

Final Transcript

Investors Unite Pagliara Lawsuit Call

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SPEAKERS

Tim Pagliara
Barr Flinn
Tom Connally
John Yoo

PRESENTATION

Moderator Ladies and gentlemen, thank you for standing by. Welcome to the Investors Unite teleconference call. At this time, all participants are in listen-only mode. Later we will conduct a question-and-answer session with instructions provided at that time. (Operator instructions.) As a reminder, this conference is being recorded.

I would now like to turn the conference over to our host, and executive director of Investors Unite, Mr. Tim Pagliara. Please go ahead.

T. Pagliara Good afternoon, everyone. Thank you for joining us today. I'm happy to bring you up to date on my latest efforts to bring the net worth sweep to an end. Joining me today are my attorneys, Barr Flinn and Tom Connally.

After some brief remarks, we have a special guest, Professor John Yoo from UC Berkeley School of Law. He is going to comment on his recent article in the *San Francisco Chronicle* about when the wall of secrecy in the Fannie Mae case might end. After that, we'll open it up to questions and looking forward to having a really good call for you guys.

I believe it's important to leave no stone unturned in this effort of getting to the truth; therefore, yesterday I filed a complaint in the state courts of both Delaware and Virginia seeking access to the books and records of each company that are relative to the net worth sweep.

This is my right as a stockholder under the state corporate statutes of Virginia which apply to Freddie Mac as well to state laws in Delaware

which apply to Fannie Mae. Each company rejected my written request to review these corporate records earlier in the year. I had no choice but to file suit to demand access to this information as is provided under each state law.

I'm pursuing this litigation in my capacity as an individual shareholder/stockholder of both Fannie Mae and Freddie Mac. The rights of shareholders have been trampled on at every turn in the last few years. Lawyers for the US Government have used every tool they have to impede us from pursuing our rights. As long as this is the case, I will use every tool I have to get to the truth and determine what, if any, actions will be needed down the road to rectify what has occurred under the net worth sweep.

I'm very fortunate to have two very talented attorneys that are backed by an extremely talented team of associates. At this time then, we'll hear from both of them.

First, I'd like to introduce Barr Flinn who will explain the legal basis for the filing of the claim against Fannie Mae in Delaware. Barr is a partner in the firm of Young Conaway Stargatt & Taylor in Wilmington. He is a member of the corporate counseling and litigation section and the former cochair of the litigation and trial section. I am very pleased to have his expertise and skill to represent me in the great state of Delaware. Barr?

B. Flinn

Thank you, Tim. Good afternoon, everybody. We're very excited to be involved in this important litigation and hope that we can add some significant value. As you know, Fannie Mae is a Delaware corporation; it's subject to Delaware law. Under section 220 of the Delaware General Corporation Law, Tim, as a stockholder, is entitled to inspect Fannie Mae's books and records, provided that he has proper purposes.

He has many proper purposes, including to investigate misconduct primarily by the Fannie Mae board but also by treasury and FHFA. To obtain books and records to investigate misconduct, Tim is also required to have credible bases for believing that misconduct occurred, and he has credible basis.

The bases are many and are detailed in the complaint that was filed earlier. At a high level, they concern the Third Amendment of Fannie Mae Senior Preferred Stock Purchase Agreement with treasury. As you know, in the Third Amendment, Fannie Mae agreed, for no return consideration whatsoever, to give its entire net worth in perpetuity to treasury. As you know, this is referred to as a net worth sweep.

Tim's credible basis also concern the payment of the dividends under the net worth sweep and the failure of the Fannie Mae board to take any action to protect Fannie Mae from the harm of the dividends. Under Delaware law, the board may not stand idly by while treasury, Fannie Mae's controlling stockholder, raids Fannie Mae's coffers. The boards' fiduciary duties require it to take action, but the board apparently has done nothing.

Tim's credible basis also involves Fannie Mae's investments in common securitization solutions, the common securitizations platform and the single security. These investments are made to support government policy objectives that Fannie Mae has no obligation to support and that are harmful to Fannie Mae. If the board affirmatively approved the transactions that I just mentioned, it breached fiduciary and statutory duties as well as the certificates of designation for Fannie Mae's junior preferred stock.

If the board did not approve the transactions, it apparently did not oppose them and thereby acquiesced in them breaching the same duties. In all events, the board has affirmative duty to protect Fannie Mae from harm, but it apparently has done nothing to comply with this duty.

While there is much that we all know about the transactions, there's also much about them has not been made public, particularly concerning the board's involvement in them. Tim is seeking to understand better, by the means of these complaints, what the board has been doing.

Tim served Fannie Mae with his demand for books and records on January 19th. The demand set forth Tim's proper purposes and detailed the credible basis for believing that misconduct occurred. The demand fully complied with Section 220 of the Delaware Corporation Law. Nonetheless, the demand was rejected by Fannie Mae through FHFA on January 27th. Fannie Mae rejected the demand on the ground that during FHFA's conservatorship of Fannie Mae, FHFA has succeeded to all the rights of all Fannie Mae stockholders and therefore has succeeded to Tim's inspection rights, thereby divesting Tim of those rights. That's their argument; the argument is completely wrong.

As the courts have repeatedly held, FHFA has succeeded only to the rights of stockholders to act on behalf of Fannie Mae. FHFA has not succeeded to the rights of stockholders against Fannie Mae. It, therefore, has not succeeded to Tim's right to obtain books and records from Fannie Mae.

After Fannie Mae's rejection of Tim's demand for books and records, he was permitted under section 220 under the Delaware Corporation Law to commence a summary court proceeding against Fannie Mae for an order permitting him to inspect Fannie Mae's books and records. He has now commenced such a proceeding by means of the complaint.

Section 220 proceedings are summary proceedings by statute. The Court of Chancery in Delaware typically seeks to resolve them in 45 to 60 days. That's all I have, Tim, so we're back to you.

T. Pagliara

Okay. Thank you, Barr. Next, we're going to hear from Tom Connally. Tom is representing me, not to be outdone, in the great state of Virginia against Freddie Mac. Tom is a partner in the firm of Hogan Lovells in Northern Virginia. He has vast experience in class-action, shareholder and securities litigations and numerous other aspects of corporate law.

I'm going to turn this part of the program over to Tom.

T. Connally

Thanks so much, Tim. Good afternoon, everyone. We filed Tim's complaint against Freddie Mac in the Virginia Circuit Court for Fairfax County, where Freddie Mac is located. Indeed, Freddie Mac's headquarters are just up the street from our own office here in Fairfax.

Just like Fannie Mae, Freddie Mac is a private for-profit corporation with private stockholders and a board of directors governed by Virginia law. Although it's now under the conservatorship of FHFA, Freddie Mac still follows per its own corporate bylaws, and I quote, "The corporate governance practices and procedures of the law of the Commonwealth of Virginia, including, without limitation, the Virginia Stock Corporation Act."

The applicable sections of this statute plainly provide a stockholder with the right to inspect and copy corporate records. Tim, as a stockholder, has made a demand to do just that. That demand was improperly rejected. So we brought suit to enforce Tim's rights as a Freddie Mac stockholder under the Virginia Stock Corporation Act. We're seeking board and accounting records from Freddie Mac relating to the net worth sweep for the same reasons that Barr has described.

We've met the requirements of the statute and under the act, the court should decide the case on an expedited basis. We hope to get the relief that Tim is entitled to very soon.

With that, I'll turn it back over to Tim.

T. Pagliara

Great. Thank you, Tom. Before we open it up to questions, I want to hear from our special late entry guest, Professor John Yoo from UC Berkeley School of Law. Professor Yoo served in the Office of Legal Counsel, the US Department of Justice from 2001 to 2003, where he worked on constitutional and national securities matters.

Recently, he published an article in the *San Francisco Chronicle* entitled, "Will the Fed's Wall of Secrecy in the Fannie Mae Case Fall." I actually had to take out a subscription in the *San Francisco Chronicle* to read it because it wouldn't let me read the whole thing online. I'm very honored and privileged to have you here this afternoon, Professor.

J. Yoo

Hello. Thanks for inviting me. Hello, everybody. I'm not an expert on banking law or treasury law, but what I do write about and have taught about is about executive privilege. My scholarly work is mostly about the American presidency.

When I heard about this claim of executive privilege by the Obama administration, I was really, really surprised. This is a kind of claim of privilege that really goes well beyond anything that any president has claimed before. I think it's extremely weak and most likely to be rejected by the courts. The reason for that is there is a right of presidents over executive privilege. Some of you who remember Watergate may know that this was extensively litigated during President Nixon and his troubles and his ultimate resignation from office.

In that litigation, the Supreme Court, in a case called *Nixon* said that there is the right of privilege, that the president does have has a right to keep certain kinds of communications confidential between him and his aides. Usually, that privilege is strongest when the information involves national security, diplomatic military affairs. If it doesn't, then the privilege has to be balanced against the right of other branches of government to conduct their own duties with the information.

In that case, in *Nixon* itself, it's quite a good parallel to this, in *Nixon* itself, the court said, even though there were communications between Nixon and his aides, those had to be produced in court because the court needed to do its job to resolve a case before it, in that case, the criminal trial against the Watergate burglars.

Here, I think you have a case that's far, far weaker than the *Nixon* case. In my view, as someone who's written about and actually worked on

executive privilege within the government, far weaker than, really any I've seen in a long time if ever.

First off, here's a case where the claim has nothing to do with national security, foreign affairs or military issues. This is a case involving domestic financial transactions.

Second, and I think this is really quite telling, this is not really a claim of privilege about communications between the president and his aides or even between the president and directly accountable officials. These are communications involving an agency which allegedly is supposed to be an independent agency at the time and then the successor agencies are.

I'm not aware of any claim of executive privilege before involving an independent agency. In fact, the whole theory of executive privilege is that it has to be between the president and his closest advisers. It would make no sense for executive privilege to involve an agency that under a constitutional system doesn't have to obey the president and is not really considered a presidential advisor.

But even if that were not the case, it seems to me under the balancing test of *Nixon*, any privilege would have to give way because this is a claim, to me, this is a claim of a taking of property, one of the rights guaranteed to all of us in the Constitution and the Bill of Rights and in the Fourteenth Amendment.

The court has to have this information in order to perform its constitutional duty of resolving cases, defending the individual right to property. I find, just to wrap up, I find that the claim is really, to me, unfounded as a matter of constitutional law. Then the sweeping nature of it, to claim so many documents, thousands and thousands of documents, is really a kind of claim that hasn't been seen in terms of terms of bulk and volume subjects than any I can remember.

Even Nixon didn't go this far in terms of his claims of executive privilege. I do expect, ultimately, that either the judge here in the Federal Claims Court or on appeal in the Federal Circuit Court of Appeals in Washington, DC, that the government will ultimately lose its claim of executive privilege. If it were smart, it would see that coming down the road and pull back its claim so as not to lose in federal court in any permanent way, which would actually hurt the presidency in the long run.

Thank you for listening.

- T. Pagliara Thank you, Professor Yoo. Now, at this time, I'd like to open the floor up for questions. Remember, we have Barr Flinn who is representing me in the case against Fannie Mae; Tom Connally, who is representing me in a case against Freddie Mac; and then, Professor Yoo, talking about executive privilege and his recent article in the *San Francisco Chronicle*.
- Operator, we're ready for our first question if we've got one in the queue.
- Moderator (Operator's instructions.) We will go directly to the line of Clay Constantinou. Please go ahead, your line is open.
- C. Constantinou Thank you. Good afternoon, everyone. The question I have, do any of us that are just private, individual investors have to join any of the pending litigations in order to be able to claim our losses?
- T. Pagliara Barr, why don't you handle that one first?
- B. Flinn Sure. There are a number of pending litigations that relate to Fannie Mae and the net worth sweep and also to Freddie Mac that don't involve what we're doing right now for Tim. As it relates to those of the pieces of litigation, that's not a question I could answer; you'd have to ask it to somebody else.
- T. Connally As it relates to the complaints that we brought on behalf of Tim against Fannie Mae and Freddie Mac, those are just for him to receive books and records from the companies. If we're successful, he will receive those books and records. For that to happen, no one else needs to join that complaint.
- Now, if he receives those books and records, it's possible that could be subject to some confidentiality restraints. The court sometimes requires that confidential information be kept confidential. Although, in this case, I'm not sure it's going to be a lot of confidential information, so much of it may be able to be shared.
- I hope that answers your question.
- T. Pagliara Great. Just to confirm, this is just a request for information. There's no damages attached to it. Operator, can we have the next question, please?
- Moderator Our next question comes from the line of Isaac Poltansky. Please go ahead.

I. Poltansky Hi, guys. Thanks for holding the call. Tim, this question is really for you. We followed this issue for a number of years now, ever since the sweep. With all these legal actions, I'm left with the question of whether there is a grand legal strategy, whether the shareholders are playing 3D chess in some ways, or if they're just throwing lawsuits at the wall to see what sticks. I'm having trouble trying to pull together which it is because of how many cases are outstanding at this point in different jurisdictions over different claims. Really, just a top-level discussion of what the litigation strategy overall is would be hugely helpful.

T. Pagliara I can only speak for myself, and there is no grand strategy, I'm not part of any grand strategy. I want information. I want to know how this board function. I want to know what they did and how they feel like they have acting in the best interests of the shareholders through the books and records that we've requested, and that's it.

I think the other litigation kind of speaks for itself and it's driven by factors relevant to each individual plaintiff in those cases.

Next question, operator.

Moderator Our next question is from the line of Lara Kamath. Please go ahead.

L. Kamath Thank you for holding the call. I've heard in various message boards about statutes of limitations in filing these cases. I know it has been, what seven years, since the agencies went into conservatorship. What do you guys think about such a delay and how that is going to affect legal claims, mainly statutes of limitations.

The second question I have is that most of the cases appear to be or should be related to the constitutional issues. [Indiscernible] itself is violating the Constitution and so are there actions by the defendants violating the Constitution. Why is it that these cases are not being based on constitutional violations? Thank you.

T. Pagliara Let me just say there is a case in front of Judge Sweeney, several cases that have been consolidated in the US Court of Claims, and that's where issues related to the Constitution are properly heard. To answer the first part of your question, I'll refer the statute of limitations to the specific cases that I have brought, both first to Barr Flinn as it pertains to Fannie Mae and then to Tom as it pertains to Freddie Mac.

B. Flinn Sure. The question was brought, it sounded like it was talking about cases other than ones that Tim brought. Again, we're not going to comment on

those. As it relates to the ones that Tim has brought, at least the Fannie Mae portion, we do not have a limitations period issue on the filing of the books and records complaint.

The books and records complaint seeks to investigate conduct by the board. As for whether that conduct, whether there be any limitation defenses to that conduct, is something that we can't comment on at this time.

T. Pagliara

Tom?

T. Connally

The same. Our records demand against Freddie Mac is certainly timely, and we're seeking those records in order to investigate potential claims. We'll evaluate any potential limitations issues that might affect those claims when Tim makes a decision about how to proceed after we get the books and records we're entitled to.

T. Pagliara

Next question, operator.

Moderator

Thank you. (Operator's instructions.) Next, we have Carissa Chappell. Please go ahead.

C. Chappell

Hi. I just wanted to know, is there a set time limit when both courts must respond to the request of information lawsuit?

T. Pagliara

Barr and Tom, again?

B. Flinn

Yes, I'd be happy to handle that. There is not a specific deadline by which the Delaware court needs to resolve Tim's action for books and records. That said, it is by statute meant to be a summary proceeding, which would mean a rapid proceeding. Our court has repeatedly stated that it would seek to resolve books and records actions within 45 to 60 days of the filing of the complaint. It sometimes happens for various reasons that a case could go on longer than that.

T. Connally

Generally, in Virginia, there is no set time for the courts to resolve this case, but the statute does provide for the courts to resolve the matter expeditiously. Our Virginia courts already move pretty quickly to begin with, so when they move expeditiously, we're talking really a relatively short period of time compared to other litigation you may be familiar with.

T. Pagliara

I've got a question for Professor Yoo before we take another question from our call-in line. Professor Yoo, we've had many of these calls over

the past couple of years. One of the guests on the program was Professor Epstein at NYU.

J. Yoo He now has a podcast called Law Talk every two weeks.

T. Pagliara Then you'll know one of his phrases he says, when you engage in litigation with the federal government, he talks about how difficult it is. You can be 100% right and still lose 50% of the time. What I'd like you to do is just comment from a bird's eye view looking down after you've reviewed some of this and especially what went into your article on executive privilege, comment on the fairness that American citizens have to deal with in taking on a challenge like this with the federal government. It's expensive, it's time-consuming. It feels like a David and Goliath type battle every day.

J. Yoo I sympathize. I have to say, I was a Justice Department official. At one point you could maybe say at one point in my life it was to make it hard for people like you. I actually think this is different because I think there's a lot of cost. What Richard is talking about is there's a lot of cost in terms of time, litigations costs. The government has a lot of manpower at its disposal, it gets a lot of deference from the courts, from federal judges, especially in technical areas like finance; however, I would say that one area where the courts have become over time more favorable of the plaintiffs has been in the area of takings of property.

I'm not an expert in this area of law, but in the constitutional realm, there was a litigation like this many years ago involving the S&L crisis where the government came in and essentially wiped out what was called goodwill value, the intangible assets that banks had based on their reputation. The wiped it out and it made a lot cheaper for the government to take over those S&Ls.

At that time, a lot of people thought that the government would win all those cases, but actually in the end in this same process, in this same court you're going through, after many years, actually, many years of determined effort, the government lost and had to pay out billions of dollars in damages essentially on the same theory you have.

When I hear about the facts of your case, I think this is a constitutional takings case. What makes it hard is that it's not real estate, which is what the framers really would have had in mind when they wrote the property takings clause. Now it's financial, intangible financial assets.

The Supreme Court has said that the takings clause applies to that too. Even in that case, it is true that the burdens and the obstacles can look very high for the plaintiffs. I would just say in the taking theory, though, I wouldn't be as discouraged.

You're going to the Court of Federal Claims and in the Federal Circuit, it's a court that's especially designed for these kinds of takings claims against the government. The idea is that the judges will not just be experts in it, but they can accelerate matters because they're so familiar with these kinds of claims. You'll get a faster hearing than you would if it had come up in one of the courts in one of the circuits like out here in California, for example.

It's hard to know exactly, for me, whether you're going to win or lose, and I certainly take Richard's point, but I wouldn't be as discouraged as you might be.

T. Pagliara Terrific. Alright, operator, next question.

Moderator Next question is from Bill Malone. Please go ahead.

B. Malone Good afternoon. Thank you very much, Tim. Congratulations. Two comments. One, actually for your attorneys and Professor Yoo and then a question. Professor Yoo, I'm not a lawyer so I'll leave it to lawyers or others to suggest how you do this, but I would certainly encourage you to file an amicus brief, either in Tim's cases or the other notable cases that have been referred to. Everyone knows, I think, what those are.

I would not presume that the federal judges know what it is you think, you believe, and what you feel strongly about based on your experience. Again, however, that can be done, I would really encourage you to do that. No need for you to respond, I just want to plant the seed with you.

And on the question for your lawyers, the boards of both companies seem very comfortable, excuse my phrase, hiding, hiding behind the fact that the FHFA and the treasury protect them from any responsibility, liability. I'm just wondering how either of your guys expect to get around what really has been a reverse transfer of authority and responsibility for corporate activities, to the eye of the beholder at some point, but my feeling is that watching these things for a long, long time that neither board has a huge stake and major decisions are made by the regulator if not by treasury.

With that, I'll back off and listen to your guys.

T. Pagliara

Barr?

B. Flinn

Yes, I'm happy to deal with that. We address this a bit in the complaint that was filed against Fannie Mae, so I'm happy commenting on it to some degree. FHFA's powers under the HERA statute are limited to state law powers. It's going to be a slightly long answer so bear with me for a minute. It just simply succeeds under HERA to the powers of Fannie Mae and its stockholders, board and management.

Those powers are governed by state law. So, for example, just a recent decision out of the Ninth Circuit which made the same point, saying that FHFA stands in the shoes of Fannie Mae and its stockholders, board and management.

The stockholders, board and management of a Delaware corporation are undoubtedly subject to Delaware law, so FHFA is subject to Delaware law and the exercise of its powers as it relates to Fannie Mae. Under Delaware law, FHFA cannot direct somebody at Fannie Mae, such as the board, to breach its fiduciary duties. Under Delaware law, FHFA cannot direct the board of a Delaware corporation, such as Fannie Mae, to stand down from taking action that its fiduciary duties require it to take.

To put it a little bit—look to focus now on the board and the perspective of the board, the board as a board of a Delaware corporation has fiduciary duties. It can't defend an action that it's breached its fiduciary duties on the ground that somebody else told it to do it. If the board is somehow comfortable that it's got some cover from FHFA, that's just not right.

Under the HERA statute, treasury is acting as a commercial actor with FHFA, it can't do anything—sorry, it's acting as a commercial actor with Fannie Mae. It can't, under HERA, do anything with the preferred stock that Fannie Mae itself does not agree to.

T. Connally

I certainly agree with what Barr said. The FHFA directives won't relieve the Freddie Mac board of their duties and obligations to the company and the shareholders. Unfortunately, we don't know what the Freddie Mac board's position is on these issues. They didn't even respond to Tim's letters and demands.

What we did is we got a response from FHFA. 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

stockholder, but rather, and this is a quote, “directly and exclusively to FHFA.”

The Virginia Stock Corporation Act and Virginia law have no application, and Freddie Mac paid the net worth sweep dividends to treasury merely because FHFA said so. There’s simply no authority for any of those positions. They are just wrong, and we look forward to establishing that in this litigation for Tim.

T. Pagliara Okay. I’ll tell you one thing, if I was a board member, I’d be out of my comfort zone. We’ve got time for one more question and we’ll take it. Operator?

Moderator Thank you. Our next question comes from Barry West. Please go ahead.

B. West Tim, thank you very much. You should go to someone else, because Bill Malone asked the exact same question I wanted asked. Thank you, again, very much.

T. Pagliara Why don’t we call it an afternoon. Check the Investors United website frequently. We’ll be posting additional updates as time goes on. I want to thank our special guest, Professor Yoo, for sharing his valuable time with us.

Again, I want to personally thank my attorneys, Barr Flinn, Tom Connally, their respective firms, for helping us shed some light on this matter and pursuing the truth that we’re all after.

Again, thank you. Have a good afternoon.

Moderator That does conclude your conference for today. Thank you for your participation. You may now disconnect.