this material fact to investors, bank regulators or the SEC. The purpose of these transactions was to artificially conceal losses in the value of the transferred assets from both regulators and the investing public and thereby inflate and maintain PNC's stock price.

3. AIG-FP initially presented the idea to PNC whereby non-performing assets of PNC could be transferred to special purpose entities purportedly "owned" by AIG-FP in order to hide losses in the value of those assets. Prior to pitching the idea to PNC, however, AIG-FP received material advice from E&Y with respect to the development and marketing of the SPE

product. As part of this advice, E&Y provided a formal written opinion letter, issued pursuant to Statement of Auditing Standards No. 50 (the "Marketing SAS-50 Opinion Letter"), to AIG-FP stating that the accounting treatment for such a transaction complied with Generally Accepted Accounting Principles ("GAAP"). In fact, E&Y was knowingly referenced in AIG-FP's promotional materials, which were used in marketing the special purpose entity-type structure to public companies, as having blessed the accounting treatment for the proposed transaction.

4. When special purpose entities are established and maintained in accordance with specified requirements of GAAP, they do not have to be consolidated in the financial statements of the transferor of the assets. However, non-consolidation is only permissible under GAAP when: (i) an independent third party is the majority owner of the special purpose entity; (ii) the independent third-party provides a substantive capital investment in and has control over the special purpose entity; ***and*** (iii) the majority owner has substantive risks and rewards of ownership of the special purpose entity. If the special purpose entity does not meet ***all three*** of these "transfer of ownership" criteria, its financial results must be consolidated with the true owner's results in order to comply with GAAP.

5. Once PNC was presented with the idea of the SPE transactions, PNC then turned to E&Y, as its outside auditor, for an opinion as to the appropriate accounting treatment. The same individuals at E&Y who assisted AIG-FP in creating and structuring the special purpose entity structure, and who provided the Marketing SAS-50 Opinion Letter to AIG-FP, including an E&Y national partner who specialized in "consolidations," once again blessed the accounting for the transactions, this time for the benefit of PNC, and provided SAS-50 opinion letters for each of the PAGIC transactions (collectively, the "PAGIC SAS-50 Opinion Letters").

6. Prior to entering into the first PAGIC transaction and continuously throughout the Class Period, the accounting department and members of PNC's senior management had discussions with E&Y concerning, among other things, the millions of dollars that AIG-FP would receive for purportedly *managing* the special purpose entities it established with AIG-FP for PNC. As articulated herein, in reality, E&Y knew or recklessly disregarded that such fees were not for management services, but rather, were fees for structuring the PAGIC transactions and for lending PNC the "use" of AIG-FP's balance sheet. E&Y also knew or recklessly disregarded that the PAGIC transactions required PNC to pay the entire "management fee" to AIG for the length of the agreement up front. E&Y knew or recklessly disregarded that these payments to AIG-FP had the effect of reducing the initial investment by AIG in the respective SPEs to a level below the absolute bare minimum 3% level required by GAAP. As such, E&Y knew or recklessly disregarded that transferring PNC's non-performing assets to three SPEs purportedly "owned" by AIG-FP did not satisfy GAAP because the subsidiary established by AIG-FP did not provide a substantive capital investment in, nor have control over, the SPEs. In addition, E&Y also knew or recklessly disregarded that, by virtue of the structure of the three SPEs, PNC, and not the AIG-FP subsidiary, retained the substantive risks and rewards of ownership of the assets transferred to each special purpose entity. Nevertheless, E&Y failed to address these issues, or even mention the management fees, in each of the three PAGIC SAS-50 Opinion Letters that it provided to PNC for the three SPE transactions that PNC entered into during the Class Period.

7. Accordingly, all PAGIC Defendants well knew or recklessly disregarded that the SPE transactions did not represent a true transfer of economic risk as PNC retained such a

significant interest in the special purpose entities, and that the "transfers" represented nothing more than a sham to remove the non-performing assets from PNC's financial statements.

8. In addition to initially approving the transaction as a consultant to AIG-FP and thereafter reviewing the same transaction purportedly as PNC's auditor, E&Y also substantially assisted in the preparation of PNC's quarterly financial statements and corresponding earnings releases and once again, through the PAGIC SAS-50 Opinion Letters, favorably passed on the accounting treatment it had previously designed, suggested, adopted and was marketing along with AIG-FP.

9. In this regard, E&Y assured PNC that the special purpose entity structure satisfied GAAP, despite significant red flags that would have alerted an auditor acting with requisite professional care, diligence and skepticism, and in performance of its duties as required by Generally Accepted Auditing Standards ("GAAS"), that the special purpose entities were specifically intended to conceal losses and thereby inflate and maintain PNC's stock price in violation of GAAP. In fact, based upon advice from another national accounting firm ("National Accounting Firm A"), other public companies that AIG and E&Y had marketed the special purpose entity structure to, both prior to and during the Class Period, refused to engage in such transactions. Specifically, in May 2001, National Accounting Firm A had identified several "soft spots" in E&Y's accounting analysis of the special purpose entity structure specifically relating to the fact that any fees paid directly or indirectly to AIG-FP would have the effect of taking AIG-FP's initial investment below the 3% absolute bare minimum threshold required by GAAP. Indeed, as a result of National Accounting Firm A's noted concern, E&Y was asked by a national insurance company to prepare yet another Marketing SAS-50 Opinion Letter that specifically addressed the management fee issue. Although E&Y provided the insurance

company with a revised Marketing SAS-50 Opinion Letter prior to PNC closing PAGIC III, E&Y failed to address these concerns in any of its PAGIC SPE-50 Opinion Letters that it drafted and provided to PNC, stating instead that the accounting treatment for each PAGIC transaction complied with GAAP.

10. That GAAP had not been satisfied in connection with the transfers was not only apparent to the PAGIC Defendants from the very face of the transactions, but was also brought to the Defendants' attention by federal regulators, who formally questioned PNC and E&Y about PNC's accounting treatment of the SPEs during the Class Period. Nevertheless, in the face of these high-flying red flags and direct warnings, PNC's financial results, based upon specific guidance provided by E&Y, continued to be reported on a non-consolidated basis in violation of GAAP.

11. As such, the sham special purpose entity structure allowed the Misrepresentation Defendants (the PNC Defendants and E&Y) to prepare, review and/or disseminate materially false and misleading statements regarding PNC's reported or announced financial results. Among other things, these Defendants misrepresented: (i) the amount of PNC's non-performing assets in the second, third and fourth quarters of 2001; (ii) PNC's net income and earnings per share for the third and fourth quarters of 2001, as well as PNC's net income and EPS for 2001; (iii) key financial ratios related to asset quality and loan levels for the second, third and fourth quarters of 2001; (iv) PNC's purported compliance with GAAP and/or statements that PNC's financial results were being fairly presented; (v) the nature and extent of services being provided to PNC by E&Y; (vi) the extent to which PNC and E&Y disagreed on the appropriateness of a press release issued by PNC on January 17, 2002 (just days after federal regulators ordered that

the SPEs be consolidated); and (vii) the extent of government oversight that PNC would be subject to in light of the undisclosed activities described herein.

12. This, however, was not merely a misunderstanding about complex accounting rules. As all of the Defendants were fully aware, or recklessly disregarded, these transactions were utilized to misrepresent the purported success PNC was having in its widely-proclaimed strategy of divesting non-performing assets, a corporate initiative which had commenced in September of 1998. By the beginning of the Class Period, PNC could no longer maintain its strategy of reducing its level of non-performing assets through legitimate business means. It was at this point in time when the PAGIC Defendants began implementing the secret, end-of-quarter, transfers of PNC's non-performing assets to the three special purpose entities without disclosure or consolidation in violation of the federal securities laws.

13. As evidenced in an e-mail to be further discussed herein, the PAGIC Defendants (the PNC Defendants and E&Y) also knew or recklessly disregarded that removing the non-performing assets from PNC's financial statements would permit such assets to escape scrutiny by federal regulators, including the Office of the Comptroller of the Currency (the "OCC").

14. Instead of disclosing the material fact that announced "reductions" or "stability" in non-performing assets during the Second and Third Quarters of 2001 were directly attributable to PNC's transactions with the special purpose entities, the Misrepresentation Defendants falsely proclaimed that such positive developments were due to "continued" actions to downsize its institutional lending business.

15. In stark contrast to such statements, not only was the undisclosed transfer of non-performing assets to special purpose entities an entirely "new" (as opposed to "continued") and unlawful action, the statements also created the materially false impression that PNC's corporate

initiative of divesting non-performing assets was still experiencing success, when, in fact, the strategy was now dependent upon PNC entering into sham transactions and improperly accounting for such transactions, with the full knowledge, blessing and substantial participation of E&Y.

16. At the same time that Misrepresentation Defendants were disseminating to the SEC and investing public false financial results and misrepresentations regarding "successful" divestitures of non-performing assets, and while secretly responding to federal regulators' formalized inquiries concerning the PAGIC transactions, PNC was in the process of conducting two separate ***billion*** dollar securities offerings and E&Y and AIG-FP were marketing the product to other potential customers.

17. Upon concluding its investigation into PNC's treatment for special purpose entities, on January 11, 2002, members of the Federal Reserve Board (the "FRB") informed PNC that it had reached the conclusion that the accounting treatment for the PAGIC transactions violated both Regulatory Accounting Principles ("RAP") and GAAP, and formally directed PNC to consolidate the results of all three SPEs for 2001 for regulatory reporting purposes. The FRB also informed PNC that it had already discussed its decision to require consolidation with the SEC, including the SEC's Office of Chief Accountant.

18. On January 13, 2002, when advised of the FRB's decision, although aware of the fact that PNC had not disclosed to investors that it was even using SPEs and that PNC's treatment of the SPEs violated GAAP, E&Y strongly advised PNC to delay issuance of its earnings release scheduled for January 17, 2002 until E&Y had an opportunity to address the appropriate accounting treatment for the SPE transactions with the SEC's Office of Chief Accountant. Stunningly, E&Y threatened to withhold issuing an unqualified audit opinion for

PNC's Form 10-K for 2001 if PNC did not appeal the FRB's directive to the SEC's Chief Accountant -- even though, by this time, both PNC and E&Y knew or recklessly disregarded that there was no difference between GAAP and RAP in this regard.

19. On January 15, 2002, a meeting was held between the FRB and senior management of PNC, during which the FRB explained, in detail, the basis for its directive to PNC to consolidate the results of the special purpose entities and specifically advised PNC that non-consolidation was not appropriate. The FRB also explained to PNC that, consistent with federal banking laws, both RAP and GAAP required consolidation of the special purpose entities. PNC immediately relayed the FRB's position to E&Y.

20. Having already advised the market that its financial results for year-end and fourth quarter 2001 would be issued on January 17, 2002, on that date, the PNC Defendants determined that they had no choice but to issue financials on a non-consolidated basis. Notwithstanding E&Y's position that PNC should delay issuance of the January 17 release, and its prior threat to withhold its unqualified audit opinion, E&Y still substantially assisted PNC in drafting the January 17, 2002 press release.

21. The January 17, 2002 press release, however, failed to disclose the federal regulator's investigation of PNC, the FRB's conclusion that non-consolidated results were materially misleading for reporting purposes, or of E&Y's "new" advice that results be delayed until the effects of consolidation could be fully assessed by the SEC's Office of Chief Accountant.

22. Just twelve days later, on January 29, 2002, the PNC Defendants surprised the investing community by announcing that PNC would restate its earnings for the second and third quarters of fiscal 2001 and revise its fourth quarter and year-end 2001 earnings to reflect the

consolidation of three special purpose entities. The investing public was further advised that PNC's year-end 2001 earnings were being reduced by $155 million and that earnings per share would decrease from the reported $1.91 to $1.38 per share, thereby wiping out 38% of earnings for the year. These announcements caused PNC's stock price to drop from a close of $61.87 per share on January 28th to a close of $55.71 per share on January 30, 2002, a 10% drop in just two days of trading on extremely heavy volume.

23. In connection with the restatement announcement, PNC also announced that the "recently" received "advice" from the FRB regarding the accounting for special purpose entities had differed from advice PNC had received previously from E&Y. However, the investing public was not informed that the "advice" from the FRB was actually *a directive* to consolidate and that said "advice" was received six days prior to PNC's issuance of non-consolidated results in connection with its January 17th press release. Based upon this fact and PNC's behavior throughout the regulatory investigation, the Misrepresentation Defendants also knew or recklessly disregarded that PNC would be subject to increased regulatory scrutiny and oversight in the future, but failed to disclose this material fact to the investing public. Furthermore, the Misrepresentation Defendants failed to disclose that E&Y had specifically advised against PNC issuing the January 17th press release with its inclusion of 2001 Fourth Quarter and Year-End financial results prepared on a non-consolidated basis. Thus, the restatement press release constituted additional materially false and misleading statements, which did not remove the entirety of the artificial inflation that was still present in PNC's stock price at that time.

24. On January 30, 2005, the day following the announcement, E&Y disclosed, for the first time, that it had played a role in developing the special purpose entity structure for AIG, and then, as PNC's auditor, had opined on the accounting of each SPE transaction. Although

E&Y's disclosure informed the market, for the first time, of its dual role with respect to the SPE transactions, E&Y entirely rejected any notion that such a role was improper by assuring the market that there was no conflict of interest in acting on both sides of the SPE transactions. E&Y also falsely stated in its January 30th announcement that it had "concurred" with regulators' directive to consolidate the SPE transactions, when, in reality, E&Y had threatened PNC to withhold its unqualified year end audit opinion if PNC agreed with the regulators and simply announced its results on a non-consolidated basis.

25. By virtue of these misrepresentations, the material fact that PNC's own management was directly involved in the accounting fraud and had made materially false and misleading statements to the investing public with actual knowledge of their falsity continued to be concealed by the PNC Defendants.

26. On March 29, 2002, the PNC Defendants, with E&Y's approval and assistance, formally restated PNC's financial results by filing amended Forms 10-Q for the Second and Third Quarters ended June 30, 2001 and September 30, 2001, respectively, with the SEC. As, pursuant to GAAP, restatements are only required when the originally filed financial results are misstated as a result of an oversight or a misuse of facts that existed at the time, the Misrepresentation Defendants had now admitted that the originally filed financial results for PNC's Second and Third Quarters of 2001 were materially false and misleading when issued.

27. PNC also filed a Form 10-K for the full year 2001, which included an unqualified audit opinion for 2001 authored by E&Y. The 2001 Form 10-K revealed that the $1.91 year-end earnings per share figures originally announced by PNC on January 17, 2002 were overstated by a staggering 52%. In total, $190 million or $0.65 per share was wiped out. PNC's 2001 Form 10-K, which also included Fourth Quarter 2001 results, revealed that the 2001 Fourth Quarter

loss of ($1.15) per share announced on January 17th was understated by 24%, as the true fourth quarter loss was ($1.52) per share. The 2001 Form 10-K further disclosed that PNC had charged $240 million against pre-tax income as a result of valuation write-downs relating to consolidation of the special purpose entities.

28. As E&Y had been terminated as PNC's outside auditor in December of 2001, PNC was required as part of the instructions to Form 8-K to advise the SEC of any material disagreements PNC and E&Y had prior to the issuance of the Form 10-K. E&Y, as the terminated auditor, was required to submit a letter to the SEC either agreeing or disagreeing with PNC's characterization of any material disagreements. Despite purporting to comply with the instructions of Form 8-K, neither party included any mention of PNC's failure to follow E&Y's advice in connection with the January 17th press release, as they affirmatively represented that no material disagreements existed as of March 29, 2002, the date of PNC's Form 10-K filing. These representations were materially false and misleading as the Misrepresentation Defendants all had first hand knowledge of the material disagreement, having participated in meetings following the directive being issued by the FRB in January 2001, yet failed to disclose it.

29. Had the facts and circumstances surrounding this disagreement been disclosed in the Form 10-K, as required by Item 304 of Regulation S-K, the investing public would have been alerted that PNC management was directly implicated in the fraudulent conduct alleged herein and was ignoring the directive of federal regulators in connection with the accounting establishment of the special purpose entities thereby subjecting the Company to an increased risk of additional government oversight in light of its conduct. As a result, even after the restated financials were filed on March 29, 2002, PNC's stock price still remained artificially inflated.

30. On July 18, 2002, the last day of the Class Period, the SEC announced that as a result of "accounting improprieties" and in particular, a "misuse of special purpose entities," it had issued a Cease and Desist Order against PNC. For the first time, the investing public learned that this was not merely a situation where complicated accounting rules were innocently misunderstood by a company, its executives, and its accountants. In this regard, the Cease and Desist Order specifically referenced the false and misleading statements PNC had made regarding PNC's purported success in selling non-performing assets and the material fact that PNC had continued to issue materially false and misleading financial results just days after being advised that reporting financial statements on a non-consolidated basis was misleading. Furthermore, the SEC's Order specifically mentioned the fact that the purpose in establishing the special purpose entities was to remove PNC's non-performing assets from its books, as the specific accounting treatment desired was no longer possible.

31. On that same day, federal regulators announced that it had entered into an agreement with PNC to address matters relating to compliance with GAAP, and consolidation of assets of SPEs on PNC's regulatory reports and public financial statements.

32. Accordingly, through the disclosures concerning actions taken by the SEC and federal regulators against PNC, the market was finally alerted to the fact that PNC's restatement was not the result of some mere accounting issue, but to PNC entering into sham transactions, the purpose of which – as known by E&Y as both an architect of the SPE type structure and as PNC's consultant on the SPE transactions -- was to artificially conceal losses in the value of the transferred assets from both regulators and the investing public.

33. The market's reaction to the disclosures made in the Cease and Desist Order and federal regulator's agreement caused the stock price to dramatically decline, this time dropping

15% on July 18, 2002 and an additional 6.55% on July 19, 2002. Overall, PNC's stock price had fallen from a close of $46.60 per share on July 17, 2002 to $37.09 per share on July 19, 2002, in just two days on trading volume that was more than thirteen times greater than the average volume during the Class Period. This price was a far cry from PNC's Class Period high of $69.80 per share reached on August 22, 2001.

34. That there was no legitimate purpose in forming these entities other than to remove non-performing assets from PNC's books is further evidenced by the fact that although a fourth PAGIC entity was created and due diligence purportedly performed by the PAGIC Defendants, the project was dropped entirely following the announcement of the restatement in January of 2002.

35. Subsequent to the conclusion of the Class Period, on June 2, 2003, in a Form 8-K filing, PNC announced that PNC and the DOJ had entered into the PNC DPA wherein PNC agreed to pay $115 million dollars in fines and restitution ($90 million to a government established restitution fund, and $25 million in fines) relating to its conduct in connection with the creation and accounting for the special purpose entity transactions at issue in this litigation, and that the investigation is continuing with respect to third parties who participated in the formation of these entities.

36. On or about November 30, 2004, AIG announced that it had also reached an agreement with the DOJ and the SEC wherein AIG agreed to pay $46 million in restitution to PNC shareholders and $80 million in fines relating to the conduct of AIG, AIG-FP and AIG-FP PAGIC Equity Holdings, Inc., in connection with the creation and accounting for the SPE transactions at issue in this litigation. The DOJ has since directed that, of the $80 million that

AIG has paid in fines, $20 million be paid to the restitution fund (accordingly, in total, AIG has paid $66 million to the restitution fund, and $60 million in fines).

37. On December 7, 2004, E&Y announced that it was being investigated by the SEC with respect to its role in connection with the SPEs at issue in this litigation.

38. In addition to having actual knowledge or recklessly disregarding the scheme or the falsity of the statements being made by or on behalf of PNC, each of these Defendants were financially motivated to engage in this fraudulent activity. E&Y was receiving not only significant internal and external auditing fees from PNC (approximately $3.9 million in 2001 alone), but also, millions of dollars in consulting fees from PNC (approximately $14.94 million in 2001) – including consulting services related to the SPE transactions. As further detailed herein, for much of the Class Period, E&Y failed to disclose its role in consulting PNC on these transactions, or the amount of fees that it earned for such services, and when E&Y did disclose this information, E&Y materially misrepresented its conflicting role with respect to the SPE transactions -- a role that permitted Defendants to mislead the market throughout the Class Period. Not only was PNC paying E&Y significant consulting fees with respect to the SPEs, but E&Y was also receiving fees from AIG-FP in connection with the creation of the special purpose entities. In fact, as AIG-FP was marketing the idea to other potential clients by utilizing E&Y's Marketing SAS-50 Opinion Letter, E&Y was motivated to ignore obvious problems with the structure so as to earn more potential fees -- even when such problems were raised by National Accounting Firm A.

JURISDICTION AND VENUE

39. The claims asserted herein arise under and pursuant to Sections 10(b) and 20(a) of the Exchange Act, 15 U.S.C. §§ 78j(b) and 78(a), and the rules and regulations promulgated by the SEC, including Rule 10b-5, 17 C.F.R. § 240.10b-5.

40. This Court has jurisdiction over the subject matter of this action pursuant to 28 U.S.C. § 1331 and Section 27 of the Exchange Act, 15 U.S.C. § 78aa.

41. This Court has pendent jurisdiction over Plaintiffs' common law claims pursuant to 28 U.S.C. § 1367.

42. Venue is proper in this District pursuant to Section 27 of the Exchange Act, and 28 U.S.C. § 1391(b). PNC maintains its principal place of business in this District and many of the acts and practices complained of herein occurred in substantial part in this District.

43. In connection with the acts alleged in this SAC, Defendants, directly or indirectly, used the means and instrumentalities of interstate commerce, including, but not limited to, the mails, interstate telephone communications and the facilities of the national securities markets.

THE PARTIES

PLAINTIFFS

44. Lead Plaintiffs Specialists DPM, LLC; Teamsters Local 272 Labor & Management Pension Fund; Joint Industry-Engineers Union Local 30 Pension Fund; and Teamsters Local 210 Pension Fund purchased PNC securities at artificially inflated prices during the Class Period, as set forth in their certifications previously filed with the Court and have been damaged thereby.

DEFENDANTS

THE PAGIC DEFENDANTS

PNC

45. Defendant PNC is incorporated in the Commonwealth of Pennsylvania and maintains its corporate headquarters at One PNC Plaza, 249 Fifth Avenue, Pittsburgh, Pennsylvania. PNC is a bank holding company and a financial holding company. As of January 28, 2002, there were approximately 283,000,000 shares of PNC common stock issued and

outstanding. During the Class Period, PNC common stock was actively traded on the New York Stock Exchange ("NYSE") under the ticker symbol "PNC." PNC is a Settling Defendant in the Partial Settlement.

THE INDIVIDUAL DEFENDANTS

46. Defendant James E. Rohr ("Rohr") was the Chairman, President and Chief Executive Officer of PNC during the Class Period. As such, defendant Rohr was responsible for overseeing all aspects of PNC's operations and on numerous occasions made public statements on PNC's behalf regarding PNC's financial condition, future prospects and the purported success PNC was having with its initiative to rid its financial statements of non-performing assets. Defendant Rohr signed PNC's September 18th Registration Statement, which incorporated by reference PNC's materially false and misleading Form 10-Q for the second quarter of 2001. Defendant Rohr was also an officer or director, or acting in such capacity in connection with the October 23rd Prospectus Supplement, such that he bears responsibility for the false and misleading statements appearing therein. Defendant Rohr also signed PNC's materially false and misleading 2001 Form 10-K. Defendant Rohr is a Settling Defendant in the Partial Settlement.

47. Defendant Robert L. Haunschild ("Haunschild") was the Senior Vice President and Chief Financial Officer of PNC during the Class Period. As such, Haunschild was responsible for PNC's financial, treasury and accounting functions. Defendant Haunschild signed PNC's materially false and misleading Form 10-Q for the second quarter of 2001, and PNC's September 18, 2001 Registration Statement. Defendant Haunschild was also an officer or director, or acting in such capacity in connection with the October 23rd Prospectus Supplement, such that he bears responsibility for the false and misleading statements appearing therein. Defendant Haunschild also signed PNC's materially false and misleading 2001 Form 10-K. On

August 28, 2002, Haunschild resigned from PNC reportedly to "pursue other interests." Defendant Haunschild is a Settling Defendant in the Partial Settlement.

48. Defendant Samuel S. Patterson ("Patterson") was the Controller of PNC during the Class Period. As such, defendant Patterson was PNC's principal accounting officer. Defendant Patterson signed PNC's September 18, 2001 Registration Statement, which incorporated by reference PNC's materially false and misleading Form 10-Q for the second quarter of 2001. Defendant Patterson was also an officer or director, or acting in such capacity in connection with the October 23rd Prospectus Supplement, such that he bears responsibility for the false and misleading statements appearing therein. Defendant Patterson also signed PNC's materially false and misleading 2001 Form 10-K. Defendant Patterson is a Settling Defendant in the Partial Settlement.

49. Defendants Rohr, Haunschild and Patterson are collectively referred to hereafter as the "Individual Defendants" and, collectively, along with PNC, as the "PNC Defendants."

50. The Individual Defendants, because of their positions of control and authority as officers and/or directors of PNC, were able to and did control the content of the various SEC filings, press releases and other public statements pertaining to PNC during the Class Period. Each Individual Defendant was provided with copies of the documents alleged herein to be misleading prior to their issuance and/or had the ability and/or opportunity to prevent their issuance or cause them to be corrected. Accordingly, each of the Individual Defendants is responsible for the accuracy of the public reports and press releases detailed herein and is therefore primarily liable for the misrepresentations contained therein. The Individual Defendants are also liable as controlling persons of PNC.

E&Y

51. Defendant E&Y is a partnership which maintains its headquarters at 787 Seventh Avenue, New York, New York. During all relevant times, E&Y served as auditor and consultant for PNC. E&Y also served as a consultant with respect to AIG-FP. In its capacity as a consultant for AIG-FP, E&Y assisted in designing, structuring and promoting the utilization of special purpose entities that PNC ultimately used to transfer the troubled and/or non-performing assets off its balance sheet in an attempt to avoid recognizing a loss from impairment in the value of such assets. E&Y also assisted AIG-FP in developing and marketing this same general structure to other publicly traded companies prior to and during the Class Period. PNC was a long time and significant client of E&Y and a major source of income for E&Y's Pittsburgh office. Defendant E&Y has served PNC in various capacities for many years and had earned significant fees for performing these accounting services. In fact, during fiscal 2001, PNC paid approximated $18 million in fees to E&Y. Of this amount, approximately 83% ($15 million) was associated with consulting and other services provided by E&Y for PNC. In 2001, although undisclosed during the Class Period, E&Y also earned significant fees related, in part, to E&Y's evaluation of accounting treatment for the PAGIC transactions and its involvement in rendering important judgments in the preparation of PNC's interim 2001 financial statements and provided specific guidance to PNC with respect to the PNC Defendants' decision not to disclose the SPE transactions. Under all of these circumstances, E&Y had an obligation to the investing public not to engage in deceptive conduct or to conceal material non-public information in violation of the federal securities laws.

52. Each of the PAGIC Defendants is liable as a primary violator for participating in a fraudulent scheme and course of business that operated as a fraud or deceit on purchasers of PNC securities during the Class Period. The fraudulent scheme and course of business was designed

to and did: (i) deceive the investing public, including Lead Plaintiffs and other Class members; (ii) artificially inflate the price of PNC securities during the Class Period; and (iii) cause Lead Plaintiffs and other members of the Class to purchase PNC securities at inflated prices.

53. Each of the PAGIC Defendants knew or recklessly disregarded that the deceptive conduct would adversely affect the integrity of the market for PNC's securities and would and did cause the price of PNC's securities to become artificially inflated, until all of the material facts and circumstances concerning the PAGIC transactions, including the increased government oversight of PNC which stemmed directly from the PAGIC Defendants' conduct was finally disclosed to the market at the end of the Class Period. Each of the PAGIC Defendants acted knowingly or in such a reckless manner as to constitute a fraud and deceit upon Plaintiffs and the other members of the Class.

THE MISREPRESENTATION DEFENDANTS

THE PNC DEFENDANTS

54. The PNC Defendants are also being charged with making, issuing and/or disseminating materially false and misleading public statements or omissions in connection with the issuance of PNC's financial results throughout the Class Period in violation of Section 10(b) and Rule 10b-5. The specific materially false and misleading statements or omissions will be further detailed herein.

E&Y

55. E&Y is also being charged with failing to disclose material non-public information which rendered PNC's financial reporting false and misleading. In this regard, E&Y consented to the use of its unqualified audit opinion for the 2000 year-end financial results which was incorporated in PNC's September 18th Registration Statement (defined below) and its October 23rd Prospectus Supplement (defined below). The September 18th Registration

Statement incorporated by reference PNC's materially false and misleading Form 10-Q for the Second Quarter of 2001, while the October 23rd Prospectus Supplement included materially false and misleading financial information regarding the 2001 Third Quarter and incorporated by reference PNC's materially false and misleading Form 10-Q for the Second Quarter of 2001.

56. As E&Y provided specific and material guidance to PNC with respect to several of the materially false and misleading statements made during the Class Period, including: (i) PNC's earnings releases for the second and third quarters for 2001; (ii) PNC's Form 10-Qs for those quarters, which included PNC's financial statements originally filed with the SEC for those quarters; (iii) PNC's earnings release for 2001, dated January 17, 2002, and (iv) PNC's January 29, 2002 press release, in which the PNC Defendants announced that PNC was restating its financial results for the second and third quarters of 2001, E&Y was a "maker" of these statements under the federal securities laws. Furthermore, through PNC's numerous public filings, the public was well aware that E&Y was PNC's independent auditor, as well as E&Y's role with respect to preparing PNC's financial statements.

57. In addition, E&Y made material misrepresentations in its letter to the SEC attached as an Exhibit to PNC's December 18, 2001 Form 8-K regarding the services that it provided to PNC during the Class Period. In this regard, as further described below, E&Y failed to disclose the consulting services it was providing to PNC in connection with the SPEs, as well as its role in marketing, structuring, and opining on the SPEs. E&Y also made material misrepresentations concerning the permissibility of its dual and conflicting role, as well as about the facts concerning the federal regulatory directed to PNC to consolidate the SPEs.

58. E&Y also made a material misrepresentation in its letter to the SEC attached as an Exhibit to PNC's 2001 Form 10-K filed on March 29, 2002, regarding whether any material disagreements had arisen between PNC and E&Y preceding the filing of the Form 10-K.

COMMON LAW DEFENDANT

59. In connection with the Partial Settlement, PNC and its subsidiaries have assigned to the Class certain claims they possess against various parties in connection with the establishment of the special purpose entities, as well as the legal and accounting opinions and advice received in connection with PNC's public disclosures concerning the special purpose entities. In addition to seeking damages based primarily upon the fees paid to these various entities by PNC, the Class is also seeking the return of any money that PNC had to pay to regulators, as restitution or to lawyers or accountants in connection with the investigation into the fraud, on behalf of PNC.

E&Y

60. Defendant E&Y is being charged with violations of common law with respect to the professional services it provided to PNC during the Class Period. In this regard, E&Y violated numerous ethical standards further detailed herein, by consulting for parties on different sides of the same transaction, first opining on the structure of the special purpose entities for AIG-FP and thereafter performing the same services for PNC. In fact, in the Marketing SAS-50 Opinion Letter that E&Y had prepared for AIG-FP to market the SPE type structure, E&Y itself opined that companies who entered into the transactions should consult their "continuing accountants" as to whether the transaction violated GAAP, which they knew in the case of PNC was E&Y. In addition to taking on its dual and conflicting role, E&Y failed to exercise the skill and knowledge normally exercised by members of its profession in providing consulting services. Similarly, in its role as PNC's public auditor, E&Y failed to exercise the skill and

knowledge normally exercised by members of its profession in providing auditing services as its audits were not conducted in accordance with GAAS.

CLASS ACTION ALLEGATIONS

61. Plaintiffs bring this action as a class action pursuant to Federal Rules of Civil Procedure 23(a) and (b)(3) on behalf of a class (the "Class") consisting of all persons who purchased PNC common stock, who purchased call options on PNC common stock, or who wrote (sold) put options on PNC common stock from July 19, 2001 through July 18, 2002, inclusive (the "Class Period"), and the PNC Incentive Savings Plan on behalf of its present and former participants and beneficiaries who purchased or otherwise acquired PNC common stock during the Class Period through the PNC Incentive Savings Plan.

62. Excluded from the Class are E&Y, the PNC Defendants, AIG Financial Products Corp., Arnold & Porter LLP, Buchanan Ingersoll PC, any entity in which the PNC Defendants, AIG Financial Products Corp., Arnold & Porter LLP, or Buchanan Ingersoll PC have a controlling interest or is a parent or subsidiary of or is controlled by E&Y, PNC, AIG Financial Products Corp., Arnold & Porter LLP, or Buchanan Ingersoll PC, and the officers, directors, partners, members, employees, affiliates, legal representatives, heirs, predecessors, successors and assigns of any of the Defendants, AIG Financial Products Corp., Arnold & Porter LLP, or Buchanan Ingersoll PC, except that this exclusion shall not apply to persons in their capacity as present or former participants or beneficiaries of the PNC Incentive Savings Plan. Also excluded from the Class are any putative Class Members who exclude themselves by filing a request for exclusion in accordance with the requirements set forth in the Notice.

63. The members of the Class are so numerous that joinder of all members is impracticable. While the exact number of Class members is unknown to Plaintiffs at this time and can only be ascertained through appropriate discovery, Plaintiffs believe there are, at a

minimum, thousands of members of the Class who traded during the Class Period. PNC had approximately 284 million shares of its common stock outstanding as of July 18, 2002.

64. 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. Among the questions of law and fact common to the Class are:

(i) Whether the federal securities laws were violated by the deceptive scheme engaged in by the PAGIC Defendants as alleged herein;

(ii) Whether the federal securities laws were violated by the materially false and misleading statements or omissions of the Misrepresentation Defendants as alleged herein;

(iii) Whether the Misrepresentation Defendants and PAGIC Defendants acted with scienter in committing deceptive conduct or issuing materially false and misleading statements;

(iv) Whether the market prices of PNC's securities during the Class Period was artificially inflated by virtue of the conduct of the PAGIC Defendants and/or the PAGIC Defendants complained of herein; and

(v) Whether the members of the Class have sustained damages and, if so, what is the proper measure of damages.

65. Plaintiffs' claims are typical of the claims of the members of the Class as Plaintiffs and the other members of the Class each sustained damages arising out of the wrongful conduct of the PAGIC Defendants and the Misrepresentation Defendants in violation of federal law as complained of herein.

66. Plaintiffs will fairly and adequately protect the interests of the members of the Class and has retained counsel competent and experienced in class actions and securities litigation. Plaintiffs have no interests antagonistic to or in conflict with those of the Class.

67. A class action is superior to other available methods for the fair and efficient adjudication of the controversy since joinder of all members of the Class is impracticable.

Furthermore, because the damages suffered by the individual Class members may be relatively small, the expense and burden of individual litigation make it impossible for the Class members individually to redress the wrongs done to them. Plaintiffs anticipate no unusual difficulties in the management of this action as a class action.

SUBSTANTIVE ALLEGATIONS

THE SCHEME OF THE PAGIC DEFENDANTS

68. Each of the PAGIC Defendants engaged or participated in the implementation of manipulative and deceptive devices to inflate PNC's reported profits and financial condition, made or participated in the making of false and misleading statements and participated in a scheme to defraud or a course of business that operated as a fraud or a deceit on purchasers of PNC's publicly traded securities during the Class Period.

69. AIG-FP initially presented the idea to PNC whereby non-performing assets of PNC could be transferred to special purpose entities purportedly "owned" by AIG-FP in order to hide losses in the value of those assets. Prior to pitching the idea to PNC, however, AIG-FP first obtained an opinion from E&Y in the form of the Marketing SAS-50 Opinion Letter, which opined that the accounting treatment for the proposed SPE transaction complied with GAAP. In fact, AIG-FP included specific references to E&Y's participation in structuring the proposed transactions, with E&Y's knowledge and consent, in promotional materials utilized in marketing the proposed transaction to PNC and others.

70. Once PNC was presented with the idea, PNC also turned to E&Y for an opinion as to the appropriate accounting treatment. The same individuals at E&Y who provided the opinion to AIG-FP, including Michael Joseph, an E&Y national partner, once again blessed the accounting for the transactions, this time, for the benefit of PNC.

71. After agreeing upon the proposed structure, the PAGIC Defendants, in PNC's Second, Third and Fourth Quarters of 2001, created three secretly controlled partnerships that served to hide millions of dollars in losses and to conceal hundreds of millions of dollars in non-performing assets by moving them off PNC's balance sheet. In fact, a fourth special purpose entity was in the midst of being created when government regulators pulled the plug on the scam. This scheme operated as a fraud and deceit on the purchasers of PNC's publicly traded securities.

72. The following details of the transactions utilized by the PAGIC Defendants to form the special purpose entities are set forth in documents and testimony of PNC and/or AIG and are fully corroborated by the SEC Complaint and the Statement of Facts of the DPA between PNC and the DOJ, as well as the SEC Complaint and the Statement of Facts of the DPA between AIG-FP and the DOJ.

SPE I

73. On June 28, 2001, AIG-FP, acting through a subsidiary, organized the first special purpose entity as a Delaware limited liability company ("SPE I" or "PAGIC I"). In connection with the closing transactions, which took place just three days before the close of PNC's 2001 Second Quarter, AIG-FP received $36,576 worth of SPE I's Class B common stock and $11,558,940 worth of SPE I's Class B preferred stock in exchange for a cash contribution of $11,595,517. PNC, through a nonbank subsidiary [PNC ICLC], contributed $365.8 million in cash to SPE I and received $365.8 million worth of SPE I's Class A preferred stock in exchange for its investment. As a result, AIG-FP appeared to have contributed the bare minimum of 3% of the total equity contribution ($377 million). However, as part and parcel of the transaction, AIG-FP received an upfront fee of $2.7 million in connection with the closing of the transaction. While this fee was characterized as a "management fee" in the closing documents, in reality, the PAGIC Defendants all knew or recklessly disregarded that the fee was a structuring fee or a fee

for the use of AIG-FP's balance sheet, as, among other things, the fee was: (i) paid by PNC on the day that the SPE transactions closed or shortly thereafter in its entirety, as opposed to fees that were earned for management services to be rendered to PAGIC I over time; (ii) the cash "waterfall" for PAGIC I included a cash trapping feature to fund AIG-FP's management fee account for five years before using cash for any other purpose; and (iii) AIG-FP would forfeit unearned fees if PNC liquidated the SPE entities early. Thus, AIG-FP's true initial investment fell below the absolute bare minimum 3% threshold required under GAAP, as GAAP requires any structuring fees to be offset against initial investments. Nevertheless, the PAGIC I SAS-50 Opinion Letter issued by E&Y did not address the fact that the payment of "management" fees to AIG-FP in the SPE I transaction reduced AIG-FP's "substantive capital investment" below the 3% threshold, and therefore that PAGIC I should have been included in PNC's financial statements and regulatory reports. In fact, as articulated herein, starting in May 2001, National Accounting Firm A had directly raised concerns over the identically structured "management" fee with respect to another proposed special purpose entity transaction. E&Y ultimately provided another public company with a revised Marketing SAS-50 Opinion Letter in connection with National Accounting Firm A's request. Nevertheless, E&Y's PAGIC I SAS-50 Opinion Letter in June of 2001 for SPE I did not address AIG-FP's management fee at all.

74. Prior to E&Y issuing its PAGIC I SAS-50 Opinion Letter, PNC reviewed a draft of the Opinion Letter, and asked E&Y why the draft omitted addressing the management fee. E&Y responded that it was a business issue, not an accounting issue, and did not revise or otherwise alter its Opinion Letter. Ultimately, as discussed below, the PAGIC I Opinion Letter was finalized and provided to PNC, after PAGIC I had already been formally established and non-performing assets had been transferred by PNC to PAGIC I.

75. In addition, SPE I's Class A preferred stock was non-cumulative and non-voting and could be converted at any time into Class A common stock. Thus, the SPE I Class A common stock, which was owned almost exclusively by PNC, when issued upon conversion, would confer upon PNC 99.99% of SPE I common shares which could only be voted for one specific purpose - to cause an orderly liquidation of SPE I. If PNC never elected to convert its SPE I Class A preferred stock, the stock was mandatory redeemable at its face amount of $365.8 million in 30 years. If PNC elected to convert its SPE I Class A preferred stock to SPE I Class A common stock and then voted to liquidate SPE I, AIG-FP's Class B preferred stock was entitled to a liquidation preference of up to $ 11,463,424.

76. Although AIG-FP's SPE I Class B common stock purported to give it control over the affairs of the special purpose entity, including the authority to declare dividends on the Class A preferred stock held by PNC, AIG-FP did not have the authority to liquidate SPE I during the first five years of its existence, except with PNC's consent. PNC, on the other hand, could cause a liquidation of SPE I at any time, without AIG-FP's consent. This feature was critical to the structure because if the non-performing assets PNC had transferred to SPE I improved in value, PNC could recapture the benefit of that improvement by converting its Class A preferred stock to Class A common stock and voting to liquidate SPE I.

77. Accordingly, the SPE I transaction did not satisfy the GAAP requirement that the majority owner of the SPE have substantive risks and rewards of ownership of the assets of the SPE.

78. PNC's $365.8 million cash contribution to SPE I was used as follows: (a) approximately $285 million was used to purchase troubled commercial loans and unfunded commitments directly from PNC Bank, (b) approximately $78 million was used to purchase a

zero-coupon U.S. Treasury security that would mature in 30 years in its face amount of $365 million, and (c) approximately $3 million was used to pay an up front $2.7 million "management fee" to AIG-FP at the closing of the first special purpose entity. Thus, AIG-FP's initial investment was immediately reduced. In fact, the special purpose entity was required to pay a management fee of approximately $2.7 million per year for the first five years of SPE I's existence and 75 basis points (i.e., 0.75%) of the total assets of SPE I per year thereafter to AIG-FP.

79. The $2.7 million up-front management fee, when coupled with the liquidation preference, guaranteed that AIG-FP would turn a profit on its initial capital investment, thereby removing all risk of ownership for AIG-FP.

80. That the "management fees" were primarily compensation to AIG for structuring the PAGIC transactions and for taking the assets and liabilities of the PAGIC entities onto its balance sheet, and not for providing management services to the SPEs, is further evidenced by the fact that AIG recognized the entire amount of the present value of fees for the initial five years of the PAGIC I transaction in its financial statements for the year ending December 31, 2001. Had AIG considered such fees to be for managing the structure, under GAAP, it could not have recognized the entirety of the yearly management fees for all years after it provided its management services for only that year.

81. The special purpose entity structure also provided for PNC Bank, PNC's principal banking subsidiary, to service all of the loans transferred to SPE I in exchange for a loan servicing fee of 50 basis points (i.e., 0.5%) of the aggregate loan amounts, or approximately $1.5 million per year. PNC retained the relevant loan records and established bank accounts for loan

collections. As the loan servicer, PNC received payments, was responsible for valuing the loans on an annual basis, and developed action plans for managing the workout of the loans.

82. PNC recorded the Class A preferred stock received from SPE I as debt securities available for sale (valued at $365,800,000), while removing from the loan portfolio of PNC Bank, the loans that were transferred to SPE I. The SEC order specifically found that PNC had understood that, had the non-performing loans and assets remained on its books, it ultimately would have had to recognize losses resulting from such assets in its earnings.

83. Although E&Y provided PNC with a draft of its Opinion Letter for SPE I prior to June 28, 2001, SPE I's closing date, PNC did not obtain a final, signed Opinion Letter from E&Y until on or around July 18, 2001. Nevertheless, E&Y backdated the Opinion Letter to June 21, 2001, in order to reflect a date prior to the closing of SPE I, prior to turning the letter over to regulators.

SPE II

84. On September 27, 2001, AIG-FP, acting through the same subsidiary, organized the second special purpose entity as a Delaware limited liability company ("SPE II" or "PAGIC II"). In connection with the closing transactions, which once again took place just three days before the close of PNC's 2001 Third Quarter, AIG-FP contributed $16,918,904 in cash to SPE II. The terms of the transaction, including the liquidation preference in SPE I, were very similar to the terms of SPE I. Once again, AIG-FP was identified as the managing member of SPE II, and SPE II was required to pay AIG-FP an up-front "management fee" at the closing and periodically thereafter, thereby immediately reducing AIG-FP's initial investment.

85. PNC, through a non-bank subsidiary, contributed a total of $538,816,528 of assets to SPE II: $326,896,933 in loans and $211,919,595 in cash. In exchange, PAGIC II issued to PNC Bank shares of Class A preferred stock in PAGIC II. PNC Bank immediately assigned

these shares to the same non-bank subsidiary of PNC that held shares of PAGIC I, and the shares were maintained on PNC's financial statements as debt securities available for sale.

86. The terms of the Class A preferred stock in SPE II were very similar to the terms of the SPE I Class A preferred, and PNC entered into an agreement to continue to service the transferred loans. PNC's cash contribution was used to cover unfunded commitments and letters of credit with respect to the loans ($89,493,162), the purchase of a zero-coupon Treasury bond ($118,493,760), expenses, and the first year's management fee ($3,682,672), payable at closing to AIG-FP. As a result, AIG-FP's true initial investment fell below the 3% threshold required by GAAP.

87. Once again, AIG-FP's cash contribution to SPE II was never at risk. As was the case with SPE I, although PNC's payment of structuring fees to AIG for SPE II reduced AIG's "substantive capital investment" below the absolute bare minimum 3% level required by GAAP for non-consolidation of the SPEs by PNC, E&Y's PAGIC II SAS-50 Opinion Letter failed to address the fact that the prepayment of structuring fees reduced AIG-FP's "substantive capital investment" below the 3% level, and therefore that SPE II should have been consolidated in PNC's financial statements and regulatory reports. As was the case with E&Y's Opinion Letter with SPE I, E&Y's Opinion Letter for SPE II did not address AIG's "management" fee at all, and was not provided to PNC until several months after SPE II was closed. Nevertheless, E&Y once again backdated its Opinion Letter for SPE II to September 21, 2001 (or six days prior to the closing of SPE II on September 27, 2001) prior to turning it over to regulators.

SPE III

88. On November 30, 2001, AIG-FP, acting through the same subsidiary, organized the third special purpose entity as a Delaware limited liability company ("SPE III" or "PAGIC III"). In connection with the closing transactions, AIG-FP contributed $8,021,417 in cash to SPE

III. The terms of the transaction, including the liquidation preferences in SPEs I and II, were very similar to the terms of SPEs I and II. Once again, AIG-FP was identified as the managing member of SPE III, and SPE III was required to pay AIG-FP an up front "management fee" at the closing and periodically thereafter.

89. PNC, through a non-bank subsidiary, contributed approximately $252 million in cash and equity assets (including venture capital investments and related commitments) to SPE III in exchange for its Class A preferred stock. PNC recorded the SPE III Class A shares as debt securities available for sale (valued at $252 million). A nonbank subsidiary of PNC was retained to service the venture capital assets. PNC's cash contribution was used to cover certain unfunded commitments, to purchase a U.S. Treasury zero-coupon bond, and to cover expenses, including the first year's management fee of $1,716,950 payable at closing to AIG-FP. SPE III also purchased a guaranteed investment contract from AIG-FP which could be drawn upon to satisfy unfunded commitments. As a result, AIG-FP's true initial investment fell below the 3% absolute bare minimum threshold required by GAAP.

90. Once again, AIG-FP's cash contribution to SPE III was never at risk.

91. Although E&Y did not finalize its Opinion Letter on SPE III until on or around December 12, 2001, two weeks after SPE III closed on November 30, 2001, E&Y back-dated its Opinion Letter to November 29, 2001. December 12, 2001 was one day prior to the date on which E&Y assisted PNC in providing its regulatory response letter and material to the federal bank regulators.

92. In sum, prior to being caught by federal banking regulators, the PAGIC Defendants had caused PNC to transfer $592 million in loans (of which $132 million was non-performing loans), and $170 million in venture capital investment to special purpose entities

without disclosing any material facts regarding such transfers. As a result, these Defendants are liable for this artifice to defraud under Section 10(b) of the Exchange Act.

Prior to and During the Class Period AIG-FP and E&Y
Market the SPE Structure to Other Public Companies

93. In March 2001, even before PNC was introduced to PAGIC, these structures were being marketed by AIG-FP and E&Y to other public companies. Similar to the promotional materials that were ultimately provided to PNC, the promotional materials provided to these other public companies stated that the contemplated accounting treatment for the structure was "based upon advice from Ernst & Young."

94. According to the SEC AIG Complaint, on May 29, 2001, representatives of potential customer "National Insurance Company A" met with National Accounting Firm A, its outside auditor, to discuss "soft spots" that the auditor had noted in its analysis of the accounting for the proposed special purpose entity type transaction. Specifically, the "soft spot" included concerns that AIG-FP's capital investment might fall below the absolute bare minimum (3%) capital investment required for non-consolidation of the special purpose entity by National Insurance Company A if AIG-FP received a "large prepayment of its fees or it its fees were not received in exchange for services rendered by AIG." On that same day, National Insurance Company A informed AIG-FP of the "soft spots" that National Accounting Firm A had recognized.

95. Also, on that same day, in response to National Accounting Firm A's noted concern, AIG modified the proposed SPE type structure for National Insurance Company A to increase AIG's capital investment from 3% to 5%. National Insurance Company A also requested, and E&Y prepared, a revised Marketing SAS-50 Opinion Letter that addressed modifications to the structuring fees. E&Y, however, did not inform PNC of National

Accounting Firm A's concerns over the "soft spots," or that it had resulted in E&Y preparing another Marketing SAS-50 Opinion Letter in response to the request of National Insurance Company A. In contrast, E&Y advised PNC that other national accounting firms had agreed with E&Y regarding the appropriate accounting treatment.

96. On November 20, 2001, National Insurance Company A received a revised draft of E&Y's SAS-50 letter which addressed the prepayment of the "structuring fee" directly to AIG-FP by National Insurance Company A and reads as follows:

> We also considered the effect of the structuring fee required to be paid by Investor to the Class B Common holder, as managing member, during the life of the transaction and for a minimum period of five years. Our consideration focused on whether this fee could represent a return of the initial investment of the independent third party investor in the Class B interest thereby indicating that its initial investment is inadequate. We observe, however, that even if the amount of the required payments (.50% of assets for five years) were deducted from the initial investment by [AIG] in the Class B interest, its initial investment would still exceed the minimum amount required by EITF Topic D-14. Therefore, without further considering the nature of such payment, we concluded that it does not affect the adequacy of the initial investment required by Topic D-14.

97. Thus, notwithstanding the fact that E&Y's revised the Marketing SAS-50 Opinion Letter intentionally attempts to avoid addressing the impact of prepayment of fees or structural fees due to an increase in the initial investment, E&Y affirmatively acknowledges the possibility that such fees could reduce the initial investment and upset the structure's true purpose. Nevertheless, E&Y did not address the issue in any of the Opinion Letters that it provided to PNC concerning the PAGIC transactions, and did not inform PNC of the revised Marketing SAS-50 Opinion Letter it provided to National Insurance Company A.

98. On November 29, 2001, E&Y provided a final version of the revised SAS-50 Opinion Letter to AIG-FP at the request of National Insurance Company A and National Accounting Firm A, which contained the identical statements as the November 20, 2001 draft.

National Insurance Company A did not consummate the proposed special purpose entity transaction and E&Y did not revise its advice to PNC.

99. In May 2001, AIG proposed the SPE type transaction to "National Insurance Company B," which asked its auditor, also National Accounting Firm A, to review the proposed transaction. Also in May 2001, an AIG employee informed National Insurance Company B about the "soft spots" that National Accounting Firm A had identified in its accounting analysis while reviewing the proposed SPE transactions for National Insurance Company A. National Insurance Company B did not consummate the proposed SPE-type transaction.

100. At the request of National Insurance Company C, who AIG-FP had provided marketing materials with respect to the SPE type product, which included a representation that GAAP treatment for the transactions was "based upon related advice from Ernst & Young," AIG sent National Insurance Company C a term sheet in which AIG-FP increased its equity investment for a proposed SPE from 3% to 5%. The request for an increased investment was based upon the advice of National Accounting Firm A, who was also National Insurance Company C's outside auditor. Thus, it appears that at least one accounting firm has no difficulty reporting the same advice to multiple clients. National Insurance Company C did not consummate the proposed SPE transaction.

MATERIAL MISREPRESENTATIONS MADE DURING THE CLASS PERIOD

PNC's July 19, 2001 Press Release, Analyst Reports, PNC's July 25th Prospectus Supplement and PNC's 2001 Second Quarter Form 10-Q

101. On July 19, 2001, the first day of the Class Period, the PNC Defendants issued a press release announcing PNC's financial results for the second quarter and six months ended June 30, 2001. The press release included the following materially false and misleading statements:

(a) In the section entitled "Second Quarter 2001 Highlights," the PNC Defendants claimed that "[n]onperforming assets remained relatively stable, increasing $4 million during the quarter to $390 million at June 30, 2001."

(b) In the section entitled "Asset Quality Review," the PNC Defendants announced that "the ratio of nonperforming assets to total loans, loans held for sale and foreclosed assets was .85 percent at June 30, 2001, compared with .81 percent at March 31, 2001 and .67 percent at June 30, 2000." The PNC Defendants attributed the increase in the above-mentioned ratio to "the downsizing of the loan portfolio."

(c) In the section entitled "Second Quarter 2001 Balance Sheet Review," the PNC Defendants stated that "[t]he corporation has been pursuing a number of initiatives designed to improve the risk and return characteristics of its lending businesses. These include the sale of the residential mortgage banking and credit card businesses and the continued downsizing of the indirect automobile lending portfolio."

(d) Defendant Rohr was quoted in the release as saying that "we are pleased that asset quality remained ***relatively stable as a result of continued actions to downsize our institutional lending business."*** [Emphasis supplied].

102. Prior to PNC issuing the July 19, 2001 press release, E&Y reviewed a draft of the release that, unlike the version that was disseminated to the market, disclosed the SPE I transaction. After reviewing the draft, however, E&Y provided specific guidance to PNC to omit any reference to SPE I, contending that singling it out from the other sales transactions in which PNC engaged might call into question the accounting treatment of SPE I. Based upon E&Y's guidance, the reference to SPE I was removed from the final release.

103. On July 20, 2001, an analyst from Keefe, Bruyette and Woods stated the following which was based upon information provided directly by the PNC Defendants:

> "Asset quality remains a bright spot. Credit administration remains a strength at PNC, as management's efforts at reducing the bank's risk profile have paid off. Specifically, non-performing assets amounted to $390 million in the quarter, ***a very modest one percent increase when compared to the first quarter results. The nonperforming asset ratio came in at a very low 86 basis points of related assets***. Net charge-offs amounted to $45 million, a substantial decline when compared to the prior quarter figure of $80 million. On a go forward basis, ***PNC***

expects asset quality measures to remain generally stable, with net charge-offs coming in at the higher end of the 35 to 45 basis points earlier guidance." [Emphasis supplied.]

104. On July 25, 2001, the PNC Defendants filed a Prospectus Supplement to a Prospectus dated October 22, 1999 (the "July 25th Prospectus Supplement") relating to the offer and sale by a subsidiary of PNC of $300 million of floating rate senior notes due August 1, 2003 and $700 million of 5.75% senior notes due August 1, 2006. The PNC Defendants stated that the proceeds from the offering would be used for, among other things, advances to PNC and its subsidiaries to finance their activities. This statement was materially false and misleading as no disclosure was made that such financing of activities could include purchases of securities from special purpose entities in exchange for non-performing assets of PNC.

105. On August 14, 2001, the PNC Defendants filed PNC's 2001 Second Quarter Form 10-Q with the SEC, which was signed by Defendant Haunschild, and which repeated the materially false and misleading financial results that the Misrepresentation Defendants issued in the July 19th press release.

106. In addition, as reflected in the following chart appearing in PNC's 2001 Second Quarter Form 10-Q, the PNC Defendants claim to have sold $110 million in non-performing assets from January 1 through June 30, 2002.

CHANGE IN NONPERFORMING ASSETS

In millions	2001	2000
January 1	$372	$325
Transferred from accrual	371	190
Returned to performing	(13)	(3)
Principal reductions	(96)	(73)
Sales	(110)	(11)

Charge-offs and other	(134)	(75)
June 30	$390	$353

107. As reflected in the following chart which also appeared in the 10-Q, among the "Securities Available For Sale" was a line entry for $439 million in "other debt," which was materially overstated as it secretly included $366 million of PNC's investment in the first SPE I.

DETAILS OF SECURITIES AVAILABLE FOR SALE

In millions	Amortized Cost	Fair Value
JUNE 30, 2001		
Debt Securities		
U.S. Treasury and government agencies	$ 1,467	$ 1,439
Mortgage-backed	7,643	7,601
Asset-backed	1,333	1,317
State and municipal	67	69
Other debt	439	439
Corporate stocks and other	401	393
Total Securities available for sale	$11,350	$11,258

108. PNC's Second Quarter 2001 Form 10-Q also stated that:

> The unaudited consolidated interim financial statements include the accounts of PNC and its subsidiaries, most of which are wholly owned. Such statements have been prepared in accordance with accounting principles generally accepted in the United States. All significant intercompany accounts and transactions have been eliminated. In the opinion of management, the financial statements reflect all adjustments of a normal recurring nature necessary for a fair statement of results for the interim periods presented.

109. The above-quoted statements appearing in the July 19th press release, the July 20th analyst report, the July 25th Prospectus Supplement and the 2001 Second Quarter 10-Q were materially false and misleading when made for the following reasons:

(a) With just three days remaining in the 2001 Second Quarter, the PAGIC Defendants had caused PNC to enter into transactions with a special purpose entity. PNC provided the overwhelming majority of the assets for this entity, a subsidiary of AIG-FP served as the purported owner and managing member of the entity, in exchange for an annual management fee payable up front to AIG-FP and a liquidation preference approximating its initial investment, and E&Y had provided specific guidance to both PNC and AIG-FP with respect to the transaction. The sole purpose for the creation of this entity was to allow PNC to remove non-performing assets from its books;

(b) The reported $390 million in non-performing assets was materially understated by 21% as the reported figures failed to include approximately $84 million in non-performing assets which had been transferred to SPE I just three days before the end of the quarter;

(c) Even if the accounting for the transferred assets was performed in accordance with GAAP, which for the reasons set forth herein it was not, it was materially misleading to report that non-performing assets had remained "relatively stable" during the quarter without disclosing the circumstances surrounding the "transfer of non-performing assets." In order to make the statements that were made not materially misleading, such disclosures should have included, at a bare minimum, the purpose of the transfer, the date of transfer, PNC's interest in the special purpose entity, the structure of the special purpose entity, the nature of the assets transferred and E&Y's involvement in the creation of PAGIC I;

(d) The reported ratio of nonperforming assets to total loans, loans held for sale and foreclosed assets of .85% was also understated by 21% as the reported figure failed to include the nonperforming assets still owned by PNC which were effectively "parked" in the special purpose entity. Once again, it was materially false and misleading to attribute the increase in the ratio to the "downsizing of the loan portfolio," without providing the additional disclosures set forth in the preceding subparagraphs;

(e) It was materially false and misleading to claim that PNC had sold $110 million of non-performing assets since January 1, 2001, without also disclosing the material facts set forth above and, in particular, that 76% of such "sales" ($84 million), were made to SPE I created by the PAGIC Defendants with three days left in the quarter. In fact, PNC effectively purchased its own non-performing assets as PNC contributed cash to the

special purpose entity which was immediately utilized to purchase such assets from PNC;

(f) It was materially false and misleading to characterize $439 million as "other debt" in securities available for sale, without explaining that $366 million of this amount related to PNC's investment in SPE I. In fact, among other things, because PNC had retained too substantial of an interest in SPE I, PNC's actual interest was in the assets themselves and not in the Preferred Stock issued to PNC by SPE I, as described below;

(g) It was materially false and misleading to continue touting the reportedly successful "corporate strategy" of reducing exposure to non-performing assets by referring to "continued" actions to downsize the loan portfolio, without disclosing that the strategy was now dependent upon sham transactions whereby the PAGIC Defendants transferred a material portion of PNC's non-performing assets just days before the end of the quarter to SPE I, while still maintaining a significant interest and effective control of the assets that were in violation of GAAP; and

(h) PNC's financial results were not fairly presented, nor were they prepared in accordance with GAAP for the reasons set forth below.

110. It was also materially false and misleading to omit disclosure of the risks associated with utilizing special purpose entities, including the risk that losses would ultimately have to be recognized on transferred assets if the special purpose entity structure did not comply with GAAP and the assets purportedly held in these special purpose entities had to come back on PNC's books as assets "held for sale." This omission was exacerbated by the fact that the Misrepresentation Defendants failed to disclose the existence of the FRB's inquiry into SPE I, making it more likely that the assets would ultimately have to be returned to PNC and reflected on PNC's books.

111. E&Y also reviewed, consulted with, and provided specific guidance to PNC with respect to the financial information set forth in the July 19, 2001 press releases, which were repeated in PNC's 2001 Second Quarter Form 10-Q, as well as the PAGIC Defendants' decision not to disclose the SPE I transaction itself, and thus, is also liable for the misrepresentation

contained therein. Consequently, all of the Misrepresentation Defendants substantially participated in the issuance of the false and misleading statements and omissions set forth above.

The PNC Defendants and E&Y Continue to Issue False and Misleading Statements Even While Federal Regulators Investigate the PAGIC Transactions

112. In early September 2001, the PNC Defendants were contacted by and met with representatives of the OCC and FRB concerning questions about SPE I. These initial meetings led to three distinct questions being posed by federal regulators on September 26, 2001, concerning SPE I: (i) whether the SEC reviewed E&Y's opinions concerning PAGIC; (ii) whether E&Y's national office reviewed and agreed with E&Y's letter opinions; and (iii) whether AIG was consolidating the loans that were included in the PAGIC I transaction.

113. Immediately after federal regulators made their initial inquiry, PNC sought guidance from E&Y in answering the regulators' questions. Based upon its discussions with E&Y, PNC informed the federal regulators that it had not asked the SEC to review the SPE I transaction because it was comfortable with E&Y's advice, and because E&Y had verbally represented that other E&Y clients had entered into transactions that were very similar to SPE I. PNC also informed the federal regulators that E&Y's national office had signed off on the SPE I transaction and had helped AIG to develop the PAGIC structure, which had also been considered by two other accounting firms. The regulators were also advised that PNC did not know what AIG was consolidating with respect to its own financials. However, PNC and E&Y were now on notice that AIG's accounting treatment was a relevant inquiry as to the treatment of the overall structure for PNC.

PNC's September 18th Registration Statement

114. On September 18, 2001, PNC filed with the SEC a shelf registration statement (the "September 18th Registration Statement"), signed by all of the Individual Defendants, that

would allow PNC to offer and sell over time approximately $4 billion of common stock, preferred stock, warrants, guarantees, depositary shares and debt securities. The September 18th Registration Statement incorporated by reference, among other things, the 2001 Second Quarter Form 10-Q, and was therefore, materially false and misleading for the same reasons set forth in the preceding section.

115. Included in the September 18th Registration Statement was E&Y's representation that PNC's year-end 2000 financial statements were fairly presented and prepared in compliance with GAAP. In this regard, the Registration Statement reads as follows:

> We consent to the reference to our firm under the caption "Experts" in the Registration Statement on Form S-3 and the related Prospectus of The PNC Financial Services Group, Inc. and PNC Funding Corp for the registration of $4,297,000,000 of common stock, preferred stock, guarantees, depositary shares, warrants and debt securities and to the incorporation by reference therein of our report dated January 31, 2001, with respect to the consolidated financial statements of The PNC Financial Services Group, Inc. incorporated by reference in its Annual Report on Form 10-K for the year ended December 31, 2000 filed with the Securities and Exchange Commission.

116. However, by virtue of, among other things, the fact that E&Y had approved the very structure of the special purpose entity, first on behalf of AIG-FP, and later, on behalf of PNC, and thus, knew or recklessly disregarded that SPE I did not permit PNC to remove the non-performing assets from its financial statements without consolidating the results, and that PNC had not disclosed the existence of the special purpose entity in its 2001 Second Quarter Form 10-Q, E&Y had an obligation to disclose these material facts to the SEC and/or the investing public, rather than simply attesting to the accuracy of the prior year's results.

117. On October 18, 2001, the PNC Defendants issued a press release announcing PNC's results for the third quarter of 2001 ended September 30, 2001. In that release, the Misrepresentation Defendants made numerous false and misleading statements including the following:

(a) PNC reported net earnings of $298 million or $1.02 per diluted share for the quarter;

(b) The press release also included among its "Third Quarter 2001 Highlights" the fact that nonperforming assets declined to $374 million at September 30, 2001 compared with $390 million at June 30, 2001;

(c) In the section entitled "Asset Quality Review" the ratio of nonperforming assets to total loans, loans held for sale and foreclosed assets was reported to be .85 percent at September 30, 2001 compared with .85 percent at June 30, 2001 and .68 percent at September 30, 2000; and

(d) The above-referenced ratio was reported to have remained "flat" compared with the prior quarter as it was claimed that the benefit of a decrease in nonperforming loans was offset by a reduction in loans outstanding.

118. PNC's well-publicized corporate initiative was also repeated in the October 18th press release as follows:

> "The Corporation has been pursuing a number of initiatives designed to improve the risk and return characteristics of its lending businesses. These include the sale of the residential mortgage banking and credit card businesses and downsizing certain non-strategic lending businesses."

119. Defendant Rohr was also quoted in the October 18th press release as saying:

> [O]ur diverse mix of businesses, including solid performance from our Regional Community Bank, BlackRock and PFPC, drove earnings that were within the range of analysts' estimates while we added to loan loss reserves and ***reduced nonperforming assets.*** [Emphasis supplied].

120. By October 23, 2001, federal regulators had formalized their concerns regarding PNC's accounting treatment for the first two special purpose entity transactions in a letter sent to PNC. Specifically, the FRB requested that PNC provide relevant cites in GAAP and other information that supported PNC's position with respect to its accounting treatment of PAGIC I and II. Although the FRB letter recognized that E&Y had issued Opinion Letters concerning the PAGIC transactions, it stated that the FRB was "not convinced by the arguments presented." The FRB requested that PNC respond to the FRB's formalized inquiry by December 2001.

121. Once again, PNC turned to E&Y for assistance in preparing a response to the regulators' inquiries. In fact, within days of PNC receiving the October 23 letter, E&Y assured PNC that its opinion concerning the accounting for the SPEs, which PNC had relied upon with respect to its accounting treatment of the PAGIC transactions, was correct. Although PNC did not submit a formal response to the FRB's October 23 letter until December 12, 2001, PNC, with E&Y's substantial participation, prepared numerous draft responses in October and November 2001. By this time, unbeknownst to PNC, E&Y had already been alerted to the "soft-sports" identified by National Accounting Firm A as set forth above.

122. On October 23, 2001, the same day that PNC received the formalized FRB inquiry, the PNC Defendants filed with the SEC a Prospectus utilized in the offer and sale of approximately $1 billion worth of debt securities, be sold on or about October 29, 2001 (the "October 23rd Prospectus Supplement"). Approximately $600 million of floating rate senior notes due in 2004 and $400 million of 5.75% senior notes due in 2006 were being sold pursuant to this offering.

123. The October 23rd Prospectus Supplement included a section titled "Recent Developments" in which the materially false and misleading statements regarding PNC's 2001 Third Quarter income, earnings per share, non-performing asset levels and related ratios set forth in the October 18th press release were repeated once again without reference to any transactions with SPE I or SPE II. This Prospectus also incorporated by reference, PNC's materially false and misleading Form 10-Q for the 2001 Second Quarter.

124. In the October 23rd Prospectus Supplement, it was reported that the proceeds from the offering would be used for, among other things, advances to PNC and its subsidiaries to finance their activities. This statement was materially false and misleading as no disclosure was

made that such financing of activities could include purchases of securities from special purpose entities in exchange for non-performing assets of PNC.

125. The October 23rd Prospectus Supplement included a section which reflects that E&Y, once again, consented to the inclusion of its imprimatur of PNC's financial results, which reads as follows:

> Ernst & Young, LLP, independent auditors, have audited PNC's consolidated financial statements incorporated by reference in PNC's Annual Report on Form 10-K for the year ended December 31, 2000, as set forth in their report, which is incorporated by reference in this document. PNC's consolidated financial statements are incorporated by reference in reliance on Ernst & Young LLP's report, give on their authority as experts in accounting and auditing.

126. Also included in the October 23rd Prospectus Supplement under a section entitled "General Information" is the following description of E&Y's role in preparing financial statements of PNC:

> (4) . . . Ernst & Young provided various audit and other services for PNC during 2000. Such services included an audit of annual consolidated financial statements, interim reviews of quarterly consolidated financial statements, review and consultation connected with certain filings with the Securities and Exchange Commission, internal control reviews required by regulatory authorities and certain contractual agreements or requested by PNC's management or internal audit staff, consultation on tax, financial accounting and reporting matters, and meetings with the audit committee of the Board of Directors of PNC.

127. Shortly thereafter, in anticipation of a November 1, 2001 conference call to be held between PNC and the FRB, PNC and E&Y discussed the FRB's stated concerns with respect to the PAGIC transactions and reviewed a proposed agenda for the November 1 call. E&Y once again assured PNC that its accounting treatment of the SPEs was correct.

128. During the November 1 call, in which E&Y participated, the accounting treatment for the SPE transactions was discussed at length, including the risk and reward and independent equity issues. After the call, notwithstanding the FRB's stated "concerns" about PAGIC I and II, E&Y repeated its assurances to PNC that PAGIC I and II did not have to be consolidated.

129. On November 14, 2001, the PNC Defendants filed PNC's 2001 Third Quarter Form 10-Q with the SEC for the quarter ended September 30, 2001. The Third Quarter 10-Q, which was signed by Defendant Haunschild, and repeated the materially false and misleading statements made in the October 18th press release.

130. Prior to PNC issuing the Third Quarter 10-Q, E&Y reviewed drafts of the Form 10-Q and provided the PNC Defendants with specific guidance with respect to the contents of the finalized version. Specifically, upon the direction of E&Y, the PNC Defendants deleted a reference to PAGIC as a "securitization" that has been made in a previous draft. As the Misrepresentation Defendants knew or recklessly disregarded, had PAGIC II been referred to as a securitization pursuant to FASB's Statement of Financial Accounting Standards ("SFAS"), PNC would have been required to disclose certain qualitative aspects of the PAGIC II transaction in its financial statements.

131. SFAS No. 140 provides accounting and financial reporting standards for transfers of financial assets. These standards focus on control, and provide that a transfer of financial assets is to be accounted for as a sale only if the transferor surrenders control over such assets. The transferor is deemed to have surrendered control over the financial assets if, among other things, the transferor does not maintain effective control over the transferred assets through an ability to unilaterally cause the holder to return specific assets.

132. In this regard, ¶¶ 52 through 54 of SFAS No. 140 provide that:

> ...[A]ny unilateral right to reclaim specific assets transferred to a qualifying SPE maintains the transferor's effective control over those assets if the right conveys more than a trivial benefit to the transferor.

* * * *

133. A right to reclaim specific transferred assets by paying their fair value when reclaimed generally does not maintain effective control, because it does not convey a more than

trivial benefit to the transferor. ***However, a transferor has maintained effective control if it has such a right and also holds the residual interest in the transferred assets. For example, if a transferor can reclaim such assets at termination of the qualifying SPE by purchasing them in an auction, and thus at what might appear to be fair value, then sale accounting for the assets it can reclaim would be precluded. Such circumstances provide the transferor with a more than trivial benefit and effective control over the assets, because it can pay any price it chooses in the auction and recover any excess paid over fair value through its residual interest.***

[Emphasis Supplied]

134. PNC's Third Quarter Form 10-Q contained the following additional false statements:

(a) Consolidated non-interest income for PNC was reported to have increased 13% to $789 million;

(b) Weighted Average Life of Securities Available for Sale was reported at five years and two months, as compared to four years and five months at December 31, 2000;

(c) The PNC Defendants also stated that PNC is currently evaluating strategies to mitigate the "impact of the revenue volatility of [the Equity Management] business," a business comprised of venture capital activities;

(d) Corporate Service Revenue was reported at $78 million for the 2001 Third Quarter.

135. As reflected in the following chart, in the 2001 Third Quarter 10-Q, $162 million in non-performing assets were claimed to have been sold since January 1, 2001:

CHANGE IN NONPERFORMING ASSETS

In millions	2001	2000
January	$372	$325
Transferred from accrual	513	291
Returned to performing	(14)	(3)

Principal reductions	(143)	(125)
Sales	(162)	(31)
Charge-offs and other	(192)	(103)
September 30	$374	$354

136. As reflected in the following chart which also appears in PNC's 2001 Third Quarter 10-Q, an entry for $978 million in the "other debt" portion of Securities Available for Sale appears:

DETAILS OF SECURITIES AVAILABLE FOR SALE

In millions	Amortized Cost	Fair Value
SEPTEMBER 30, 2001		
Debt Securities		
U.S. Treasury and government agencies	$ 1,053	$ 1,059
Mortgage-backed	6,509	6,561
Asset-backed	2,472	2,601
State and municipal	65	68
Other debt	978	983
Corporate stocks and other	533	517
Total Securities available for sale	$11,610	$11,689

137. The Misrepresentation Defendants also represented in the 2001 Third Quarter Form 10-Q that:

> The unaudited consolidated interim financial statements include the accounts of PNC and its subsidiaries, most of which are wholly owned. Such statements have been prepared in accordance with accounting principles generally accepted in the United States. All significant intercompany accounts and transactions have been eliminated. In the opinion of management, the financial statements reflect all adjustments of a normal recurring nature necessary for a fair statement of results for the interim periods presented.

138. The above-quoted statements appearing in the October 18th press release, the October 23rd Prospectus Supplement and the 2001 Third Quarter Form 10-Q were each materially false and misleading for the following reasons:

(a) Once again, just three days prior to the close of the 2001 Third Quarter, the PAGIC Defendants caused PNC to enter into another set of transfers to form a second special purpose entity. The structure was essentially the same as the first special purpose entity, with all of the same parties playing the same roles. In this regard, PNC provided the majority of the assets, including non-performing assets, a subsidiary of AIG-FP served as the purported owner and managing member of the second special purpose entity and E&Y had provided guidance with respect to the accounting treatment for both PNC and AIG-FP. The purpose of this second special purpose entity was the same as the first -- to allow PNC to remove non-performing assets from its books;

(b) Even if the accounting for the transferred assets was performed in accordance with GAAP, which for the reasons set forth below, it was not, it was materially misleading to refer to downsizing initiatives or to report that non-performing assets had remained "flat" during the quarter, without disclosing the circumstances surrounding the "transfers" to the first two special purpose entities. It was also materially false and misleading to refer to a "benefit" of a decrease in non-performing assets without disclosing that this "benefit" was achieved, in material part, by PNC "selling" non-performing assets to itself. In order to make the statements that were made not materially misleading, such disclosures should have included, at a bare minimum, the purpose of the transfers, the dates of the transfers, PNC's interest in the two special purpose entities, the structure of the special purpose entity and the nature of the assets transferred;

(c) The $374 million reported in non-performing assets was materially understated by approximately 29% as the reported figure failed to include

$152 million in non-performing assets which had been transferred to the two special purpose entities;

(d) The reported ratio of nonperforming assets to total loans, loans held for sale and foreclosed assets of .85% was understated by 38.8% as the reported figure failed to include the non-performing assets still owned by PNC which were essentially "parked" in the two special purpose entities. The true ratio was 1.18%, an increase from the prior quarter and almost twice the ratio of the prior year;

(e) It was also misleading for the Misrepresentation Defendants to discuss "earnings that were within the range of analysts' estimates" and that such earnings had been achieved while PNC had "reduced nonperforming assets," without disclosing the material fact that such results were only achieved through the use of special purpose entity transactions;

(f) The $298 million in reported net income and the corresponding $1.02 in earnings per share were each materially overstated by approximately 17% as the reported figures failed to include $51 million in losses resulting from non-performing assets which had been transferred to the two special purpose entities, losses which GAAP required to be included with PNC's results;

(g) Because, among other reasons, PNC had retained too substantial of an interest in the assets transferred to the two special purpose entities, PNC's actual interests were in the assets themselves and not in the preferred stock issued to PNC by these special purpose entities, as described below. As a result, the "other debt" portion of "Securities Available for Sale," originally reported at $978 million, was materially overstated on PNC's September 30, 2001 balance sheet by approximately $638 million as the figure included PNC's ownership of preferred stock in the first two special purpose entities;

(h) In stark contrast with the originally reported 5 years and 2 months, as reflected in the restatement, Weighted Average Life of Securities Available for Sale was, in reality, 2 years and 11 months, an overstatement of 43.5%. In addition to constituting a material overstatement, this statement contributed heavily to the false impression that PNC was cleaning up its balance sheet by removing low quality assets, when in fact, asset quality was actually worsening as evidenced by the shortened life span of PNC's Securities Available for Sale;

(i) As with the prior quarter, it was not disclosed that the reportedly successful "corporate strategy" of reducing exposure to non-performing assets was entirely dependent upon sham transactions whereby the PAGIC Defendants transferred a material portion of PNC's non-performing assets just days before the end of the quarter to special purpose entities while still

maintaining a significant interest and effective control of the assets in violation of GAAP;

(j) It was materially false and misleading to claim that PNC had sold $162 million of non-performing assets since January 1, 2001, without also disclosing that approximately 85% of such "sales" ($137 million) were made to the first two special purpose entities with only days remaining in the respective quarters. As set forth below, PNC was essentially "selling" its non-performing assets to entities it completely controlled, thereby selling assets to itself;

(k) Corporate Services Revenue, originally reported at $78 million, was, in reality, a loss of $3 million;

(l) PNC's consolidated non-interest income originally reported at $789 million, was overstated by 10%, as true non-interest income was $707 million for the quarter;

(m) It was materially false and misleading to discuss the fact that PNC was "currently evaluating" strategies to mitigate the impact of losses from venture capital activities, when in fact, the PAGIC Defendants had already decided on a course of action whereby troubled investments would be transferred to the third special purpose entity on November 30, 2001;

(n) PNC's financial results were not fairly presented, nor were they prepared in accordance with GAAP for the reasons set forth below; and

(o) Neither the Prospectus, nor the 2001 Third Quarter Form 10-Q made any mention whatsoever regarding the FRB's inquiries into PNC's accounting for the first special purpose entity, despite the fact that the letter from the FRB was received prior to the filing of the Prospectus and the 2001 Third Quarter 10-Q, or that PNC had turned to its auditor, E&Y, immediately after it received the FRB's letter for assistance in preparing a response to the regulators inquiries.

139. The reported figures for the nine months ended September 30, 2001 relating to income, levels of non-performing assets, securities available for sale and related ratios were each materially false and misleading for these same reasons.

140. In addition to the material misstatements issued in connection with the October 18th Press Release, the October 23rd Prospectus Supplement and PNC's 2001 Third Quarter Form 10-Q, the Misrepresentation Defendants failed to disclose the risks associated with

utilizing special purpose entities, including losses related to purportedly transferred assets which would come back onto PNC's financial statements as assets held for sale if the special purpose entity is not formed and maintained in accordance with GAAP.

141. PNC and E&Y presented their formal response to the FRB's inquiry in a letter dated December 12, 2001. Among other things, PNC further clarified its decision to not consolidate the SPE I letter stating that:

> PNC's accounting treatment for the transaction clearly complies with GAAP in all respects.
>
> * * *
>
> PNC's views on this matter were reviewed and concurred with by Ernst & Young at both the local and national levels prior to the transaction. Ernst & Young has provided its written opinion that consolidation of PAGIC by PNC is not permitted under GAAP. ***Ernst & Young has advised us of its understanding that other national accounting firms have reviewed the transaction structure and concurred in this conclusion with respect to completed transactions.*** [Emphasis added].
>
> PNC Bank obtained a true-sale opinion from the law firm of Buchanan Ingersoll with respect to the [PAGIC] transaction.

142. E&Y's representation that other national accounting firms had signed off or concurred with the accounting treatment, was, at the very least, materially misleading as E&Y's had actual knowledge of National Accounting Firm A's concerns regarding "soft spots" in the accounting.

143. On or about December 18, 2001, in a Form 8-K filing, PNC announced that E&Y would no longer serve as its outside auditor purportedly due to newly enacted rules by the SEC that precluded independent accounting firms from providing audit clients with certain non-audit services. In this regard, PNC represented the following:

> Ernst & Young LLP currently is The PNC Financial Services Group, Inc.'s [] independent auditor of the Company's financial statements. Ernst & Young LLP also provides internal audit services to PNC.

144. No mention was made, however, of the specific special purpose entity services that E&Y was providing to PNC at this time. Consequently, this filing was materially false and misleading as it failed to disclose other services provided by E&Y to PNC, for which PNC received significant fees, including the material fact that E&Y had designed and structured the SPEs, and advised PNC in connection with three separate SPE transactions that had taken place during 2001, but which had not been consolidated in PNC's financial statements.

FRB Orders PNC to Consolidate the SPEs

145. On January 11, 2002, having reviewed PNC's December 12, 2001 response, the FRB informed PNC that it would have to consolidate the SPEs, directly questioning whether risk and reward had been transferred and whether the transactions satisfied the 3% rule. The FRB also informed PNC that it had consulted on these issues with the Enforcement and Division and Chief Accountant's Office of the SEC prior to issuing its directive to PNC.

146. On January 12 and 13, 2002, PNC met with E&Y to discuss the FRB's directive. E&Y told PNC that it expressly disagreed with the FRB's directive, and that PNC should petition the SEC to review the FRB's directive. E&Y informed PNC that there was a "zero chance" that PNC would lose the issue before the SEC. E&Y also recommended that PNC delay issuance of its earnings release scheduled for January 17, 2002 until PNC had an opportunity to assess fully the impact of consolidation on PNC's financial reports and to address the appropriate accounting treatment for the special purpose entity transactions with the SEC's Office of Chief Accountant.

147. On January 15, 2002, PNC met with FRB in Washington D.C. to discuss the FRB's directive. At the meeting, the FRB explained, in detail, the basis for its directive to PNC to consolidate the results of the special purpose entities, and why non-consolidation was not appropriate. The FRB informed PNC that, among other things, it did not believe that risk was transferred to AIG-FP and that PNC still had the risk of the loans transferred to the SPEs. The

FRB also expressed its belief that the PAGIC transactions were intended to hide PAGIC from federal regulators.

148. Although the FRB noted that, for regulatory purpose, PAGIC had to be consolidated pursuant to RAP, it also made clear that it believed there was no difference between GAAP and RAP. The FRB again informed PNC that it had conferred with the SEC in reaching its decision.

149. The FRB's stated concerns that the SPEs were designed and structured by the PAGIC Defendants to remove PNC's non-performing assets from the scrutiny of federal regulators was well-founded. In this regard, a June 18, 2001 email from Thomas Garbe, PNC's Director of Accounting Policy, sent to defendant Patterson concerning the "Proposed Transaction with AIG," reads as follows:

> This is the most critical project on our plate. ***We are awaiting a draft of the BI opinion to review and clear with Rich H[uesken, an E&Y partner].*** I understand that AIG has agreed that the zero coupon will be a government bond. The preferred stock will now end up on PNCIC's books outside of OCC scrutiny (Bob's request). ***We cleared the mechanics of this move with Rich H[uesken] this afternoon*** and are assuming that tax attorneys will have no problem with this change. [Emphasis added].

<u>January 17, 2002 Press Release</u>

150. On January 17, 2002, the PNC Defendants issued a press release announcing its year-end financial results for 2001. Prior to issuing the release, PNC, E&Y, and a law firm that represented PNC, met and held numerous discussions concerning the contents of the press release. Although E&Y had specifically advised against issuing the January 17th press release with its inclusion of 2001 Fourth Quarter and Year-End financial results, and had in fact threatened to withhold its unqualified opinion, E&Y nonetheless played a substantial role in what information was included and excluded from the final release. Based on E&Y's guidance, the

press release not only failed to consolidate the SPEs, but it also failed to disclose the fact that the FRB had required consolidation.

151. The press release included the following materially false and misleading statements:

(a) A net loss of ($326 million) or ($1.15) per diluted share for PNC's 2001 Fourth Quarter was reported. The PNC Defendants explained, however, that the loss was due to PNC's previously announced strategy to accelerate and reposition PNC's banking and venture capital business, and thus, when these charges were excluded, earnings for the 2001 Fourth Quarter would have been $289 million or $1.01 per diluted share.

(b) For PNC's full year 2001 results, the PNC Defendants announced earnings of $567 million or $1.91 per diluted share.

(c) Among the "Asset Quality Review" section of the release, the PNC Defendants claimed that "[a]sset quality measures benefited from actions taken during 2001 to reduce PNC's lending risk and improve returns. Total nonperforming assets were $268 million at December 31, 2001 compared with $374 million and $372 million at September 30, 2001 and December 31, 2000, respectively."

(d) The ratio of nonperforming assets to total loans, loans held for sale, and foreclosed assets was reported at .64 percent at December 31, 2001.

(e) Corporate services revenue was reported at $75 million for the 2001 Fourth Quarter.

(f) Securities available for sale was reported at $14.686 billion as of December 31, 2001; and

(g) The PNC Defendants claimed that as of December 31, 2001, the Equity Management division had $424 million in venture capital investments.

152. The PNC Defendants also claimed that during the year ended December 31, 2001, PNC sold $164 million in assets as reflected in the following chart:

CHANGE IN NONPERFORMING ASSETS

December 31, 2001 - in millions	Quarter ended	Year ended

Beginning of period	$374	$372
Transferred from accrual	146	659
Returned to performing	(14)	(28)
Principal reductions	(69)	(212)
Sales	(2)	(164)
Charge-offs and other	(167)	(359)
December 31	$268	$268

153. Defendant Rohr also falsely represented in the January 17th press release as stating that:

> By completing the repositioning of our banking businesses, we further enhance our earnings mix, strengthen our balance sheet and improve our risk profile.

154. The PNC Defendants also claimed in the January 17th press release that:

> Over the past year, PNC continued to reduce leverage, improve risk/return characteristics of its lending businesses and reduce exposure to earnings volatility from its venture capital portfolio. As a result, loans were reduced $12.7 billion during 2001 to $37.9 billion on December 31, 2001 through a number of initiatives, including residential mortgage securitization and runoff, transfers to hold for sale and managed reductions of institutional loans, and sales of institutional loans to subsidiaries of a third-party financial institution. Venture capital assets were reduced to $424 million through a sale to a subsidiary of the same institution and valuation discounts.

155. The above-quoted statements appearing in the January 17th press release were each materially false and misleading when made for the following reasons:

(a) Once again, during the 2001 Fourth Quarter, the PAGIC Defendants had created and caused PNC to enter into another set of transfers to PAGIC III without disclosing this material fact. The structure was essentially the

same as PAGIC I and II, with all of the same parties playing the same roles. In this regard, PNC provided the majority of the assets, including non-performing assets, a subsidiary of AIG-FP served as the purported owner and managing member of PAGIC III and E&Y had previously advised both PNC and AIG-FP with respect to the transaction;

(b) The $268 million in non-performing assets for the 2001 Fourth Quarter reported in the press release was materially understated by 31% as the reported figure failed to include $123 million in non-performing assets which had been transferred to the three special purpose entities by year end;

(c) Even if the accounting for the transferred assets was performed in accordance with GAAP, which for the reasons set forth below it was not, it was materially misleading to report that asset quality measures had benefited from actions taken during 2001 and to give the impression that the level of non-performing assets was declining quarter over quarter and year over year, without disclosing the circumstances surrounding the special propose entity "transfers." In order to make the statements that were made not materially misleading, such disclosures should have included, at a bare minimum, the purpose of the transfers, the dates of transfers, PNC's interest in the three special purpose entities, the structure of the special purpose entities, the nature of the transferred assets and E&Y's role in designing and recommending the SPE structure;

(d) The benign reference to sales to "subsidiaries of a third party financial institution" in the January 17th press release, does not even come close to approaching a sufficient disclosure that PNC was entering into transactions with special purpose entities in order to remove non-performing assets from its book. In fact, the disclosure that PNC was consolidating the results of these "subsidiaries" of AIG-FP for bank regulatory purposes without providing any explanation why such consolidation was necessary or why consolidation was not appropriate for filings made with the SEC, exacerbated its non-disclosure. Furthermore, the press release did not disclose the impact that consolidation might have on PNC's announced 2001 earnings of $1.91 per share. Had the true structure of the special purpose entities been disclosed, analysts and the investing public could have seen that PNC was still exposed to the risks which accompanied the non-performing assets which were purportedly being removed from PNC's financial statements. Had such a disclosure taken place, the investing public could have had a chance to evaluate the risks associated with utilizing such entities, including losses which would have to be recognized in connection with the special purpose entities; and the substantial likelihood that PNC would be subjected to legislative regulatory scrutiny and oversight as a result of ignoring the directive of federal regulators. PNC would be subjected to increased regulatory scrutiny and oversight in the future,

(e) Also no mention was made of the fact that PNC was consolidating the results of the third party subsidiaries for regulatory purposes, not at its discretion, but rather, as a result of a directive from the bank regulators who had specifically explained to PNC's senior management that non-consolidation was materially misleading ***before*** the PNC Defendants had issued the January 17th press release which reported PNC's results on a non-consolidated basis.

(f) The $326 million in net loss ($1.15 per share) reported in the press release for PNC's 2001 Fourth Quarter, before extraordinary charges, was materially understated by 24% as the reported figures failed to include $104 million in losses resulting from losses on non-performing assets which had been transferred to special purpose entities ($0.37 per share), and which GAAP required to be included with PNC's results as detailed below;

(g) The $567 million in net income ($1.91 per share) reported in the press release for PNC's 2001 year end, was materially overstated by 52% as the reported figures failed to include $155 million in losses ($0.55 per share) on non-performing assets which had been transferred to three special purpose entities during 2001, and $35 million in losses from discontinued operations ($0.10 per share) which PNC had failed to record in the 2001 First Quarter relating to its sale of its residential mortgage banking business;

(h) The reportedly successful "corporate strategy" of reducing exposure to non-performing assets was entirely dependent upon sham transactions whereby the PAGIC Defendants transferred a material portion of non-performing assets to special purpose entities while still maintaining a significant interest and effective control of the assets in violation of GAAP, as detailed below;

(i) As reflected in the Form 10-K ultimately filed on March 29, 2002, the true ratio of nonperforming loan to total loan, loans held for sale and foreclosed assets was .93% as of December 31, 2001, meaning that the originally reported ratio of .64% was understated by 45%. It was also disclosed that, in reality, of the $164 million in nonperforming assets purportedly sold during 2001, 85% ($139 million) were sold to special purpose entities which PNC controlled;

(j) The Form 10-K also disclosed that in stark contrast to the claim that PNC's Corporate Services division had achieved $75 million in revenue in the 2001 fourth quarter, this division had actually lost ($89 million) in the quarter;

(k) It was further revealed that the amount of venture capital assets reported on January 17th at $424 million was understated by $150 million as

venture capital assets were $574 million as of December 31, 2001, an understatement of 35%; and

(l) Defendant Rohr's statement about completing the repositioning of PNC's banking business was materially misleading without disclosing that PNC had completed its initiative only through the use of sham transactions with special purpose entities.

PNC ANNOUNCES THE NEED TO RESTATE

156. On January 29, 2002, the PNC Defendants surprised the investing community by announcing that PNC would restate its previously issued financial statements for the second and third quarters of fiscal year 2001 and revise its fourth quarter and year end earnings for 2001, which were previously announced on January 17th, but which had yet to be filed with the SEC. In the January 29th press release, PNC announced that 2001 year-end earnings had been overstated by 38% as earnings would be reduced by $155 million resulting in earnings per share for the year of $1.38, as compared to the previously announced $1.91 per share. It was further announced that these restatements would cause PNC's non-performing assets at year end 2001 to rise by $125 million (approximately 47%) from $268 to $393 million.

157. The market responded to PNC's partial disclosure as the price of PNC stock closed on January 29, 2002 down $5.79 or nearly 10% at $56.08 in extremely heavy trading volume of 6,305,100 shares.

158. In connection with the restatement announcement, PNC also announced that the "recently" received "advice" from the FRB regarding the accounting for SPEs had differed from advice PNC had previously received from E&Y. However, the investing public was not informed that the "advice" from the FRB was actually a directive to consolidate and that said "advice" was received just days prior to PNC's issuance of non-consolidated results in connection with its January 17th press release. Furthermore, neither the PNC Defendants nor E&Y itself acknowledged publicly that E&Y had specifically advised against issuing the January

17th press release with its inclusion of 2001 Fourth Quarter and Year-End financial results prepared on a non-consolidated basis – ***and that E&Y had threatened to withhold issuing an unqualified audit opinion for PNC's Form 10-K for 2001 if PNC did not challenge federal regulators directive to the SEC's Chief Accountant.*** Thus, these statements were also materially false and misleading, as they did not remove the entirety of the artificial inflation that was still present in PNC's stock price at the time the announcements were made.

159. By virtue of these misrepresentations, the Misrepresentation Defendants were able to continue concealing the material fact that PNC's management was directly involved in the PAGIC scheme, that the PNC Defendants and E&Y had made materially false and misleading statements to the investing public with actual knowledge of their falsity and that PNC had rejected the directive of federal bank regulators.

160. In its role as PNC's auditor, as well as substantially assisting AIG-FP with the design and structure of the PAGIC product, and as a "maker" of the false and misleading statements referenced above, E&Y had a duty to correct any public statements issued by or on behalf of PNC which were false or misleading and therefore had an obligation to publicly challenge the non-consolidated results.

161. On January 30, 2002, the day following PNC's restatement announcement, E&Y disclosed, for the first time, that it had played a role in developing the special purpose entity structure for AIG, and then, as PNC's auditor, had opined on the accounting of each SPE transaction. E&Y, however, entirely rejected any notion that such a role was improper by assuring the market that there was no conflict of interest in acting on both sides of the SPE transactions. According to Larry Parnell, an E&Y spokesperson: "If [E&Y] had felt there was a

conflict, we wouldn't have done it." Mr. Parnell also stated that E&Y had "concurred" with respect to the federal regulators' directive concerning consolidation of the SPEs.

162. The statements in the preceding paragraph were materially false and misleading as E&Y knew, or recklessly disregarded, that its dual rule with respect to the SPE transactions represented a serious and debilitating conflict. Indeed, in the E&Y Marketing SAS-50 Opinion, E&Y stated that:

> The ultimate responsibility for the decision on the appropriate application of generally accepted accounting principles for an actual transactions rests with the preparers of financial statements ***who should consult with their continuing accountants.*** [Emphasis added].

163. Notwithstanding the directive given by E&Y as the author of the Marketing SAS-50 Opinion to other prospective clients, E&Y, as PNC's "continuing accountant," recklessly opined on PNC's accounting of the SPE transactions, which, among other things, enabled E&Y to collect significant fees for consulting and auditing services that it provided to PNC during the Class Period. Accordingly, E&Y's statement that a dual role with respect to the SPE transactions did not create a "conflict," was knowingly false and misleading. Furthermore, E&Y's representation that it had "concurred" with federal regulators' directive was also materially false and misleading in light of the E&Y's rejection of federal regulators' directive.

164. On February 7, 2002, unbeknownst to the investing public and to PNC, E&Y revoked its own Marketing SAS-50 Opinion Letter – the letter which PNC relied upon in deciding to enter into the PAGIC transactions and which AIG-FP utilized in marketing the PAGIC structure to other public companies, thereby precluding AIG-FP from marketing the structure to other entities.

165. On February 19, 2002, just three weeks after the PNC Defendants had chopped $155 million off of PNC's previously reported year-end 2001 earnings, the PNC Defendants

announced that as a result of a purported bookkeeping error, PNC had incorrectly accounted for the sale of its mortgage banking business in 2001 and would have to restate its 2001 earnings for a second time.

166. On March 29, 2002, the PNC Defendants filed amended Forms 10-Q for the Second and Third Quarters ended June 30, 2001 and September 30, 2001. Among other things, PNC's earnings per share for the Third Quarter, originally reported at $1.02 per share, were now being reported at $0.84 per share, representing an 18% overstatement. The PNC Defendants also filed PNC's Form 10-K for the full year 2001. The 2001 10-K revealed that the $1.91 year-end earnings per share figure originally announced by PNC on January 17, 2002 was overstated by a staggering 52%, as a result of the two restatements. In total, $190 million or $0.65 per share was wiped out. PNC's 2001 Form 10-K, which also included Fourth Quarter 2001 results, revealed that the 2001 Fourth Quarter loss of ($1.15) per share announced on January 17th was understated by 24%, as the true fourth quarter loss was ($1.52) per share. The 2001 Form 10-K further disclosed that PNC had charged $240 million against pre-tax income as a result of valuation write-downs relating to consolidation of the special purpose entities.

167. Also included in the Form 10-K was an announcement that E&Y had been terminated as PNC's outside auditor. In this regard, on December 18, 2001, PNC had previously filed a Form 8-K announcing that it was terminating E&Y from serving as PNC's outside auditor based upon new SEC rules and guidelines which suggested that it was inappropriate for an outside auditor to also act as an internal auditor for the same client. As set forth above, the December 18th statement omitted material information as it failed to advise the investing public that E&Y was providing advisory services to PNC in connection to designing, promoting and structuring of the SPE transactions.

168. Furthermore, when an outside auditor is terminated, pursuant to Item 304(a)(1) of Regulation S-K ("Changes in and Disagreements With Accountants on Accounting and Financial Disclosure"), the public company ("registrant") is required to make several disclosures including the following:

> . . . . (iv) state whether during the registrant's two most recent fiscal years and subsequent interim period preceding such resignation, declination or dismissal there were any disagreements with the former accountant on any matter of accounting principles or practices, ***financial statement disclosure***, or auditing scope or procedure, which disagreement(s), if not resolved to the satisfaction of the former accountant, would have caused it to make reference to the subject matter of the disagreement(s) in connection with its report. . . The disagreements required to be reported in response to this Item include both those resolved to the former accountant's satisfaction and those not resolved to the former accountant's satisfaction. Disagreements contemplated by this Item are those that occur at the decision-making level; i.e., between personnel of the registrant responsible for presentation of its financial statements and personnel of the accounting firm responsible for rendering its report. (Emphasis added).

169. Pursuant to Item 304(a)(3), E&Y was provided with a copy of the disclosures to be made by PNC pursuant to Item 304(a), along with a request that E&Y furnish PNC with a letter addressed to the SEC stating whether it agrees with the disclosures made by PNC and if not, stating the respects in which it does not agree. PNC was then required to file E&Y's letter as an exhibit to its public filing.

170. Item 9 of PNC's Form 10-K filing on March 29, 2002 ("Changes in and Disagreements With Accountants on Accounting and Financial Disclosure"), reads as follows:

> In addition to serving as the independent auditor of the Corporation's 2001 consolidated financial statements, Ernst & Young, LLP executes the Corporation's internal audit program under the direction of PNC's corporate audit staff. Ernst & Young, LLP also provides various tax and nonattest and advisory services to the Corporation.
>
> Under rule amendments regarding auditor independence adopted by the SEC, beginning August 5, 2002, independent accountants will no longer be permitted to provide audit clients with certain non-audit services. Accordingly, PNC has decided to have separate internal and independent audit providers commencing with fiscal 2002. Ernst & Young, LLP has acted as independent auditor with

respect to the Corporation's 2001 financial statements and will continue to perform various internal audit, tax, and nonattest and advisory services to the Corporation. PNC has engaged Deloitte and Touche LLP as the Corporation's principal accountants to audit the Corporation's 2002 financial statements. These actions were recommended by the Audit Committee and approved by the Corporation's Board of Directors on December 18, 2001. Ernst & Young's LLP's role as the Corporation's independent auditor will cease upon the filing of this Form 10-K.

Ernst & Young LLP's reports on the Corporation's financial statements for the past two fiscal years did not contain an adverse opinion or a disclaimer of opinion and were not qualified or modified as to uncertainty, audit scope or accounting principles. During the two most recent fiscal years ***and any subsequent interim period preceding the date of this Form 10-K***, (i) there were no disagreements with Ernst & Young, LLP on any matter of accounting principles or practices, ***financial statement disclosure***, or auditing scope or procedure, which disagreements, if not resolved to the satisfaction of Ernst & Young, LLP, would have caused Ernst & Young, LLP to make reference to the subject matter of the disagreement in connection with its reports in the financial statements for such years, and (ii) there were no reportable events as defined in Item 304 of Regulation S-K.

The Corporation has provided Ernst & Young, LLP with a copy of the disclosure in this Item 9 and has requested that Ernst & Young LLP furnish the Corporation with a letter to update the letter previously provided pursuant to Item 304(a)(3) of Regulation S-K, which was included as Exhibit 16 of the Corporation's Form 8-K dated December 18, 2001. The updated letter is included as Exhibit 16 to this Form 10-K. Item 9, Page 10, PNC's 3/29/02 Form 10-K. [Emphasis added].

171. Attached as Exhibit 16 to PNC's Form 10-K was a copy of a letter from E&Y to the SEC which reads as follows:

Ladies and Gentlemen:

We have read Item 9 of the PNC Financial Services Group, Inc.'s Form 10-k dated March 29, 2002, and are in agreement with the statements contained in Paragraphs 1 through 4 on Page 10 therein.

Yours very truly,

/s/ Ernst & Young LLP

Pittsburgh, Pennsylvania

172. In the subsequent interim period between E&Y's termination in December of 2001 and March 29, 2002, the filing date of PNC's Form 10-K, contrary to the public

representations surrounding E&Y's termination set forth in the preceding paragraphs, E&Y and PNC had a material disagreement regarding the issuance of the January 17th press release which reported results for the fourth quarter and year end of 2001 on a non-consolidated basis. In this regard, E&Y had specifically advised PNC not to publish its financial statements on a non-consolidated basis, prior to allowing E&Y to petition the SEC's office of Chief Accountant. In fact, E&Y threatened PNC that it would not to issue an unqualified audit opinion for PNC's Form 10-K for 2001 if PNC did not appeal the federal regulator's directive to the Chief Accountant. Nevertheless, PNC felt that it had no choice but to issue such results as the public had previously been advised that results would be announced on January 17, 2002. This "disagreement," which included E&Y's threat to withhold its unqualified audit opinion, was required to be disclosed in connection with Item 9 of the 2001 Form 10-K.

173. As a result, the Misrepresentation Defendants made another false and misleading statement in the 2001 Form 10-K with respect to the purported lack of any material disagreements between PNC and E&Y in any "subsequent interim period preceding the date of this Form 10-K."

174. The issuance of the restatement announcement on January 29, 2002 and the actual restated figures filed on March 29, 2002 did not alleviate the Misrepresentation Defendants of their disclosure obligations. Item 304(a)(1)(iv) of Regulation S-K is explicit in this regard; "The disagreements required to be reported in response to this Item include both those resolved to the former accountant's satisfaction and those not resolved to the former accountant's satisfaction." Disagreements are broadly defined as set forth in Paragraph 4 of the instructions to Item 304 to include, "any difference of opinion concerning any matter of accounting principles or practices,

financial statement disclosure, or auditing scope or procedure. . . . It is not necessary for there to have been an argument to have had a disagreement, merely a difference of opinion."

175. Had the Misrepresentation Defendants disclosed the circumstances surrounding the disagreement, the investing public would have learned that PNC's management was directly implicated in the fraudulent scheme and was not following the advice of the FRB, the OCC, the SEC and its own auditors, by issuing the January 17th press release with actual knowledge of its falsity. As a result, the investing public was not aware that PNC was now more likely than not to be subjected to increased regulatory scrutiny based upon its conduct. This would have removed any artificial inflation still present in the stock.

176. Furthermore, as E&Y had an obligation to speak completely and truthfully, it had a duty to disclose its integral role in designing and structuring the SPE products, and that it had requested AIG-FP to cease using its Marketing SAS-50 Opinion Letter when marketing the PAGIC product – the letter that PNC relied upon in deciding whether to enter into the PAGIC transactions.

177. On July 18, 2002, the last day of the Class Period, the SEC announced that as a result of "accounting improprieties" and in particular, a "misuse of special purpose entities," it had issued a Cease and Desist Order against PNC to which PNC had agreed. For the first time, the investing public learned that through these special purpose entities, the PAGIC Defendants had transferred $762 million of PNC's assets, $302 million of which consisted of troubled, volatile and/or underperforming loans and venture capital investments, to three separate subsidiaries it had formed with AIG-FP. The investing public also learned for the first time that the express purpose of the transactions was to remove these assets from PNC's financial statements. The SEC Order also specifically found that PNC's transactions with the special

purpose entities violated GAAP and that PNC should have consolidated the results of the special purpose entities on its financial statements. Although PNC did not admit or deny liability, it consented to the Order.

178. PNC also entered into an agreement with federal regulators to address matters relating to PNC's compliance with RAP and GAAP, consolidation of assets of SPEs on PNC's regulatory reports and public financial statements, and corporate governance policies and practices. Among other things, PNC agreed to adopt a plan set forth by federal regulators to improve PNC's management structure, corporate governance, risk management practices, regulatory communications, and internal controls.

179. Along these lines, the gravity of PNC's agreement with regulators, which directly arose from federal regulators' beliefs that the PAGIC Defendants had entered into the SPE transactions to conceal PNC's non-performing assets not only from the investing public, but from regulators as well, is evidence by the reaction of securities analysts to PNC's disclosures concerning the settlements. For example, on July 19, 2002, an analyst from Credit Suisse, First Boston, Van Hesser, noted that, as a consequence of the agreement between PNC and regulators, which was a direct result of the Defendants' substantial participation in the creation, marketing, structuring and misrepresentations concerning the PAGIC transactions, "***PNC will also need prior approval [from federal regulators] to add new directors or to employ new senior executives***." (Emphasis added).

180. Similarly, that securities analysts believed that the SEC's Cease and Desist Order was a result of the PAGIC Defendants efforts to conceal PNC's non-performing assets from regulators, as opposed to a mere accounting error, is evidenced by the comments made by two

analysts from Bear Stearns, David Hilder and Kerstin Ramston, in a report issued on July 23, 2002:

> Clearly, the SEC's goal is to show that it will come down on those who publish misleading financial statements with "hobnail boots . . . . No regulators these days wants to be viewed as "soft" on off balance sheet entities, ***and the SEC's harsh language suggests a zero tolerance policy for using off-balance sheet entities to disguise economic realities***." (Emphasis added).

181. The market's reaction to the material disclosures concerning the settlement with the SEC and federal bank regulators, which alerted the market that the PNC Defendants and E&Y were directly involved in improper accounting practices, had ignored regulators' requests, and that the PNC Defendants had made materially misleading statements during the Class Period regarding PNC's purported success with its divestment of nonperforming assets, caused PNC's stock price to dramatically decline again as it dropped 15% at the close on July 18, 2002 and another 6.5% on the following day to close at $37.09, a far cry from its Class Period high of $69.80 on August 22, 2001.

Subsequent Developments

182. Subsequent to the conclusion of the Class Period, on June 2, 2003, in a Form 8-K filing, PNC announced that PNC ICLC, a subsidiary of PNC, and the Criminal Division, Fraud Section of the United States Department of Justice had entered into a Deferred Prosecution Agreement (the "PNC DPA") wherein PNC agreed to pay $115 million dollars in fines and restitution relating to its conduct in connection with the creation and accounting for the special purpose entity transactions at issue in this litigation and that the investigation is continuing with respect to third parties who participated in the formation of these entities.

183. The PNC Defendants also announced that they "accept[] and acknowledge[] responsibility for [the] behavior set forth in the Statement of Facts" (the "PNC SOF") attached to the PNC DPA, which describes PNC's wrongful behavior during the Class Period. In this

regard, the PNC Defendants have acknowledged the truth of many material allegations set forth herein, including the following:

- Each SPE transaction violated the GAAP requirements for non-consolidation of SPEs (PNC SOF ¶ 2);

- PNC's second and third quarter 2001 regulatory reports and financial statements did not conform with GAAP for such off-balance sheet treatment (*Id.*); and

- PNC improperly treated the transfers of assets to the SPE entities as sales qualifying for nonconsolidation, when it should have included the assets of the SPE entities in PNC's regulatory reports and financial statements, *i.e.*, consolidated those assets into those statements and reports. *Id.*

184. In addition, the PNC Defendants have also affirmatively acknowledged that they acted with the requisite fraudulent intent as evidenced by the following admitted facts:

- PNC and AIG-FP agreed to have the SPEs pay fees to AIG-FP, characterizing those fees as "management fees," while PNC knew that the "management fees" included compensation related to matters beyond the management services to be provided to the SPE entities by AIG-FP. PNC SOF ¶ 9.

- PNC knew that this de facto "structuring fee" or "balance sheet rental fee" reduced AIG-FP's capital investment below the minimally acceptable level under GAAP needed to qualify as a substantive capital investment for nonconsolidation. *Id.*

- PNC understood that what was characterized as "management fees" included payments to AIG-FP to compensate AIG-FP for, among other things, the costs and burdens associated with the consolidation of assets on AIG-FP's balance sheet. *Id.*

- In order to obtain the off-balance-sheet treatment of the SPE entities, PNC and AIG-FP did not disclose the existence of a de facto structuring fee or a balance sheet rental fee, and executed documents in each of the SPE transactions that characterized the fees as "management fees." PNC SOF ¶¶ 9-10.

185. In addition to admitting many of the material facts at issue in this litigation, the PNC Defendants further detailed the significant role played by defendant E&Y in connection with the fraudulent scheme. For example, the PNC Defendants acknowledged that:

- The SPE structure was designed and marketed by a . . . and a national accounting firm [E&Y]. . . as an allegedly innovative structure for permitting off-balance sheet treatment of troubled assets. PNC SOF ¶ 4.

- In its original regulatory and financial reports filed with the Federal Reserve

> Board and the SEC, respectively, for the second and third quarters of 2001, PNC treated the SPE entities as valid SPEs and applied the accounting treatment that [E&Y] had indicated would be applicable to valid SPEs, *i.e.*, a de-consolidation and reclassification of the underlying SPE assets. PNC SOF ¶ 6.

186. The DOJ has also indicated in the PNC DPA that its investigation was continuing with respect to others who played a role in the fraudulent scheme. PNC SOF ¶¶ 2, 5.

187. In this regard, on November 30, 2004, it was announced that AIG-FP Equity PAGIC Holdings Corp. had entered into a Deferred Prosecution Agreement (the "AIG DPA"), with the Fraud Section of the DOJ, Criminal Division, which also included a related agreement between the government and AIG-FP, attached to the AIG DPA as Exhibit A. Simultaneously therewith, AIG had entered into a settlement with the SEC. Among other things, these agreements collectively required the AIG entities to pay disgorgement and prejudgment interest in the amount of $46 million to PNC shareholders harmed by the misconduct, as well as a fine in the amount of $80 million. The DOJ has since directed that, of the $80 million dollars that AIG has paid in fines, $20 million be paid to the Restitution Fund (accordingly, in total, AIG has paid in excess of $66 million to the restitution fund, and $60 million in fines). Attached as Appendix A to Exhibit A of the AIG DPA is an "Agreed Statement of Facts" which will be hereinafter referred to as the "AIG SOF."

188. Among other things, the AIG SOF confirmed that AIG FP had developed the special purpose entity structures "in consultation with a national accounting firm (`National Accounting Firm [E&Y]')." AIG SOF ¶ 2, and that AIG-FP had "requested and received opinion letters from National Accounting [E&Y] issued pursuant to Statement of Auditing Standards No. 50 ('SAS-50 letters') addressing the application of . . . GAAP to these SPE transactions." *Id.*

189. In addition, it is also clear from the AIG DPA that E&Y was specifically referenced in the marketing materials as AIG-FP's outside accounting advisor and that E&Y

opined that under GAAP, entities such as PNC would not have to consolidate the special purpose entities. AIG SOF ¶ 5. In fact, E&Y was specifically advised by AIG-FP that AIG-FP would be utilizing its SAS-50 Opinion Letters in marketing the PAGIC products. *Id.* at 13.

190. It is also evident that E&Y recognized the sensitivity of the strict 3% ownership interest rule as it applied to special purpose entity transactions. In this regard, as originally structured, PAGIC I would have required an affiliate of AIG-FP to issue a 30 year zero coupon note to be purchased and held by PAGIC I. On or about April 23, 2001, an E&Y partner, who was responsible for drafting the SAS-50 Opinion Letter, informed an employee of AIG of E&Y's concern that the resulting interest from the issuance of a zero coupon note by AIG could be viewed as a return of capital to AIG, thereby taking AIG-FP's investment below the 3% threshold. SEC AIG Compl. ¶ 23. Pursuant to EITF Issue No. 96-21, "***To the extent that fees reduce the equity capital investment below the minimum amount required, the owners of record would not be considered to have made a substantive residual equity capital investment*** that is at risk...." [Emphasis Supplied].

191. As a result, after E&Y advised PNC of this concern on June 18, 2001, PNC requested AIG-FP to change the identity of the issuer of the 30 year zero coupon note from an AIG-FP affiliate to some other issuer. E&Y had specifically requested the change because although it believed that the structure still works, "there was a risk that the SEC might view the issuance of the coupon note by an affiliate of AIG-FP as a return of capital invested by AIG-FP in the PAGIC entity." AIG SOF ¶ 45. It was at that time that a bond issued by the US Treasury was substituted for the 30 year zero coupon issued by an affiliate of AIG-FP. *Id.* The first PAGIC transaction closed on June 28, 2001.

192. Thus, in addition to having actual knowledge that National Accounting Firm A was challenging the structure of the transaction on behalf of its own client in a separately contemplated transaction which was similar to the SPE's at issue in this case, even within E&Y there was a tacit realization that any fees earned by AIG-FP in connection with the PAGIC transactions would have to be scrupulously examined to ensure that any fees earned by AIG-FP were related to continuing services being provided as opposed to fees for structuring the transaction and/or for the use of its balance sheet in hiding the assets. E&Y knew enough about the true nature of the transaction to understand that the fees were intended to compensate AIG-FP for structuring the transaction and taking the assets and liabilities onto its balance sheet and not for providing management services.

193. In fact, AIG-FP recognized the fees as being fully earned immediately for the entire initial five year period for the PAGIC transactions and took the position that it had performed all services necessary to earn the initial five years of the fees at the outset of each PAGIC transaction. AIG SOF ¶¶ 49-50. As a result, with some relatively simple due diligence, E&Y could have learned, to the extent it didn't know already, by requesting accounting treatment information from AIG-FP or its auditor, that these fees really were not management fees, and thus, had to be deducted from AIG-FP's purported capital investments in the SPE transactions. That such information was important to the overall analysis of the appropriate accounting treatment was indicated by the FRB in its first three questions asked of PNC, as set forth above. Despite having access to all of the closing documents which set forth that all of the purported "management fees" to be earned by AIG-FP over the first five years of the agreement were to be paid upfront upon the closing of the transaction and that regulators were asking how

AIG was treating the transactions, E&Y nonetheless approved the accounting for the transactions.

194. Just as PNC had done when it entered into its DPA with the government, AIG-FP and the Department of Justice agreed that the PAGIC transactions failed to satisfy GAAP due to AIG-FP's failure to own at least 3% of PAGIC's assets. The DOJ specifically found that under GAAP structuring fees paid to an investor in the special purpose entity should be deducted from the investor's capital investment for determining if the investor meets the 3% threshold.

FALSE AND MISLEADING FINANCIAL STATEMENTS AND FINANCIAL DISCLOSURES

Violations of GAAP

195. As set forth in Financial Accounting Standards Board ("FASB") Statements of Concepts ("Concepts Statement") No. 1, a fundamental objective of financial reporting is to provide accurate and reliable information concerning an entity's financial performance during the period being presented. Concepts Statement No. 1, paragraph 42, states:

> Financial reporting should provide information about an enterprise's financial performance during a period. Investors and creditors often use information about the past to help in assessing the prospects of an enterprise. Thus, although investment and credit decisions reflect investors' and creditors' expectations about future enterprise performance, those expectations are commonly based at least partly on evaluations of past enterprise performance.

196. At all relevant times during the Class Period, the Misrepresentation Defendants represented that PNC's financial statements were prepared in conformity with GAAP, which are recognized by the accounting profession and the SEC as the uniform rules, conventions and procedures necessary to define accepted accounting practice at a particular time. SEC Regulation S-X states that financial statements filed with the SEC that are not prepared in compliance with GAAP are presumed to be misleading and inaccurate. 17 C.F.R. § 210.4-01(a)(1).

197. The representations that PNC's financial statements were prepared in accordance with GAAP were materially false and misleading because the Misrepresentation Defendants knew, or recklessly ignored that through the PAGIC transactions, PNC had employed improper accounting practices, in violation of GAAP and the SEC's financial reporting requirements, to falsely overstate and misrepresent its operating results and financial condition during 2001.

198. PNC's financial results filed and announced during the Class Period were presented in violation of GAAP and SEC rules and regulations as a result of the failure to consolidate the results of the aforementioned special purpose entities. In so doing, PNC's earnings were materially inflated during the Class Period, its non-performing assets were materially understated and the oft-repeated representations that PNC was reducing its exposure to loss on its loan portfolio were materially false and misleading.

199. FASB's Emerging Issues Task Force ("EITF") Topic D-14 provides accounting guidance concerning the transfer of assets to and the consolidation of a special purpose entity. Pursuant to EITF Topic D-14:

> Generally, the SEC staff believes that for non-consolidation and sales recognition by the sponsor or a transferor to be appropriate, the majority owner (or owners) of the SPE [special purpose entity] must be an independent third party who has made a substantive capital investment in the SPE, has control of the SPE and has substantive risks and rewards of ownership of the assets of the SPE (including residuals). Conversely, the SEC staff believes that non-consolidation and sales recognition are not appropriate by the sponsor or transferor when the majority owner of the SPE make only a nominal investment, the activities of the SPE are virtually all on the sponsor's or transferor's behalf, and the substantive risks and rewards of ownership of the assets or debt of the SPE rest directly or indirectly with sponsor and transferor.

200. As noted at length above, prior to the Class Period, PNC identified a substantial amount of its loans and other assets which were "troubled" assets. Generally, a debt is considered to be "troubled" when a concession, that a creditor would not otherwise consider, is granted to the debtor by the creditor due to the debtor's financial difficulties. SFAS NO. 15, ¶ 2.

In an attempt to reduce PNC's risk of loss on such assets, the PAGIC Defendants designed and implemented a deceptive scheme whereby, unbeknownst to the investing public, certain volatile, troubled and/or non-performing assets were transferred by PNC to PAGIC entities. The form of such transfer was to "sell" such assets to a purportedly independent third party, however, in substance, these special purpose entities did not possess the risks and rewards that owners typically assume when they acquire assets.

201. In essence, the PAGIC Defendants wanted it both ways; that is, to eliminate PNC's risk of loss on the transferred assets while allowing PNC to retain the ability to benefit from a future increase in the fair value of such currently non-performing assets. Such efforts, however, represented nothing more than a deliberate attempt to circumvent a fundamental tenet of GAAP which holds that the substance of the arrangement, rather than its legal form, determines the appropriate accounting treatment. *See*, *e.g.,* Concept Statement No. 2, ¶ 160, ABP Opinion No. 21, ¶ 12, AICPA Accounting Interpretation ("AIN") of APB Opinion No. 25, #1.

202. Moreover, the accounting treatment implemented by the PAGIC Defendants did not comply with GAAP's specific guidance set forth in EITF Topic D-14. In this regard, the provisions of the agreements for the establishment of each special purpose entity provided that AIG-FP, the supposed "owner" of the special purpose entity, was completely protected from loss on its investment. Conversely, AIG-FP could not effectively enjoy the benefit ensuing from any gains on the assets transferred by PNC because PNC retained effective control over the liquidation of the special purpose entities, as described above.

203. In addition, PNC bore substantial risk on the assets transferred to the special purpose entities because: (1) the dividends on the preferred stock PNC received in consideration

of the assets transferred were non-cumulative and payable only if those loans performed or were sold; and (2) the dividends on the non-cumulative preferred stock were payable only after payment of, among other things, the management fee to AIG-FP, and even then only with the approval of AIG-FP.

204. As a result of the foregoing provisions, PNC, and not AIG-FP, possessed the substantive risks and rewards of ownership of the assets transferred to the special purpose entities. Accordingly, PNC was precluded from treating such transfers as sales and was required to consolidate the financial statements of the special purpose entities with its own during the Class Period.

205. Moreover, PNC was otherwise precluded under GAAP from treating the asset transfers as sales and not consolidating the financial statements of the special purpose entities with its own during the Class Period. For example, GAAP, in EITF Issue No. 90-15, interpreted the requirement that a third party's substantive capital investment in the special purpose entity must be equivalent to an equity investment of no less than 3%, **although a greater investment could be necessary depending on the facts and circumstances of each case.** With respect to the special purpose entities at issue here, AIG-FP's initial investments did not satisfy this minimal threshold due to the fact that AIG-FP was receiving an immediate return on its investment in the form of a management fee payable to AIG-FP at the closing of the transaction, thereby immediately reducing AIG-FP's initial investment below the required threshold. Pursuant to EITF Issue No. 96-21, "To the extent that fees reduce the equity capital investment below the minimum amount required, the owners of record would be considered to have made a substantive residual equity capital investment that is at risk...." In fact, in light of the facts and circumstances of the PAGIC transactions, an investment by AIG-FP well in excess of 3%

probably was required in order to satisfy GAAP, as opposed to AIG-FP's actual investment of less than 3%. As a result, the PAGIC Defendants' failure to consolidate the financial results of the special purpose entities with those of PNC, was in violation of GAAP.

206. In addition to the aforementioned violations of GAAP, in situations such as this - - where the attainment of a particular financial reporting result is a primary purpose of the establishment of the special purpose entity - - accountants and publicly traded companies must be mindful that even if the transactions meet GAAP's technical requirements, the overall fairness, accuracy and completeness of the presentation made in financial statements must be evaluated in order to prevent misleading presentation.

207. PNC's Class Period financial statements were false and misleading and failed to comply with GAAP because they improperly failed to identify and describe important judgments associated with its accounting for PAGIC. Indeed, neither the second and third quarter 2001 10-Qs nor their corresponding earning press releases, disclosed PAGIC explicitly, PNC instead chose to bury it in its loan sales. Accordingly, investors were unable to assess the appropriateness of, or the risks and rewards associated with, PNC's accounting for the PAGIC entities.

208. GAAP provides that the usefulness of financial statements in making economic decisions depends significantly upon the user's understanding of the accounting policies followed by a company. APB 22 Disclosure of Accounting Policies ¶ 7 (April 1972). In fact, GAAP states that information about the accounting policies adopted by a reporting company is "essential" for financial statement users. APB 22 ¶ 8. Accordingly, GAAP, in ¶ 12 of APB 22 provides:

> In general, the disclosure should encompass important judgments as to appropriateness of principles relating to recognition of revenue and allocation of

asset costs to current and future periods; in particular, it should encompass those accounting principles and methods that involve any of the following:

(a) A selection from existing acceptable alternatives

(b) Principles and methods peculiar to the industry in which the reporting entity operates, even if such principles and methods are predominantly followed in that industry;

(c) Unusual or innovative applications of generally accepted accounting principles (and, as applicable, of principles and methods peculiar to the industry in which the reporting entity operates).

(d) In discharging their professional responsibilities, members may encounter conflicting pressures from among each of those groups. In resolving those conflicts, members should act with integrity, guided by the precept that

(e) when members fulfill their responsibility to the public, clients' and employers' interests are best served. ET § 53 – Article II

209. In sum, the Misrepresentation Defendants presented PNC's financial position and results of operations during the Class Period in a manner which violated GAAP. In addition to the accounting improprieties articulated above, these Defendants presented PNC's financial statements during the Class Period in a manner which violated at least the following additional provisions of GAAP:

(a) The principle that financial reporting should provide information that is useful to present and potential investors and creditors and other users in making rational investment, credit and similar decisions. (FASB Statement of Concepts No. 1, ¶ 34);

(b) The principle that the financial reporting should provide information about the economic resources of an enterprise, the claims to those resources, and the effects of transactions, events and circumstances that change resources and claims to those resources. (FASB Statement of Concepts No. 1, ¶ 40);

(c) The principle that financial reporting should provide information about an enterprise's financial performance during a period. "Investors and creditors often use information about the past to help in assessing the prospects of an enterprise. Thus, although investment and credit decisions reflect investors' and creditors' expectations about future enterprise performance, those expectations are commonly based at least partly on evaluations of past enterprise performance." (FASB Statement of Concepts No. 1, ¶42);

(d) The principle that financial reporting should provide information about how management of an enterprise has discharged its stewardship responsibility to owners (stockholders) for the use of enterprise resources entrusted to it. "To the extent that management offers securities of the enterprise to the public, it voluntarily accepts wider responsibilities for accountability to prospective investors and to the public in general." (FASB Statement of Concepts No. 1, ¶ 50);

(e) The principle that financial reporting should be reliable in that it represents what it purports to represent. That information should be reliable as well as relevant is a notion that is central to accounting. (FASB Statement of Concepts No. 2, ¶¶ 58-59);

(f) The principle of completeness, which means that nothing material is left out of the information that may be necessary to ensure that it validly represents underlying events and conditions. (FASB Statement of Concepts No. 2, ¶ 79);

(g) The principle that financial reporting should be verifiable in that it provides a significant degree of assurance that accounting measures represent what they purport to represent. (FASB Statement of Concepts No. 2, ¶ 81); and

(h) The principle that conservatism be used as a prudent reaction to uncertainty to try to ensure that uncertainties and risks inherent in business situations are adequately considered. (FASB Statement of Concepts No. 2, ¶¶ 95,97).

210. Further, the undisclosed adverse information concealed by the Misrepresentation Defendants during the Class Period is the type of information that, because of SEC regulations, regulations of the national stock exchanges and customary business practice, is expected by investors and securities analysts to be disclosed and is known by corporate officials and their legal and financial advisors to be the type of information that is expected to be and must be disclosed.

211. E&Y knew, among other things, that if PNC maintained effective control over the PAGIC entities, GAAP required consolidation (the inclusion of all assets, liabilities, and losses) into PNC's consolidated financial statements. Determined to earn enormous fees associated with the guidance, E&Y abandoned its professional duty to remain independent, objective, and

skeptical. The effort put forth by E&Y included the consultation and involvement of partners at the highest level of E&Y, including top partners at E&Y's National Office. In this regard, PNC upon learning that E&Y had provided an opinion on the proposed AIG transaction, wanted to make sure that E&Y's National Office had approved the Marketing SAS-50 Opinion Letter. PNC subsequently learned that Michael Joseph was the principal author of the letter and that Norm Strauss another high ranking partner in the National Office, also approved the letter.

212. E&Y also worked with PNC in creating and perpetuating the improper accounting practices. In this collaboration with PNC, E&Y violated the professions fundamental principles of integrity, objectivity, and due professional care. Indeed, E&Y knew about PNC's fraudulent accounting for the PAGIC entities, but ignored them or covered them up. For example, a draft of the second quarter 2001 earnings release made reference to PAGIC. However, E&Y recommended that the reference to PAGIC be removed because singling out PAGIC from among the various sale transactions in which PNC had engaged somehow called into doubt the sham accounting treatment of PAGIC. In addition, an early draft of the third quarter 2001 referred to PAGIC as a "securitization," but the reference was deleted from the finalized version at E&Y's direction.

213. The PNC Defendants have also now acknowledged that E&Y provided guidance letters to PNC in connection with each of the SPE transactions. These guidance letters, after being back-dated by E&Y, were supplied to federal regulators in the course of their investigation into the accounting for the transactions.

214. The PNC Defendants have also now confirmed that E&Y assisted them in preparing their formal response to the federal regulators' inquiry and that E&Y was consulted after PNC was advised by regulators that the accounting for the SPE transactions did not comply

with GAAP and that there was no difference between regulatory reporting and GAAP in this respect.

215. In addition, interim financial statements filed with the SEC are required to be reviewed by independent auditors.[1] GAAS, AU § 722, requires AU § 722, that auditors perform, among other things, the following procedure when reviewing interim financial statements:

> Reading the interim financial information to consider whether, on the basis of information coming to the accountant's attention, the information to be reported conforms with generally accepted accounting principles.

216. In reviewing PNC's interim 2001 financial statements, E&Y approved and provided specific guidance to PNC with respect to PNC's accounting for the transfers of assets to the special purpose entities and knew, or recklessly disregarded, that PNC would be issuing financial statements to investors that was based upon false and misleading accounting. Indeed, E&Y knew that PNC's erroneous interim 2001 financial statements would be filed with the SEC on Form 10-Q and would be included in PNC's October 25, 2001 Prospectus Supplement, as it consented to the inclusion of its 2000 audit opinion in the same document.

217. Defendant E&Y violated these above standards and, with PNC, filed materially misstated financial information with the SEC for the quarters ended June and September 30, 2001 as well as for the year ended December 31, 2001. As PNC's accountant and auditor, E&Y had a duty to correct any public statements issued by or on behalf of PNC which were materially false or misleading. Moreover E&Y made important judgments in preparing PNC's interim 2001 financial statements, including providing specific guidance to PNC to not consolidate the SPEs with those financial statements and to remove any reference to the PAGIC transactions from the financials.

---

[1] SEC, Audit Committee Disclosure, 1999 SEC LEXIS 2713 (December 22, 1999)

218. Defendant E&Y knew, or recklessly ignored, that PNC's second and third quarter interim 2001 financial statements failed to disclose the information required by SFAS No. 140. In addition, Defendant E&Y knew, or recklessly ignored that GAAP, in numerous respects, precluded PNC from accounting for its arrangements with the special purpose entities as sales. Indeed, by accounting for PNC asset transfers to the special purpose entities as sales, E&Y knew, or recklessly ignored, that such accounting was nothing more than a deliberate attempt to circumvent a fundamental tenet of GAAP which holds that the substance of a transaction, rather than its legal form, should determine its accounting treatment.

219. Even though E&Y advised the PNC Defendants not to issue the January 17th press release which reported financial results for the year end and fourth quarter 2001 on a non-consolidated basis, E&Y violated the requirements of Section 10A of the Securities Exchange Act, which requires auditors of public companies to design procedures to provide reasonable assurance of detecting illegal acts and to identify material related party transactions. Section 10A of the Securities Exchange Act requires an auditor to notify the SEC if he or she becomes aware of information indicating that an illegal act has, or may have occurred, if management or the Board of the company fails to take appropriate remedial actions with respect to the illegal acts.

220. In addition, as explained above, E&Y also made its own affirmative misrepresentation by agreeing with PNC in the March 29, 2002 Form 10-K that no material disagreements had arisen between PNC and E&Y prior to that filing.

221. Based upon these collective facts, which include those concerning E&Y's substantial participation on both sides of the SPE transactions, E&Y was intimately involved in all aspects of the accounting for the special purpose entities, as well as the defense of the

accounting by PNC, and is being charged with violating the federal securities laws for both deception and misrepresentation under Section 10(b) of the Exchange Act.

ADDITIONAL ALLEGATIONS OF SCIENTER

222. The facts alleged herein compel a strong inference that all of the Misrepresentation Defendants and PAGIC Defendants acted with scienter in either forming the special purpose entities or in making material false and misleading statements to the investing public. In this regard, the Misrepresentation Defendants knew that the public statements issued or disseminated in the name of PNC were materially false and misleading; knew or recklessly disregarded that such statements would be issued or disseminated to the investing public; and knowingly and substantially participated or acquiesced in the issuance or dissemination of such statements as primary violators of the federal securities laws. In addition, the PAGIC Defendants caused PNC to engage in irregular accounting practices, and in turn, caused PNC to report artificially inflated financial results. These accounting violations evince a willfulness that demonstrates the PAGIC Defendants' actual knowledge of the fraud.

223. In addition, E&Y, which was collecting millions of dollars in fees to act as an auditor and consultant for PNC and as a consultant to AIG-FP, created, structured and knowingly approved the special purpose entity transactions as described herein. In fact, E&Y allowed its audit opinion for the 2000 year-end, to be utilized in connection with PNC's two separate billion dollar offerings during the Class Period, knowing that the offering documents contained misleading financial results. E&Y was marketing the use of special purpose entity transactions to several potential clients and thus, had an additional motive to participate in the deceptive conduct alleged herein as it was attempting to expand its consulting services to entities such as PNC. Even after E&Y was terminated as PNC's outside auditor, it was still motivated to conceal PNC's fraud by virtue of the fact that PNC continued to retain E&Y as its internal

auditor and consultant and tax advisor. Consequently, had E&Y made the required disclosures in connection with its termination as auditor, and thereby implicated PNC's management directly in the fraudulent conduct alleged herein and advised the investing public of the true facts surrounding the fraud, it would have lost millions of dollars in revenue resulting from its continuing engagements.

APPLICABILITY OF PRESUMPTION OF RELIANCE: FRAUD-ON-THE-MARKET DOCTRINE

224. At all relevant times, the market for PNC securities was an efficient market for the following reasons, among others:

(a) PNC common stock met the requirements for listing, and was listed and actively traded on the NYSE, a highly efficient and automated market;

(b) As a regulated issuer, PNC filed periodic public reports with the SEC and the NYSE;

(c) PNC regularly communicated with public investors via established market communication mechanisms, including through regular disseminations of press releases on the national circuits of major newswire services and through other wide-ranging public disclosures, such as communications with the financial press and other similar reporting services; and

(d) PNC was followed by several securities analysts employed by major brokerage firms who wrote reports, which were distributed to the sales force and certain customers of their respective brokerage firms. Each of these reports was publicly available and entered the public marketplace.

225. As a result of the foregoing, the market for PNC's securities promptly digested current information regarding PNC from all publicly available sources and reflected such information in PNC's stock price. Under these circumstances, all purchasers of PNC securities, and those who wrote (sold) put options on PNC common stock during the Class Period, suffered similar injury through their transactions of PNC securities at artificially distorted prices and a presumption of reliance applies.

NO SAFE HARBOR

226. The statutory safe harbor provided for forward-looking statements under certain circumstances does not apply to any of the allegedly false statements pleaded in this SAC. Many of the specific statements pleaded herein were not identified as "forward-looking statements" when made. To the extent there were any forward-looking statements, there were no meaningful cautionary statements identifying important factors that could cause actual results to differ materially from those in the purportedly forward-looking statements. Alternatively, to the extent that the statutory safe harbor does apply to any forward-looking statements pleaded herein, the Misrepresentation Defendants are liable for those false forward-looking statements because at the time each of those forward-looking statements was made, the particular speaker knew that the particular forward-looking statement was false, and/or the forward-looking statement was authorized and/or approved by an individual who knew that those statements were false when made.

COUNT I

(VIOLATION OF SECTION 10(B) OF THE EXCHANGE ACT AND RULE 10b-5 FOR FALSE AND MISLEADING STATEMENTS BROUGHT AGAINST THE MISREPRESENTATION DEFENDANTS)

227. Plaintiffs repeat and reallege each and every allegation contained in the foregoing paragraphs as if fully set forth herein.

228. During the Class Period, the Misrepresentation Defendants (the PNC Defendants and E&Y) made various deceptive and untrue statements of material facts and omitted to state material facts in order to make the statements made, in light of the circumstances under which they were made, not misleading to Plaintiffs and the other members of the Class. The purpose and effect of these false and misleading statements was, among other things, to deceive the investing public, including Plaintiffs and the other members of the Class, and to induce Plaintiffs

and the other members of the Class into purchasing PNC securities during the Class Period at artificially inflated prices.

229. During the Class Period, the Misrepresentation Defendants knowingly and/or recklessly issued, caused to be issued, participated in the issuance of, the preparation and/or issuance of materially false and misleading statements to the investing public as particularized above.

230. As a result of the Misrepresentation Defendants' dissemination of and/or failure to correct the false and misleading statements set forth above, the market price of PNC securities was artificially inflated during the Class Period. Unaware of the false and misleading nature of the statements described above, Plaintiffs and the other members of the Class relied, to their detriment, on the integrity of the market price of the stock in purchasing PNC securities. Had Plaintiffs and the other members of the Class known the truth, they would not have purchased PNC shares or would not have purchased such shares at the inflated prices that they did.

231. Plaintiffs and the other members of the Class have suffered damages as a result of the wrongs herein alleged in an amount to be proved at trial.

232. By reason the foregoing, the Misrepresentation Defendants have violated Section 10(b) of the Exchange Act and Rule 10b-5 promulgated thereunder and are liable to Plaintiffs and the other members of the Class for damages which they suffered in connection with their purchases of PNC securities during the Class Period.

COUNT II

(FOR VIOLATIONS OF SECTION 10(B) AND RULE 10b-5 THEREUNDER AGAINST THE PAGIC DEFENDANTS BASED UPON DECEPTIVE PRACTICES)

233. Plaintiffs repeat and reallege the allegations set forth above as though fully set forth herein at length.

234. During the Class Period, the PAGIC Defendants (the PNC Defendants and E&Y) participated in a deceptive scheme pursuant to which, over the course of three consecutive quarters, these Defendants secretly created three SPEs in order to remove certain volatile, troubled and non-performing loans and venture capital investments from PNC's financial statements without disclosing this material fact to investors, bank regulators or the SEC. The purpose of these transactions was to artificially conceal losses in the value of the transferred assets from both regulators and the investing public and thereby inflate and maintain PNC's stock price.

235. This Claim is brought pursuant to Section 10(b) of the Exchange Act and Rule 10b-5 promulgated thereunder, on behalf of Plaintiffs and other members of the Class who purchased or otherwise acquired PNC securities against all of the PAGIC Defendants. This Claim is based upon the deceptive practices of all PAGIC Defendants.

236. The PAGIC Defendants carried out a plan, scheme and course of conduct which was intended to and did: deceive the investing public, including Plaintiffs and other members of the Class by means of material misstatements and omissions, as alleged herein; inflate and maintain the market price of PNC securities artificially; and induce Plaintiffs and other members of the Class to purchase or otherwise acquire PNC securities at artificially inflated prices. In furtherance of this unlawful scheme, plan and course of conduct, the PAGIC Defendants took the actions set forth herein.

237. The PAGIC Defendants employed devices, schemes, and artifices to defraud and/or engaged in acts, practices and a course of business which operated as a fraud and deceit upon Plaintiffs and other members of the Class in an effort to artificially inflate and maintain high market prices for PNC's common stock in violation of Section 10(b) of the Exchange Act

and Rule 10b-5. The PAGIC Defendants are sued as primary participants in the unlawful conduct charged herein.

238. The PAGIC Defendants, individually and in concert, directly and indirectly, by the use of means or instrumentalities of interstate commerce and/or of the mails, engaged and participated in a continuous course of conduct to conceal their unlawful practices and course of business which operated as a fraud and deceit upon Plaintiffs and other members of the Class.

239. The PAGIC Defendants had actual knowledge of or recklessly disregarded the material fact that PNC's reported financial statements and announced financial results were materially misstated and/or omitted material information necessary for statements made to not be misleading due to the fact that the existence of the special purpose entities was not being disclosed, and that PNC was not accounting for their results appropriately. In this regard, the purpose of the establishment of the special purpose entities was to remove troubled, non-performing assets from the financial statements of PNC to make them appear more attractive, and to avoid the scrutiny of federal regulators.

240. Plaintiffs and the other members of the Class have suffered damages as a result of the wrongs herein alleged in an amount to be proved at trial.

241. By reason the foregoing, the PAGIC Defendants have violated Section 10(b) of the Exchange Act and Rule 10b-5 promulgated thereunder and are liable to Plaintiffs and the other members of the Class for damages which they suffered in connection with their purchases of PNC securities during the Class Period.

COUNT III

(VIOLATION OF SECTION 20(a) OF THE EXCHANGE ACT BROUGHT AGAINST THE INDIVIDUAL DEFENDANTS)

242. Plaintiffs repeat and reallege each and every allegation contained in each of the foregoing paragraphs as if set forth fully herein.

243. The Individual Defendants acted as controlling persons of PNC within the meaning of section 20(a) of the Exchange Act as alleged herein. By virtue of their high-level positions, and active participation in and/or awareness of PNC's day-to-day operations, each Individual Defendant had the power to influence and control and did influence and control, directly or indirectly, the decision-making of PNC, including the content and dissemination of the various statements and SEC filings that plaintiffs allege are false and misleading. The Individual Defendants were provided with, or had unlimited access to copies of PNC's reports, press releases, public filings and other statements alleged herein 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, and were thus culpable participants in the fraud alleged herein.

244. In particular, the Individual Defendants had direct and supervisory involvement in the day-to-day operations of PNC and, therefore, are presumed to have had the power to control or influence the particular transactions giving rise to the securities violations as alleged herein, and exercised the same.

245. By virtue of their positions as controlling persons, the Individual Defendants are liable pursuant to section 20(a) of the Exchange Act. As a direct and proximate result of the wrongful conduct, Plaintiffs and the other members of the Class suffered damages in connection with their purchases of PNC's securities during the Class Period.

COMMON LAW CLAIMS:

ADDITIONAL ALLEGATIONS SUPPORTING COMMON LAW CLAIMS

E&Y

246. As described in greater detail above, in form, the PAGIC transfers were structured by E&Y and AIG-FP such that it would appear as if PNC "sold" troubled and/or non-performing assets to special purpose entities in exchange for preferred stock. In substance, however, the "purchasers" of the transferred assets (*i.e.*, the special purpose entities) did not possess the risks and rewards of ownership as necessitated by GAAP to allow PNC to treat such transfers as a sale.

247. After AIG FP proposed the initial design, E&Y assured AIG-FP that the SPEs were "feasible," and the design was then proposed to PNC. E&Y was knowingly included in the promotional materials used by AIG-FP in pitching the idea to PNC, which stated that the contemplated accounting treatment was "based upon advice from Ernst & Young."

248. In E&Y's SAS-50 Opinion Letter, dated April 23, 2001, which AIG had requested from E&Y for purposes of marketing the SPE structure, and, which was provided to PNC prior to it deciding to enter into the first SPE transaction, E&Y formally evaluated the then-hypothetical SPEs in light of GAAP. Despite acknowledging FASB Statement 94's opinion that "consolidated financial statements are more meaningful than separate statements and are usually necessary for a fair presentation when one of the companies in the group directly or indirectly has a controlling financial interest in the other companies," E&Y concluded that the hypothetical SPEs "should not be included in [PNC's] consolidated financial statements."

249. E&Y's conclusion in support of the appropriate GAAP accounting treatment of the hypothetical SPEs was based upon negligently drawn deductions, including: (i) that under the facts and circumstances of this structure, an equity investment of 3% would satisfy GAAP; (ii) that AIG-FP would legitimately own 3% of the assets of the SPE; (iii) that AIG-FP controlled the

SPE; and (iv) that AIG-FP would bear "the entirety of the residual risks and rewards of ownership." By virtue of having structured the transaction in the first place for AIG-FP, and having agreed to utilize it as a promotional tool with multiple clients, E&Y was well aware or negligently disregarded the material fact that AIG-FP was simply lending its balance sheet to PNC and that there was no true economic purpose for the transactions other than to remove non-performing assets from PNC's books.

250. Once AIG-FP pitched the idea of the special purpose entity structure to PNC, PNC retained E&Y to provide it with a written opinion (*i.e.*, separate and apart from the April 23, 2001, Marketing SAS-50 Opinion Letter E&Y provided to AIG-FP) regarding the appropriate accounting treatment under GAAP for the use of the SPEs -- *notwithstanding the fact that E&Y assisted in the creation and design of the proposed special purpose entity structure.* Despite this obvious conflict, E&Y acted on both sides of the same transaction. That the very same individuals at E&Y who provided the opinion to AIG-FP blessed the accounting for the transactions for the benefit of PNC only exacerbated this conflict.

251. In an Opinion Letter addressed to PNC dated June 21, 2001, E&Y approved the structure of the first special purpose entity, concluding that the "transaction should result in removing the Loans from PNC's balance sheet." PNC considered the analysis of the accounting treatment of the SPE transactions as crucial to its decision to enter into PAGIC I. In fact, prior to entering into PAGIC I, the PNC Defendants, in considering whether to enter into the PAGIC transactions, made a specific inquiry to E&Y's engagement team as to who had authored the E&Y April 23, 2001 SAS-50 Opinion Letter. E&Y informed PNC that Michael Joseph was the principal author of the opinion, and that Norm Strauss, another high ranking partner in E&Y's national office, had personally approved the letter.

252. In reliance on E&Y's advice, with just three days remaining in the 2001 Second Quarter, PNC entered into the previously described transactions with PAGIC I.

253. In another Opinion Letter, dated September 21, 2001, E&Y approved the structure of SPE II, concluding that the "transaction should result in removing the Loans from PNC's balance sheet."

254. In reliance on E&Y's advice, with just three days remaining in the 2001 Third Quarter, PNC entered into the previously described transactions with SPE II.

255. Notwithstanding the fact that, in response to "soft spots" identified in the accounting structure by National Accounting Firm A in May 2001, E&Y prepared and provided National Insurance Company A with a revised SAS-50 Letter purportedly addressing the issues raised by National Accounting Firm A. However, E&Y neither informed PNC of the revised SAS-50 Letter, or the "soft spots" that National Accounting Firm A had recognized.

256. In a third Opinion Letter, dated November 29, 2001, E&Y approved the structure of SPE III, concluding that the "transaction should result in removing the Interests [including venture capital investments and related commitments] from PNC's balance sheet."

257. In reliance on E&Y's advice, PNC entered into the previously described transactions with PAGIC III.

258. At all relevant times, E&Y represented that the PAGIC entities and the transactions that created them all conformed with GAAP, which are recognized by the accounting profession and the SEC as the uniform rules, conventions and procedures necessary to define accepted accounting practice at a particular time. SEC Regulation S-X states that financial statements filed with the SEC that are not prepared in compliance with GAAP are presumed to be misleading and inaccurate. 17 C.F.R. § 210.4-01(a)(1).

259. In fact, each of the final, signed opinion letters that E&Y prepared on PNC's behalf were back-dated to a date prior to the closing of each respective transaction. Although E&Y's June 21, 2001 Opinion Letter (which had actually been received by PNC on or about July 18, 2001) was included as part of the closing binder on SPE I that PNC submitted to federal regulators in September 2001, E&Y did not disclose to the federal regulators that the Opinion Letter had been back-dated to reflect a date prior to the closing of that transaction.

260. In addition, for the reasons set forth above, E&Y's Opinion Letters in support of the SPEs were not prepared in accordance with the requirements enunciated in GAAS.

261. E&Y negligently ignored that PNC's second and third quarter interim 2001 financial statements failed to disclose the information required by SFAS No. 140 as described above. In addition, E&Y negligently ignored that GAAP, in numerous respects, precluded PNC from accounting for its arrangements with the SPEs on a non-consolidated basis.

262. E&Y performed quarterly reviews of PNC's interim financial information throughout the relevant period, including the first quarter of 2001. PNC's quarterly financial reports consistently materially misstated the true financial condition of PNC in violation of GAAP.

263. E&Y's failure to honor its contractual obligations to PNC and failure to comply with professional standards when conducting its quarterly reviews of PNC's financial statements led to material misrepresentations in PNC's 10-Q filings during the relevant time period, and precluded proper notification to PNC by E&Y of ongoing material accounting irregularities.

264. Had E&Y conducted its interim financial statement reviews in accordance with GAAS, it could not have approved for the transfers of assets to the special purpose entities since PNC's financial statements were not prepared in conformity with GAAP.

265. GAAS requires an auditor to plan and perform its work with "due professional care." This standard imposes a responsibility upon each professional within the auditor's organization to observe the standards of field work and reporting. Furthermore, due care requires an auditor to exercise professional skepticism. The standard describes professional skepticism, in relevant part, as follows:

> Professional skepticism is an attitude that includes a questioning mind and a critical assessment of the audit evidence. The auditor uses the knowledge, skill, and ability called for by the profession of public accounting to diligently perform, in good faith and with integrity, the gathering and objective evaluation of the evidence. (AU 230, ¶ 7)

266. Had E&Y exercised the required due professional care, it would not have been able to approve PNC's accounting on the materially misstated PNC financial statements.

267. E&Y, with PNC, filed materially misstated financial information with the SEC for the quarters ended June and September 30, 2001 as well as for the year ended December 31, 2001. As an auditor of PNC, E&Y had a duty to correct any public statements issued by or on behalf of PNC which were false or misleading. Moreover, E&Y made important judgments in preparing PNC's interim 2001 financial statements, and provided specific guidance to PNC to not specifically mention the SPE transactions in these statements.

268. As later revealed, PNC's financial statements during 2001 contained vast material irregularities relating to the misuse of special purpose entities. PNC first announced its intention to restate its earnings for the Second and Third Quarters of fiscal 2001 and revise its fourth quarter and year-end 2001 earnings on January 29, 2002. On March 29, 2002, PNC formally restated PNC's financial results by filing amended Forms 10-Q for the Second and Third quarters ended June 30, 2001 and September 30, 2001 with the SEC.

269. GAAP, in the form of Accounting Principles Board Opinion ("APB") No. 20, Accounting Changes, provides the guidance for when a Company is required to restate its previously issued financial statements. APB No. 20 states, in relevant part as follows:

> Restating financial statements of prior periods may dilute public confidence in financial statements and may confuse those who use them. Financial statements previously prepared on the basis of accounting principles generally accepted at the time the statements were issued should therefore be considered final except for changes in the reporting entity or corrections of errors.

270. Under GAAP, the fact that PNC restated previously reported financial information is an admission that a material error occurred in its publicly disseminated financial information, which was not an error in estimation or judgment. APB No. 20 ¶13. The facts and circumstances giving rise to the restatement existed at the time when financial results were publicly disclosed. If this were not the case, GAAP would not have mandated the correction and restatement of PNC's previously disclosed financial results.

271. E&Y held and continues to hold itself out as an international professional accounting and auditing firm qualified to perform public accounting and auditing services, including independent audits. E&Y had a duty to maintain and comply with, and should be held to, the generally accepted accounting and auditing standards by which a public auditor is obligated to conduct an audit. E&Y, by maintaining and complying with GAAS, had a duty to insure that the financial statements of PNC complied with GAAP in all material respects.

272. As such, E&Y had a duty to address in its Opinion Letters that it provided to PNC, the "soft spots" recognized by National Accounting Firm A in the proposed accounting treatment of those transactions. In fact, the soft spots were directly brought to E&Y's attention when it was asked to issue a modified SAS-50 Opinion Letter for National Insurance Company A, a company that considered entering into a SPE-type transaction (but which ultimately did not). As set forth above, notwithstanding the fact that, on November 20, 2001, E&Y provided

National Insurance Company A with a draft of a revised SAS-50 letter that addressed the prepayment of the "structuring fee" directly to AIG-FP by National Insurance Company A, E&Y blessed the accounting structure of PAGIC III on PNC's behalf, which closed on November 30, 2001, through an Opinion Letter provided to PNC which failed to address the structuring fee issue.

273. On November 20, 2001, National Insurance Company A, in response to its previous request for increased participation by AIG-FP, received a revised draft of E&Y's SAS-50 letter which addressed the prepayment of the "structuring fee" directly to AIG-FP by National Insurance Company A.

274. That E&Y tacitly recognized that the substantive investment issue concerning special purpose entities, and how the 3% ownership interest rule applied, is evident by E&Y's stated concern to AIG that the interest from the issuance of a zero coupon note by AIG could be viewed as a return of capital to AIG, and thereby take AIG-FP's investment below the 3% threshold. In fact, E&Y specifically advised PNC to request AIG-FP to change the identity of the issuer of the 30-year zero coupon note from an AIG-FP affiliate to some other issuer. Nonetheless, E&Y negligently failed to address the 3% ownership interest issue in its Opinion Letters for the PAGIC transactions.

275. E&Y, as PNC's independent accountant and auditor at all relevant times, had unfettered access to PNC's books, records, and personnel. E&Y, as an international public accounting firm, and a member of the AICPA certainly had knowledge of the requirements of GAAP and GAAS.

276. E&Y's recommendation to exclude the special purpose entities from PNC's consolidated financial statements and its failure to correct false or misleading public statements

made by PNC allowed PNC to report 2001 year-end earnings per share of $1.91 when, in truth, the earnings were overstated by $190 million or 52%. As set forth herein, had E&Y complied with its contractual duties and the standards of the accounting profession, it would have detected that PNC's special purpose entity transactions did not accord with GAAP, and thus E&Y acted negligently, breached its contractual duty to PNC and made negligent misrepresentations to PNC which were repeated by PNC to bank regulators, the SEC and the investing public, all during the course of E&Y's employment by PNC.

277. Had it not been for E&Y's actions described above, PNC would not have suffered the damages, costs and expenses alleged herein.

COMMON LAW CLAIMS

COUNT IV

ACCOUNTING MALPRACTICE (NEGLIGENCE)

278. Plaintiffs repeat and reallege each of the foregoing paragraphs as if fully set forth herein, except to the extent any allegations above contain any facts which are unnecessary or irrelevant for purposes of stating a claim for negligence.

279. This count is brought by Plaintiffs, on behalf of PNC, to recover damages from E&Y arising from E&Y's negligence. Plaintiffs have been assigned the claims of PNC and its subsidiaries as part and parcel of the Partial Settlement and thus, have standing to assert this claim.

280. E&Y was specifically retained by PNC for the purpose of providing accounting and advisory services to PNC in connection with PNC's public reporting of its financial results. It was specifically intended and understood by both PNC and E&Y that PNC would be relying upon E&Y's expertise and that such opinions and guidance would be utilized by PNC in conducting its business transactions.

281. As PNC's independent auditor and accounting advisor, E&Y had a duty to PNC to prevent and to correct any public statements issued by or on behalf of PNC which were materially false or misleading and to provide appropriate accounting advice.

282. E&Y breached this duty not only by issuing three faulty opinions on the appropriate accounting treatment for the creation and transfer to three special purpose entities, but also by failing to comply with GAAS in auditing PNC's interim financial results and allowing PNC to issue materially false and misleading statements about its operations.

283. In addition, E&Y, by consulting for parties on different sides of the same transaction and thereby taking on a dual and conflicting role, *i.e.*, first opining on the structure of the special purpose entities for AIG-FP and thereafter performing the same services for PNC, failed to exercise the skill and knowledge normally exercised by members of its profession in providing consulting services.

284. In providing its recommendation letters on the three proposed SPEs, E&Y negligently ignored the material fact that GAAP precluded PNC from accounting for its arrangements with the special purpose entities as sales that could be removed from PNC's balance sheet because the purchasers of the transferred assets did not possess the requisite risks and rewards of ownership, PNC retained effective control over the special purpose entities, and because AIG-FP did not make a sufficiently large investment in the special purpose entities to be "substantive" as required by GAAP.

285. Despite significant red flags that would have alerted (and in fact did with respect to National Accounting Firm A) an auditor acting with requisite professional care, diligence and skepticism, and in performance of its duties as required by GAAS, that the special purpose entities were solely intended to conceal losses and thereby fraudulently inflate and maintain

PNC's stock price, E&Y designed, recommended and ultimately approved PNC's accounting for the transfers of assets to the special purpose entities, in violation of GAAP and the SEC's financial reporting requirements.

286. In fact, on May 29, 2001, more than one month prior to the close of PAGIC I, National Accounting Firm A, as part of its analysis for another public company that AIG-FP had marketed the special purpose entities structure to, alerted AIG-FP of "soft spots" with respect to the accounting for structure that E&Y assured PNC satisfied GAAP. According to the AIG SOF, the subject of the "red flags," included whether "capital investment might fall below the minimum (3%) capital investment required by GAAP for deconsolidation of the SPE by [the other public company] if AIG-FP received a 'larger prepayment' of its fees or of its fees were not received in exchange for services rendered by AIG-FP." ¶ 24. In response, AIG-FP proposed to increase its capital investment to that company from the 3% minimum to 5%. ¶ 25. Nevertheless, even with this modification, the Company passed on the proposed special purpose entity transactions. ¶ 28. E&Y did not inform PNC about its revised SAS-50 Opinion Letter that it had drafted and provided to National Insurance Company A as a result of National Accounting Firm A's concern over the "red flags" in the proposed SPE transactions, which were very similar to the PAGIC transactions that PNC entered into during the Class Period.

287. In addition, in reviewing PNC's interim 2001 financial statements, E&Y not only approved PNC's accounting for the transfers of assets to the special purpose entities, and negligently disregarded that PNC would be issuing financial statements to investors that was based upon false and misleading accounting, but also provided specific guidance to PNC not to disclose the existence of the SPE structures themselves in these financial statements.

288. PNC, with E&Y's substantial participation, filed materially false and misleading financial information with the SEC for the quarters ended June 30, 2001 and September 30, 2001, and assisted in the preparation of materially false and misleading financial results being announced for the fourth quarter and year ended December 31, 2001. As PNC's auditor, and as one of the parties that created and structured the SPE structure, E&Y violated the AICPA Code of Professional Conduct by knowingly making and permitting PNC to make materially false and misleading entries in its financial statements.

289. E&Y also failed to comply with professional standards when conducting its quarterly reviews of PNC's financial statements led to material misrepresentations in PNC's 10-Q filings during the relevant time period, and precluded proper notification to PNC by E&Y of ongoing material accounting irregularities.

290. Had E&Y conducted its interim financial statement reviews in accordance with GAAS, it could not have approved for the transfers of assets to the special purpose entities since PNC's financial statements were not prepared in conformity with GAAP, and it would not have threatened to withhold issuing an unqualified audit opinion for PNC's Form 10-K for 2001 if PNC did not appeal the FRB's directive to the SEC's Chief Accountant.

291. E&Y's conduct as described above constitutes negligence, in that it breached its duty to PNC as follows: (a) E&Y designed, promoted and gave its professional approval of special purpose entities for use by PNC that were not in accordance with GAAS; and (b) E&Y failed to correct public statements issued by or on behalf of PNC which were false or misleading.

292. Had it not been for E&Y's negligence in connection with the establishment, accounting for and reporting of the PAGIC transactions, PNC would not have suffered damages, costs and expenses as alleged herein.

293. As a direct and foreseeable result of E&Y's failure to exercise due care in the performance of its professional duties and as a result of its negligent conduct, PNC has sustained very significant damages, including without limitation: (i) significant fees paid to E&Y for its audit and consulting services during 2001 alone; (ii) $25 million in fines and penalties; (iii) $90 million in disgorgement; (iv) $20 million for the cost of investigations into the fraud; and (v) other related expenses in an amount to be proven at trial. By virtue of the assignment of such claims pursuant to the Partial Settlement, the Class is entitled to pursue such damages on PNC's behalf.

COUNT V

ACCOUNTING MALPRACTICE (BREACH OF CONTRACT)

294. Plaintiffs repeat and reallege each of the foregoing paragraphs as if fully set forth herein, except to the extent any allegations above contain any facts which are unnecessary or irrelevant for purposes of stating a claim for breach of contract.

295. This count is brought by Plaintiffs, on behalf of PNC, to recover damages from E&Y arising from E&Y's breach of contract. Plaintiffs have been assigned the claims of PNC and its subsidiaries as part and parcel of the Partial Settlement and thus, have standing to assert this claim.

296. E&Y was specifically retained by PNC for the purpose of providing accounting and advisory services to PNC in connection with PNC's public reporting of its financial results. It was specifically intended and understood by both PNC and E&Y that PNC would be relying upon E&Y's expertise and that such opinions and guidance would be utilized by PNC in conducting its business transactions.

297. Had E&Y complied with its contractual duties and the standards of the accounting profession, it would have detected that PNC's special purpose entity transactions did not accord

with GAAP, and thus E&Y breached its contractual duty to provide appropriate accounting advice and to assist PNC in not making materially false and misleading statements about its financial results. In the event that PNC did make a misstatement concerning its financial results, E&Y had a contractual duty to correct PNC financial statements to the extent that such statements were based upon false and misleading accounting.

298. Under the terms of E&Y's contractual engagements with PNC and in accordance with the representations of the opinion letters prepared by E&Y, E&Y expressly and by implication agreed to carry out the opinion letters in accordance with GAAS and GAAP. E&Y further agreed to correct any public statements issued by or on behalf of PNC which were false and misleading.

299. E&Y breached its contractual duties in the following respects:

(a) E&Y failed to examine PNC's financial statements in accordance with GAAS as set forth herein;

(b) E&Y approved PNC's interim 2001 financial statements accounting for the transfers of assets to the special purpose entities when it knew or should have known that those financial statements were not presented in conformity with GAAP;

(c) E&Y negligently failed to notify PNC and other relevant authorities of the existence of the conditions described above and thus deprived PNC and others of material information necessary for the adoption of timely and appropriate safeguards; and

(d) E&Y failed to exercise the degree of care exhibited by other accountants in the profession.

300. As a reasonable, natural, foreseeable, and proximate result of E&Y's breach of its express and implied agreements, undertakings, and contractual duties, PNC was damaged thereby. As a result, E&Y is liable to PNC for the amount of fees paid to E&Y by PNC in connection with such contracts in connection with all auditing and other services it performed

with respect to the PAGIC transactions on behalf of PNC during the calendar year 2001 and 2002.

301. As a direct and foreseeable result of E&Y's failure to exercise due care in the performance of its professional duties and as a result of breaching its contractual duties, PNC has sustained very significant damages, including without limitation: (i) significant fees paid to E&Y for its audit and consulting services during 2001 alone; (ii) $25 million in fines and penalties; (iii) $90 million in disgorgement; (iv) $20 million for the cost of investigations into the fraud; and (v) other related expenses in an amount to be proven at trial. By virtue of the assignment of such claims pursuant to the Partial Settlement, the Class is entitled to pursue such damages on PNC's behalf.

COUNT VI

NEGLIGENT MISREPRESENTATION

302. Plaintiffs repeat and reallege each of the foregoing paragraphs as if fully set forth herein, except to the extent any allegations above contain any facts which are unnecessary or irrelevant for purposes of stating a claim for negligent misrepresentation.

303. This count is brought by Plaintiffs, on behalf of PNC, to recover damages from E&Y arising from E&Y's negligent misrepresentation. Plaintiffs have been assigned the claims of PNC and its subsidiaries as part and parcel of the Partial Settlement and thus, have standing to assert this claim.

304. E&Y was specifically retained by PNC for the purpose of providing accounting and advisory services to PNC in connection with PNC's public reporting of its financial results. It was specifically intended and understood by both PNC and E&Y that PNC would be relying upon E&Y's expertise and that such opinions and guidance would be utilized by PNC in conducting its business transactions.

305. In connection with its performance of the subject accounting and opinions, E&Y negligently made material misrepresentations or omitted material information in the opinion letters it prepared for PNC by representing that the assets and results of the special purpose entities did not have to be consolidated with PNC's results.

306. E&Y negligently misrepresented to PNC that GAAP allowed for the aforementioned accounting treatment despite the fact that: (i) the purchasers of the transferred assets did not possess the requisite risks and rewards of ownership; (ii) PNC retained effective control over the special purpose entities; and (iii) AIG-FP did not make a sufficiently large investment in the special purpose entities to be "substantive" as required by GAAP.

307. E&Y also negligently represented to PNC that other national accounting firms had reviewed the transaction structure of SPE I and concurred with E&Y with its conclusion that consolidation of the SPE by PNC was not permitted under GAAP without advising PNC that it was aware that at least one firm, National Accounting Firm A, had identified "soft spots" in the accounting treatment in a similar transaction that could directly bear on the PAGIC treatment.

308. Justifiably relying on E&Y's negligent misrepresentations and omissions, PNC accounted for the special purpose entities on a non-consolidated basis, repeated E&Y's misrepresentations in its public filings and press releases and incorporated these misrepresentations into its public filings with bank regulators, the SEC and the investing public.

309. As a direct and foreseeable result of E&Y's negligent misrepresentations and omissions, PNC has sustained very significant damages, including without limitation: (i) significant fees paid to E&Y for its audit and consulting services during 2001 alone; (ii) $25 million in fines and penalties; (iii) $90 million in disgorgement; (iv) $20 million for the cost of investigations into the fraud; and (v) other related expenses in an amount to be proven at trial.

310. In addition, as a result of E&Y's negligent misrepresentations, PNC's stock price declined, causing significant loss of market capitalization; PNC's financial integrity was questioned by government regulators, the SEC, Wall Street analysts, the general public, and PNC's investors, customers, suppliers, lenders and employees; PNC was forced to pay for unforeseen accounting services in restating its financial results; PNC incurred substantial and unanticipated expenses in connection with its public relations; and PNC has been damaged by E&Y's misconduct in an amount at least equal to the waste of valuable corporate assets, goodwill and business opportunities. By virtue of the assignment of such claims pursuant to the Partial Settlement, the Class is entitled to pursue such damages on PNC's behalf.

WHEREFORE, Plaintiffs, on their own behalf and on behalf of the Class, prays for judgment as follows:

(A) Declaring this action to be a proper class action and certifying Plaintiffs as class representatives under Rule 23 of the Federal Rules of Civil Procedure;

(B) Awarding monetary damages against all Defendants in favor of Plaintiffs and the other members of the Class for all losses and damages suffered as a result of the wrongdoings alleged herein, together with interest thereon;

(C) Awarding Plaintiffs the fees and expenses incurred in this action, including reasonable allowance of fees for Plaintiffs' attorneys and experts;

(D) Granting Plaintiffs and the other members of the Class such other and further relief as the Court may deem just and proper.

JURY TRIAL DEMANDED

Plaintiffs hereby demand a trial by jury.

Dated: March 28, 2005 **LAW OFFICE OF ALFRED G. YATES, JR.**

By: ______________________________

Alfred G. Yates, Jr., Esq.
519 Allegheny Building
429 Forbes Avenue
Pittsburgh, PA 15219
(412) 391-5164

Liaison Counsel for Plaintiffs

MILBERG WEISS BERSHAD
& SCHULMAN LLP
David J. Bershad, Esq.
Barry A. Weprin, Esq.
Bruce D. Bernstein, Esq.
One Pennsylvania Plaza - 49th Floor
New York, NY 10119-0165
(212) 594-5300

SCHIFFRIN & BARROWAY LLP
David Kessler, Esq.
Michael K. Yarnoff, Esq.
280 King of Prussia Road
Radnor, PA 19087
(610) 667-7706

SCHOENGOLD SPORN LAITMAN
& LOMETTI, P.C.
Samuel Sporn, Esq.
Jay P. Saltzman, Esq.
19 Fulton Street
New York, NY 10038
(212) 964-0046

Co-Lead Counsel for Plaintiffs