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UNITED STATES COURT OF FEDERAL CLAIMS

MICHAEL E. KELLY, FBOP CORPORATION, RIVER CAPITAL ADVISORS, INC. and FBOP CORPORATION ON BEHALF OF CALIFORNIA NATIONAL BANK, PARK NATIONAL BANK, SAN DIEGO NATIONAL BANK, PACIFIC NATIONAL BANK, BANKUSA, NORTH HOUSTON BANK, MADISON STATE BANK, COMMUNITY BANK OF LEMONT, CITIZENS NATIONAL BANK AND RIVER CAPITAL ADVISORS, INC.

Plaintiffs,

v.

THE UNITED STATES OF AMERICA,

Defendant.

No. **21-1949L**

COMPLAINT

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Table of Acronyms and Abbreviations

1992 Act	Federal Housing Enterprises Financial Safety and Soundness Act of 1992
Fannie Mae	Federal National Mortgage Association
FHFA	Federal Housing Finance Agency
Freddie Mac	Federal Home Loan Mortgage Corporation
GSE	Government Sponsored Enterprise
HERA	Housing and Economic Recovery Act of 2008
HUD	U.S. Department of Housing and Urban Development
MBS	Mortgage-Backed Security
OFHEO	Office of Federal Housing Enterprise Oversight
SPSPAs	Senior Preferred Stock Purchase Agreements
Treasury	U.S. Department of Treasury

I. NATURE OF THE ACTION

1. This action raises constitutional and related claims arising from the United States Government's September 2008 imposition of conservatorships on the government sponsored enterprises, Federal National Mortgage Association ("***Fannie Mae***") and Federal Home Loan Mortgage Corporation ("***Freddie Mac***") (together, "***GSEs***"). Plaintiff Michael E. Kelly ("***Mr. Kelly***") is CEO and sole common shareholder of Plaintiff FBOP Corporation ("***FBOP***"). FBOP was a bank holding company that held nine banks: (1) Park National Bank; (2) San Diego National Bank; (3) Pacific National Bank; (4) BankUSA; (5) North Houston Bank; (6) Madison State Bank; (7) Community Bank of Lemont; (8) Citizens National Bank; and (9) California National Bank ("***FBOP Subsidiaries***"). FBOP has standing and asserts claims for relief on behalf of the FBOP Subsidiaries, which owned $898,448,392 in GSE preferred shares when the conservatorships were unlawfully imposed on the GSEs on September 6, 2008. FBOP also has standing and asserts claims for relief on behalf of Plaintiff River Capital Advisors, Inc. ("***River Capital***"), an FBOP wholly-owned non-bank subsidiary that held approximately $40 million in GSE preferred shares when the conservatorships were unlawfully imposed. River Capital alternatively has standing to bring direct claims on its own behalf. The Government's actions ultimately deprived the FBOP Subsidiaries and River Capital of their individual rights as shareholders, including dividends and voting rights, and destroyed the economic value of Plaintiffs' shares. The imposition of the conservatorships violated Plaintiffs' constitutional rights under the Fifth Amendment, as well as Plaintiffs' contractual rights. Based on the facts set forth herein, Plaintiffs assert three causes of action: (1) unlawful taking and/or illegal exaction, as a direct claim; (2) unlawful taking and/or illegal exaction, alternatively as a derivative claim; and (3) breach of implied regulatory contract.

2. Created by Congress, Fannie Mae and Freddie Mac are United States government-sponsored enterprises responsible for guaranteeing most home mortgages. Both Fannie Mae and

Freddie Mac were shareholder-owned corporations during the 2008 financial crisis. The GSEs remain shareholder-owned corporations. In 2006 and 2007, the GSEs issued new series of preferred shares. The Government created a variety of incentives to encourage financial institutions, including banks such as the FBOP Subsidiaries, to purchase GSE preferred shares. Those incentives allowed national banks to invest in the GSEs' perpetual preferred stock without limits and to concentrate up to 100% of their Tier 1 capital in GSE preferred stock, designating such investments as sound and of no significant risk.

3. The Federal Housing Finance Agency ("***FHFA***"), the regulator of the GSEs, placed them into conservatorship on September 6, 2008. On September 7, 2008, the U.S. Department of the Treasury entered into Senior Preferred Stock Purchase Agreements ("***SPSPAs***") with both GSEs, pursuant to which Treasury was issued $1 billion in senior preferred stock, as well as common stock warrants that gave Treasury a 79.9% ownership interest in the GSEs.

4. This action seeks relief solely for the Government's actions as regulator in imposing the conservatorships, and not for its actions as conservator after placing the GSEs into conservatorship on September 6, 2008. In exercising its regulatory power on that date, the FHFA imposed conservatorships on the GSEs in violation of the law. Under the Housing and Economic Recovery Act of 2008 ("***HERA***"), the FHFA was permitted to place the GSEs into conservatorship, but only under specific and exclusive prerequisites enumerated by Congress. 12 U.S.C. § 4617(a)(3)(A)-(L). None were satisfied as of September 6, 2008. Although the Government purported to gain the consent of the GSEs' boards, that consent was invalid, as it was obtained by coercion and given only under duress.

5. The immediate impact of the Government's actions on September 6 and 7 was to deprive the private shareholders, including Plaintiffs, of their property rights as shareholders,

including the loss of their dividend and voting rights, and to destroy the economic value of the shares themselves. Given the Government's efforts to encourage banks such as the FBOP Subsidiaries and River Capital to invest in the GSEs, the Government's destruction of the shareholders' rights and the value of their property was a dramatic departure from Plaintiffs' reasonable expectations when they purchased the GSE shares.

6. Furthermore, the Government's actions violated its commitments to the GSE shareholders. The Government had permitted banks to satisfy their capital requirements with GSE stock and impliedly guaranteed the investments.

7. GSE shareholders were offered no compensation whatsoever for the loss of their rights. The results for the FBOP Subsidiaries and River Capital were catastrophic.

8. As noted above, FBOP was a community bank holding company that held the nine FBOP Subsidiaries and River Capital. At the time of the conservatorships, FBOP was the largest privately held bank holding company in the country. From late 2007 through early 2008, with the support and encouragement of Government regulators, FBOP Subsidiaries purchased GSE preferred shares. These shares had a Combined Net Book Value of $898,448,392 as of September 10, 2008. As a result, under the applicable regulatory regime, FBOP's Tier 1 capital requirements were satisfied. As also noted above, River Capital, an FBOP wholly-owned non-bank subsidiary, held approximately $40 million in GSE preferred shares when conservatorship was imposed. River Capital purchased and held GSE preferred shares later purchased by and transferred to the individual FBOP Subsidiaries. Given this transfer of ownership, both FBOP Corporation and River Capital purchased GSE shares due to the same government incentives discussed below.

9. When the GSE shares lost their value in the immediate aftermath of the conservatorships, the FBOP Subsidiaries proximately became insolvent due to diminution of value of GSE holdings. Despite FBOP's diligent efforts to apply for funding under the Troubled Asset Relief Program ("***TARP***") and to obtain private capital, the FBOP Banking Subsidiaries were placed into receivership on October 30, 2009. With the loss of the FBOP Banking Subsidiaries, FBOP became insolvent. On October 5, 2012, FBOP entered into an Assignment for the Benefit of Creditors ("***ABC Agreement***"), whereby FBOP assigned charters, articles of incorporation, corporate records, stock certificates, ownership, and/or indicia of ownership, of its subsidiaries, and other assignable assets, to an ABC Trust for the benefit of FBOP creditors.

10. The ABC Trustee liquidated and distributed significant proceeds to beneficiaries of the ABC Trust. Subsequent to distribution of all other monetizable assets of FBOP's former subsidiaries, all charters, articles of incorporation, corporate records, stock certificates, ownership, and/or indicia of ownership, of FBOP's former subsidiaries, reverted back and/or were assigned to FBOP. To the extent initially transferred to the ABC Trust, if at all, any and all claims arising out of or related to ownership, valuation, control or use of common or preferred stock interests issued by either GSE that could have been brought by FBOP's former subsidiaries also reverted back and/or were assigned to FBOP. FBOP currently owns and controls 100% of all interests, if any, in former subsidiaries, and owns and controls all rights to assert any and all claims arising out of or related to ownership, valuation, control or use of common or preferred stock interests issued by either GSE that could have been brought by FBOP's former subsidiaries.

11. The Government's actions in imposing conservatorship on the GSEs constituted a taking or, in the alternative, an illegal exaction in violation of the Fifth Amendment. These actions

also constituted a breach of an implied regulatory contract between the Government and the FBOP Subsidiaries.

II. PARTIES

12. Plaintiff FBOP Corporation was an Illinois-based community bank holding company and the largest privately-owned bank holding company in the United States. Plaintiff River Capital Advisors, Inc. was an FBOP wholly-owned non-bank subsidiary. At all relevant times, FBOP held the nine FBOP Subsidiaries and River Capital.

13. Plaintiff Michael E. Kelly is the Chairman and Chief Executive Officer of FBOP Corporation. He was and remains the sole common shareholder of FBOP, which was sole common shareholder of the FBOP Subsidiaries and River Capital. Mr. Kelly is President and sole director of River Capital Advisors, Inc. Mr. Kelly has standing to bring direct claims on behalf of himself, FBOP, FBOP Subsidiaries and River Capital. Alternatively, Mr. Kelly has standing to bring claims on behalf of himself and FBOP, derivatively on behalf of FBOP and derivatively on behalf of the FBOP Subsidiaries and River Capital.

14. FBOP has standing and asserts claims for relief on behalf of the nine FBOP Subsidiaries: (1) Park National Bank; (2) San Diego National Bank; (3) Pacific National Bank; (4) Bank USA; (5) North Houston Bank; (6) Madison State Bank; (7) Community Bank of Lemont; (8) Citizens National Bank; and (9) California National Bank. FBOP also has standing and asserts claims for relief on behalf of River Capital, an FBOP wholly-owned non-bank subsidiary. River Capital alternatively has standing to bring direct claims on its own behalf. At all relevant times, FBOP Subsidiaries and River Capital were common and/or preferred shareholders of Fannie Mae and/or Freddie Mac.

15. Defendant United States of America (the "***Government***") includes the Federal Housing Finance Agency ("***FHFA***") and its agents acting at its direction, and the United States Treasury and its agents acting at its direction.

III. JURISDICTION AND VENUE

16. This Court has jurisdiction pursuant to 28 U.S.C. §§ 1491(a) and 2501. Venue is proper under 28 U.S.C. § 1491(a).

IV. RELEVANT CONSTITUTIONAL PROVISION

17. Plaintiffs' claims are governed by the Fifth Amendment to the United States Constitution, which provides that no person shall "be deprived of life, liberty, or property, without due process of law; nor shall private property be taken for public use, without just compensation."

V. FACTUAL BACKGROUND

A. Mr. Kelly and FBOP Corporation

18. In 1981, Mr. Kelly formed an investment group that acquired the First Bank of Oak Park. Mr. Kelly became its President and CEO. Within five years, the First Bank of Oak Park's worth had doubled and it had become a top performing bank. The First Bank of Oak Park was frequently rated first in Illinois based on its return on assets and equity. In 1986, Mr. Kelly formed FBOP, a bank holding company with Mr. Kelly as the sole common shareholder. FBOP acquired 100% of The First Bank of Oak Park.

19. In the 1990s, FBOP began to expand. During the farm crisis in the Midwest, and then during a real estate crisis in Texas, FBOP purchased failed assets from the FDIC in areas where the FDIC had closed banks. FBOP's on-the-ground efforts enabled its personnel to meet with individual loan holders to create realistic payment plans. This strategy proved successful, served communities struggling with economic crises, and fueled tremendous growth for the bank

holding company. FBOP's successful loan restructuring approach provided it with sufficient capital to acquire several other banks.

20. FBOP experienced enormous success. It posted record profits for twenty-five consecutive years. What was initially a $60 million community bank in 1981 became a large multi-bank holding company. The FBOP Subsidiaries owned $19.4 billion in assets and held $15.4 billion in deposits. By September 2009, FBOP had nine subsidiaries: (1) Park National Bank; (2) San Diego National Bank; (3) Pacific National Bank; (4) Bank USA; (5) North Houston Bank; (6) Madison State Bank; (7) Community Bank of Lemont; (8) Citizens National Bank; and (9) California National Bank. Together, the FBOP Subsidiaries operated 150 branches, approximately one-third of which were in low- to moderate-income census tracks. FBOP became the largest privately held bank holding company in the country, with approximately 2,400 employees. FBOP Subsidiaries never engaged in subprime lending, predatory lending, or excessive executive compensation.

21. On January 21, 2010, Mr. Kelly testified at a hearing before the U.S. House of Representatives, Subcommittee on Financial Institutions and Consumer Credit. His written statement entered for the record ("***Kelly Statement***") and other testimony are available online.[1]

22. As detailed in the Kelly Statement, FBOP was known for its strong underwriting, cited by third parties as "A quality," as well as its robust credit systems and practices recognized

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[1] *The Condition of Financial Institutions: Examining the Failure and Seizure of an American Bank*, Hearing Before the Subcommittee on Financial Institutions and Consumer Credit of the Committee on Financial Services, U.S. House Of Representatives, One Hundred Eleventh Congress, Second Session (Jan. 21, 2010) at pp. 10-12 (opening testimony); pp. 14-26, 32-37, 46-48 (legislator comments and questioning); and pp. 112-30 (Kelly Statement), https://archives-financialservices.house.gov/Media/file/hearings/111/Printed%20Hearings/111-97.pdf (last visited September 30, 2021).

as "best in class." FBOP consistently enjoyed positive relationships with government regulators, including the FDIC, the Office of the Comptroller of the Currency ("***OCC***"), the Federal Reserve, and the state banking commissions in Arizona, California, Illinois, and Texas. Regulators were so confident in FBOP's strategies and expertise that they would frequently bring deals for potential acquisition of failing or failed banks directly to FBOP.

23. As detailed in the Kelly Statement, throughout its expansion, FBOP focused on community reinvestment and engagement. Although FBOP was a large holding company, FBOP's banks operated as community banks committed to providing financial products and services to individuals, local businesses, and not-for-profit corporations, including small businesses and borrowers who would have been rejected by larger lenders. FBOP frequently opened branches in geographic areas other banks were reluctant to enter. The corporation and Mr. Kelly himself were active in community groups in areas where FBOP had branches.

24. As detailed in the Kelly Statement, FBOP continued this commitment even in times of macroeconomic distress. In 2007 and 2008, for example, FBOP banks invested in the communities they served by making community investments totaling $55 million, which represented 28% of its profits in those years. FBOP also made $17 million in contributions at the holding company level. In late 2007, six of the nine FBOP Subsidiaries were rated "outstanding" for their community reinvestment efforts, a rating bestowed on only 8% of banks in the United States. FBOP did not once pay a common stock dividend to its sole common shareholder, Michael Kelly. All profit was reinvested in the banks or the community.

B. Fannie Mae and Freddie Mac

1. Background and Share Structure

25. Fannie Mae was chartered by Congress in 1938. It was privatized in 1968 under the Housing and Urban Development Act of 1968. Freddie Mac was chartered by Congress in

1970. It was privatized in 1989 under the Financial Institutions Reform, Recovery, and Enforcement Act. Both Fannie Mae and Freddie Mac were created to provide increased liquidity and stability to the secondary mortgage market by securitizing mortgage loans as mortgage-backed securities.

26. As for-profit, publicly traded companies, Fannie Mae and Freddie Mac were able to raise funds from the private capital market. Both were traded on the New York Stock Exchange until June 2010. Immediately prior to the conservatorships, Fannie Mae had more than 597 million preferred shares in 17 different series (with a total redemption value of approximately $21 billion) and one billion common stock shares outstanding (with a value of more than $7 billion). Freddie Mac had more than 464 million preferred shares in 24 different series (with a total redemption value of approximately $14 billion) and approximately 650 million common stock shares outstanding (with a value of approximately $3.3 billion).

27. Preferred GSE shares, like those purchased by FBOP, had certain rights attached. For example, shareholders had the right to receive a portion of the company's assets in the event of liquidation or dissolution. They also had the right to receive (and did receive) dividend payments. Shareholders were also entitled to vote on amendments to the certificate of designation for their share series. Finally, shareholders had the right to transfer their shares.

2. Pre-2008 Regulation and Investment Incentives

28. Up until 2008, the GSEs were regulated under the terms of the shareholder-friendly Federal Housing Enterprises Financial Safety and Soundness Act of 1992 ("***1992 Act***"). The 1992 Act established the Office of Federal Housing Enterprise Oversight ("***OFHEO***") as the chief regulator of the GSEs. It also set capital requirements. The 1992 Act gave OFHEO the power to undertake safety and soundness examinations of the GSEs, as well as various enforcement powers, including conservatorship. It delineated the specific circumstances under which OFHEO had the

authority to place the GSEs into conservatorship, however, including by the consent of a majority of either the company's shareholders or board of directors, and in the event of significant or critical undercapitalization. There was no receivership mechanism under the 1992 Act. The 1992 Act provided certain shareholder protections which included a reasonable economic return, that regulators must ensure the GSEs were adequately capitalized and operating safely, mandatory and discretionary exit from conservatorship and a prohibition against a conflict of interest by the conservator.

29. Under 2006 Consent Agreements with OFHEO, the GSEs were subject to increased capital requirements. To meet these requirements, the GSEs issued new series of preferred shares. The Government established regulatory incentives targeted at community banks to encourage them to purchase the preferred shares. At the time FBOP purchased its GSE shares, GSE preferred shares were considered an attractive investment with relatively high yields and very low risks.

30. There were strong government incentives to invest in the GSEs in order to recapitalize the GSEs under the 2006 Consent Agreements. These incentives were provided by the Treasury, the Office of the Comptroller of the Currency ("***OCC***"), the Office of Thrift Supervision ("***OTS***"), the Federal Reserve and the Federal Deposit Insurance Corporation ("***FDIC***"). Significantly, the Comptroller's 2008 Handbook was in effect a marketing brochure for GSE preferred shares identifying the many incentives for banks to buy GSE preferred stock. Among the government incentives, national banks could invest, "without limitation," in perpetual GSE preferred stock—banks are not allowed to invest in equity instruments while U.S. Government and Agency bonds are the other asset a bank may invest in without dollar limitations; the FDIC permitted banks to invest up to 100% of their Tier 1 capital in GSE preferred securities while other investments were generally restricted to 10% of Tier 1 capital; GSE stock was

considered to be relatively risk-free; National banks assigned a 20% capital risk weighting for GSE stock—the same risk weighting for U.S. Agencies bonds, AAA rated investments or cash—while most other investments had a 50% or 100% risk weighting; the FDIC provided that investments in GSE preferred securities does not represent a significant risk to the Deposit Insurance Fund; banks also received a special tax advantage under IRS rules where GSE preferred share dividends were eligible for a 70% tax deduction; and GSE preferred stock was perceived by the market to have the implicit guarantee of the U.S. Government.

31. At the time that FBOP acquired its investments, GSE stock was rated "AA-" by S&P; "A1" by Moody's; and "A+" by Fitch. Regulators assigned national banks like FBOP a 20% capital risk weighting for GSE preferred stocks, which is the same risk weighting as U.S. bonds or cash. There was no relevant reporting from the Securities and Exchange Commission that would enable investors to make any independent analysis of the GSEs, as is available with other types of investments.

32. Due to strong Government incentives, FBOP Subsidiaries and River Capital were not alone in investing substantial capital in GSE preferred securities. Many other banks were similarly incentivized to make such investments.

C. FBOP's Investments

33. Convinced by these incentives, in late 2007 and early 2008, FBOP Subsidiaries purchased preferred stocks in the GSEs. These shares had a Combined Net Book Value of $898,448,392 as of September 10, 2008.

34. FBOP Subsidiaries and River Capital purchased Series O Fannie Mae preferred stock. Series O stock had a dividend rate of 7% and a liquidation preference of $50.00 per share. Holders of Series O shares had the right to vote on proposed changes to the terms of their stock series.

FBOP Subsidiary Series O Fannie Mae Preferred Stock Share Holdings and Share Values as of September 10, 2008			
Name of Bank	**Book Value of Shares**	**Book Value Per Share**	**Number of Shares**
Park National Bank	$63,389,491	$49.14	1,290,000
California National Bank	$157,364,390	$51.77	3,039,618
San Diego National Bank	$84,699,020	$48.62	1,742,071
Pacific National Bank	$42,640,605	$52.50	812,202
North Houston Bank	$21,258,917	$42.52	500,000
Madisonville State Bank	$11,884,833	$42.45	280,000
Bank USA	$5,090,000	$42.42	120,000
Citizens National Bank	$2,546,750	$42.45	3,039,618
River Capital Advisors, Inc. [FBOP Non-Bank Holding]	$4,992,333	$42.67	117,000

35. In addition, California National Bank purchased 1,600,000 shares of Series S preferred stock in Fannie Mae, which as of September 10, 2008, had a total book value of $40,056,000, and a per share book value of $25.04. Series S stock had a dividend rate of 8.25% and a liquidation preference of $25.00 per share. Holders of Series S shares had the right to vote on proposed changes to the terms of their stock series.

36. FBOP Subsidiaries and River Capital purchased Series Z preferred stock in Freddie Mac. Series Z stock had a dividend rate of 8.375% and a liquidation preference of $25.00 per share. Holders of Series Z shares had the right to vote on proposed changes to the terms of their stock series.

FBOP Subsidiary Series Z Freddie Mac Preferred Stock Share Holdings and Share Values as of September 10, 2008			
Name of Bank	**Book Value of Shares**	**Book Value Per Share**	**Number of Shares**
Park National Bank	$48,804,368	$25.69	1,900,000
California National Bank	$237,400,318	$25.87	9,176,900
San Diego National Bank	$86,455,926	$25.71	3,363,100
Pacific National Bank	$41,656,000	$25.40	2,452,202
North Houston Bank	$25,000,000	$25.00	1,000,000
Madisonville State Bank	$14,000,000	$25.00	560,000
Citizens National Bank	$3,000,000	$25.00	120,000
Bank USA	$6,000,000	$25.00	240,000
River Capital Advisors, Inc. [FBOP Non-Bank Holding]	$2,209,441	$16.37	135,000

37. Government regulators were aware that FBOP Subsidiaries had invested a substantial portion of their Tier 1 capital in the GSE preferred shares, and never raised any concerns.

38. Absent Government incentives, FBOP Subsidiaries and River Capital would not have made such a substantial investment in GSE stock.

D. Financial Crisis and Imposition of the Conservatorships

1. HERA Allowed the FHFA to Impose a Conservatorship Only if Specific Statutory Requirements Were Satisfied

39. At the end of 2007, the U.S. economy went into decline. To shore up the mortgage market, HUD increased the GSEs' Government-mandated affordable housing goals and required them to devote a larger share of their business to offering low interest mortgages.

40. The Government began to take steps that undermined market confidence in the GSEs in order to manufacture grounds for their nationalization. On February 13, 2008, Congress raised the conforming loan limits for the GSEs to $729,750. This increased the exposure of the GSEs to subprime loans and thereby threatened their financial health. As the then-Director of the FHFA acknowledged, the GSEs "have been reducing risks in the market but concentrating mortgage risks on themselves."

41. On March 10, 2008, Barron's published a critical article about Fannie Mae that suggested the company was insolvent. The article was sourced by the White House with full knowledge of the Treasury. As detailed by the Financial Crisis Inquiry Commission ("***FCIC***"), in advance of the article, a member of the Bush administration sent the Undersecretary to the Treasury (via email) a report identified as the source for the Barron's article, stating that the report should be used to "help inform potential internal Treasury discussions about the potential costs and benefits of nationalization."

42. On March 19, 2008, OFHEO (at Treasury's behest) eased capital restraints on the GSEs in exchange for the agreement of the GSEs to raise significant capital at some undetermined point in the future. This change exacerbated the accumulation of high-risk holdings by the GSEs. Requiring the GSEs to take such risky steps reveals, in hindsight, that the Government was laying the groundwork to impose a conservatorship apart from whether conservatorship could be lawfully

imposed under HERA. As detailed by author Timothy Howard in *The Mortgage Wars*, the former CFO of Fannie Mae later stated that Treasury Secretary Henry Paulson's "action to not just allow but actually encourage Fannie Mae and Freddie Mac to add new mortgages with no firm commitment to raise capital to back them is understandable only if by then he had concluded that Treasury would be able to use the road map from the GSE insolvency paper . . . to put the GSEs into receivership or conservatorship."

43. Although not publicly revealed until 2011, throughout the summer of 2008, the Government continued to destabilize the GSEs through press leaks and leaks to Wall Street executives and hedge fund managers that GSE conservatorship was imminent. This included a meeting between Secretary Paulson and Wall Street executives before the passage of HERA in which Secretary Paulson revealed that the GSEs would be placed into conservatorship. Barron's published a second article based on information from White House sources predicted an imminent takeover of the GSEs on August 18, 2008. As discussed below, the Government takeover did not occur immediately as Secretary Paulson tried to suggest in the leaks. Furthermore, there were no statutory grounds to impose a conservatorship. But these leaks, as the Government intended, caused GSE share price to drop significantly. This is classic governmental conduct preceding a governmental nationalization or massive expropriation.

44. Throughout this period, Government officials and regulators made repeated public statements, in contrast to what hedge funds were told in private, emphasizing the sound financial status of the GSEs. On March 31, 2008, for example, the Director of OFHEO classified the GSEs as adequately capitalized. On July 10, 2008, Secretary Paulson and Chairman of the Federal Reserve Ben Bernanke testified before the House of Representatives that both GSEs were adequately capitalized, and the Director of the OFHEO issued a news release stating the same.

Secretary Paulson specifically emphasized that there was no sudden deterioration in conditions at the GSEs that motivated their support for HERA.

45. On July 24, 2008, with Treasury's support, HERA was enacted. HERA established the Federal Housing Finance Authority to regulate and supervise the GSEs. HERA gave the FHFA greater regulatory authority than the OFHEO held under the 1992 Act.

46. Despite the government incentives discussed above, encouraging investors such as the FBOP Subsidiaries and River Capital to purchase GSE preferred shares, proposed protection for individual shareholders who had been holding preferred stock in Fannie Mae and Freddie Mac did not pass Congress. Congressman Barney Frank, then chairman of the House Financial Services Committee, stated that the treatment of preferred stocks in Fannie Mae and Freddie Mac arose during the negotiations of the 2008 Act. Concern focused on community banks and individual investors who had purchased preferred shares and would be affected by the legislation. In a letter to constituents on the financial crisis dated October 11, 2008, Congressman Frank explained his proposal: "At my urging, in order to ensure that community banks and other institutions holding the preferred stock of Fannie Mae and Freddie Mac receive some protection, the bill allows losses from such preferred stock to be treated as ordinary loss for tax purposes." Congressman Frank also explained why his proposal did not become law: "While I fought also for inclusion in the bill of protections for individual investors who had been holding preferred stock in Fannie Mae and Freddie Mac, this set of issues falls under the jurisdiction of the Ways and Means Committee, rather than the Financial Services Committee. As a result, I had less influence over the final form of that part of the bill, and despite my efforts, the bill does not include protections for individual investors who held preferred stock in either of the two companies."

47. As detailed in the Kelly Statement, Congress passed the legislation providing assistance to community banks holding preferred shares that would have allowed carryback provisions for GSE losses. On February 12, 2009, the congressional budget conference committee eliminated the five-year net operating loss carryback provisions for all but small business entities. The carryback provisions for GSE losses, which had previously passed both houses, would have resulted in $200 million of additional capital for the FBOP Subsidiaries.

48. HERA required notice and an opportunity for hearing to establish that the GSEs were in an unsafe or unsound financial condition. HERA also permitted the FHFA to become either conservator or receiver for the GSEs only under specified conditions: (A) if the GSE's assets were less than its obligations to its creditors and others; (B) if the GSE had experienced substantial dissipation of assets or earnings due to violation of the law or unsafe or unsound practices; (C) if an unsafe or unsound condition to transact business exists; (D) if there is any willful violation of a final cease and desist order; (E) concealment by a GSE of its books or refusal to submit the books for inspection; (F) if the GSE was unlikely to be able to meet its obligations or the demands of its creditors; (G) if the GSE had incurred or was likely to incur losses that would deplete all or substantially all of its capital and there was no reasonable prospect of becoming adequately capitalized; (H) if there were violations of law or unsafe or unsound business practices that are likely to cause insolvency or substantial dissipation of assets or earnings or weaken the GSE's condition; (I) upon consent of the board of directors or shareholders; (J) if the GSE was undercapitalized or significantly undercapitalized and either had no prospect of becoming adequately capitalized or failed to become adequately capitalized; (K) if the GSE was critically undercapitalized; or finally (L) if the GSE had engaged in money laundering.

49. Contemporaneous statements from Government representatives and regulators affirm that the purpose of HERA was to strengthen confidence in the GSEs and ensure their stability, not to put them into conservatorship. For example, during the congressional debate addressing enactment of HERA, Senator Isakson (R-GA) stated that the bill represented "an infusion of confidence the financial markets need," and emphasized that the GSEs "are strong."

50. Even after the passage of HERA, the GSEs remained solvent. Fannie Mae declared dividends on its preferred and common stock in August 2008, which it could not do if it was insolvent. In addition, on August 22, 2008, the FHFA notified the GSEs that they were adequately capitalized and exceeded their regulatory capital requirements. There was thus no evidence or suggestion by the Government that the financial situation of the GSEs merited conservatorship.

2. The Conservatorships Were Imposed in Violation of HERA by Coercing the Boards' Consent

51. Despite the foregoing, on September 6, 2008, the Government moved to place both GSEs into conservatorship. The GSEs were blindsided. Although the FHFA claimed that it imposed the conservatorship only after receiving consent from the boards of both GSEs, as set forth below, that consent was based on misinformation, coercion, and threats of economic harm. It was therefore involuntary.

52. The final decision in regard to the GSE future came during a series of marathon meetings over Labor Day weekend at the Treasury. Attendees included Secretary Paulson; a dozen Treasury officials; Chairman Bernanke; Federal Reserve Governor Kevin Warsh; the Federal Reserve general counsel; Art Murton of the FDIC, a top banking official; Morgan Stanley; Director Lockhart and Mr. Lockhart's team, which included FHFA outside legal counsel from Arnold & Porter and Wachtell, Lipton, Rosen & Katz phoning in from New York. According to Secretary Paulson's memoir *On the Brink, Inside the Race to Stop the Collapse of the Global Financial*

System, Sheila Bair, chairperson of the FDIC, sent her best examiner to "help write the case" and finally Director Lockhart "managed to get his examiners to sign off on what [... was] needed. Either [... Director Lockhart] had worn those examiners down *or they had come to realize that immediate conservatorship was the best way for them to resolve this dangerous situation with their reputation intact* (emphasis added)." Treasury Secretary Paulson stated in regard to the FHFA, "They needed to be led to the conclusion they know was right. Doing so would in effect overturn the work they'd done for years." On September 4, 2008, the FHFA wrote to the boards of the GSEs and informed them that they were undercapitalized and required immediate recapitalization. The FHFA did not give the GSEs any time to address the concerns, however, raised in these letters.

53. In *On the Brink*, Secretary Paulson recalled that he met with President George W. Bush a mere three days before the conservatorships and informed him: "We're going to move quickly and take them by surprise. The first sound they'll hear is their heads hitting the floor." He acknowledged that the plan was to "ambush Fannie and Freddie" "[f]or the good of the country." Had they attempted to discuss the plan with the GSE boards, Secretary Paulson knew "they'd fight." Lacking the necessary statutory basis to impose a conservatorship based on the GSEs' financial condition, the Government had to rely on another statutory basis: consent of the GSE boards. The only way the Government could gain their consent was to take them by surprise and quickly coerce their agreement.

54. As also detailed in *On the Brink*, on September 5, 2008, Paulson, Bernanke, and Lockhart met with representatives of the GSEs and directed them to give their consent to conservatorship. If they did not agree, "we would seize them." In that meeting, Paulson falsely informed the GSE executives that the Government "ha[d] the grounds to do this on an involuntary basis, and we will go that course if needed." He made clear that "[a]ny Treasury investment would

be conditioned on conservatorship." The FCIC later concluded that "[e]ssentially the GSEs faced a Hobson's choice: take the horse offered or none at all."

55. As also detailed in *On the Brink*, Paulson indicated that he would go after the GSE leadership personally if they did not agree. He told the boards that if they consented to conservatorship, he would make clear that they were not to blame: "Obviously we preferred that they voluntarily acquiesce. But if they did not, we would seize them. . . . I left unspoken what I would say publicly if they didn't acquiesce." Those present at the meetings reported that the Government suggested that if they did not agree their reputations were at risk.

56. The Government was able to take advantage of the terms of HERA, which provided that the board "shall not be liable to the shareholders or creditors of the regulated entity for acquiescing in or consent" to conservatorship. 12 U.S.C. 1367(a)(6).

57. On September 6, 2008, the boards of the GSEs met and, as the Government gave no choice but to do, agreed to conservatorship. Daniel Mudd, the former CEO of Freddie Mac, later gave a speech in which he stated that "we were given 24 hours to accede to a government takeover—or else the government would effectively go to war against the company." Mudd made clear that the Government's approach was not regulatory practice, as he was not afforded any opportunity to address the Government's concerns. Rather, as detailed by the FCIC, the Government's plain goal "was really to force conservatorship."

58. Although there are other statutory bases on which the FHFA can impose conservatorship, if the conditions are found to be met, the FHFA explicitly states on its public

website that the GSEs "were placed into conservatorship upon the consent of each board of directors," not on any other statutory basis.[2]

59. Consent based on coercion, false information, and improper threats, like those to which the GSE boards were subjected, is invalid.

60. Neither the GSE boards nor the GSE shareholders had any advance notice of the Government's plan. The Government did not express any concerns about the solvency of the GSEs that they could have addressed or provide them with any information whatsoever. To the contrary, at all times prior to imposing conservatorship, the Government in public repeatedly expressed its confidence in the financial health of the GSEs. The Government's surprise attack reflected an effort to strong arm the GSE boards into consent since the Government knew it could not impose conservatorship on any other statutory basis.

61. The other statutory bases for conservatorship were not satisfied. Although the GSEs had experienced some financial losses, they remained solvent and adequately capitalized. On August 22, 2008, the FHFA sent letters to the GSEs stating that they were adequately capitalized and exceeded regulatory capital requirements. Likewise, on August 25, 2008, the respected investment firm BlackRock, retained by the Government to offer an independent opinion, concluded that Freddie Mac's "long-term solvency does not appear endangered—we do not expect Freddie Mac to breach critical capital levels even in stress case." FHFA Director Lockhart later admitted to the FCIC that "[Fannie Mae] was adequately capitalized the day we put them into conservatorship." Andrew Ross Sorkin of the New York Times stated that the takeover of the GSEs happened in an "odd way" as there didn't appear to be an actual crisis—auctions were

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[2] *See* https://www.fhfa.gov/Conservatorship (last visited Sept. 29, 2021).

taking place and the GSEs were able to sell paper. Mr. Sorkin suggested that it seemed almost as if this decision had been made a month ago and that the prior month "was all theater."

62. At the time conservatorship was imposed on the GSEs, Fannie Mae's excess core capital was $9.4 billion and Freddie Mac's was $2.7 billion. Contemporary reporting affirmed that the GSEs were not in crisis. Sorkin of the New York Times wrote that "[e]ven if neither raises another dollar of capital over the next year, we estimate that both companies will likely remain above their statutory minimum requirements."

63. Subsequent forensic accounting reports have reached the same conclusion: the GSEs were solvent in September 2008. The Government used non-cash accounting adjustments to create a false impression that the GSEs were insolvent because they thought conservatorship, as detailed below, would facilitate two objectives: (1) reassuring foreign governments holding GSE debt; and (2) shoring up the nation's mortgage market at a time of severe economic crisis. Neither objective provided grounds for imposing a conservatorship under HERA.

64. The GSEs' assets were significantly greater than their liabilities at the time the conservatorships were imposed. As of June 30, 2008, Fannie Mae had $344.8 billion of short-term assets, which far exceeded the GSE's $247.0 billion in short-term liabilities. Freddie Mac had $745.4 billion of short-term assets and $356.4 billion in short-term debt.

65. The GSEs' assets were increasing. From December 31, 2005, to June 30, 2008, Fannie Mae's assets increased from $834.1 billion to $896.6 billion. Fannie Mae's earnings increased in the first half of 2008 over earnings in the second half of 2007. Freddie Mac's assets grew from $798.6 billion to $879.0 billion.

66. Fannie Mae's core capital exceeded the FHFA-directed and statutory minimum capital requirement and its total capital exceeded its required risk-based capital. Freddie Mac's

total capital exceeded its statutory risk-based capital requirement. Each GSE was in full compliance with all capital requirements established by OFHEO.

67. Given the recognized solvency of the GSEs, the purpose of the conservatorships was not to save the GSEs, but rather to nationalize them to reassure foreign governments holding GSE debt and to shore up the nation's mortgage market at a time of severe economic crisis. Although neither objective provided grounds for imposing a conservatorship under HERA, the forced nationalization enabled the Government to ensure that the GSEs continued to take on toxic mortgage debt from other financial institutions and thereby inject liquidity into the mortgage market. The Government sacrificed shareholders such as the FBOP Subsidiaries and River Capital to facilitate these policy goals despite lack of statutory grounds for imposing the conservatorships.

3. The Conservatorships Eliminated Shareholder Rights and Destroyed Shareholder Value

68. On September 7, 2008, the Treasury and the GSEs entered into SPSPAs whereby Treasury invested billions of dollars into the GSEs in exchange for $1 billion in senior preferred shares. These senior preferred shares also included a liquidation preference and dividend rights. The SPSPAs thereby ensured that the GSEs remained under Government control and would never return to their previous status as shareholder-owned companies.

69. As analyst Derek Pilecki suggested, the dividends paid on the Treasury draws became, by the Government's design, deliberately worthless—to the shareholders. Mr. Pilecki stated: "I call the dividend payments on the Treasury's senior preferred stock Zombie Dividends because Treasury Secretary Paulson wanted the GSEs dead at the time he put them into Conservatorship. He forced them to pay a 10% dividend rate to the Treasury on its senior preferred stock investment. No other financial institution has had to actually pay to the government a 10% rate like the GSEs have."

70. As with any other publicly traded company, owners of Fannie Mae and Freddie Mac stock were vested with specific rights attendant to their ownership. These rights were specifically enumerated in each GSE's by-laws and the prospectuses and registration statements for each GSE's common stock and series of preferred stock.

71. The by-laws and offering documents for Fannie Mae's and Freddie Mac's common stock enumerated specific rights held by each GSE's common shareholders, and these rights were typical of those rights usually associated with the private property interest represented by common stock in a shareholder-owned company. For example, these included the right of the GSEs' common shareholders to transfer their shares of stock and to vote for candidates for boards of directors and shareholder proposals. The owners of Fannie Mae's and Freddie Mac's common stock also had the right to receive a portion of the GSEs' assets in the event of dissolution or liquidation.

72. The offering documents for Fannie Mae's preferred stock enumerated specific rights held by its preferred shareholders typical of those rights often held by preferred stockholders in a shareholder-owned company. For instance, these shares were transferrable. Likewise, the offering circular for Fannie Mae's Series T preferred shares, like numerous other series of its preferred stock offerings, indicated that holders of those shares would have the right to receive a portion of Fannie Mae's assets in the event of dissolution or liquidation. In addition, Fannie Mae preferred shareholders had the right to vote on amendments to their series' certificate of designation, subject only to narrow exceptions.

73. Similarly, the offering documents for Freddie Mac's preferred stock enumerated specific rights held by its preferred shareholders typical of those rights often held by preferred stockholders in a shareholder-owned company. For instance, these shares of preferred stock were

transferrable. Likewise, the offering circular for Freddie Mac's Series Z preferred shares, like numerous other series of its preferred stock offerings, indicated that holders of those shares would have the right to receive a portion of the Freddie Mac's assets in the event of dissolution or liquidation. In addition, Freddie Mac preferred shareholders had the right to vote on amendments to their series' certificate of designation, subject only to narrow exceptions.

74. The GSEs were ordered to cease paying dividends on their preferred and common stock. Although this stock would remain outstanding, on June 16, 2010, the FHFA ordered the GSEs to delist their common and preferred shares from the New York Stock Exchange. The loss of rights and value suffered by shareholders on account of the Government's actions is noted in Fannie Mae's Form 10-K for the year ending December 31, 2011, issued under the FHFA's control: "Because we are in conservatorship, our common shareholders currently do not have the ability to elect directors or to vote on other matters. The conservator eliminated common and preferred stock dividends (other than dividends on the senior preferred stock issued to the Treasury) during the conservatorship, and we are no longer managed with a strategy to maximize shareholder returns."

75. The unlawful imposition of conservatorships under HERA also destroyed the economic value of the shares. On September 8, 2008, Fannie Mae common stock shares closed trading at $0.73 per share. Freddie Mac common stock shares closed trading at $0.88 per share. The preferred shares' book value dropped from approximately $50.00 (for Fannie Mae) and $25 (for Freddie Mac) to $3.00. The conservatorships rendered the shares effectively worthless.

76. The Government offered no compensation to GSE shareholders despite its seizure of shareholders' voting and dividend rights, and the utter destruction of share value that resulted directly from its actions. Indeed, as detailed in his memoir *On the Brink,* Secretary Paulson himself

stated that "[c]ommon and preferred shareholders alike were being wiped out." Furthermore, the Government had no plan to restore their lost property. Again, Secretary Paulson admitted as much in *On the Brink* when he informed shareholders that "the odds were low that they would ever recapture the equity value that had been lost" and admitted that "we'd basically killed the shareholders" of the GSEs.

4. Foreign Investment in the GSEs Pressured the Government to Impose Conservatorships Despite the Lack of Any Ground Under HERA

77. The ratings agencies and investors had high confidence in the security of GSE stock because of the Government's open support for the GSEs. A number of foreign governments had significant holdings in GSE debt— Japan held $120 billion, Russia held $170 billion and China held $350 billion. These foreign governments had purchased GSE debt with the understanding that the GSE debt was guaranteed by the U.S. Government. The Government has since acknowledged the ambiguities leading investors to purchase what they believed to be low-risk, government guaranteed securities.

78. On September 7, 2008, the day after the Government imposed the conservatorships, Secretary Henry M. Paulson, Jr. made a public statement referring to "the ambiguities in the GSE Congressional charters, which have been perceived to indicate government support for agency debt and guaranteed mortgage-backed securities." On September 24, 2008, in a speech to the nation, President Bush acknowledged that "[b]ecause [… the GSEs] were chartered by Congress, many believed they were guaranteed by the federal government." Following the failure of Bear Stearns in March 2008, representatives of the governments holding significant GSE debt asked Treasury officials to explicitly confirm this understanding. An explicit guarantee would have placed the GSEs on government books and doubled the U.S. deficit—a politically untenable solution.

79. China was the largest external investor in the GSEs. As reported by BBC News, Secretary Paulson was in close and regular contact with the Chinese Government as he "didn't want them to dump the [GSE] securities on the market and precipitate a bigger crisis." Secretary Paulson learned Russian officials had urged the Chinese Government to sell off GSE holdings to force the U.S. Government to guarantee GSE debt.

80. A sell-off would cause significant harm to the U.S. economy in the midst of the financial crisis. A sell-off by Russia began in January 2008, followed by a sell-off by China in July 2008. According to Benn Steil, an analyst with the Council on Foreign Relations, during this sell-off, "the yield spread between GSE debt and U.S. Treasury debt soared. From 2003 to 2007 it averaged 34 basis points. When Russia started selling GSE debt in January 2008, it stood at 57 basis points. When China started selling in July 2008, it hit 86 basis points. As GSE debt was widely used as collateral in the U.S. repo market, the rising spread forced U.S. financial institutions to pony up more and more securities to support their borrowing." Steil added that this sell-off "exacerbated the growing credit crunch."

5. The Government Bypassed Lawful Options to Impose the Conservatorships

81. The Government had lawful options, other than an unlawful imposition of conservatorship. The lawful options would have reassured foreign governments with significant GSE holdings and prevented a sell-off of GSE debt.

82. The Government could have expressly guaranteed GSE debt for a fee. In fact, according to the FCIC, the Treasury had "guarantee legislative language" on stand-by and stated an express guarantee could be executed swiftly. An express guarantee would have placed the GSEs on government books and doubled the U.S. deficit—a politically untenable solution at the time.

83. The Government also had the option to nationalize the GSEs. Nationalization would require including GSE operations in the federal budget, effectively doubling the U.S. deficit—a politically untenable solution at the time. Furthermore, nationalization would require compensation of GSE shareholders. Because an explicit guarantee and nationalization were politically untenable solutions, Treasury needed to find a way to induce these governments to continue holding and buying GSE debt without issuing the explicit guarantee demanded by foreign governments or nationalizing the GSEs.

84. The imposition of a perpetual conservatorship was seen as the answer to this problem. As former Secretary Paulson stated to the media in 2014, the Chinese sell-off of GSE debt "just drove home to me how vulnerable I felt until we had put Fannie and Freddie into conservatorship." Following the imposition of conservatorship, China would later increase GSE holdings to $430 billion, which would help to support the U.S. economy in the midst of the financial crisis.

E. FBOP Subsidiaries and FBOP Failed Due to the Conservatorships' Destruction of Shareholder Value

85. As detailed in the Kelly Statement, prior to the imposition of the conservatorships, Plaintiffs enjoyed a strong financial position. The FBOP Subsidiaries were all well-capitalized. Regulators recognized FBOP's sound financial state. For example, immediately prior to the conservatorships, FBOP had received approval by three regulatory agencies to acquire a $3 billion problem financial institution in Southern California. Indeed, FBOP's position was so sound that the corporation received those approvals within forty-eight hours.

86. But the conservatorships of the GSEs proved catastrophic for Plaintiffs. As noted above, the FBOP Subsidiaries immediately lost their voting and dividend rights. The value of their shares dropped from $896 million to less than $1 per share. They were consequently unable to

meet their capital requirements. There was never any suggestion on the part of any regulator that FBOP's problems resulted from any mismanagement or undue risk FBOP had taken. Regulators understood that FBOP's crisis resulted directly from the GSE conservatorships.

87. The Government was aware of the destruction the conservatorships wrought on banks they had previously encouraged to invest in GSE stock. To that end, the Government created TARP, a loan program for banks.

88. The Comptroller of the Currency, John C. Dugan, contacted Mr. Kelly personally by phone the day before TARP was announced on October 14, 2008. The Comptroller called to inform Mr. Kelly that TARP funding would be available. The Comptroller urged Mr. Kelly to immediately seek the TARP funding. Comptroller Dugan explained that "this is the solution—this is designed for you."

89. As detailed in the Kelly Statement, on September 9, 2008, FBOP had "began to work with its investment bankers […] in an effort to raise $600 million in capital to offset the [… GSE] losses. In later September and early October, […] FBOP met with a series of potential investors. Despite the market's general antipathy at the time for bank capital instruments, the FBOP story resonated with investors and was favorably received." With "the announcement of the [… TARP] in October 2008 and the encouragement of the regulators that TARP funds would be available to help recapitalize FBOP led [… FBOP] to believe that [… a solution had been found to the] GSE losses."

90. As detailed in the Kelly Statement, FBOP began to focus on obtaining TARP funding in light of the TARP special provisions giving preference to financial institutions which suffered losses on GSE holdings. Also, an unintended consequence of TARP was that private

capital and debt markets froze and obtaining private capital infusions for institutions such as FBOP became impossible.

91. As detailed in the Kelly Statement, FBOP applied for TARP funds on October 14, 2008. On October 20, 2008, FBOP received a verbal assurance from the OCC that its application had been approved. However, on October 21, 2008, its application was deferred because FBOP, unlike the other large banks that applied for funding, was not publicly traded. The OCC advised that FBOP would have to wait until the next round of TARP funding.

92. On November 17, 2008, the Treasury issued TARP guidelines for non-publicly traded institutions. FBOP resubmitted its application. FBOP was again deferred with regulators requesting additional information. When the new administration took office in January 2009, TARP was suspended. By the time the program reopened, FBOP's situation had deteriorated and FBOP no longer meet TARP criteria.

93. FBOP attempted to find additional capital throughout 2009 in a "capital market that had been unreceptive to privately held bank capital needs, particularly for organizations stigmatized by not receiving TARP. Furthermore, regulators were unreceptive. For example, shortly before the closure of the FBOP Subsidiaries, FBOP attempted to inject $40 million from a separate funding institution under the FBOP umbrella, Treemont Capital. As a bank holding company, FBOP's sole purpose was to support the FBOP Subsidiaries. Therefore, FBOP took capital from Treemont, an FBOP non-bank subsidiary, to transfer that capital to the FBOP Subsidiaries in order to meet the capital requirements of the FBOP Subsidiaries. The OCC disallowed the capital as not meeting regulatory approval. The OCC then refused to return the $40 million in Treemont capital to the non-bank subsidiary.

94. Likewise, in October 2009, FBOP asked for a one-week extension from the FDIC head of liquidation in Chicago, in anticipation of the passage of the Workers, Homeowners, and Business Assistance Act of 2009. The legislation would have would have allowed FBOP to carry back the GSE losses for five years, resulting in the realization of approximately $200 million of additional capital for the FBOP Subsidiaries. The FDIC denied the FBOP request for a one-week extension. One week later, as expected, on November 6, 2009, the Workers, Homeowners, and Business Assistance Act of 2009 would be signed into law.

95. On October 30, 2009, seven of the nine FBOP Subsidiaries were placed in receivership by the FDIC. The two remaining FBOP Subsidiaries were healthy and viable. The FDIC invoked *rarely used* cross guaranty authority to place the two remaining FBOP Subsidiaries in receivership. The cross guaranty was intended to mitigate FDIC costs and prevent abuses that had occurred during the thrift crisis when holding companies moved bad assets to troubled banks and allowed "good banks" to flourish. This situation did not apply to FBOP. Its problems were directly related to unexpected GSE losses and not concentrating bad assets in troubled banks. According to the Board of Governors of the Federal Reserve System, the FDIC had "issued cross-guaranty liability assessments related to eight banks from 1989—1992 with none again until FBOP." On October 30, 2009, the FDIC entered into a purchase and assumption agreement with U.S. Bank, to assume all of the deposits and essentially all of the assets of the nine FBOP Subsidiaries.

96. Ironically, on the exact same day, Treasury Secretary Geithner was in Chicago to award $50 million in investment tax credits for worthy projects which provided substantial community benefit. The investment tax credits were awarded to FBOP and Park National Bank and presented personally to Mr. Kelly in recognition of FBOP's community efforts.

97. FBOP was rendered insolvent due to the failure of the FBOP Subsidiaries. Due to this insolvency, FBOP was forced to liquidate assets. FBOP was forced to sell the $40 million in GSE shares held by River Capital in January 2009.

98. On October 5, 2012, FBOP entered into the ABC Agreement, whereby FBOP assigned charters, articles of incorporation, corporate records, stock certificates, ownership, and/or indicia of ownership, of its subsidiaries, and other assignable assets, to an ABC Trust for the benefit of FBOP creditors.

99. The ABC Trustee liquidated and distributed significant proceeds to beneficiaries of the ABC Trust. Subsequent to distribution of all other monetizable assets of FBOP's former subsidiaries, all charters, articles of incorporation, corporate records, stock certificates, ownership, and/or indicia of ownership, of FBOP's former subsidiaries, reverted back and/or were assigned to FBOP. To the extent initially transferred to the ABC Trust, if at all, any and all claims arising out of or related to ownership, valuation, control or use of common or preferred stock interests issued by either GSE that could have been brought by FBOP's former subsidiaries also reverted back and/or were assigned to FBOP. FBOP currently owns and controls 100% of all interests, if any, in former subsidiaries, and owns and controls all rights to assert any and all claims arising out of or related to ownership, valuation, control or use of common or preferred stock interests issued by either GSE that could have been brought by FBOP's former subsidiaries.

100. As detailed in the Kelly Statement, FBOP Subsidiaries failed solely due to GSE holdings alone. The collapse of the FBOP Subsidiaries resulted directly and entirely from the imposition of the GSE conservatorship. The Government would later recognize that the failure of FBOP, the FBOP Subsidiaries and River Capital were the direct result of GSE holdings. In fact, during subsequent sworn testimony before Congress, a representative of OCC, FBOP's primary

regulator, did not dispute that it was the imposition of the conservatorship that caused the failure of FBOP, rather than bad lending decisions and practices by FBOP, or other unsound banking practices. Furthermore, in the lawsuit captioned *O'Donnell v. Bank of America*, the Government admitted that the proximate cause of the failure of the FBOP Subsidiaries was the diminution of value in the banks' GSE holdings.[3]

101. In sum, the Government in effect lured investors such as Mr. Kelly into a trap by incentivizing substantial investment in the GSEs and then nationalizing them. The Government thereby eliminated individual and personal shareholder rights such as the right to vote, and destroyed the economic value of the shares. The Government's reasons for imposing conservatorships—to reassure foreign investors with substantial holdings and to shore up the sinking mortgage market—did not provide grounds for imposing a conservatorship under HERA. As a result, Mr. Kelly and other investors with a stake in the GSEs at the time of the abrupt conservatorships lost everything they had invested in the GSEs—in Mr. Kelly's case, virtually his entire net worth.

VI. TOLLING OF THE STATUTE OF LIMITATIONS

102. The six-year statute of limitations governs the timeliness of Plaintiffs' claims. 28 U.S.C. § 2501. Given the proposed class action also before this Court in *Washington Federal v. United States*, No. 1:13-cv-00385, the statute of limitations on Plaintiffs' individual claims for relief below, both direct and derivative, was tolled between June 10, 2013 (the date the original *Washington Federal* complaint was filed) and July 16, 2020 (the date the Court in *Washington Federal* unsealed its Opinion and Order dismissing that action).

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[3] *Edward O'Donnell v. Bank of America*, No. 12-cv-1422, ECF No. 40 at ¶¶153-56 (S.D.N.Y. Oct. 24, 2012) (complaint-in-intervention of the United States of America).

VII. SHAREHOLDER DERIVATIVE ALLEGATIONS

103. The GSEs are controlled by the FHFA, which as conservator has the powers of the board of directors. The unlawful taking was a direct result of Government action, specifically, FHFA and Treasury action. The Government therefore has a clear conflict of interest that renders it unable to bring a claim on behalf of the GSEs. Due to the conflict of interest, a presuit demand to initiate a derivative action would have been futile. In pleading the futility of presuit demand, Plaintiffs reserve their right to amend as necessary to conform with any legal guidance provided in the anticipated opinion in *Fairholme Funds, Inc. v. United States* (Fed. Cir. No. 20-1912 (submitted after argument on Aug. 4, 2021).

104. In bringing shareholder derivative claims in the alternative below, Mr. Kelly will fairly and adequately represent the interests of shareholders or members who are similarly situated in enforcing the rights of the GSEs. This action is not a collusive one to confer jurisdiction that this Court would otherwise lack.

105. Plaintiffs aver that they reasonably believe all factual allegations, made upon information and belief and the investigation of their counsel, will likely have evidentiary support after a reasonable opportunity for further investigation and discovery.

VIII. CAUSES OF ACTION

FIRST CLAIM FOR RELIEF (DIRECT CLAIM) UNLAWFUL TAKING AND/OR ILLEGAL EXACTION IN VIOLATION OF THE UNITED STATES CONSTITUTION

106. Plaintiffs incorporate by reference and reallege each and every allegation of the preceding paragraphs as though fully set forth herein.

107. The Fifth Amendment provides for due process of law and that no private property shall "be taken for public use, without just compensation."

108. In imposing the conservatorships over the GSEs and in taking and/or illegally exacting more than 1 billion shares of the common stock and approximately 597 million shares of the preferred stock of Fannie Mae (with a redemption value of approximately $21 billion) and approximately 650 million shares of the common stock and approximately 464.1 million shares of the preferred stock of Freddie Mac (with a redemption value of approximately $14 billion) without just compensation, the Government destroyed the rights and value of the property interests tied to the common and preferred stock of the GSEs held by Plaintiffs, nullified their reasonable, investment-backed expectations, and violated the fundamental principles of the Due Process and Takings Clauses of the United States Constitution.

109. In taking private property, the Government is required to adhere to due process of law and to respect the legal rights of affected parties.

110. The Government violated the statutory, contractual, and constitutional rights of Plaintiffs in taking and/or illegally exacting virtually all the value of the above referenced preferred shares of both Fannie Mae and Freddie Mac that they owned, without providing just compensation.

111. The conservatorships were not lawfully imposed. The conditions required for conservatorship delineated in HERA were not satisfied. Specifically: (A) both GSEs were solvent as of September 6, 2008; (B) the GSEs had not experienced any substantial dissipation in their assets or earnings due to any legal violations or unsafe or unsound practices; (C) the GSEs were not transacting business under unsafe or unsound conditions; (D) the GSEs had not committed any violations of a cease and desist order; (E) the GSEs had not concealed any records from the FHFA; (F) the GSEs were likely to be able to pay their obligations and meet the demands of their creditors; (G) the GSEs had not and were not likely to incur losses that would have depleted their capital; (H) the GSEs had not committed any violation of any law or used any unsafe practice likely to

cause insolvency or weaken the companies' condition; (J) the GSEs were not undercapitalized without the prospect of becoming adequately capitalized; (K) the GSEs were not critically undercapitalized; and (L) the GSEs had not committed money laundering.

112. The GSEs did not validly consent to the conservatorships. The Government falsely informed the GSEs that they had no choice but to consent or the Government would impose conservatorship regardless. Government officials did not give the boards any meaningful notice. Furthermore, they suggested that the board members would face personal reputational risk if they did not consent. As the boards' consent was based on false information, coercion, and improper threats, it was not a legally valid basis on which to impose a conservatorship.

113. As a holder of $898,448,392 of preferred shares in both GSEs, FBOP Subsidiaries had the right to dividend payments. FBOP Subsidiaries also had voting rights to protect those dividend rights. FBOP Subsidiaries had a property interest in these rights, as well as in the value of the shares themselves. As a holder of approximately $40 million of GSE preferred shares the FBOP wholly-owned non-bank subsidiary, River Capital, had the right to dividend payments. River Capital also had voting rights to protect those dividend rights. River Capital had a property interest in these rights, as well as in the value of the shares themselves.

114. Through the conservatorship, in violation of the Fifth Amendment, the Government seized the rights attached to the shares and rendered the shares effectively worthless. The FBOP Subsidiaries and River Capital were thereby deprived of all use and benefit of their shares. As the shares had been rendered worthless, the FBOP Subsidiaries and River Capital could no longer make economically beneficial use of the shares; their sale value was negligible, particularly since they no longer had voting or dividend rights attached to the shares.

115. When FBOP Subsidiaries and River Capital purchased GSE preferred shares, the banks and non-bank subsidiary had no reason to believe that the Government would impose a conservatorship on the GSEs, let alone a conservatorship that utterly destroyed any share value and terminated voting and dividend rights attached to those shares. The Government had never before done so, even though conservatorships were permitted under the 1992 Act.

116. When FBOP Subsidiaries and River Capital purchased preferred shares, the GSEs were financially sound. In the lead up to the conservatorships, Government representatives had repeatedly affirmed the financial health, including the solvency and adequate capitalization, of the GSEs. FBOP Subsidiaries therefore had no reason to expect that the Government would destroy the value of the investments.

117. By imposing conservatorship on the GSEs, the Government took Plaintiffs' property to facilitate two public policy aims that did not provide statutory grounds for the imposition of conservatorship under HERA: (1) to reassure foreign governments holding GSE debt; and (2) to bolster the sinking mortgage market. The Government never compensated FBOP Subsidiaries or River Capital for the seizure and destruction of their property rights. The Government thereby disproportionately impacted a small group to benefit the public in violation of Plaintiffs' Fifth Amendment rights. Even when the Government takes or illegally exacts private property to serve public purposes, the United States Constitution requires the payment of "just compensation."

118. To the extent Plaintiffs' claims are for illegal exaction, Plaintiffs paid money to the Government, in effect, including in the form of losses on dividends and losses due to the use of the GSEs to facilitate objectives not supporting a conservatorship under HERA and due to the Government's violation of the Fifth Amendment.

119. Plaintiffs suffered harm distinct from that suffered by the GSEs. Plaintiffs' dividend and voting rights are not held by the GSEs; they belong only to shareholders. Furthermore, Plaintiffs were directly harmed by the destruction of their share value because FBOP Subsidiaries and River Capital were placed into receivership as a direct result of the Government's taking of their property rights in the GSE preferred shares.

120. Plaintiffs are therefore entitled to just compensation for the Government's taking of their property and/or illegal exaction in an amount to be determined at trial.

SECOND CLAIM FOR RELIEF (ALTERNATIVE DERIVATIVE CLAIM) UNLAWFUL TAKING AND/OR ILLEGAL EXACTION IN VIOLATION OF FIFTH AMENDMENT TO THE UNITED STATES CONSTITUTION

121. Plaintiffs incorporate by reference and reallege each and every allegation of the preceding paragraphs as though fully set forth herein.

122. In the alternative to a direct taking and/or illegal exaction claim, Plaintiffs make a derivative claim for takings and/or illegal exaction as holders of preferred GSE shares as of the date of the conservatorships.

123. The Fifth Amendment provides for due process of law and that no private property shall "be taken for public use, without just compensation."

124. As a preferred shareholder at the time of the conservatorships, FBOP Subsidiaries and River Capital have standing to bring a derivative claim for unlawful taking and/or illegal exaction on behalf of the GSEs.

125. As CEO and sole common shareholder of FBOP, Mr. Kelly is permitted to bring a derivative claim on behalf of FBOP, the FBOP Subsidiaries and River Capital.

126. Each GSE had a property interest in its net worth, which was decimated by the imposition of the conservatorships.

127. The GSEs are therefore entitled to just compensation for the Government's taking and/or illegal exaction of their property in an amount to be determined at trial.

THIRD CLAIM FOR RELIEF (DIRECT CLAIM)
BREACH OF IMPLIED REGULATORY CONTRACT

128. Plaintiffs incorporate by reference and reallege each and every allegation of the preceding paragraphs as though fully set forth herein.

129. The Government employed a number of incentives to encourage banks to purchase GSE preferred stocks. These included assigning banks a 20% capital risk weighting for the preferred stocks, which was the same risk weighting as U.S. agencies or cash and permitting banks to invest up to 100 percent of their Tier 1 capital in the preferred stocks.

130. Investments in the GSEs served Government interests by injecting capital into the GSEs that could then be used by the GSEs to buy up greater numbers of mortgages, thereby bolstering the housing market. GSE preferred stock came with the strongly implied guarantee that the Government would not allow them to fail and would ensure that the investments rendered the investing banks secure.

131. FBOP Subsidiaries were aware of these regulatory promises and accepted the Government's offer by making an $898,448,392 investment in GSE preferred stocks. River Capital was also aware of these regulatory promises and accepted the Government's offer by making an approximately $40 million investment in GSE preferred stocks. FBOP Subsidiaries and River Capital thereby entered into an implied regulatory contract with the Government.

132. At no point did any regulators express any concerns whatsoever about FBOP Subsidiaries' investments.

133. Despite the incentives and the Government's backing of the GSEs, the Government put the GSEs into conservatorship and destroyed the value of the FBOP Subsidiaries' investment.

Because the FBOP Subsidiaries had put their Tier 1 capital in GSE preferred shares in reliance on the Government's incentives, FBOP Subsidiaries were unable to meet their capital requirements. As a direct result, approximately a year later, the FDIC put the FBOP Subsidiaries into receivership. This took place despite the Government's commitments regarding the safety of the investment and its specific efforts to encourage banks like FBOP Subsidiaries to put their Tier 1 capital in the GSEs. The Government's actions constituted a breach of its implied regulatory contract with FBOP Subsidiaries.

134. Specifically, as detailed above, the Government's breach of implied regulatory contract did not occur over a significant period of time. The Government began providing incentives in 2006; the FPOP Subsidiaries and River Capital purchased GSE shares in 2007 and 2008; Congress passed HERA in July 2008; and the Government imposed the conservatorships in September 2008 and placed the FBOP Subsidiaries and River Capital into receivership in October 2009.

135. As a result of the Government's breach of an implied regulatory contract, FBOP has suffered damages amounting to the enterprise value of FBOP, its Subsidiaries, and River Capital, including lost profits. This value will be determined at trial.

PRAYER FOR RELIEF

WHEREFORE, Plaintiffs demand judgment in their favor on their direct and derivative causes of action against Defendant, the United States of America, as follows:

A. Finding that the Defendant has taken and/or illegally exacted Plaintiffs' private property in violation of the Due Process and Takings Clauses of the United States Constitution;

B. Determining and awarding Plaintiffs damages suffered by them by virtue of the Defendant's taking and/or illegal exaction in an amount to be determined at trial;

C. Determining and awarding Plaintiffs damages for breach of implied regulatory contract;

D. Prejudgment and post-judgment interest, together with any and all further costs, disbursements and reasonable attorneys' and experts' fees; and

E. Granting all other relief as this Court may deem just and appropriate.

DATED: October 1, 2021

By ______________________________

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