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CIVIL INTAKE  
2016 MAR 14 AM 8:21  
JOHN T. FREY  
CLERK, CIRCUIT COURT  
FAIRFAX, VA

IN THE CIRCUIT COURT OF FAIRFAX COUNTY

TIMOTHY J. PAGLIARA, )  
 )  
 Plaintiff, )  
 v. )  
 )  
 FEDERAL HOME LOAN MORTGAGE )  
 CORPORATION, )  
 8200 Jones Branch Drive )  
 McLean, Virginia 22102, )  
 )  
 Defendant. )

2016 - 03860  
Case No. CL \_\_\_\_\_

**COMPLAINT FOR INSPECTION OF CORPORATE RECORDS**

Plaintiff Timothy J. Pagliara (“Mr. Pagliara” or the “Stockholder”), by and through undersigned counsel, brings this Complaint for Inspection of Corporate Records against Defendant Federal Home Loan Mortgage Corporation (“Freddie Mac” or the “Company”), applying for an order to permit his inspection and copying of corporate records under Virginia Code Sections 13.1-771 and -773. The Code provides that the “court shall dispose of an application under this subsection *on an expedited basis.*” Va. Code Ann. § 13.1-773B (emphasis added). In support of his application, Mr. Pagliara states the following:

**NATURE OF THE ACTION**

1. Stockholder has made a demand to inspect corporate records of Freddie Mac (the “Demand”), as is his right under the Virginia Stock Corporation Act (“VSCA”). That Demand has been improperly refused.

2. Freddie Mac is a private, for-profit corporation, with private stockholders and a board of directors, governed by Virginia law. Although it is now under the conservatorship of the

Federal Housing Finance Agency (“FHFA”), Freddie Mac still follows “the corporate governance practices and procedures of the law of the Commonwealth of Virginia, including without limitation the Virginia Stock Corporation Act as the same may be amended from time to time.” Freddie Mac Bylaws § 11.3(a) (adopted July 13, 2015).

3. Mr. Pagliara is a private owner of publicly traded stock in Freddie Mac, stock which is also explicitly governed by Virginia law. This application is a direct claim to enforce his individual rights as a shareholder to obtain corporate records under the VSCA.

4. Mr. Pagliara seeks these corporate records primarily for the purpose of investigating potential claims arising from the “Net Worth Sweep,” a series of enormously unfair transactions between Freddie Mac and its controlling stockholder, the United States Department of the Treasury (“Treasury”).

5. During the financial crisis in 2008, Treasury wanted for its own policy reasons to take control of Freddie Mac and its sister corporation, the Federal National Mortgage Association (“Fannie Mae”) (together with Freddie Mac, the “Companies”). Although facing challenges resulting from the crisis, neither of the Companies was in danger of insolvency. Treasury nonetheless caused the Companies’ regulator, FHFA, to put them into conservatorship in September 2008.

6. At the same time, by agreement struck between Treasury and FHFA, Treasury obtained warrants to acquire 79.9% of the Company’s common stock, plus 1,000,000 shares of senior preferred stock (“Senior Preferred Stock”). In exchange, the Treasury agreed to provide up to \$100 billion in funding (later increased to \$200 billion) to the Company. To the extent the Company drew on Treasury’s funding, it would owe Treasury an annual dividend of roughly 10% of the total money drawn. The stock purchase agreement with Treasury also prohibits the

Company from taking certain actions without Treasury's approval, including making any changes to its capital structure, paying any dividends to any stockholder other than to Treasury, or seeking to terminate FHFA's conservatorship.

7. Beginning in the third quarter of 2008, FHFA had Freddie Mac make a number of non-cash accounting adjustments substantially depressing its net worth, requiring Freddie Mac to draw heavily on Treasury's funding, and thereby increasing both Treasury's hold over the Company and the dividends due to Treasury under its Senior Preferred Stock.

8. By 2012, the Company had weathered the financial crisis and returned to stable profitability. It also had become clear that many of the non-cash accounting adjustments depressing the Company's net worth would be reversed. This was welcome news for the Company's private stockholders; the Company would be able to pay back the draws from Treasury, redeem the Senior Preferred Stock, and terminate the conservatorship in safe, sound and solvent condition. The Company could re-commence paying dividends to the Company's other stockholders, including junior preferred stockholders like Mr. Pagliara.

9. But the Company's profitability threatened Treasury's control over the Company and the flow of dividends paid to Treasury. So, in August 2012, Treasury engineered the Net Worth Sweep. The stock purchase agreement between the Company and Treasury was amended, and the dividend of 10% on the funds Freddie Mac had drawn from Treasury was replaced with a dividend equal to the entire positive net worth of the Company. An essentially identical arrangement was imposed on Fannie Mae.

10. Under the aptly named Net Worth Sweep, instead of a 10% dividend on the funding it provided to Freddie Mac, Treasury would get, in perpetuity, the entire positive net worth of the Company at the end of every quarter.

11. Treasury publicly stated two goals in instituting the Net Worth Sweep: (a) “winding down” (not conserving) Freddie Mac and Fannie Mae; and (b) “mak[ing] sure that every dollar of earnings each firm generates is used to benefit taxpayers.”

12. There was no consideration to Freddie Mac or its stockholders for this change—the Company got nothing from Treasury. And the Company gave up, essentially, everything—all its positive net worth, in perpetuity.

13. In every quarter since the Net Worth Sweep commenced, if the Company shows any positive value on its balance sheet, the Company gives Treasury a dividend that brings its net worth back to zero (leaving only a small capital reserve, which itself decreases to zero by 2018).

14. The Net Worth Sweep has resulted in a massive increase in dividends to Treasury. Under the pre-Sweep terms of the stock purchase agreement with Treasury, even assuming no redemptions of the Senior Preferred Stock, Freddie Mac would have paid roughly \$23 billion in cash dividends on the Senior Preferred Stock from 2013 through the first quarter of 2016. Instead, under the Net Worth Sweep, Freddie Mac will have paid more than \$74 billion in dividends—roughly \$51 billion more—over the same period, without redeeming any of the Senior Preferred Stock. And there is no end in sight.

15. Added to the dividends paid to Treasury before the Net Worth Sweep, Freddie Mac has now paid Treasury more than \$98 billion in dividends on its Senior Preferred Stock. That is roughly \$27 billion more than Freddie Mac received in Treasury funding. And Treasury still has a liquidation preference on its Senior Preferred Stock of more than \$72 billion, an amount that has to be fully redeemed before the Company can declare any dividends to its other stockholders.

16. As demonstrated by his Demand for corporate records, and this detailed Complaint, there is much that Mr. Pagliara knows about the Net Worth Sweep and related transactions. There also is much that Mr. Pagliara may reasonably infer from what he knows. Nonetheless, there is much that Mr. Pagliara does not know, particularly about the participation of the Company's board of directors in those transactions.

17. For example, Mr. Pagliara does not know whether the board of directors expressly approved the Net Worth Sweep, opposed it internally, or simply sat passively by while the Company's positive net worth was given to Treasury. Mr. Pagliara also does not know whether the board of directors approved the dividends paid pursuant to the Net Worth Sweep, opposed them internally, or simply let them be paid. His Demand seeks corporate records to answer these questions and many others, so that Mr. Pagliara can better evaluate potential claims that he may bring.

18. Mr. Pagliara seeks the requested corporate records in good faith and in furtherance of proper purposes. He has satisfied all of the requirements to obtain them under the VSCA. As set forth herein, he is entitled—on an expedited basis—to an order to permit inspection and copying of the records demanded.

### **JURISDICTION**

19. Under Virginia Code Section 13.1-773B, the Stockholder “may apply to the circuit court in the city or county where the corporation's principal office is located . . . for an order to permit inspection and copying of the records demanded.”

## THE PARTIES

### The Stockholder

20. Mr. Pagliara is the beneficial owner of stock in Freddie Mac. Mr. Pagliara purchased 173,300 shares of Freddie Mac's 2007 Fixed-to-Floating Rate Non-Cumulative Perpetual Preferred Stock (ticker symbol: FMCKJ) on January 8, 2009, and he has held these shares continuously since purchase. Mr. Pagliara purchased 173,300 shares of Freddie Mac's 6.02% Non-Cumulative Perpetual Preferred Stock (ticker symbol: FMCKL) on November 3, 2009, and he has held these shares continuously since purchase. Verified documentary evidence of the Stockholder's beneficial ownership is attached as Exhibit A to Exhibit 1 of his Demand. *See Demand, Ex. A hereto.*

21. Mr. Pagliara is the founder of CapWealth Advisors LLC, an SEC-registered investment advisory firm in Franklin, Tennessee. CapWealth Advisors LLC manages over \$1 billion in client assets and provides wealth management services for individuals, families, foundations, and institutions. Among other accolades and industry recognition, *Barron's* magazine named Mr. Pagliara Tennessee's top financial advisor in 2012, 2013, 2014 and 2015.

22. Mr. Pagliara also is the founder of Investors Unite, a coalition of private investors from all walks of life, committed to the preservation of shareholder rights for those invested in Freddie Mac and Fannie Mae. Investors Unite works to educate Freddie Mac and Fannie Mae shareholders and lawmakers on the importance of reforming the Companies in a way that will return to shareholders what they are contractually and legally owed, but have not been paid. Although Mr. Pagliara formed Investors Unite, he is not acting on behalf of Investors Unite in this litigation.

## **Freddie Mac**

23. Freddie Mac is a federally chartered, for-profit, publicly traded corporation. It maintains its principal place of business in Fairfax County, Virginia.

24. Freddie Mac was established by the Federal Home Loan Mortgage Corporation Act (the "Corporation Act") in 1970 to make the secondary mortgage market more competitive and efficient, primarily by offering an alternative to Fannie Mae, which serves a similar function.

25. Freddie Mac and Fannie Mae purchase residential mortgages originated by private banks and bundle those mortgages into mortgage-backed securities. Together, the Companies purchase nearly 90% of all new home mortgages in the United States. Through securitization, they bundle pools of mortgages into flexible and liquid financial instruments, which are then sold to investors on the open market. The investors in these mortgage-backed securities are paid from the principal and interest payments flowing back from the original mortgages in the bundle.

26. This secondary market for mortgages creates an additional flow of mortgage capital by replenishing lending funds of mortgage originators (the banks) directly, and more immediately, than requiring the banks to wait decades for periodic payments from the borrowers. The secondary market also encourages lending by spreading out the risks borne by mortgage lenders. Freddie Mac and Fannie Mae thus create additional liquidity for private banks, which enables the banks to extend additional home purchase loans.

27. There is no federal corporate law, and Freddie Mac was required by federal regulation to select one of the following bodies of corporate law for its corporate governance: the law of the jurisdiction where its principal office is located; Delaware general corporation law; or the Revised Model Business Corporation Act. 12 C.F.R. § 1710.10(b); *see also* 12 C.F.R. § 1239.2(b).

28. At all relevant times, Freddie Mac has elected to follow and be governed by Virginia corporate law, the law of the jurisdiction where its principal office is located. Section 11.3(a) of its current bylaws (adopted July 13, 2015), provides that “the Corporation shall follow the corporate governance practices and procedures of the law of the Commonwealth of Virginia, including without limitation the Virginia Stock Corporation Act as the same may be amended from time to time.”

### **Freddie Mac Is Owned by Its Stockholders**

29. As provided by the Corporation Act, Freddie Mac is owned by private stockholders. Until FHFA’s conservatorship in September 2008 (discussed below), Freddie Mac was a self-sustaining business funded by private capital raised by issuance of publicly traded common and preferred stock listed on the New York Stock Exchange.<sup>1</sup>

30. When purchasing their stock in Freddie Mac, private stockholders, including Mr. Pagliara, relied upon the rights and protections of Virginia’s corporate laws. The certificates of designation for the FMCKJ and FMCKL preferred stock held by Mr. Pagliara both expressly state the following:

This Certificate and the respective rights and obligations of Freddie Mac and the holders of the Non-Cumulative Preferred Stock with respect to such Non-Cumulative Preferred Stock shall be construed in accordance with and governed by the laws of the United States, provided that the law of the Commonwealth of Virginia shall serve as the federal rule of decision in all instances except where such law is inconsistent with Freddie Mac’s enabling legislation, its public purposes or any provision of this Certificate.

31. Under Virginia law, the VSCA is incorporated into the contract between a stock corporation like Freddie Mac and its stockholders like Mr. Pagliara.

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<sup>1</sup> In June 2010, the Companies’ regulator, FHFA, ordered Freddie Mac and Fannie Mae to delist from the NYSE, saying the decision was based on the Companies’ weak stock price, not due to any change in condition at the Companies or the outlook for their future. Freddie Mac’s stock stopped trading on the NYSE on July 7, 2010; since July 8, 2010, Freddie Mac’s stock has continued to be traded over the counter, through the OTC bulletin.



## **Freddie Mac Is Governed by its Board of Directors**

32. Freddie Mac is governed by its board of directors (the “Board,” and each director a “Director). Absent a stockholder agreement to the contrary, Section 13.1-673B of the VSCA requires corporations to have a board of directors, and “all corporate powers shall be exercised by or under the authority of, and the business and affairs of the corporation managed under the direction of, its board of directors.” Likewise, under the Corporation Act, Freddie Mac is “a body corporate under the direction of a Board of Directors. Within the limitations of law and regulation, the Board of Directors shall determine the general policies that govern the operations of the Corporation.” 12 U.S.C. § 1452(a)(1).

33. Freddie Mac’s Board currently comprises the following persons: Christopher S. Lynch, Non-Executive Chairman; Raphael W. Bostic; Carolyn H. Byrd; Lance F. Drummond; Thomas M. Goldstein; Richard C. Hartnack; Steven W. Kohlhagen; Donald H. Layton; Sara Mathew; Saiyid T. Naqvi; Nicolas P. Retsinas; Eugene B. Shanks; and Anthony A. Williams. Mr. Lynch receives \$290,000 per year in compensation from Freddie Mac. Each of the other Directors who is not also a Freddie Mac employee receives \$160,000 per year.

## **STOCKHOLDER’S RIGHT TO INSPECT CORPORATE RECORDS**

### **Shareholder Rights to Inspect Corporate Records under the VSCA**

34. The VSCA provides shareholders with statutory rights to inspect and copy corporate records. Va. Code Ann. § 13.1-771. These shareholder rights cannot be abolished or limited by the corporation’s articles of incorporation or bylaws. *Id.* at -771E. Section 13.1-771A provides any shareholder with the right, upon demand at least five business days before the requested inspection, to inspect and copy certain records of the corporation. Va. Code Ann. § 13.1-771.

35. Broader categories of corporate records are available for inspection and copying to a shareholder who meets the requirements of Section 13.1-771D. Those requirements are: (1) the shareholder has either been a shareholder for at least six months immediately preceding the demand, or owns at least five percent of all of the outstanding shares; (2) the shareholder's demand is made in good faith and for a proper purpose; (3) the shareholder describes with reasonable particularity his purpose and the records he seeks to inspect; and (4) the records requested are directly connected with that purpose. Va. Code Ann. § 13.1-771D.

36. For purposes of shareholder rights to inspect corporate records, "shareholder" includes a beneficial owner of stock. Va. Code § 13.1-771G. Furthermore, "[a] shareholder's agent or attorney has the same inspection and copying rights as the shareholder the agent or attorney represents." Va. Code Ann. § 13.1-772A.

#### **Stockholder Made a Proper Demand for Inspection of Corporate Records**

37. On January 19, 2016, Mr. Pagliara served a Demand on Freddie Mac and the Board to inspect records of Freddie Mac in accordance with Section 13.1-771 of the VSCA. A copy of the Demand is attached hereto as Exhibit A and incorporated herein by reference.

38. As evidenced by the Demand and addressed herein, Mr. Pagliara meets all requirements of the VSCA: (1) he is and has been a beneficial owner of stock in Freddie Mac for more than six months; (2) his request is made in good faith and for several proper purposes; (3) his proper purposes and the records requested are set forth with particularity in the Demand; and (4) his Demand seeks records that are directly connected with his proper purposes.

#### **Stockholder's Demand Was Unreasonably Refused**

39. Freddie Mac did not respond to the Demand within five business days. Indeed, the Board never responded at all to the Demand. Instead, FHFA responded on January 28, 2016,

refusing the demand without addressing its merits. A copy of FHFA's response is attached hereto as Exhibit B and incorporated by reference.<sup>2</sup>

40. In refusing the demand, FHFA asserted that, as conservator, it has succeeded to all rights of the stockholders of Freddie Mac, and thus, the Stockholder has no right to the demanded inspection of corporate records. Under well-established law, as conservator FHFA only succeeds to the rights of stockholders to act on behalf of the corporation and to bring certain derivative claims on behalf of the corporation. FHFA does not succeed to the rights of stockholders to bring direct claims to enforce their own individual rights. This Complaint for Inspection of Corporate Records is just such a direct claim.

41. Under Section 13.1-773B of the VSCA, a shareholder whose demand to inspect corporate records is refused may file an application for a court-ordered inspection of the requested records. Section 13.1-773B further provides that "[t]he court shall dispose of an application under this subsection on an expedited basis." Mr. Pagliara now seeks that relief.

42. Freddie Mac has refused the Stockholder's demanded inspection without a reasonable basis for doubt about the right of the Stockholder to inspect the records demanded. Under Section 13.1-773C, Mr. Pagliara is thus entitled to recover his costs, including reasonable counsel fees, incurred in enforcing his right to inspection. Va. Code Ann. § 13.1-773C.

### **STOCKHOLDER'S INVESTIGATION OF POTENTIAL CLAIMS**

43. Stockholder is investigating potential claims that he may assert with respect to the Net Worth Sweep and other conduct of Freddie Mac, the Board, FHFA and Treasury, as further described below. Stockholder seeks corporate records in aid of that investigation.

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<sup>2</sup> FHFA's initial response asserted that "Investors Unite has no basis on which to seek inspection of Freddie Mac records." *See* Ex. B. Stockholder's counsel wrote back to FHFA clarifying, as plainly stated in the Demand itself, that Mr. Pagliara was the Stockholder seeking inspection. *See* Feb. 4, 2016 Letter from T. Connally to A. Pollard, Ex. C hereto and incorporated herein. FHFA's General Counsel, Mr. Pollard, noted the clarification by e-mail. *See* Feb. 4, 2016 E-mail from A. Pollard to T. Connally, Ex. D hereto and incorporated herein.

**I. Freddie Mac's Business and the Financial Crisis.**

44. Freddie Mac was a profitable business every year from the time it was privatized in 1989 through 2006. Freddie Mac's reported net income from 2000-2006 is shown in the table below:

<b>Year</b>	<b>Net Income</b>
2000	\$3.666 billion
2001	\$3.158 billion
2002	\$10.090 billion
2003	\$4.816 billion
2004	\$2.937 billion
2005	\$2.130 billion
2006	\$2.211 billion

45. Freddie Mac declared and paid dividends on its common and preferred stock almost every quarter. The table below shows Freddie Mac's dividend payments from 2000-2006:

<b>Year</b>	<b>Cash Dividends on Preferred and Common Stock</b>
2000	\$652 million
2001	\$774 million
2002	\$845 million
2003	\$934 million
2004	\$1.046 billion
2005	\$1.299 billion
2006	\$1.579 billion

46. As a result of the financial crisis, Freddie Mac ended its long, uninterrupted string of profitable quarters by recording a quarterly loss of \$2 billion in the third quarter of 2007 and a loss of \$2.5 billion in the fourth quarter of 2007. Freddie Mac recorded losses of \$151 million and \$821 million in the first two quarters of 2008, respectively. Those losses largely reflected a decline in the market value of its holdings of mortgage-backed securities, a drop driven by declining home prices and increased default rates.

47. But even following those losses, Freddie Mac continued to generate enough cash through its operations to pay its debts, it remained more than adequately capitalized under applicable regulatory requirements, and it had ample ability to access the debt market. Freddie Mac had the capacity to weather the financial crisis and return to profitability thereafter.

48. In July 2008, James Lockhart, Director of the Office of Federal Housing Enterprise Oversight (“OFHEO”), Freddie Mac’s and Fannie Mae’s primary regulator at the time, said the following about the Companies:

OFHEO has been monitoring and continues to monitor closely Fannie Mae, Freddie Mac, and the mortgage and financial markets.

...

As I have said before, they are adequately capitalized, holding capital well in excess of the OFHEO-directed requirement, which exceeds the statutory minimums. They have large liquidity portfolios, access to the debt market and over \$1.5 trillion in unpledged assets.

49. That same month, Henry Paulson, Secretary of the Treasury, and Ben Bernanke, Chairman of the Federal Reserve, testified before Congress that the Companies were “adequately capitalized.”

50. In August 2008, Freddie Mac stated publicly that it was not seeking aid from the Treasury or the Federal Reserve. At that time, Freddie Mac had outstanding 726 million shares of common stock and 464 million shares of preferred stock.

## **II. Pressured by Treasury, FHFA Becomes Conservator of Freddie Mac.**

51. In July 2008, Congress passed the Housing and Economic Recovery Act of 2008 (“HERA”), thereby creating FHFA and installing it, in place of OFHEO, as the primary regulator of Freddie Mac and Fannie Mae. HERA gave FHFA the power to put the entities it regulated, including Freddie Mac and Fannie Mae, into either conservatorship or receivership. 12 U.S.C § 4617(a).

52. Under HERA, the purposes of conservatorship are very different from the purposes of receivership. Conservatorship is a process to stabilize a troubled institution with the objective of returning it to normal business operations. FHFA has acknowledged when issuing regulations under HERA that “[a] conservator’s goal is to continue the operations of a regulated entity, rehabilitate it and return it to a safe, sound and solvent condition.” Conservatorship and Receivership, 76 Fed. Reg. 35,724, 35,730 (June 20, 2011). In contrast to conservatorship, which is aimed at preserving a company and restoring it to a safe, sound and solvent condition, receivership is the process for the liquidation of a company.

53. Despite the adequate capitalization of Freddie Mac and Fannie Mae, Treasury had concluded that, for policy reasons, it should take control of Freddie Mac and Fannie Mae so it could use them as intermediaries to inject additional liquidity into mortgage markets. According to Secretary Paulson, “I’d come to the conclusion that taking them over was the best way to avert a meltdown, keep mortgage financing available, stabilize markets, and protect the taxpayer.” Henry M. Paulson, Jr., *On the Brink: Inside the Race to Stop the Collapse of the Global*

*Financial System* at 3. “I concluded that the only solution was to get FHFA to put the GSEs into receivership.”<sup>3</sup> *Id.* at 162.

54. Lockhart, now Director of the newly created FHFA, understandably resisted. As Secretary Paulson explained, “I pressed [FHFA Director Lockhart] on the need for receivership, but he repeatedly told me that this would be difficult to do quickly because FHFA’s most recent semiannual regulatory exams had not cited capital shortfalls.” *Id.* at 163.

55. Treasury’s pressure to have FHFA take control of the Companies was successful. On September 7, 2008, less than two months after Director Lockhart, Secretary Paulson, and Chairman Bernanke had all said that Freddie Mac and Fannie Mae were adequately capitalized, FHFA appointed itself as conservator of Freddie Mac and Fannie Mae.

56. Although FHFA was the entity that formally placed Freddie Mac into conservatorship, Treasury controlled the decision. As Secretary Paulson explained, “[m]any of the actions I took—seizing control of the quasi-governmental mortgage giants Fannie Mae and Freddie Mac . . . were deeply distasteful to me.” *Id.* at xiv. Former Representative Barney Frank said of Secretary Paulson, “he exercised those conservatorship powers.” *Id.* at xli.

57. In making the announcement of FHFA’s conservatorship, Director Lockhart explained that conservatorship was “a statutory process designed to stabilize a troubled institution with the objective of returning the entities to normal business operations [and that] FHFA will act as the conservator until they are stabilized.” FHFA also released a “fact sheet” that stated “conservatorship is the legal process in which a person or entity is appointed to establish control and oversight of a Company to put it in sound and solvent condition.” In 2010, Acting Director of FHFA Edward J. DeMarco confirmed that the only “post-conservatorship outcome[] . . . that FHFA may implement today under existing law is to reconstitute the two

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<sup>3</sup> “GSEs” stands for “Government Sponsored Entities” and refers to the Companies.

companies under their current charters.” Letter from Edward J. DeMarco, Acting Director, FHFA, to Chairmen and Ranking Members of the Senate Committee on Banking, Housing, and Urban Affairs and to the House Committee on Financial Services at 7 (Feb. 2, 2010).

58. Consistent with this stated purpose, FHFA’s powers as conservator under HERA may be used only as “(i) necessary to put the regulated entity in a *sound and solvent condition*, and (ii) appropriate to carry on the business of the regulated entity and *preserve and conserve the assets and property of the regulated entity*.” 12 U.S.C. § 4617(b)(2)(D) (emphasis added).

59. When FHFA is appointed as conservator of a corporation, the rights of the stockholders are not extinguished. As conservator, FHFA temporarily succeeds only to the rights of the corporation, and certain rights of its stockholders, board and managers to act on behalf of the corporation:

SUCCESSOR TO REGULATED ENTITY.—The Agency shall, as conservator or receiver, and by operation of law, immediately succeed to—

(i) all rights, titles, powers, and privileges of the regulated entity, and of any stockholder, officer, or director of such regulated entity with respect to the regulated entity and the assets of the regulated entity; and

(ii) title to the books, records, and assets of any other legal custodian of such regulated entity.

12 U.S.C. § 1367(b)(2)(A).

60. Indeed, United States Court of Appeals for the Ninth Circuit recently confirmed this very same point:

Nor does the Federal Housing Finance Agency’s conservatorship transform Fannie Mae and Freddie Mac into federal instrumentalities. We agree that the FHFA has “all the rights, titles, powers and privileges of” Fannie Mae and Freddie Mac. However, this places FHFA in the shoes of Fannie Mae and Freddie Mac, and gives the FHFA *their* rights and duties, not the other way around.



*United States v. Aurora Loan Servs., Inc.*, No. 14-15031, slip op. at 2 (9th Cir. Feb. 22, 2016) (emphasis in original, internal citations omitted).

61. In contrast, when FHFA is appointed as receiver under HERA, “the Agency shall place the regulated entity in liquidation and proceed to realize upon the assets of the regulated entity in such manner as the Agency deems appropriate . . .” 12 U.S.C. § 4617(b)(2)(E). FHFA’s appointment as receiver terminates the stockholders’ rights, preserving only their claims to proceeds of the liquidation. 12 U.S.C. § 4617(b)(2)(K)(i) (FHFA’s appointment as receiver “shall terminate all rights and claims that the stockholders and creditors of the regulated entity may have against the assets or charter of the regulated entity or the Agency arising as a result of their status as stockholders or creditors. . .”).

62. After FHFA appointed itself as conservator, Freddie Mac’s common and preferred stock continued to trade on the New York Stock Exchange, and FHFA’s fact sheet about the conservatorship acknowledged that “stockholders will continue to retain all rights in the stock’s financial worth; as such worth is determined by the market.” Director Lockhart assured Congress shortly after imposition of the conservatorship that Freddie Mac’s and Fannie Mae’s “shareholders are still in place; both the preferred and common shareholders have an economic interest in the companies . . .”

### **III. FHFA Displaces then Reconstitutes Freddie Mac’s Board.**

63. Consistent with FHFA’s succession as conservator to certain rights of the corporation’s stockholders, board and managers to act on behalf of the corporation, HERA further provides that FHFA “may, by regulation or order, provide for the exercise of any function by any stockholder, director, or officer of any regulated entity for which [FHFA] has been named conservator or receiver.” 12 U.S.C. § 4617(b)(2)(C).

64. As Freddie Mac is a corporation governed by Virginia law, the corporate powers of Freddie Mac, its stockholders, Board, and management are governed by Virginia corporate law. The powers that FHFA has succeeded to as conservator under HERA, and those it is authorized to exercise as conservator under HERA, are thus also governed by Virginia's corporate law.

65. As noted, upon appointing itself conservator of Freddie Mac, FHFA succeeded to certain rights of Freddie Mac's Board to act on behalf of the corporation. When it became conservator, FHFA displaced and dismissed the then-current Directors.

66. On November 24, 2008, FHFA reconstituted Freddie Mac's Board and delegated back to the Board all or a subset of the board powers to which FHFA had succeeded when the conservatorship took effect. On December 18, 2008, FHFA appointed 11 Directors to serve on the reconstituted Board, three of whom were on the Board prior to the conservatorship and eight of whom were new to the Board. FHFA announced that the Board would fulfill the same role as a typical corporate board, including overseeing compensation, audits and governance.

67. To the extent the Board has powers, it has commensurate duties. Both those powers, and the commensurate duties, are defined and governed by Virginia law.

68. Under the structure that FHFA established, certain Board actions were subject to FHFA approval, and FHFA could block Freddie Mac from taking some actions approved by the Board if consistent with FHFA's fiduciary duties. But FHFA could not make the Board take or approve any action.

69. In particular, the Board is vested with authority to declare dividends. Under the VSCA and the Corporation Act, the declaration and payment of dividends is entrusted to the discretion of the Board. *See* Va. Code Ann. § 13.1-653A ("A board of directors *may* authorize

and the corporation *may* make distributions to its shareholders . . .”) (emphasis added); *see also* 12 U.S.C. § 1452(b)(1) (Freddie Mac may make capital distributions, “as may be declared by the Board of Directors.”).

70. Like other aspects of Freddie Mac’s corporate governance, the Directors’ conduct is governed by Virginia law. Section 13.1-690 of the VSCA requires a director to discharge his duties “in accordance with his good faith business judgment of the best interests of the corporation.” Indeed, in a letter to FHFA in 2014, Freddie Mac acknowledged that “[t]he applicable provisions of Virginia law, which Freddie Mac has elected to follow pursuant to FHFA regulations, . . . examine[] a director’s ‘good faith business judgment of the best interests of the corporation,’ amplified by case law that focuses on the process followed by directors in making their decisions.” May 15, 2014 Letter from A. Myara to A. Pollard at 5.

#### **IV. Treasury Takes a Controlling Interest in the Company through Senior Preferred Stock.**

71. HERA gave Treasury temporary and limited authority to invest in the Companies’ stock. This authority lasted until December 31, 2009. In exercising this limited authority, Treasury was required to consider “the need to maintain [each Company’s] status as a private shareholder-owned company” and to “plan for the orderly resumption of private market funding or capital market access.” 12 U.S.C. §§ 1455(l)(1)(C), 1719(g)(1)(C).

72. HERA required that any investment by Treasury must be on terms agreeable to Freddie Mac:

Nothing in this subsection requires [Freddie Mac] to issue obligations or securities to the Secretary [of the Treasury] without mutual agreement between the Secretary and [Freddie Mac].

12 U.S.C. § 1455(l)(1)(A).

73. The day after conservatorship was imposed on the Companies, FHFA entered into on behalf the Companies two virtually identical senior preferred stock purchase agreements (the “PSPAs”) with Treasury.

74. Under the Freddie Mac PSPA, Treasury purchased a newly created and issued class of securities in Freddie Mac, the Senior Preferred Stock. Freddie Mac’s Senior Preferred Stock was created pursuant to a Senior Preferred Stock Certificate of Designation (“Senior Preferred Stock Certificate of Designation”) that sets forth the rights, powers and preferences of the Senior Preferred Stock.

75. Under the PSPA, Treasury received 1,000,000 shares of Freddie Mac’s newly created Senior Preferred Stock in exchange for a funding commitment that initially allowed Freddie Mac to draw up to \$100 billion from Treasury. In a “fact sheet” released by Treasury in 2008 addressing the PSPA, Treasury admitted that “[t]his number is unrelated to the Treasury’s analysis of the current financial conditions of the GSEs.” Rather, the “amount was chosen to demonstrate a strong commitment to the GSEs’ creditors and mortgage backed security holders.”<sup>4</sup>

76. The 1,000,000 shares of Senior Preferred Stock had an initial aggregate liquidation preference equal to \$1 billion (\$1,000 per share), which would be increased by any additional amounts drawn on Treasury’s funding commitment. In other words, Treasury’s liquidation preference on its Senior Preferred Stock increased by one dollar for each dollar Freddie Mac received from Treasury under the funding commitment. If Freddie Mac were to

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<sup>4</sup> Effective May 6, 2009, Freddie Mac and Treasury entered into the First Amendment to the PSPA, increasing Treasury’s funding commitment to Freddie Mac from \$100 billion to \$200 billion. Effective December 24, 2009, Freddie Mac and Treasury entered into the Second Amendment to the PSPA. This amendment again increased Treasury’s funding commitment to the amount Freddie Mac needed to cover quarterly net worth deficits from 2010 to 2012, and thereafter to an amount established by a formula that might be greater (but not less) than \$200 billion.

liquidate (through receivership), Treasury would be entitled to recover the full liquidation preference of its Senior Preferred Stock before any other stockholder could recover anything.

77. Through the PSPAs, Freddie Mac and Fannie Mae also each provided Treasury with warrants to purchase 79.9% of their respective common stock, and they agreed to covenants barring each Company from taking certain actions without Treasury's approval, including making any changes to its capital structure, paying any dividends to any stockholder other than to Treasury, or seeking to terminate FHFA's conservatorship.

78. The Senior Preferred Stock diluted, but did not eliminate, the economic interests of the Companies' private stockholders. The warrants to purchase 79.9% of the Companies' common stock gave Treasury "upside" via economic participation in the Companies' future profitability, but this upside would be shared with private common stockholders, who still retained rights to the Companies' residual value by virtue of their stock ownership.

79. The Senior Preferred Stock of each of the Companies ranks senior to all other classes and series of stock and initially provided for a cash dividend to Treasury equal to 10% of the outstanding liquidation preference. If the Companies did not timely pay the dividend in cash, the value of the dividend would be added to the liquidation preference—effectively amounting to an in-kind dividend payment. Starting with such an in-kind dividend payment, the dividend rate would increase to 12% of the liquidation preference until all dividends in arrears had been paid in cash, at which time the dividend rate would return to 10%.

80. The Senior Preferred Stock Certificate of Designation, consistent with the VSCA, vested the Board with discretion to declare dividends thereunder: "holders of outstanding shares of Senior Preferred Stock shall be entitled to receive, ratably, *when, as and if declared by the Board of Directors, in its sole discretion*, out of funds legally available therefor, cumulative cash

dividends at the annual rate per share equal to the then-current Dividend Rate on the then-current Liquidation Preference.” Senior Preferred Stock Certificate of Designation § 2(a).

**V. FHFA Requires Freddie Mac to Make Accounting Adjustments that Increased Dividends to Treasury on its Senior Preferred Stock.**

81. Beginning in the third quarter of 2008, FHFA (at Treasury’s direction) required Freddie Mac to make non-cash accounting adjustments substantially depressing its net worth, requiring Freddie Mac to draw heavily on Treasury’s funding.

82. FHFA made overly pessimistic and unrealistic assumptions about Freddie Mac’s future financial prospects, triggering negative adjustments to Freddie Mac’s balance sheet, most notably write-downs of significant deferred tax assets and the establishment of large loan loss reserves, which caused significant non-cash losses. Although reflecting nothing more than accounting assumptions about Freddie Mac’s future prospects and having no effect on the cash flow Freddie Mac was generating, these non-cash losses temporarily decreased the Freddie Mac’s reported net worth by more than \$22 billion.

83. These negative accounting adjustments had the effect of significantly increasing the liquidation preference on Treasury’s Senior Preferred Stock and, therefore, the dividends owed to Treasury. Because the Company was showing a negative net worth on its balance sheet, as a result of the FHFA-required write-downs, Freddie Mac made \$44.6 billion in draws from Treasury under the PSPA in 2008. These draws from Treasury increased Treasury’s liquidation preference dollar for dollar, and thereby increased the dividends due to Treasury (set at 10% of its liquidation preference if paid in cash, 12% if paid in kind).

84. In total, Freddie Mac made draws of \$71.3 billion on Treasury’s commitment: \$44.6 billion in 2008; \$6.1 billion in 2009; \$13.0 billion in 2010; \$7.6 billion in 2011; and \$200

million in 2012. With the additional \$1 billion liquidation preference provided upon entry into the PSPA, by the time of the last draw, Treasury's liquidation preference was \$72.3 billion.

#### **VI. Freddie Mac's Return to Profitability Threatens Treasury's Control and Dividends.**

85. By the second quarter of 2012, the Companies had worked through their crisis-related issues and were paying 10% annualized cash dividends on the Senior Preferred Stock, without drawing on the funding commitment from Treasury. Based on the improving housing market and the high quality of the newer loans backed by the Companies, it was apparent that they had returned to stable profitability and were, in fact, poised for massive profitability.

86. The return to profitability made it inevitable that the Companies would be reversing many of the non-cash accounting losses they had incurred under the conservatorship, and the reversal of those paper losses would result in a significant increase in the Companies' net worth.

87. Given the broad-based recovery in the housing industry that had occurred by the middle of 2012, the Board, FHFA and Treasury fully understood that Freddie Mac was on the verge of generating significant profits, far in excess of the dividends owed on the Senior Preferred Stock. Indeed, in early August 2012, Freddie Mac reported positive net income of \$3 billion for the second quarter of 2012, and the Company did not have to draw from Treasury's commitment under the PSPA to pay its dividend to Treasury. Freddie Mac likewise did not need a draw to pay the cash dividend on the Senior Preferred Stock in the third and fourth quarters of 2012.

88. In light of the Companies' return to profitability, stockholders of Freddie Mac reasonably believed that the Company would be allowed to pay down Treasury's liquidation preference, redeem the Senior Preferred Stock, and terminate the conservatorship, consistent

with the purpose of the conservatorship and FHFA's stated intent at the time the conservatorship was imposed on Freddie Mac.

89. On the other side of the same coin, these same circumstances, in which Freddie Mac would have the resources to pay down the liquidation preference and redeem the Senior Preferred Stock, threatened Treasury's control over, and dividends from, Freddie Mac.

## **VII. Treasury Imposes the Net Worth Sweep.**

90. While Freddie Mac and Fannie Mae were entering a boom cycle in the fall of 2012, Treasury itself faced a looming financial crisis. The federal government is, by law, subject to a debt ceiling that limits the amount that it can owe. The government was predicted to reach that ceiling by the end of 2012, absent (1) an increase in the debt ceiling, (2) sharp cuts to federal programs, or (3) a massive influx of revenue. As Treasury has explained on its website, collision with the debt ceiling "would have catastrophic economic consequences."

91. An increase in the debt ceiling and cuts to federal programs were not politically feasible. Treasury's only option was to find a massive influx of revenue somewhere. Treasury decided to take the money from Freddie Mac and Fannie Mae stockholders. Rather than conserve and preserve them, Treasury would force the wind down of both Companies while extracting every bit of value on the way down.

92. On August 17, 2012, just two weeks after Freddie Mac and Fannie Mae announced net incomes of \$3 billion and \$5 billion, respectively, for the second quarter of 2012, both Freddie Mac and Fannie Mae entered into Third Amendments to their PSPAs.

93. Under the Third Amendments, Treasury is entitled to receive, on a quarterly basis, cumulative cash dividends in an amount equal to *the entire net worth of Freddie Mac and Fannie Mae*, leaving only a small capital reserve that is scheduled to equal zero on January 1, 2018 (the



“Net Worth Sweep”). If the dividends under the Net Worth Sweep are not paid in cash, they will cumulate and be added to the liquidation preference on the Senior Preferred Stock.

94. After the Third Amendment, Section 2(c) of the Certificate of Designation for the Freddie Mac Senior Preferred Stock provides as follows:

For each Dividend Period from January 1, 2013, holders of outstanding shares of Senior Preferred Stock shall be entitled to receive, ratably, when, as and if declared by the Board of Directors, in its sole discretion, out of funds legally available therefor, *cumulative cash dividends in an amount equal to the then-current Dividend Amount. . . .*

For each Dividend Period from January 1, 2013, through and including December 31, 2017, the “Dividend Amount” for a Dividend Period means the amount, if any, by which *the Net Worth Amount at the end of the immediately preceding fiscal quarter, less the Applicable Capital Reserve Amount, exceeds zero*. For each Dividend Period from January 1, 2018, the “Dividend Amount” for a Dividend Period means the amount, if any, by which the Net Worth Amount at the end of the immediately preceding fiscal quarter exceeds zero. In each case, “Net Worth Amount” means (i) the total assets of the Company (such assets excluding the Commitment and any unfunded amounts thereof) as reflected on the balance sheet of the Company as of the applicable date set forth in this Certificate, prepared in accordance with GAAP, less (ii) the total liabilities of the Company (such liabilities excluding any obligation in respect of any capital stock of the Company, including this Certificate), as reflected on the balance sheet of the Company as of the applicable date set forth in this Certificate, prepared in accordance with GAAP. “Applicable Capital Reserve Amount” means, as of any date of determination, for each Dividend Period from January 1, 2013, through and including December 31, 2013, \$3,000,000,000; and for each Dividend Period occurring within each 12-month period thereafter, \$3,000,000,000 reduced by an equal amount for each such 12-month period through and including December 31, 2017, so that for each Dividend Period from January 1, 2018, the Applicable Capital Reserve Amount shall be zero.

PSPA Third Amendment § 3 (emphasis added).

95. The Third Amendment provides no end date for the Net Worth Sweep.

96. In sum, as the name provides, under the Net Worth Sweep, Treasury is entitled to receive as dividends every quarter and in perpetuity *all of the net worth in Freddie Mac*, leaving only a small and decreasing capital reserve.

97. The Net Worth Sweep has resulted in a massive increase in dividends to Treasury. Absent the Third Amendment, even assuming no redemptions, Freddie Mac would have paid roughly \$23 billion in dividends on the Senior Preferred Stock from 2013 through the first quarter of 2016. Instead, under the Third Amendment, Freddie Mac will have paid more than \$74.4 billion in dividends over the same period,<sup>5</sup> without redeeming any of the Senior Preferred Stock:

Fiscal Quarter	Dividend Paid
2013 Q1	\$5.827 billion
2013 Q2	\$6.971 billion
2013 Q3	\$4.357 billion
2013 Q4	\$30.436 billion
2014 Q1	\$10.435 billion
2014 Q2	\$4.499 billion
2014 Q3	\$1.890 billion
2014 Q4	\$2.786 billion
2015 Q1	\$850 million
2015 Q2	\$746 million
2015 Q3	\$3.913 billion

<sup>5</sup> This total, and the table below, includes the dividend payment for the first quarter of 2016 announced by Freddie Mac on February 18, 2016, which is scheduled to be paid at the end of the quarter.

Fiscal Quarter	Dividend Paid
2015 Q4	\$0
2016 Q1	\$1.740 billion

### VIII. Potential Claims Arising from the Net Worth Sweep

98. The Third Amendment was egregiously unfair to Freddie Mac. For no consideration whatsoever, Freddie Mac's entire residual value was given to Treasury. The Net Worth Sweep and the dividends paid thereunder give rise to numerous potential claims being investigated by the Stockholder.

99. The only possible motivations behind the Net Worth Sweep are (a) to take money to which Treasury was not previously entitled and (b) to wind down the Companies. Even though the purpose of the conservatorship was to conserve and preserve the Companies' assets, Treasury has confirmed that winding down Freddie Mac and Fannie Mae was precisely its intent. On August 17, 2012, Treasury issued a press release that states the following, among other things:

The US Department of Treasury announced today a set of modifications to the Preferred Stock Purchase Agreements (PSPAs) between the Treasury Department and Federal Housing Finance Agency (FHFA) as conservator of Fannie Mae and Freddie Mac (the Government Sponsored Entities or GSEs) *that will help expedite the wind down of Fannie Mae and Freddie Mac*, make sure that every dollar of earnings each firm generates is used to benefit taxpayers . . .

\* \* \*

With today's announcement, we are taking the next step toward responsibly *winding down Fannie Mae and Freddie Mac* . . .

\* \* \*

The agreements will replace the 10 percent dividend payments made to Treasury on its preferred stock investments in Fannie Mae and Freddie Mac with a quarterly sweep of every dollar of profit that each firm earns going forward. This will help achieve several

important objectives, including . . . [a]cting upon the commitment made in the Administration’s 2011 White Paper *that the GSEs will be wound down and will not be allowed to retain profits, rebuild capital, and return to the market in their current form.*

100. Because the Net Worth Sweep—by Treasury’s own admission—is not designed to conserve and preserve Freddie Mac’s assets, it is fundamentally inconsistent with FHFA’s powers as conservator. As explained above, FHFA as conservator is authorized to act only as “(i) necessary to put the regulated entity in a *sound and solvent condition*, and (ii) appropriate to carry on the business of the regulated entity and *preserve and conserve the assets and property of the regulated entity.*” 12 U.S.C. § 4617(b)(2)(D) (emphasis added). Neither the Net Worth Sweep, nor any of the dividends paid thereunder, were intended to put Freddie Mac in a “sound and solvent condition” or to “preserve and conserve the assets and property of the regulated entity.” Instead, because of the Net Worth Sweep, Freddie Mac must operate at the edge of insolvency, making it fundamentally unsafe and unsound. By its very nature, the Net Worth Sweep is antithetical to FHFA’s mission as conservator.

101. Neither are the Net Worth Sweep nor the dividends paid thereunder consistent with Virginia’s corporate law, which controls Freddie Mac’s corporate governance and, by extension, FHFA’s actions as conservator and the Board’s exercise of authority delegated from FHFA. Under the VSCA, all of Freddie Mac’s “corporate powers shall be exercised by or under the authority of, and the business and affairs of the corporation managed under the direction of, its board of directors,” and a Director must act “in accordance with his good faith business judgment of the best interests of the corporation.” Va. Code Ann. §§ 13.1-673(B), -690(A).

102. The authority to declare dividends is specifically entrusted to the Board under the VSCA, the Corporation Act, and the PSPA. Whether the authority was exercised by the Board or

FHFA, the power to approve dividends under the Net Worth Sweep was not exercised in accordance with the fiduciary duties applicable to that authority.

103. FHFA and Treasury have both made clear that the Net Worth Sweep “ensures all [Freddie Mac’s] earnings are used to benefit taxpayers.” The declaration and payment of such dividends is plainly not action taken based on good faith business judgment of the best interests of the Company or its stockholders.<sup>6</sup>

104. The dividends under the Net Worth Sweep also are, or will soon become, a violation of Section 13.1-653 of the VSCA, which prohibits a corporation from issuing dividends if doing so would result in (i) the corporation becoming unable to pay its debts as due in the usual course business, or (ii) the corporation’s total assets becoming less than its total liabilities. Freddie Mac continues to pay billions of dollars in discretionary cash dividends to Treasury, while operating on the cusp of insolvency.

105. These actions also constitute breaches of contract. The Certificates of Designation for Mr. Pagliara’s preferred stock are contracts between Mr. Pagliara and Freddie Mac, contracts that incorporate the VSCA. The failure of the Company, under the direction of the Board (or FHFA exercising the power of the Board), to issue dividends and otherwise act in accordance with the VSCA breaches these contracts.

106. The Net Worth Sweep and the dividends paid thereunder also breach the implied covenants of good faith and fair dealing in the Certificates of Designation for Mr. Pagliara’s

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<sup>6</sup> Even crippled by the Net Worth Sweep, Freddie Mac has wasted assets on initiatives not intended to benefit Freddie Mac’s stockholders. In October 2013, Freddie Mac and Fannie Mae formed Common Securitization Solutions, LLC (“CSS”), a joint venture to develop and operate the Common Securitization Platform (the “CSP”). The CSP is intended to eventually replace elements of Freddie Mac’s and Fannie Mae’s separate, proprietary systems for securitizing mortgages and related back-office and administrative functions, as well as to ultimately provide a common platform for other market participants. From 2012 to mid-2015, Freddie Mac and Fannie Mae spent approximately \$146 million supporting CSS and the development of the CSP. Spending Freddie Mac’s assets on CSS and the CSP is not consistent with either the Board’s fiduciary duties or FHFA’s role as conservator. Instead, it is simply another example of Treasury colluding with FHFA, with the Board’s approval or acquiescence, to appropriate Freddie Mac’s assets to further their own policy agenda.

preferred stock because they defeat his reasonable expectations and deny him the benefits of his bargains. As a holder of preferred stock, Mr. Pagliara might have expected Freddie Mac to issue more senior preferred stock on market terms. Those terms might include some level of dividends and liquidation preferences that must be paid before his own. But he could never have anticipated that Freddie Mac, for no consideration whatsoever, would give the entire net worth of the Company to a senior class of preferred stock, which has inverted the Company's capital structure and eliminated the Company's ability to pay dividends on his, and all other, classes of stock.

107. The Net Worth Sweep and the dividends paid to Treasury thereunder constitute corporate waste, as Freddie Mac received no consideration whatsoever for the Third Amendment.

108. The Board, FHFA and Treasury have failed to respect the Company's separate corporate existence, as required under Virginia law. They have failed to respect the proper role of the Board and the rights of Freddie Mac's private stockholders. They have treated Freddie Mac's assets as assets of Treasury even though they are owned by private stockholders. And they have used Freddie Mac to pursue government policy objectives, without regard to the harm to Freddie Mac and its stockholders. In each case, this conduct can lead to substantial liability.

109. In addition to being a clear breach of the fiduciary duty of care, the Net Worth Sweep is a breach of the fiduciary duty of loyalty. The Board and FHFA, in exercising the statutory authority of Freddie Mac's Directors, owe Freddie Mac and its stockholders a duty of utmost good faith. Accordingly, the Board and FHFA may not approve the Company's participation in transactions where there is a conflict of interest, except where they can demonstrate that the transaction was entirely fair to the corporation. Here, the counterparty to,

and only beneficiary of, the Net Worth Sweep is Treasury, the controlling stockholder of Freddie Mac.

110. Treasury is the controlling stockholder of Freddie Mac by virtue of its Senior Preferred Stock, its liquidation preference on its Senior Preferred Stock, its warrants to purchase 79.9% of the Company's common stock, and the covenants and restrictions it imposed on Freddie Mac in the PSPA. Treasury has also proven openly and publicly its ability to control FHFA to do its bidding with respect to the Companies. Thus, the Net Worth Sweep and each payment of dividends thereunder is a conflict-of-interest transaction.

111. Treasury did not pay a fair price in exchange for the Net Worth Sweep, which was the end result of an unfair process dictated by Treasury and agreed to by the Board and/or FHFA. Indeed, the Company and its stockholders other than Treasury received no additional investments or value of *any* sort in exchange for the Net Worth Sweep. The government stood on both sides of the decision to implement the Net Worth Sweep, to the benefit of Treasury and the detriment of the Company and all other stockholders.

112. Neither the Net Worth Sweep nor the dividends thereunder are fair to Freddie Mac or its minority stockholders; to the contrary, they are entirely unfair to both Freddie Mac and its minority stockholders. They are a breach of the duty of loyalty by the Board and/or FHFA, and also by Treasury, which itself owes a duty of loyalty under Virginia law as a controlling stockholder in a conflict-of-interest transaction with the corporation.

113. The Net Worth Sweep and dividends paid thereunder also constitute oppression of the interests of the minority stockholders.

114. Based upon the statutory and fiduciary breaches described above, and given statutory restrictions on Treasury acquiring new securities in Freddie Mac, the Third Amendment

was void or voidable. A board breaches its fiduciary duties when it approves dividends on stock that is void or voidable.

**IX. FHFA Rejects Stockholder's Dividend Letter to the Board.**

115. To date, the Board's role in approving or acquiescing to the Net Worth Sweep and associated dividends has been clouded. Whether the Board has had an active role, or merely been supine, the Board has still breached its duties.

116. The Board breaches its duties not merely by action, but also through any conscious failure to act. The Board may not sit passively by while—quarter after quarter—the controlling stockholder takes the entire net worth of the Company.

117. The Board's fiduciary and statutory duties are unaffected by FHFA's directions that certain corporate actions by the Board must be approved by FHFA or Treasury. The Board is required to exercise its fiduciary duty in the best interest of the Company, regardless of whether its decision is ultimately subject to the approval of a controlling stockholder or other person.

118. The Directors may be held personally liable for these breaches. For example, a director who votes for or assents to a distribution made in violation of Virginia law is personally liable to the corporation. Va. Code Ann. § 13.1-692A. While the Company's Bylaws purport to limit the liability of Directors on claims brought by or in the name of the Company or its stockholders, *see* Bylaws § 8.1, neither the Bylaws nor the VSCA allows for the limitation of liability for willful misconduct. Directors who knowingly allow—quarter after quarter—all of the Company's net worth to go to Treasury are certainly risking exposure to claims of willful misconduct.

119. Seeking clarification of the Board's role, the Stockholder sent, along with his demand for inspection of corporate records, a January 19, 2016 letter urging that the Board:



Publicly clarify the Board's role in declaring and paying dividends to [Treasury] on account of its [Senior Preferred Stock] . . . ;

Publicly declare . . . that the Board does not agree with the declaration and payment of dividends to Treasury on account of the Senior Preferred Stock, and certainly not in amounts equal to *all* the profits of the Corporation; and

Exercise your authority under Virginia law to cause the Corporation to immediately stop declaring and paying dividends to Treasury on account of the Senior Preferred Stock.

A copy of this January 19, 2016 letter to the Board (the "Dividend Letter") is attached as Exhibit E hereto and incorporated herein.

120. The Board did not respond to the Dividend Letter; FHFA did. FHFA sent a January 28, 2016 letter in response to the Dividend Letter (and in response to the Stockholder's Demand for inspection of corporate records as described below). In that letter, FHFA asserted several remarkable positions:

[Freddie Mac's] boards of directors serve on behalf of, and exercise authority as directed by the Conservator. Because any fiduciary duties of this board of directors flow directly and exclusively to the Conservator, state law principles such as those you assert in your letter are simply not applicable here. . . . [P]ayments by Freddie Mac of dividends to the United States Treasury have been made pursuant to directives of the Conservator.

*See* Ex. B hereto (internal citations, quotation marks omitted).

121. So, according to FHFA: the Board serves entirely at FHFA's direction; the Board has no powers, and no commensurate duties, other than following the directives of FHFA; any fiduciary duties the Board has flow not to the Company and its stockholders, but rather "directly and exclusively" to FHFA; the VSCA and Virginia state law have no application; and Freddie Mac has paid the Net Worth Sweep dividends to Treasury because FHFA said so. In contrast to the ample authority cited in the Dividend Letter, FHFA makes these assertions in its response

without any legal support. Nor is there support for such preposterous positions. Whether the Board agrees with these positions is not known; the Board failed to respond to the Stockholder's Dividend Letter, which requested clarification of the Board's position on these issues.

**X. Stockholder's Inspection Demand and Its Rejection**

122. In order to, among other proper purposes, investigate the improper conduct described above and potential claims relating thereto, on January 19, 2016, Mr. Pagliara sent his Demand to Freddie Mac and its Board. As is his right under Section 13.1-771 of the VSCA, Mr. Pagliara requested in the Demand the opportunity to inspect certain specified corporate records during Freddie Mac's usual business hours. These documents include Board minutes and other Board materials and accounting records relating to, among other things, the approval of the Net Worth Sweep and issuance of dividends, the level of involvement of FHFA and Treasury in managing the Company, the solvency or insolvency of the Company at the time of each dividend payment under the Net Worth Sweep, and Freddie Mac's investment in CSS and CSP. The relevant time period for the Demand is a year before the Net Worth Sweep through the date of the Demand (August 17, 2011 through and including January 19, 2016).

123. As explained in detail in the Demand, the purposes of the inspection are, among other things, to investigate potential breaches of fiduciary and statutory duty by Directors and/or officers of Freddie Mac, and to investigate FHFA and/or Treasury's involvement in such breaches of duty and other claims the Company may have against the Board, FHFA, and/or Treasury, as well as claims Mr. Pagliara himself may have against the Company, the Board, FHFA, and Treasury. Given the facts alleged herein, there is no question that the investigation of these potential claims is a "proper purpose," as there is certainly a credible basis from which a court could infer that mismanagement, waste, wrongdoing and other breaches may have occurred.

124. Mr. Pagliara's purposes for the inspection as set forth in the Demand are reasonably related to his interests as a stockholder of Freddie Mac, and the records sought to be inspected are reasonably related to Mr. Pagliara's purposes.

125. The Board's failure to clarify its role and take the requested action in response to his Dividend Letter further underscores Mr. Pagliara's need for the requested records.

126. Neither Freddie Mac nor its Board responded to the Demand. Instead, on January 28, 2016, FHFA responded to the Demand at the same time it responded to the Dividend Letter. *See* Ex. B hereto.

127. FHFA rejected the Demand, asserting that the "rights, titles, powers, and privileges" to which the conservator succeeded under HERA include all stockholder inspection rights and that "so long as Freddie Mac remains in conservatorship [the Stockholder] has no basis upon which to demand inspection of Freddie Mac records." Conspicuously, FHFA's response to the Demand did not allege that the Demand failed to comply with the requirements of Section 13.1-771 in any way.

128. FHFA's reliance on HERA to reject the Demand is misplaced. The law is clear that the "rights, titles, powers, and privileges" succession provision to which FHFA refers prevents a shareholder only from bringing derivative claims on behalf of the corporation during the conservatorship, and even then, only in certain situations. It is no bar to direct claims—like this lawsuit—seeking to assert the shareholder's individual rights. Nor is it a bar even to derivative claims that challenge a transaction in which the conservator has a conflict of interest—like the Net Worth Sweep and the dividends declared thereunder. Thus, the provision is no bar to either Mr. Pagliara's Demand or claims that Mr. Pagliara seeks to investigate through the Demand.

**CLAIM FOR RELIEF**  
**(Order to Permit Inspection under Section 13.1-773)**

129. Stockholder repeats and realleges the foregoing paragraphs as if fully set forth herein.

130. Stockholder's Demand complies with all of the requirements under Section 13.1-771 of the VSCA concerning the form and manner for demanding inspection of corporate records.

131. Stockholder's Demand is made in good faith, and his purposes are proper under Virginia law.

132. Freddie Mac has refused the inspection requested in the Demand.

133. Under Section 13.1-773, Stockholder is entitled to an order directing Freddie Mac to permit Stockholder to inspect all of the documents in his Demand.

134. Section 13.1-773 further provides that this proceeding should be resolved on an expedited basis.

**WHEREFORE**, Stockholder prays for the following relief:

A. An order to permit the immediate inspection and copying of all documents set forth in the Demand.

B. An award of the Stockholder's costs, including reasonable counsel fees, as provided in Virginia Code Section 13.1-773, incurred to obtain the inspection.

C. Such other relief as the Court deems just and appropriate.

Respectfully submitted,

Timothy J. Pagliara

By: 

N. Thomas Connally (VSB No. 36318)  
Christopher T. Pickens (VSB No. 75307)  
HOGAN LOVELLS US LLP  
Park Place II  
7930 Jones Branch Drive, Ninth Floor  
McLean, VA 22102  
(703) 610-6100 (phone)  
(703) 610-6200 (fax)  
tom.connally@hoganlovells.com  
christopher.pickens@hoganlovells.com

*Counsel for Plaintiff Timothy J. Pagliara*

Dated: March 14, 2016

**EXHIBIT A**

**DEMAND**

**Hogan  
Lovells**

Hogan Lovells US LLP  
Park Place II  
Ninth Floor  
7930 Jones Branch Drive  
McLean, VA 22102  
T +1 703 610 6100  
F +1 703 610 6200  
www.hoganlovells.com

January 19, 2016

***BY EMAIL & CERTIFIED MAIL***

Federal Home Loan Mortgage Corporation  
Office of the Secretary of the Corporation  
8200 Jones Branch Drive MS 200  
McLean, Virginia 22102

Christopher S. Lynch, Non-Executive Chairman  
Raphael W. Bostic  
Carolyn H. Byrd  
Lance F. Drummond  
Thomas M. Goldstein  
Richard C. Hartnack  
Steven W. Kohlhagen  
Donald H. Layton  
Sara Mathew  
Saiyid T. Naqvi  
Nicolas P. Retsinas  
Eugene B. Shanks  
Anthony A. Williams

Board of Directors  
c/o Corporate Secretary  
Freddie Mac  
8200 Jones Branch Drive MS 200  
McLean, Virginia 22102  
boardofdirectors@freddiemac.com

**RE: Demand for Inspection of Books and Records under Virginia Code  
Section 13.1-771**

Dear Federal Home Loan Mortgage Corporation and Ladies and Gentlemen of the Board:

We represent Timothy J. Pagliara (the "Stockholder"), the beneficial owner of stock in the Federal Home Loan Mortgage Corporation ("Freddie Mac" or the "Company"). This letter is the Stockholder's demand to inspect the books and records of the Company under the Virginia

Stock Corporation Act (the "VSCA"), specifically Virginia Code Section 13.1-771 (the "Demand").<sup>1</sup> A notarized and sworn statement appointing the undersigned to act on the Stockholder's behalf is attached hereto as Exhibit 1. Verified documentary evidence of the Stockholder's beneficial ownership is attached as Exhibit A to Exhibit 1 hereto, and such documentary evidence is a true and correct copy of what it purports to be.

**I. Books and Records to be Inspected**

Under Section 13.1-771 of the VSCA, the Stockholder hereby demands that the Company provide the Stockholder, along with the attorneys, representatives, and agents of the Stockholder, designated through the enclosed notarized and sworn statement, the opportunity to inspect the following books and records during the Company's usual business hours, and to make copies and extracts therefrom. The relevant time period for this Demand is from August 17, 2011, through and including the date of the Demand (the "Relevant Time Period"). The information subject to the Demand includes:

- (1) All Board Materials concerning the Third Amendment to Amended and Restated Senior Preferred Stock Purchase Agreement, dated August 17, 2012 (the "Net Worth Sweep"), between the United States Department of the Treasury ("Treasury") and the Company, acting through the Federal Housing Finance Agency ("FHFA") as conservator.<sup>2</sup>
- (2) All Board Materials concerning the involvement of FHFA and/or Treasury in the management of the business and affairs of the Company and the respective roles

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<sup>1</sup> Freddie Mac's Bylaws, amended and restated on July 13, 2015, designate that the VSCA controls for purposes of Freddie Mac's corporate governance practices and procedures. Freddie Mac Bylaws, § 11.3(a).

<sup>2</sup> For purposes of this Demand, the term "Board Materials" means (a) minutes of any meeting, including meetings held in person, telephonically, electronically, or via any other means, (including draft minutes and draft or proposed consents or resolutions) of the Company's board of directors or any committee thereof, (b) meeting agendas for any meeting of the Company's board of directors or any committee thereof, (c) written consents or other written resolutions adopted by the Company's board of directors or any committee thereof, (d) presentations, reports, summaries, analyses, exhibits and other written materials reviewed, considered, provided to, or prepared for the board of directors or any committee thereof in connection with any meeting, written consent, or written resolution, (e) notes or summaries of any meeting (or portion of any meeting) of the Company's board of directors or any committee thereof, and (f) any communications, recommendations or proposals with or to stockholders of the Company in connection with any consents or resolutions adopted by the Board of Directors or any committee thereof.



and responsibilities of FHFA, Treasury, and the Board of Directors of the Company (the "Board" or the "Board of Directors"), including but not limited to:

- a) All Board Materials concerning FHFA's and/or Treasury's approval of Company business decisions, transactions, policies, and/or other matters; and
  - b) All Board Materials concerning FHFA's and/or Treasury's directives and/or instructions to the Company, including "alignment directives," "letters of instruction," "advisory bulletins," and/or "external communication standards."
- (3) All FHFA and/or Treasury directives and/or instructions to the Company, including but not limited to "alignment directives," "letters of instruction," "advisory bulletins," and/or "external communication standards."
  - (4) All Board Materials concerning the declaration and/or payment of dividends to Treasury (as the holder of the Company's senior preferred stock), including but not limited to Board Materials concerning or analyzing the availability of surplus or any other lawful source for payment of any such dividend pursuant to Section 13.1-653 of the VSCA.
  - (5) All Board Materials concerning the declaration and/or payment of dividends pursuant to the Net Worth Sweep, including but not limited to Board Materials concerning or analyzing any lawful source for payment of any such dividend pursuant to Section 13.1-653 of the VSCA.
  - (6) All Board Materials concerning any report, analysis, or evaluation of the solvency or insolvency of the Company.
  - (7) Accounting records sufficient to show the net worth of the Company immediately before and after the payment of the Net Worth Sweep to Treasury for each quarter from August 17, 2012, through the present.
  - (8) Accounting records sufficient to show the aggregate par value of the issued and outstanding shares of all classes of capital stock of the Company at the times of each payment of the Net Worth Sweep from August 17, 2012, through the present.
  - (9) All Board Materials pertaining to the Company's outstanding public securities, shareholders, and debtholders, including but not limited to the conduct of the conservatorship as administered by FHFA and/or Treasury, and the impact of decisions made by FHFA and/or Treasury on the Company's outstanding public securities, shareholders and debtholders.
  - (10) All Board Materials concerning the Company's investment in Common Securitization Solutions, LLC ("CSS") or the Common Securitization Platform

(the "CSP"), whether directly or indirectly, all contracts entered into by the Company regarding CSS or the CSP, all directives, instructions, or other documents received by the Company from FHFA, Treasury, any other Executive Branch personnel (including at the White House), or Legislative Branch personnel relating to the creation and implementation of either CSS or the CSP, and any formal business plans developed by the Company with respect to its investments in CSS or the CSP.

- (11) All policies, handbooks, rules, directives, instructions, procedures, or other documents concerning FHFA's and/or Treasury's oversight of the Company's public statements, including the subject matter or content of speeches, interviews, press releases, congressional testimony, and/or the Company's website.
- (12) A list of stockholders and a stock ledger.
- (13) Books and records sufficient to show whether the Company's directors have been elected by written consent in lieu of an annual meeting in the past 13 months.
- (14) Books and records sufficient to show any directors and officers insurance policies maintained for the benefit or protection of the Company's directors.

## **II. Purposes of the Demand**

The purposes of the Demand are:

- (a) to investigate potential breaches of fiduciary duty by directors and/or officers of the Company, by FHFA, and/or by Treasury in connection with the matters discussed below;
- (b) to investigate FHFA's and/or Treasury's aiding and abetting breaches of fiduciary duty by directors and/or officers of the Company in connection with the matters discussed below;
- (c) to investigate mismanagement, waste, wrongdoing, and/or violations of law by directors and/or officers of the Company, by FHFA, and/or by Treasury in connection with the matters discussed below;
- (d) to determine the respective roles and responsibilities of FHFA and the Board of Directors in the management of the business and affairs of the Company;
- (e) to determine whether FHFA and/or the Board of Directors has improperly disregarded the corporate form of the Company and/or applicable statutes relating to the duties and responsibilities of the Board of Directors of the Company;

- (f) to determine the Company's position as to the rights of the Company's stockholders (other than Treasury);
- (g) to determine whether dividends have been declared and/or paid by the Company's Board of Directors in accordance with Virginia law;
- (h) to determine whether the Company had a lawful source out of which dividends lawfully could be declared and paid at the time of the declaration and payment of dividends pursuant to the Net Worth Sweep for each quarter from August 17, 2012 through the present, and whether the Company's directors could be personally liable for the payment of unlawful dividends under Section 13.1-692 of the VSCA;
- (i) to determine whether payments made pursuant to the Net Worth Sweep constitute a fraudulent conveyance or fraudulent transfer under applicable law;
- (j) to determine the Company's financial safety and soundness and overall risk management practices, and whether FHFA and/or the Board of Directors is ensuring that the Company operates in a safe and sound manner;
- (k) to determine the extent of independence and disinterestedness of the Board of Directors, and whether the Board has acted in good faith and consistent with its duty of loyalty to the Company, in connection with the matters described herein to determine, among other matters, whether a pre-suit demand is necessary or would be excused prior to commencing any derivative action on behalf of the Company;
- (l) to communicate with other Company stockholders regarding matters of concern to such stockholders; and
- (m) to value the stock held by the Stockholder.

### III. The Statutory and Fiduciary Duties of the Board

As you know, Freddie Mac is a federally chartered corporation established pursuant to the Federal Home Loan Mortgage Corporation Act (the "Corporation Act"), and owned by private stockholders, including the Stockholder. The Corporation Act created "a body corporate under the direction of a Board of Directors." 12 U.S.C. § 1452(a)(1); *see also* Freddie Mac Bylaws § 4.1. Under Freddie Mac's Bylaws, Virginia law is the law of decision governing Freddie Mac's "corporate governance practices and procedures." Freddie Mac Bylaws § 11.3.

Under this applicable Virginia law, the Board owes fiduciary duties to Freddie Mac and its stockholders and is therefore required to act in the best interests of Freddie Mac and its stockholders. *See* Va. Code Ann. § 13.1-690; *see also* *Byelick v. Vivadelli*, 79 F. Supp. 2d 610, 623 (E.D. Va. 1999) ("It is well-settled that '[a] Virginia corporation's directors and officers owe a duty of loyalty both to the corporation and to the corporation's shareholders'") (citations omitted). Under Virginia law, the Board also must comply with the VSCA. *See, e.g., Malon v.*

*Franklin Fin. Corp.*, No. 3:14CV671-HEH, 2014 WL 6791611, at \*4, n.4 (E.D. Va. Dec. 2, 2014) (“The decision-making process of the Franklin Board is governed by the Virginia Stock Corporation Act.”).

The Board continues to owe these fiduciary and statutory duties despite and irrespective of FHFA’s conservatorship. The Housing and Economic Recovery Act of 2008 (“HERA”) did not eliminate or alter these duties.<sup>3</sup> Although, under HERA, FHFA succeeded to the rights of Freddie Mac’s stockholders, this did not eliminate the Board’s duties.<sup>4</sup> Under the governing law, the stockholders did not even possess the power to eliminate the Board’s duties.

The Board’s statutory and fiduciary duties are similarly unaffected by FHFA’s directions that certain corporate actions by the Board must be approved by FHFA or Treasury. The Board is required to exercise its fiduciary duty in the best interest of the corporation, regardless of whether its decision is ultimately subject to the approval of a controlling stockholder or other person.<sup>5</sup> The Board’s fiduciary duties may never be delegated away from the Board. Under Virginia law, “the unbending rule is that the director must act in the utmost good faith, and this

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<sup>3</sup> HERA provides Freddie Mac’s Board of Directors with immunity from liability only for the decision to consent to the appointment of a conservator. *See* 12 U.S.C.A. § 4617 (“The members of the board of directors of a regulated entity shall not be liable to the shareholders or creditors of the regulated entity for acquiescing in or consenting in good faith to the appointment of the Agency as conservator or receiver for that regulated entity.”)

<sup>4</sup> Virginia courts have cited with approval 8 Del. C. Section 102(b)(7), which restricts opportunities for eliminating or limiting personal liability of directors to the corporation or its stockholders. *See* 8 Del. C. § 102(b)(7) (mandating that certificates of incorporation “shall not eliminate or limit the liability of a director: (i) [f]or any breach of the director’s duty of loyalty to the corporation or its stockholders; (ii) [f]or acts or omissions not in good faith or which involve intentional misconduct or a knowing violation of law; (iii) under § 174 of this title [for unlawful payment of divided or unlawful stock purchase or redemption]; or (iv) for any transaction from which the director derived an improper personal benefit”); *see also Williams v. 5300 Columbia Pike Corp.*, 891 F. Supp. 1169, 1183, n.30 (E.D. Va. 1995) (“a by-law amendment surely cannot eliminate directors’ fiduciary duty of loyalty and fairness to shareholders”) (citing 8 Del. C. § 102(b)). The applicable law is inflexible with respect to the imposition of these fiduciary duties on all directors.

<sup>5</sup> *See, e.g., Freddie Mac Current Report on Form 10-K/A*, 5 (for fiscal year ended December 31, 2008) (“The Conservator has instructed the Board that it should consult with and obtain the approval of the Conservator before taking action in . . . actions involving capital stock, dividends, the senior preferred stock purchase agreement, or the Purchase Agreement, between [Freddie Mac] and the U.S. Department of the Treasury, or Treasury, increases in risk limits, material changes in accounting policy, and reasonably foreseeable material increases in operational risk . . .”).

good faith forbids placing himself in a position where his individual interest clashes with his duty to his corporation.” *Mardel Sec., Inc. v. Alexandria Gazette Corp.*, 183 F. Supp. 7, 14-15 (E.D. Va. 1960) *aff’d*, 320 F.2d 890 (4th Cir. 1963); *see also In re Adams Labs., Inc.*, 3 B.R. 495, 497-98 (Bankr. E.D. Va. 1980) (“A director’s fiduciary duty to a corporation has been likened to a position of trust . . . [a director] must conduct himself with the utmost fidelity . . .”). The Board of Freddie Mac continues to owe all the statutory and fiduciary duties provided by Virginia law. Those fiduciary duties require the Board to act to protect the stockholders’ interests to the full extent of its power, no matter how constrained that may be.

For the above reasons, any claim asserting that the Board owes fiduciary duties only to FHFA is mistaken, and the Board may not rely upon the assertion. *See, e.g., Smith v. Van Gorkom*, 488 A.2d 858, 888 (Del. 1985) (holding that the trial court “erred in according to the [director] defendants the benefits of the business judgment rule” where “the Board was mistaken as a matter of law regarding its available courses of action” under 8 Del. C. § 251(b) with respect to a merger).

The Board remains exposed to liability on claims for breaches of statutory and fiduciary duties. The statutory prohibition on court actions that restrict or affect the conservator’s powers and functions do not bar claims that (a) challenge conduct inconsistent with the conservatorship, (b) seek monetary relief, or (c) are asserted against the Board.<sup>6</sup> Nor does it or any other portion of HERA bar stockholders from asserting claims for decisions or omissions in which FHFA and/or Treasury have a conflict of interest.<sup>7</sup> Finally, to the extent that any claim might possibly be barred by HERA, the bar would cease upon termination of the conservatorship, with the result that the members of the Board would then be newly exposed to liability for breaches that took place *during* the conservatorship.<sup>8</sup> And while the Company’s Bylaws purport to limit the

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<sup>6</sup> *See* 12 U.S.C. § 4617(f) (“Except as provided in this section or at the request of the Director [of FHFA], no court may take any action to restrain or affect the exercise of powers or functions of [FHFA] as a conservator or a receiver.”).

<sup>7</sup> *See Kellmer v. Raines*, 674 F.3d 848, 850 (D.C. Cir. 2012) (explaining that, if a “manifest conflict of interest by the conservator” had been at issue, HERA would not bar shareholder derivative actions); *First Hartford Sav. Corp. Pension Plan & Trust v. United States*, 194 F.3d 1279, 1295 (Fed. Cir. 1999) (holding, where FDIC’s statutory receivership authority includes the right to control prosecution of legal claims on behalf of bank under FDIC receivership, that FDIC could not prohibit a shareholder of the bank under receivership from bringing a derivative suit alleging breach by FDIC of a contract between the government and the bank under receivership, because FDIC had a conflict of interest when it “was asked to decide on behalf of the [bank] in receivership whether it should sue the federal government based upon breach of contract, which, if proven, was caused by the FDIC itself”).

<sup>8</sup> Debate in Congress recently confirmed, in connection with approving the Consolidated Appropriations Act, 2016 – Section 702, that the conservatorship has a finite duration, regardless of the Third Amendment and other developments. In discussing provisions in the Consolidated

liability of directors on claims brought by or in the name of the Company or its shareholders, *see* Bylaws § 8.1, neither the Bylaws nor the VSCA allows for the limitation of liability for willful misconduct. Directors who knowingly abdicate their corporate responsibility and allow—quarter after quarter—all of the Company’s profits to go to Treasury are certainly risking exposure to claims of willful misconduct.<sup>9</sup>

#### IV. Breaches of the VSCA and Fiduciary Duties

As detailed below, the Stockholder has a credible basis to believe that the Board of Directors has breached and continues to breach its statutory and fiduciary duties to Freddie Mac and its stockholders, aided and abetted by FHFA and Treasury. The Stockholder also has a credible basis to believe that FHFA and Treasury have also violated statutory and fiduciary duties owed to the Company and its stockholders.

**Section 13.1-690.** The VSCA requires that “[a]ll corporate powers shall be exercised by or under the authority of, and the business and affairs of the corporation managed under the direction of, its board of directors[.]” Va. Code Ann. § 13.1-673B. Likewise, the Corporation Act created “a body corporate under the direction of a Board of Directors.” 12 U.S.C. § 1452(a)(1). Section 4.1 of the Freddie Mac Bylaws, as amended and restated on July 13, 2015, provides: “[s]ubject to the limitations of law and regulation, the Board of Directors shall determine the general policies that govern the operations of the Corporation, and the Corporation shall be under the Direction of the Board of Directors.”<sup>10</sup>

The VSCA provides the general standards of conduct for the Board of Directors. Va. Code Ann. § 13.1-690. The VSCA’s primary command to directors is simple: “[a] director shall

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Appropriations Act concerning Treasury’s preferred stock, Senator Minority Leader Harry Reid noted that “As then-Secretary Paulson described, conservatorship was meant to be a ‘time out’ not an indefinite state of being.” Banking Committee Ranking Member Senator Sherrod Brown then added: “. . . the FHFA and Treasury Department could have placed the GSEs into receivership if the intent was to liquidate them. The purpose of a conservatorship is to preserve and conserve the assets of the entities in conservatorship until they are in a safe and solvent condition as determined by their regulator.”

<sup>9</sup> Furthermore, the members of the Board cannot knowingly abdicate their fiduciary duties and point to the conservator as the culpable actor. *Colgate v. Disthene Grp., Inc.*, 86 Va. Cir. 218 (Buckingham County Cir. Ct. 2013) (“lack of action” may be actionable under Section 13.1-690); Allen C. Goolsby & Steven M. Haas, *Goolsby & Haas on Virginia Corporations* § 9.7 (director liability under Virginia law “applies not just to actions taken by the directors, but also to any conscious failure to act”).

<sup>10</sup> Section 4.1 is designated as a Level 1 Provision and thereby deemed to constitute a provision of the Company’s articles of incorporation for purposes of the VSCA. Freddie Mac Bylaws § 11.3(b).

discharge his duties as a director, including his duties as a member of a committee, in accordance with his good faith business judgment of the best interests of the corporation.” *Id.*

Virginia law, as incorporated into federal law, also governs the Board’s ability to declare and pay dividends. Under Virginia law, dividends are voluntary; declaration and payment of dividends is entrusted to the Board’s discretion. *See* Va. Code Ann. § 13.1-653A (“A board of directors *may* authorize and the corporation may make distributions to its shareholders . . .”) (emphasis added). Likewise, the Corporation Act states that Freddie Mac may make capital distributions, “as may be declared by the Board of Directors.” 12 U.S.C. § 1452(b)(1). Consistent with these statutes, Treasury’s Amended and Restated Senior Preferred Stock Certificate, executed after the Freddie Mac Board was reconstituted by FHFA, states that holders of such stock are only entitled to cash dividend payments “when, as and if declared by the Board of Directors, in its sole discretion, out of funds legally available therefor.” Freddie Mac Amended and Restated Senior Preferred Stock Certificate of Designation ¶ 2(a). In exercising its discretion to declare and pay dividends, as in all its actions, the Board must follow its good faith business judgment of the best interests of the Company.

Notwithstanding these provisions, in 2012 FHFA and Treasury entered into the Net Worth Sweep, providing for the quarterly distribution, in perpetuity, of ultimately all of the net worth of Freddie Mac to Treasury. FHFA and Treasury have both made clear that the Net Worth Sweep “ensures all [Freddie Mac’s] earnings are used to benefit taxpayers.”<sup>11</sup> The declaration and payment of such dividends is plainly not action taken based on good faith business judgment of the best interests of the Company or its shareholders.

**Section 13.1-653.** By approving the Net Worth Sweep, the Board appears to have permitted an inevitable breach of Section 13.1-653 of the VSCA. Under that section, distributions to shareholders cannot be properly authorized if the distribution would result (i) in the corporation becoming unable to pay its debts as due in the usual course of business, or (ii) in the corporation’s total assets becoming less than its total liabilities plus the amount needed to satisfy certain shareholders’ preferential rights. Va. Code Ann. § 13.1-653C. Freddie Mac has paid out, and continues to pay out, billions of dollars in discretionary cash dividends to Treasury under this Board’s administration. At the same time, the contractual restraints on capital preservation imposed by the Senior Preferred Stock have left the Company teetering perilously on the edge of insolvency.

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<sup>11</sup> Federal Housing Finance Agency, Conservatorship, “Senior Preferred Stock Purchase Agreements,” available at <http://www.fhfa.gov/Conservatorship/Pages/Senior-Preferred-Stock-Purchase-Agreements.aspx>; *see also* U.S. Dep’t of the Treasury, Press Release, “Treasury Department Announces Further Steps to Expedite Wind Down of Fannie Mae and Freddie Mac,” (Aug. 17, 2012), available at <https://www.treasury.gov/press-center/press-releases/Pages/tg1684.aspx> (Net Worth Sweep will “make sure that every dollar of earnings [Freddie Mac] generates is used to benefit taxpayers”).

The Net Worth Sweep may already violate Section 13.1-653 of the VSCA—and certainly will violate Section 13.1-653 once the “Applicable Capital Reserve Amount” is reduced to zero beginning on January 1, 2018—because it contemplates payment of dividends to Treasury beyond the restrictions imposed by that section, that is, payment of dividends out of the Company’s capital. Stated another way, pursuant to the Net Worth Sweep, the “Dividend Amount” comprises the entire net worth of the Companies—i.e., total assets less total liabilities—plus a decreasing reserve amount. When the decreasing reserve amount is lower than the Company’s capital, the Net Worth Sweep appears to contemplate the distribution of the Company’s capital in the form of dividends. Because the Net Worth Sweep improperly authorizes payment of dividends, it violates Section 13.1-653 of the VSCA.

Courts applying Virginia law have affirmed that directors may be held personally liable for authorizing a distribution under such circumstances. *See, e.g., In re Heilig-Meyers Co.*, 328 B.R. 471, 489 (E.D. Va. 2005) (citing to Section 13.1-653C of the VSCA) (“Virginia law prohibits a corporation from paying a dividend while insolvent or if the dividend would cause insolvency”).

**Breach of the Duty of Loyalty from the Company’s Investments in CSS/CSP.** The Board also appears to have violated its fiduciary duty of loyalty by approving or permitting the Company’s investments in CSS and the CSP and pursuit of the single security.

In October 2013 the Company and the Federal National Mortgage Association (“Fannie Mae”) established CSS, a jointly owned limited liability company, to develop and eventually operate the CSP. Federal Housing Finance Agency, *An Update on the Common Securitization Platform* (Sept. 15, 2015), at 6. The CSP is intended to eventually replace certain elements of Fannie Mae and Freddie Mac’s separate and proprietary systems for securitizing mortgages and related associated back office and administrative functions, as well as to ultimately provide a common platform for other market participants. Fannie Mae Fiscal Year 2014 Form 10-K, at 30. According to FHFA, “[i]nvesting in a single platform to support single-family securitization and the Single Security will benefit *both* Enterprises and taxpayers in the long run” (emphasis added).<sup>12</sup> Moreover, the Company has pursued the single security, which will ultimately replace the Company’s securitization and tie the Company’s financial future to the fortunes of Fannie Mae. Development of the single security “is supportive of the [FHFA’s] statutory obligation to ensure the liquidity of the nation’s housing finance markets.” Federal Housing Finance Agency, *An Update on the Common Securitization Platform* (May 15, 2015), at 1.

Improving the value and profit of the Company, the necessary goal of this Board’s management of the Company, is not identified as a goal of CSS, the CSP, or the single security. The Board would breach its fiduciary duty of loyalty, and could be held personally liable for doing so, if its approval of the Company’s investments in CSS, the CSP, and the single security

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<sup>12</sup> Federal Housing Finance Agency, Policy, Common Securitization Platform, available at <http://www.fhfa.gov/PolicyProgramsResearch/Policy/Pages/Securitization-Infrastructure.aspx>.



was given for the purpose of furthering FHFA's policy objectives rather than to further the Company's interests.

Further, if the Board's deliberation process included consideration of the CSP's benefit to both Fannie Mae and Freddie Mac, that deliberation process would violate the Board's duty of loyalty. The Board owes no fiduciary duties to Fannie Mae or Fannie Mae shareholders. The Board's duty of loyalty runs solely to Freddie Mac and its shareholders. Consideration of the manner in which "both Enterprises" would benefit from the CSP violates that duty of loyalty.

**Waste from the Net Worth Sweep.** By approving the Net Worth Sweep, and the dividends paid to Treasury pursuant to the Net Worth Sweep, the Board appears to have violated its fiduciary duty not to permit corporate waste. Corporate waste occurs where "the consideration received by the corporation was so inadequate that no person of ordinary sound business judgment" would have approved the transaction. *In re Capital One Derivative S'holder Litig.*, 952 F. Supp. 2d 770, 782 (E.D. Va. 2013) (citing to Delaware law); *see also Giannotti v. Hamway*, 239 Va. 14, 25, 387 S.E.2d 725, 731 (1990) (referencing "abundant, credible evidence . . . that defendants engaged in oppressive conduct and that they misapplied and wasted corporate assets" and finding that "the burden of proof lies upon the persons who fill the position of trust and confidence to show that the transaction has been fair") (citation omitted).

The Company received *no additional consideration whatsoever* in exchange for the Net Worth Sweep, pursuant to which the Company has paid more than *\$70 billion* to Treasury. No business person of ordinary, sound judgment could possibly have concluded that the Company received adequate consideration for this massive expropriation of economic value from the Company to Treasury. As such, the Company's directors appear responsible for corporate waste.

**Unfair, Self-Dealing Transaction with Controlling Stockholder.** Treasury and the Board appear to have breached fiduciary duties in the Net Worth Sweep and the dividends paid pursuant to the Net Worth Sweep because they are unfair transactions with Freddie Mac's controlling stockholder. Treasury is the controlling stockholder of Freddie Mac because it exercises control over the Company and its Board of Directors independently and through FHFA.

As a controlling stockholder of Freddie Mac, Treasury owed a fiduciary duty of entire fairness to the Company and its minority stockholders, including a duty to exercise good faith and care and a duty to deal fairly. *Parsch v. Massey*, 79 Va. Cir. 446 (City of Charlottesville Cir. Ct. 2009), citing *Brown v. Scott County Tobacco Warehouses*, 5 Va. Cir. 75 (Scott County Cir. Ct. 1983) ("Dominant or controlling shareholders also owe minority shareholders fiduciary duties . . . [they] must exercise good faith and care . . . Any disposition of the corporation or its assets to deprive the minority holders of their just share of it or to gain for themselves at the expense of the holders of the minority of the stock *is* a breach of their duties and of trust") (emphasis in original).

Treasury did not pay a fair price in exchange for the Net Worth Sweep, which was the end result of an unfair process dictated by Treasury and agreed to by the Board. Indeed, the Company and its stockholders other than Treasury received no additional investments or value of any sort in exchange for entering into the Net Worth Sweep. Through its absolute control, the government effectively stood on both sides of the decision to implement the Net Worth Sweep, to the benefit of Treasury and the detriment of the Company and all other shareholders. The Net Worth Sweep therefore constituted an unfair, self-dealing transaction with Freddie Mac's controlling stockholder. As such, Treasury and the Board breached their fiduciary duties to the Company and to shareholders other than Treasury in implementing the Net Worth Sweep. FHFA may also be liable, at least for aiding and abetting these breaches of fiduciary duty.

**Unlawful Disregard of Corporate Form.** The Board, FHFA and Treasury have failed to respect the Company's separate corporate existence, as required under Virginia law. *See Federico v. Lincoln Military Hous., LLC*, No. 2:12CV596, 2015 WL 5123324, at \*22 (E.D. Va. Aug. 31, 2015) (noting that, generally, "[a] corporation is a 'legal entity separate and distinct from the stockholders or members who compose it'" (citation omitted)). As summarized above, it appears that they have failed to respect the proper role of the Freddie Mac Board and the rights of Freddie Mac's stockholders, have treated Freddie Mac's assets as assets of Treasury and have used Freddie Mac to pursue government policy objectives, without regard to the harm to Freddie Mac. In each case, this conduct can lead to substantial liability for the Company's directors. *See id.* ("a court may in some circumstances disregard the corporate entity and place liability directly on the members . . ."). The Stockholder requires access to the books and records of the Company to investigate this apparent breach of fiduciary duty, as well as to investigate the other apparent breaches described above.

\* \* \*

For purposes of the Demand, the Stockholder requests that the Company provide or otherwise make available all such information as soon as practically possible. In addition, the Stockholder further requests that the Company provide or otherwise make available all additions, changes, and corrections to any of the requested information from the time of this Demand to the time of any inspection.

We believe that this Demand complies with the provisions of Section 13.1-771 in all material respects. If the Company believes otherwise, we request that you contact the undersigned immediately in writing. Such correspondence shall set forth the facts that the Company contends support its position, and shall specify, as appropriate, any additional information believed to be required, so that any purported deficiencies may be addressed promptly. Under Section 13.1-771, if the Company does not respond to this Demand within five business days of the date hereof, the Stockholder will be entitled to seek appropriate relief. In any event, we look forward to discussing this Demand with you (or your counsel) at your earliest convenience.

Federal Home Loan Mortgage Corporation  
Books and Records Demand  
January 19, 2016

We look forward to your response.

Sincerely,

A handwritten signature in black ink, appearing to be 'N. Thomas Connally, III', written over a horizontal line.

N. Thomas Connally, III

Partner  
tom.connally@hoganlovells.com  
D +1 703 610 6126

Enclosure

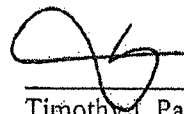
cc: Timothy J. Pagliara

**DECLARATION OF TIMOTHY J. PAGLIARA**

1. I am over the age of 18 years old and competent to testify to the following facts, of which I have personal knowledge.
2. I submit this Declaration in support of my Demand for Inspection of Books and Records of the Federal Home Loan Mortgage Corporation under Virginia Code Section 13.1-771 (the "Books and Records Demand").
3. A true and correct copy of a 2015 brokerage account statement reflecting my beneficial ownership of stock in the Federal Home Loan Mortgage Corporation is attached hereto as Exhibit A.
4. I hereby appoint N. Thomas Connally, III and the law firm of Hogan Lovells US LLP as my true and lawful attorney, with full power and authority hereby conferred, to do and perform all acts in connection with my Books and Records Demand.

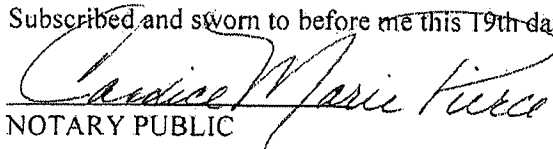
I hereby declare, under the penalty of perjury, that the foregoing is true and correct to the best of my knowledge, information, and belief.

Executed this 19th day of January, 2016.

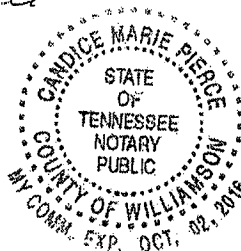


\_\_\_\_\_  
Timothy J. Pagliara

Subscribed and sworn to before me this 19th day of January, 2016.

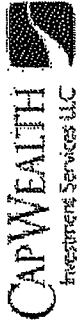
  
NOTARY PUBLIC

My Commission Expires 10-2-2016



STERNE AGEE & LEACH INC C/F  
TIMOTHY J PAGLIARA SEP IRA

FINANCIAL ADVISOR:  
TIMOTHY J PAGLIARA



**TIMOTHY J PAGLIARA SEP IRA**      **ACCOUNT NUMBER**  
**INVESTMENT ACCOUNT**      **Statement Period: 12/01/15 to 12/31/15**

STERNE AGEE

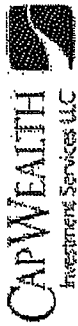
STERNE AGEE & LEACH INC C/F  
TIMOTHY J PAGLIARA SEP IRA

**TOTAL ACCOUNT VALUES**

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STERNE AGEE & LEACH INC C/F  
TIMOTHY J PAGLIARA SEP IRA

FINANCIAL ADVISOR:  
TIMOTHY J PAGLIARA



**TIMOTHY J PAGLIARA SEP IRA**  
**INVESTMENT ACCOUNT SUMMARY**

Statement Period: 12/01/15 to 12/31/15

This Period

CASH ACTIVITY

Prior Month

This Month

ASSET SUMMARY

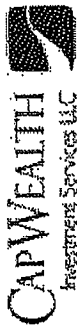
Cash or Cash Alternatives  
Equities  
Options  
Fixed Income Securities  
Total Invested Assets  
Less Debit Balance  
Total Account Value  
Total Combined Value

EARNINGS SUMMARY

Money Fund Earnings  
Dividends  
Total Income

Year-to-Date

This Period



STERNE AGEE & LEACH INC C/F  
TIMOTHY J PAGLIARA SEP IRA

SEP-IRA



**TIMOTHY J PAGLIARA SEP IRA**  
**SEP-IRA**

Statement Period: 12/01/15 to 12/31/15

This Month                      Current Year                      Prior Year

Distributions  
**IMPORTANT INFORMATION ABOUT YOU**

Under Securities and Exchange Rule 17a-3 Books and Records Requirements, the following information \* must be presented for your review. Your Broker Dealer makes investment recommendations or suitability determinations based in part on the financial information shown below originally obtained from you upon the occasion of opening your account or through adjustments as directed by you. Please review this data and if you find inaccuracies or incomplete information please call the branch office serving your account indicated on the first page of this statement.

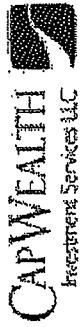
\* To prevent possible improper use of certain information (identify theft) we have omitted your social security/tax identification number as well as date of birth as shown on our records.

**MESSAGES**

Special Notice:

A copy of the full balance sheet of Sterne, Agee & Leach, Inc., is available at no cost by accessing the web site [www.sterneagee.com](http://www.sterneagee.com) or





STERNE AGEE & LEACH INC C/F  
TIMOTHY J PAGLIARA SEP IRA

SEP-IRA



PAGE 5 of 12

TIMOTHY J PAGLIARA SEP IRA

Statement Period: 12/01/15 to 12/31/15

SEP-IRA

MESSAGES

calling the following toll free number:

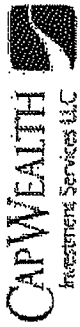
1-800-778-6257

Net Capital at September 30, 2015: \$36,333,821

Required Net Capital at September 30, 2015: \$3,285,489







STERNE AGEE & LEACH INC O/F  
TIMOTHY J PAGLIARA SEP IRA

SEP-IRA



**ACCOUNT NUMBER**

Statement Period: 12/01/15 to 12/31/15

**PORTFOLIO HOLDINGS - EQUITIES**

**Preferred Stock**

Total Shares	Description	Symbol	Price	Current Value	Est. Annual Income	Shares Purchased	Unit Cost	Cost Basis	Unrealized Gain/Loss
173,300	FEDL HOME LOAN MTC CORP SER X 6.02% PFD	FMGKL	2.65	459,245.00		173,300	0.947	164,245.00	295,000.00

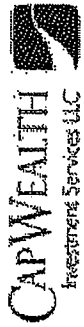
Total Preferred Stock

Percentage of Total Equities

Percentage of Total Invested Assets

**PORTFOLIO HOLDINGS - OPTIONS**

Total Contracts	Description	Underlying Symbol	Price	Current Value	Est. Annual Income	Contracts Purchased	Unit Cost	Cost Basis	Unrealized Gain/Loss
-----------------	-------------	-------------------	-------	---------------	--------------------	---------------------	-----------	------------	----------------------



STERNE AGEE & LEACH INC C/F  
TIMOTHY J PAGLIARA SEP IRA

SEP-IRA



**ACCOUNT NUMBER**

Statement Period: 12/01/15 to 12/31/15

**PORTFOLIO HOLDINGS - OPTIONS**

Total Contracts	Description	Underlying Symbol	Price	Current Value	Est. Annual Income	Contracts Purchased	Unit Cost	Cost Basis	Unrealized Gain/Loss
-----------------	-------------	-------------------	-------	---------------	--------------------	---------------------	-----------	------------	----------------------

Total Options

Percentage of Total Invested Assets

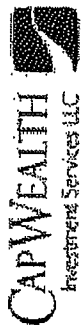
Note: The industry recently converted to the new Options Symbology Initiative format where options symbols can contain a combination of up to 22 letters and numbers. We have elected to begin displaying the underlying security symbol along with the standard contract description in lieu of the new variable length option symbol.

**PORTFOLIO HOLDINGS - FIXED INCOME - CORPORATE DEBT**

Quantity	Description	Price	Current Value	Est. Annual Income	Shares Purchased	Unit Cost	Cost Basis	Unrealized Gain/Loss	Accrued Interest
----------	-------------	-------	---------------	--------------------	------------------	-----------	------------	----------------------	------------------

Total Fixed Income - Corporate Debt

Percentage of Total Invested Assets



STERNE AGEE & LEACH INC C/F  
TIMOTHY J PAGLIARA SEP IRA

SEP-IRA



**ACCOUNT NUMBER**

Statement Period: 12/01/15 to 12/31/15

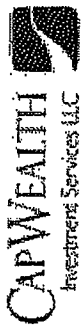
**SECURITY TRANSACTION ACTIVITY**

Date	Transaction	Quantity	Description	Price	Amount
------	-------------	----------	-------------	-------	--------

Total Securities Purchased

Total Securities Sold





STERNE AGEE & LEACH INC C/F  
TIMOTHY J PAGLIARA SEP IRA

SEP-IRA



**ACCOUNT NUMBER**

Statement Period: 12/01/15 to 12/31/15

**OTHER BOOKKEEPING**

Date	Transaction	Quantity	Description	Amount
------	-------------	----------	-------------	--------

Total Other Bookkeeping Debits



## GENERAL INFORMATION

- 1) Sterne, Agee & Leach, Inc. ("SALI") carries your account pursuant to a clearing agreement governed by FINRA Rule 4311, for your introducing broker-dealer ("IBD") whose name appears on the front page of this statement. SALI may accept without further inquiry or investigation, any instructions from your IBD relating to transactions in your account, including instructions for the withdrawal or transfer of property to or from your account. SALI is not responsible or liable for any acts or omissions of your IBD or its employees, is not responsible to supervise them, and does not provide investment advice or make suitability determinations for them. Your IBD is responsible to adhere to all applicable securities laws and regulations and for the supervision of its associated persons. Further, your IBD is also responsible for, among other things, approving the opening of accounts and obtaining necessary documents; the acceptance, and in certain instances, the execution of orders; the suitability determination of those orders; providing investment advice and the ongoing relationship it has with you. For additional information regarding the division of responsibilities between your IBD and SALI, please refer to the disclosure document you were provided at account opening.
- 2) All transactions are subject to the rules and customs of the market or exchange and the clearing house, if any, where such transactions are executed, your account agreement(s), and where appropriate, the Federal Reserve Board, the U.S. Securities and Exchange Commission and of the Financial Industry Regulatory Authority ("FINRA"). Whenever you are indebted to SALI for any amount, all securities held by it for you in any account which you have an interest shall secure your liabilities to SALI. SALI may, at its sole discretion and without notice to you, close or reduce any or all of your accounts by public or private sale or purchase of all or any securities carried in such accounts, any balance due remaining shall be promptly paid by you.
- 3) Cash received or paid and securities received or delivered are shown as-of the date of each transaction, while purchases and sales of securities are shown as-of trade date.
- 4) If this account is a margin account, this is a combined statement of your general account and special memorandum account maintained for you under Regulation T as issued by the Board of Governors of the Federal Reserve System. The permanent record of your special memorandum account is available for inspection upon your request.
- 5) A financial statement of SALI is available for your inspection at our offices. A copy will be mailed to you upon your written request or you can view it online at [www.sterneagee.com](http://www.sterneagee.com).
- 6) This statement should be retained for your records.
- 7) In order for your IBD to make proper recommendations relative to your account, it is incumbent upon you to promptly notify your IBD when your financial situation and/or investment objectives change.
- 8) SALI is required by federal law to provide you and the Internal Revenue Service with tax reporting information relative to your account. SALI does not provide tax advice. Investors must consult their own tax advisors to make appropriate tax treatment determinations. Your statement is not an official accounting of gains and losses. Please refer to your records, trade confirmations, and your Consolidated Form 1099.
- 9) **ACCOUNT PROTECTION-** SALI is a member of the Securities Investors Protection Corporation ("SIPC"). The SIPC protects clients of its member firms against the loss of their securities in the event of the member's insolvency and liquidation. Clients are insured up to a maximum of \$500,000, including up to \$250,000 in cash balances. For more information about SIPC coverage, an explanatory brochure is available at [www.sipc.org](http://www.sipc.org) or call SIPC at 202.371.8300. SALI provides

additional coverage through Lloyd's of London for \$24.5 million, including up to \$900,000 in cash balances, with an aggregate policy limit of \$100 million.

**CALLABLE SECURITIES-** Securities subject to a partial call will be processed utilizing a random lottery procedure designed to allocate called securities fairly and impartially. For further details refer to the "Callable Securities Procedures" disclosure found in the Important Disclosures section of Sterne Agee's public website, [www.sterneagee.com](http://www.sterneagee.com). A hard copy of this disclosure will be provided upon your request.

**ESTIMATED ANNUAL INCOME-** Est. Annual Income reflects the estimated amount you would earn on a security if your current position and its related income remained constant for a year.

**CASH MANAGEMENT-** SALI may provide you with a variety of ways in which to maintain funds awaiting re-investment, including: Money Market Mutual Funds, FDIC Insured Deposit Accounts, and Free Credit Balances. Please refer to our Cash Sweep Program Disclosure Statement for further information regarding these options. Money Market Mutual Fund and FDIC Insured Deposit balances may be liquidated on your order and proceeds returned to your account or remitted to you. Free Credit balances are payable upon your demand.

**Free Credit Balances-** SALI may elect to pay interest on certain balances awaiting investment and reserves the right to eliminate or otherwise change the rate or the manner in which interest on credit balances are paid at any time and without notice to you.

**Insured Deposit Program ("IDP")-** Funds swept to Sterne Agee's IDP are protected by the Federal Deposit Insurance Corporation up to applicable limits and are not protected by SIPC. If you have funds deposited into a participating Program Bank where you already have other deposits (e.g. banks accounts, CDs, etc.) held in the same capacity, all deposits are aggregated by the FDIC for purposes of determining coverage availability. It is your responsibility to monitor your deposits away from the IDP in Program Banks relative to coverage limits, and where necessary, exercise your right to instruct us not to use a particular Program Bank for your IDP deposits. Information regarding FDIC insurance is available upon request, or by visiting [www.fdic.gov](http://www.fdic.gov)

**OPEN ORDERS-** The Open Orders segment of this statement reflects open or "good until cancelled" orders not executed by the statement cut-off date. Open buy and sell stop orders are reduced by the amount of dividends or rights on ex-dates unless instructed otherwise by you. You are responsible for orders that are executed due to your failure to cancel existing open orders.

**OPTIONS CLIENTS-** Information regarding commissions and other charges related to options transactions has been included with trade confirmations. A summary of this information is available from your IBD upon your request. Please advise your IBD promptly of any material changes in your investment objectives and/or financial situation.

**PAYMENT FOR ORDER FLOW-** SALI receives compensation for directing order flow in certain equity and exchange listed options to certain broker-dealers, market centers or exchanges for execution. The source and amount of any such compensation relating to your orders will be furnished upon your written request.

**PUBLIC DISCLOSURE PROGRAM-** You may obtain an investor brochure that includes information describing the FINRA Regulation Public Disclosure Program that provides certain types of information about FINRA

member firms and their associated persons. This information is available at [www.finra.org](http://www.finra.org) or by calling the FINRA Regulation Public Disclosure Program Hotline at 800.289.9999.

**STATEMENT FREQUENCY-** Pursuant to the terms of NASD Rule 2340 and NYSE Rule 409, statements will be delivered to you monthly if there have been transactions affecting money balances and/or security positions; otherwise, statements will be delivered quarterly.

**VALUATION OF SECURITIES-** Pricing information is generally provided by a third party vendor which we believe to be reliable, though we do not guarantee its accuracy.

**Fixed Income Securities-** Values displayed on your statement are approximations and not actual market bids or offers. Actual secondary market conditions may vary substantially from the price displayed. Pricing estimates provided do not indicate a commitment from SALI or your IBD to buy or sell securities at the prices displayed. Consult your IBD if an actual bid or offer is needed.

**Certificates of Deposit (CDs)** When CDs have a maturity of one year or less from issue date, face value will be displayed. CDs with a maturity date from issue of more than one year will be displayed at a market value estimate that may not represent the actual price if sold prior to maturity.

**Low Priced and/or Illiquid Equity Securities-** Prices are derived from a third party pricing sources we believe to be reliable though SALI does not guarantee their accuracy. These prices may be based upon a limited number of transactions or quotes. Such prices are estimates and may not reflect a market price or value.

**Alternative Investments** Investments in direct participation programs, to include, but not limited to, partnerships, limited liability companies, non-traded real estate investment trusts, private equity, private debt and hedge funds are typically illiquid investments and their current values may be different than your purchase price. Unless otherwise indicated on this statement, the values shown for such investments have been provided by the management, sponsor or administrator of each program or a third-party vendor without independent verification by SALI and represent their estimate of value of the investor's participation in the program as-of a date not 18 months prior to this statement. The estimated values shown may not represent the actual market value or values that might be realized upon liquidation. If an estimated value is not provided, valuation information is not available.

**In order to protect your rights under the Securities Investor Protection Act ("SIPA"), you are advised to report any discrepancy or inaccuracy in your account to your IBD at their place of business and SALI at 800.778.6257. Any verbal communications should be re-confirmed in writing to your IBD at their place of business and to SALI at the address below. This statement will otherwise be deemed conclusive unless you notify us in writing by the last business day of the month following the end of the statement period.**

Sterne, Agee & Leach, Inc.  
2 Perimeter Park S. - Suite 100W  
Birmingham, Alabama 35243

Investments carried by SALI are not FDIC insured, unless specifically noted to the contrary, and may lose value.

**Connally, N. Thomas, III**

---

**From:** Connally, N. Thomas, III  
**Sent:** Tuesday, January 19, 2016 4:49 PM  
**To:** boardofdirectors@freddiemac.com  
**Subject:** Books and Records Demand to Freddie Mac  
**Attachments:** 01.19.2016 Books and Records letter to Freddie Mac (with exhibits).pdf

Please see the attached demand for inspection of corporate books and records.

Thank you for your attention to this matter.

Best regards, Tom Connally

**N. Thomas Connally**

Partner

Hogan Lovells US LLP

Park Place II, Ninth Floor  
7930 Jones Branch Drive  
McLean, VA 22102-3302

Tel: +1 703 610 6100

Direct: +1 703 610 6126

Fax: +1 703 610 6200

Email: [tom.connally@hoganlovells.com](mailto:tom.connally@hoganlovells.com)

[www.hoganlovells.com](http://www.hoganlovells.com)

*Please consider the environment before printing this e-mail.*

# **EXHIBIT B**

## **FHFA RESPONSE**



# Federal Housing Finance Agency

Constitution Center

400 7<sup>th</sup> Street, S.W.

Washington, D.C. 20024

Telephone: (202) 649-3800

Facsimile: (202) 649-1071

[www.fhfa.gov](http://www.fhfa.gov)

January 28, 2016

Non-Public Communication

By Electronic Mail to [tom.connally@hoganlovells.com](mailto:tom.connally@hoganlovells.com)

N. Thomas Connally, III  
Hogan Lovells US LLP  
Park Place II  
Ninth Floor  
7930 Jones Branch Drive  
McLean, VA 22102

Dear Mr. Connally:

The Federal Housing Finance Agency in its capacity as Conservator ("FHFA" or "Conservator") of the Federal Home Loan Mortgage Corporation ("Freddie Mac") has reviewed your January 19, 2016 letters to Freddie Mac's Board of Directors concerning dividend payments and demanding to inspect certain Freddie Mac records.

Please be advised that pursuant to the Housing and Economic Recovery Act of 2008, the Conservator has succeeded by operation of law to "all rights, titles, powers, and privileges of [Freddie Mac], and of any stockholder, officer, or director of [Freddie Mac]" with respect to Freddie Mac and its assets, 12 USC 4617(b)(2)(A)(i). Those "rights, titles, powers, and privileges" of the "stockholder[s]" to which the Conservator succeeded include all stockholder inspection rights. Therefore, among other reasons, so long as Freddie Mac remains in conservatorship, Investors Unite has no basis upon which to demand inspection of Freddie Mac records.

Moreover, your position on the applicable law governing the board of directors is incorrect. As noted in Freddie Mac's regularly filed disclosures, its boards of directors "serve on behalf of, and exercise authority as directed by, the Conservator." Freddie Mac 2014 10-K, at 247. Because any fiduciary duties of this board of directors flow directly and exclusively to the Conservator, state law principles such as those you assert in your letter are simply not applicable here. Finally, I note that payments by Freddie Mac of dividends to the United States Treasury have been made pursuant to directives of the Conservator.

With all best wishes, I am

Sincerely,

A handwritten signature in black ink, appearing to read 'Alfred M. Pollard', written in a cursive style.

Alfred M. Pollard  
General Counsel

**Connally, N. Thomas, III**

---

**From:** Pollard, Alfred <Alfred.Pollard@fhfa.gov>  
**Sent:** Thursday, January 28, 2016 5:58 PM  
**To:** Connally, N. Thomas, III  
**Subject:** Communication to Freddie Mac Board of Directors  
**Attachments:** S8-218-Copi16012818540.pdf

Please see attached.

If you have any questions, I may be reached at this email or at 202 649 3050.

Alfred Pollard

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# **EXHIBIT C**

# **CLARIFICATION LETTER**

**Hogan  
Lovells**

Hogan Lovells US LLP  
Park Place II  
Ninth Floor  
7930 Jones Branch Drive  
McLean, VA 22102  
T +1 703 610 6100  
F +1 703 610 6200  
[www.hoganlovells.com](http://www.hoganlovells.com)

February 4, 2016

*BY EMAIL AND US MAIL*

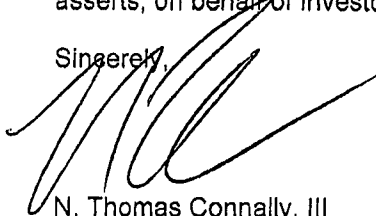
Alfred M. Pollard  
General Counsel  
Federal Housing Finance Agency  
Constitution Center  
400 7th Street, S.W.  
Washington, DC 20024  
[Alfred.Pollard@fhfa.gov](mailto:Alfred.Pollard@fhfa.gov)

Dear Mr. Pollard:

Thank you for FHFA's January 28 response on behalf of Freddie Mac to our letters of January 19. Plainly, we disagree with the legal positions FHFA has asserted. We write, however, to correct one of the factual assertions in FHFA's response. As is clear from our letters themselves, and the declaration of our client, Timothy J. Pagliara, incorporated into the books and records demand, both demand letters were sent on behalf of Mr. Pagliara, an individual beneficial owner of Freddie Mac stock.

We do not represent Investors Unite, and the demand letters were not sent, as FHFA's response asserts, on behalf of Investors Unite.

Sincerely,



N. Thomas Connally, III

Partner  
[tom.connally@hoganlovells.com](mailto:tom.connally@hoganlovells.com)  
D +1 703 610 6126

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WINORTHVA - 046513/000001 - 688845 v1

**Connally, N. Thomas, III**

---

**From:** Connally, N. Thomas, III  
**Sent:** Thursday, February 04, 2016 11:41 AM  
**To:** alfred.pollard@fhfa.gov  
**Subject:** FHFA Jan. 28 Letter  
**Attachments:** 2.4.2016 Letter to Pollard.PDF

Please see the attached letter.

Thanks, Tom Connally

N. Thomas Connally  
Partner  
Hogan Lovells US LLP  
Park Place II, Ninth Floor  
7930 Jones Branch Drive  
McLean, VA 22102-3302  
Tel: +1 703 610 6100  
Direct: +1 703 610 6126  
Fax: +1 703 610 6200  
Email: [tom.connally@hoganlovells.com](mailto:tom.connally@hoganlovells.com)

[www.hoganlovells.com](http://www.hoganlovells.com)

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**EXHIBIT D**

**POLLARD  
E-MAIL**

**Connally, N. Thomas, III**

---

**From:** Pollard, Alfred <Alfred.Pollard@fhfa.gov>  
**Sent:** Thursday, February 04, 2016 1:42 PM  
**To:** Connally, N. Thomas, III  
**Subject:** RE: FHFA Jan. 28 Letter

Thank you for your clarification. By this communication, I would provide that it is duly noted.

Alfred Pollard

-----Original Message-----

**From:** Connally, N. Thomas, III [<mailto:tom.connally@hoganlovells.com>]  
**Sent:** Thursday, February 04, 2016 11:41 AM  
**To:** Pollard, Alfred  
**Subject:** FHFA Jan. 28 Letter

Please see the attached letter.

Thanks, Tom Connally

N. Thomas Connally  
Partner  
Hogan Lovells US LLP  
Park Place II, Ninth Floor  
7930 Jones Branch Drive  
McLean, VA 22102-3302  
Tel: +1 703 610 6100  
Direct: +1 703 610 6126  
Fax: +1 703 610 6200  
Email: [tom.connally@hoganlovells.com](mailto:tom.connally@hoganlovells.com)

[www.hoganlovells.com](http://www.hoganlovells.com)

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**About Hogan Lovells**

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**EXHIBIT E**

**DIVIDEND  
LETTER**



Hogan Lovells US LLP  
Park Place II  
Ninth Floor  
7930 Jones Branch Drive  
McLean, VA 22102  
T +1 703 610 6100  
F +1 703 610 6200  
www.hoganlovells.com

January 19, 2016

***BY EMAIL & CERTIFIED MAIL***

Christopher S. Lynch, Non-Executive Chairman  
Raphael W. Bostic  
Carolyn H. Byrd  
Lance F. Drummond  
Thomas M. Goldstein  
Richard C. Hartnack  
Steven W. Kohlhagen  
Donald H. Layton  
Sara Mathew  
Saiyid T. Naqvi  
Nicolas P. Retsinas  
Eugene B. Shanks  
Anthony A. Williams

Board of Directors  
c/o Corporate Secretary  
Freddie Mac  
8200 Jones Branch Drive MS 200  
McLean, Virginia 22102  
boardofdirectors@freddiemac.com

Dear Ladies and Gentlemen of the Board:

We represent Timothy J. Pagliara, the beneficial owner of stock in the Federal Home Loan Mortgage Corporation ("Freddie Mac" or the "Corporation"). We write on our client's behalf to urge you, as members of the Board of Directors of the Corporation (the "Board" or the "Board of Directors"), to satisfy your fiduciary duties under Virginia law by taking the following steps:

1. Publicly clarify the Board's role in declaring and paying dividends to the United States Treasury ("Treasury") on account of its senior preferred stock (the "Senior Preferred Stock");

2. Publicly declare, for reasons detailed herein, including out of concern for the financial soundness of the Corporation, that the Board does not agree with the declaration and payment of dividends to Treasury on account of the Senior Preferred Stock, and certainly not in amounts equal to *all* the profits of the Corporation; and
3. Exercise your authority under Virginia law to cause the Corporation to immediately stop declaring and paying dividends to Treasury on account of the Senior Preferred Stock.

As you know, Freddie Mac is a federally chartered corporation established pursuant to the Federal Home Loan Mortgage Corporation Act (the "Corporation Act"), and owned by private stockholders, including our client. The Corporation Act created "a body corporate under the direction of a Board of Directors." 12 U.S.C. § 1452(a)(1); *see also* Freddie Mac Bylaws § 4.1. Under Freddie Mac's Bylaws, Virginia law is the law of decision governing Freddie Mac's "corporate governance practices and procedures." Freddie Mac Bylaws § 11.3(a).

Virginia law, and specifically the Virginia Stock Corporation Act (the "VSCA"), thus provides the general standards of conduct for the Board of Directors. Va. Code Ann. § 13.1-690. The VSCA's primary command to directors is simple: "[a] director shall discharge his duties as a director, including his duties as a member of a committee, in accordance with his good faith business judgment of the best interests of the corporation." *Id.*

Virginia law also governs the Board's authority to declare and pay dividends. Under Virginia law, dividends are voluntary; declaration and payment of dividends is entrusted to the Board's discretion. *See* Va. Code Ann. § 13.1-653A ("A board of directors *may* authorize and the corporation may make distributions to its shareholders . . .") (emphasis added). Likewise, the Corporation Act states that Freddie Mac may make capital distributions, "as may be declared by the Board of Directors." 12 U.S.C. § 1452(b)(1). Consistent with these statutes, Treasury's Amended and Restated Senior Preferred Stock Certificate, executed *after* the Freddie Mac Board was reconstituted by the Federal Housing Finance Agency ("FHFA" or "Conservator"), states that holders of such stock are only entitled to cash dividend payments "when, as and if declared by the Board of Directors, in its sole discretion, out of funds legally available therefor." Freddie Mac Amended and Restated Senior Preferred Stock Certificate of Designation ¶ 2(a). In exercising its discretion to declare and pay dividends, as in all its actions, the Board must follow its good faith business judgment of the best interests of the Corporation.

Notwithstanding these provisions, in 2012 FHFA and Treasury entered into the Third Amendment to Amended and Restated Senior Preferred Stock Purchase Agreement (the "Net Worth Sweep"), providing for the quarterly distribution, in perpetuity, of

ultimately all of the net worth of Freddie Mac to Treasury. FHFA and Treasury have both made clear that the Net Worth Sweep “ensures all [Freddie Mac’s] earnings are used to benefit taxpayers.”<sup>1</sup> The declaration and payment of such dividends is plainly not action taken based on good faith business judgment of the best interests of the Corporation or its shareholders.

In addition, under Virginia law, a distribution cannot be properly authorized if it would result (i) in the corporation becoming unable to pay its debts as due in the usual course of business, or (ii) in the corporation’s total assets becoming less than its total liabilities. Va. Code Ann. § 13.1-653; *see also* 12 U.S.C. § 1452(b)(2). The risk the Net Worth Sweep poses to the Corporation is obvious. During the three months “ended March 31, 2015, June 30, 2015, and September 30, 2015, [Freddie Mac] paid dividends of \$0.9 billion, \$0.7 billion, and \$3.9 billion, respectively, in cash on the senior preferred stock at the direction of [FHFA].” *Freddie Mac Quarterly Report on Form 10-Q*, 109 (for quarterly period ended September 30, 2015). In sharp contrast, “no common stock dividends were declared during the nine months ended September 30, 2015.” 2015 10-Q at 109. During the same period, the Corporation’s “Net Worth Amount at September 30, 2015 was below the 2015 Capital Reserve Amount of \$1.8 billion . . . As a result of the net worth sweep dividend we pay to Treasury, [Freddie Mac] cannot retain capital from the earnings generated by our business operations.” 2015 10-Q at 69. Legal commenters have noted that the payment of these dividends to Treasury “sets a horrible precedent and it violates the Housing and Economic Recovery Act of 2008 as well as traditional corporate law practices.” Gretchen Morgenson, Fannie and Freddie’s Government Rescue Has Come with Claws, N.Y. Times, Dec. 12, 2015 (quoting Logan Beirne, a fellow at the Information Society Project at Yale Law School).

Freddie Mac has paid out, and continues to pay out, billions of dollars in discretionary cash dividends to Treasury under this Board’s administration while the contractual restraints on capital preservation imposed by the Net Worth Sweep have left it teetering perilously on the edge of insolvency. Courts applying Virginia law have affirmed that directors may be held personally liable for authorizing a distribution under such circumstances. *See, e.g., In re Heilig-Meyers Co.*, 328 B.R. 471, 489 (E.D. Va. 2005) (citing to Section 13.1-653C of the VSCA) (“Virginia law prohibits a corporation from paying a dividend while insolvent or if the dividend would cause insolvency”).

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<sup>1</sup> Federal Housing Finance Agency, Conservatorship, “Senior Preferred Stock Purchase Agreements,” available at <http://www.fhfa.gov/Conservatorship/Pages/Senior-Preferred-Stock-Purchase-Agreements.aspx>; *see also* U.S. Dep’t of the Treasury, Press Release, “Treasury Department Announces Further Steps to Expedite Wind Down of Fannie Mae and Freddie Mac,” (Aug. 17, 2012), available at <https://www.treasury.gov/press-center/press-releases/Pages/tg1684.aspx> (Net Worth Sweep will “make sure that every dollar of earnings [Freddie Mac] generates is used to benefit taxpayers”).

The Board is also prohibited from declaring and paying dividends driven by conflicts of interest or that amount to corporate waste. Where a dividend is paid to a controlling stockholder to the detriment of other minority stockholders, as in the case of Freddie Mac's dividend payments to Treasury (the Corporation's controlling stockholder, a related party and FHFA's sister agency), that inherent conflict of interest requires close scrutiny. Such transactions are voidable unless the conflicted controlling party can establish that the transactions were fair to the corporation. See *Dunford Roofing, Inc. v. Earls*, No. 1:00CV00025, 2001 WL 396869, at \*8 (W.D. Va. Apr. 12, 2001); *Willard v. Moneta Bldg. Supply, Inc.*, 258 Va. 140, 155, 515 S.E.2d 277, 287 (1999); *Giannotti v. Hamway*, 239 Va. 14, 24, 387 S.E.2d 725, 731 (1990); accord Va. Code Ann. § 13.1-691. The Net Worth Sweep, pursuant to which Freddie Mac already has paid *more than \$70 billion* to Treasury in exchange for no additional consideration whatsoever, is in no way fair to the Corporation. Indeed, by approving or permitting the Net Worth Sweep and the ongoing dividends to Treasury, the Board appears to have violated and continues to violate the prohibition against corporate waste. *In re Capital One Derivative S'holder Litig.*, 952 F. Supp. 2d 770, 782 (E.D. Va. 2013) (corporate waste occurs where "the consideration received by the corporation was so inadequate that no person of ordinary sound business judgment" would have approved the transaction) (citing to Delaware law).

A director who votes for or assents to a distribution made in violation of Virginia law is personally liable to the corporation. Va. Code Ann. § 13.1-692A. Liability under Section 13.1-692 applies to directors' actions, and also to any conscious *failure* to act. See *Colgate v. Disthene Grp., Inc.*, 86 Va. Cir. 218 (Buckingham County Cir. Ct. 2013); Allen C. Goolsby & Steven M. Haas, *Goolsby & Haas on Virginia Corporations* § 9.7 (liability under Virginia law "applies not just to actions taken by the directors, but also to any conscious failure to act"). While the Corporation's Bylaws purport to limit the liability of directors on claims brought by or in the name of the Corporation or its shareholders, see Bylaws § 8.1, neither the Bylaws nor the VSCA allows for the limitation of liability for willful misconduct. Directors who allow—quarter after quarter—all of the Corporation's profits to go to Treasury are certainly risking exposure to claims of willful misconduct.

To date, public disclosure regarding the Board's role in declaring and paying dividends has been clouded. The Conservator has instructed the Board "that it should consult with and obtain the approval of the Conservator before taking . . . actions involving capital stock [or payment of] dividends . . ." *Freddie Mac Current Report on Form 10-K/A*, 5 (for fiscal year ended December 31, 2008). Stockholders in Freddie Mac, a publicly traded, SEC-registered corporation, deserve to know the extent to which the Board, FHFA, and any other party may be held accountable for the misallocation of the Corporation's capital and the distribution of dividends to Treasury. For this reason, we strongly urge you to remove the cloud hanging over these decisions and publicly clarify your role in the declaration and payment of dividends.



In addition, regardless of whether the Corporation has been declaring and paying dividends with Board approval or as a result of the Board's inaction, the director liability imposed on Freddie Mac directors by Virginia law for the payment of unlawful dividends is not assumed by FHFA as Conservator. The Corporation's actions have made clear that the Board of Directors is a legally constituted board subject to Virginia law. For example, in July 2015 the Corporation amended and restated its Bylaws while under conservatorship, and *retained* Section 11.3 providing that Virginia law is the law of decision governing Freddie Mac's "corporate governance practices and procedures." Likewise, these same Bylaws provide that "[s]ubject to the limitations of law and regulation, the Board of Directors shall determine the general policies that govern the operations of the Corporation, and the Corporation shall be under the direction of the Board of Directors." *Id.* § 4.1. The conservatorship plainly does not absolve the directors from fulfilling their corporate fiduciary duties under Virginia law.

Despite these fiduciary duties (and associated liabilities) of directors under Virginia law, there is no indication that the Board has made *any* effort to ensure that, under its administration, the cash dividends being declared and paid by the Corporation to Treasury on a quarterly basis comply with Virginia law. At a minimum, the Board must confirm that the dividend payments comply with VSCA Section 13.1-653C, that the payments are fair to the Corporation, and that the payments do not constitute corporate waste. Instead of doing so, Freddie Mac's Board has seemingly resolved itself to inaction. This is never an acceptable method for a corporate director to satisfy his or her fiduciary duties. *See, e.g., Colgate, supra; accord In re Citigroup Inc. S'holder Derivative Litig.*, 964 A.2d 106, 123 (Del. Ch. 2009) ("to establish oversight liability a plaintiff must show that the directors *knew* they were not discharging their fiduciary obligations or that the directors demonstrated a *conscious* disregard for their responsibilities such as by failing to act in the face of a known duty to act").

Each of you, as a member of a Virginia-law-governed corporate board of directors, has a duty to the Corporation, and to our client as a stockholder, to prevent Freddie Mac from making improperly motivated and unlawful dividend payments that threaten the Corporation's solvency. You may be held personally liable for failure to do so. As explained in our separate letter, the Board remains subject to liability for breaches of statutory and fiduciary duties despite the pendency of the conservatorship. Even if this were not so, the conservatorship will inevitably end, at which time the Board will undoubtedly be subject to liability for its actions during the conservatorship.<sup>2</sup>

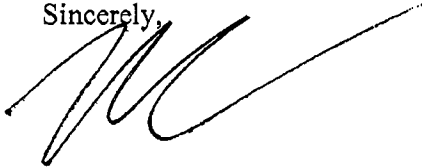
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<sup>2</sup> Debate in Congress recently confirmed, in connection with approving the Consolidated Appropriations Act, 2016 – Section 702, that the conservatorship has a finite duration, regardless of the Third Amendment and other developments. In discussing provisions in the Consolidated Appropriations Act concerning the Treasury's preferred stock, Senate Minority Leader Harry Reid noted that "As then-Secretary Paulson described, conservatorship was meant to be a 'time out' not an indefinite state of being."

Board of Directors  
Federal Home Loan Mortgage Corporation  
January 19, 2016

We urge you to take your fiduciary duties as a director seriously, and to make your voice heard by publicly declaring that the Board does not agree with the declaration and payment of unlawful dividends to Treasury. We also urge you to take whatever steps you have at your disposal to cause Freddie Mac to immediately cease declaring and paying dividends to Treasury at the expense of the Corporation's well-being.

Sincerely,



N. Thomas Connally, III

Partner  
tom.connally@hoganlovells.com  
D +1 703 610 6126

cc: Timothy J. Pagliara

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Banking Committee Ranking Member Senator Sherrod Brown then added: “. . . the FHFA and Treasury Department could have placed the GSEs into receivership if the intent was to liquidate them. The purpose of a conservatorship is to preserve and conserve the assets of the entities in conservatorship until they are in a safe and solvent condition as determined by their regulator.”

**Connally, N. Thomas, III**

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**From:** Connally, N. Thomas, III  
**Sent:** Tuesday, January 19, 2016 5:01 PM  
**To:** boardofdirectors@freddiemac.com  
**Subject:** Letter to Board of Directors  
**Attachments:** 01.19.2016 Letter to Freddie Mac Board of Directors.pdf

Please see the attached letter to the Board of Directors.

Thank you for your attention to this matter.

Best regards, Tom Connally

**N. Thomas Connally**

Partner

Hogan Lovells US LLP

Park Place II, Ninth Floor

7930 Jones Branch Drive

McLean, VA 22102-3302

Tel: +1 703 610 6100

Direct: +1 703 610 6126

Fax: +1 703 610 6200

Email: [tom.connally@hoganlovells.com](mailto:tom.connally@hoganlovells.com)

[www.hoganlovells.com](http://www.hoganlovells.com)

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