

**IN THE UNITED STATES DISTRICT COURT FOR THE  
EASTERN DISTRICT OF NORTH CAROLINA, SOUTHERN DIVISION**

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**FEDERAL DEPOSIT INSURANCE CORPORATION,  
as Receiver for COOPERATIVE BANK,**

**Plaintiff,**

vs.

**Civil Action No.:** \_\_\_\_\_

**FREDRICK WILLETTS, III, PAUL G. BURTON,  
JAMES D. HUNDLEY, HORACE THOMPSON  
KING, III, OTTIS RICHARD WRIGHT, JR., RICHARD  
ALLEN RIPPY, FRANCIS PETER FENSEL, JR.,  
DICKSON B. BRIDGER and OTTO C. "BUDDY"  
BURRELL, JR.,**

**Defendants.**

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**COMPLAINT**

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The Plaintiff, the Federal Deposit Insurance Corporation, as Receiver for Cooperative Bank, Wilmington, North Carolina ("FDIC"), files its complaint against Fredrick Willetts, III, Paul G. Burton, James D. Hundley, Horace Thompson King, III, Ottis Richard Wright, Jr., Richard Allen Rippy, Francis Peter Fensel, Jr., Dickson B. Bridger and Otto C. "Buddy" Burrell, Jr., and states:

**I. PARTIES**

1. The FDIC is a corporation organized and existing under the laws of the United States of America. 12 U.S.C. §1811, *et. seq.* The FDIC is an instrumentality of the United States of America and is charged with, among other duties, the orderly liquidation of failed banks. 12. U.S.C. §1821(d). Cooperative Bank ("Cooperative" or "the Bank") was a state-chartered, non-

member bank under the laws of the State of North Carolina, and its deposits were insured by the FDIC. On or about June 19, 2009, the North Carolina Office of Commissioner of Banks (“NCCB”) closed Cooperative and the FDIC was named Receiver. Pursuant to 12 U.S.C. §1821(d)(2)(A)(I), the FDIC as Receiver succeeded to all rights, titles, powers, and privileges of Cooperative and Cooperative’s shareholders with respect to Cooperative, including, but not limited to, Cooperative’s claims against Cooperative’s former directors and officers for negligence, gross negligence and breaches of fiduciary duty or other legal duties.

2. Fredrick Willetts, III (“Willetts”) joined Cooperative in 1972. He succeeded his father, Fredrick Willetts, Jr., as President and CEO in 1991, and as Chairman of the Board in May, 1998. He resigned as President and CEO on February 3, 2009, and as Chairman of the Board of Directors of Cooperative (“Board”) on June 9, 2009. Willetts resides in Wilmington, North Carolina.

3. Paul G. Burton (“Burton”) was a member of Cooperative’s Board from 1992 through his retirement on April 25, 2008. Burton resides in Wilmington, North Carolina.

4. James D. Hundley (“Hundley”) joined Cooperative’s Board in 1990 and served on the Board until Cooperative failed. Hundley resides in Wilmington, North Carolina.

5. Horace Thompson King, III (“King”) served on Cooperative’s Board from 1990 until Cooperative failed. King resides in Wilmington, North Carolina.

6. Ottis Richard Wright, Jr. (“Wright”) served on Cooperative’s Board from 1992 until Cooperative failed. Wright resides in Tabor City, North Carolina.

7. Richard Allen Rippy (“Rippy”) served on Cooperative’s Board from 1997 until Cooperative failed. Rippy resides in Wilmington, North Carolina.

8. Francis Peter Fensel, Jr. (“Fensel”) served on Cooperative’s Board from 1990 until Cooperative failed. Fensel resides in Wilmington, North Carolina.

9. Dickson B. Bridger (“Bridger”) joined Cooperative in 1984 as a loan officer and mortgage loan originator. By the time Cooperative failed, he was Executive Vice-President of Mortgage Lending. Although he was not a member of the Board, Bridger regularly attended Board meetings, missing only five from January 2006, until Cooperative failed. Bridger resides in Wilmington, North Carolina.

10. Otto C. “Buddy” Burrell, Jr. (“Burrell”) began his career in banking in 1970 before joining Cooperative in 1993 as Senior Vice-President, Retail Banking. When Cooperative closed, Burrell was Senior Executive Vice-President and Chief Operating Officer. Burrell also regularly attended Cooperative’s Board meetings, missing only four from January 2006, until Cooperative failed. Burrell resides in Wilmington, North Carolina.

## **II. JURISDICTION AND VENUE**

11. This Court has subject matter jurisdiction over this matter, as actions in which the FDIC is a party are deemed to arise under federal law pursuant to 12 U.S.C. §1811, *et. seq.*; 12 U.S.C. §1819(b)(1) and (2), and 28 U.S.C. §§1331 and 1345. The FDIC has the power to sue and complain in any court of law. 12 U.S.C. §1819.

12. The Court has personal jurisdiction over all of the Defendants who at all relevant times were residents of, and conducted the business of Cooperative in, the State of North Carolina.

13. Venue is proper in this District under 28 U.S.C. §1319(b), as all or substantially all of the events and/or omissions giving rise to the claims asserted herein occurred in this

District.

### **III. FACTUAL BACKGROUND**

14. Cooperative was founded in 1898 in Wilmington, North Carolina. Beginning in 1933, three generations of the Willetts family managed Cooperative until Cooperative failed in 2009. In November 2001, the Board and senior management together agreed on a new strategic goal for Cooperative to grow from \$443 million to \$1 billion in assets by the end of 2005.

Cooperative did not meet this goal by the end of 2005, but at that time Willetts and the Board reaffirmed the goal to become a \$1 billion bank and pursued an aggressive asset growth plan in furtherance of that goal. Willetts, Burton, Hundley, King, Wright, Rippy and Fensel (collectively “the Director Defendants”) were all members of the Board when the aggressive growth strategy was adopted and later reaffirmed.

15. As implemented, the aggressive growth campaign traded the conservative and safe manner in which Cooperative had operated for 100 years for a strategy that concentrated Cooperative’s lending in higher risk acquisition, development and construction (“ADC”) loans. As a result of Cooperative’s aggressive growth strategy, Cooperative’s ADC loan concentration grew from 326% of total capital in December 2005 to 469% of total capital in December 2007. In its peer group, ADC loans comprised 104% of total capital in December 2005 and 124% of total capital in December 2007.

16. The Defendants failed to manage the inherent risks associated with their aggressive growth strategy. Rather than employing methods to properly monitor and mitigate the risks associated with the highly speculative lending in which Cooperative was engaging, the Director Defendants permitted a lax loan approval process which did not include a formal loan

committee to meet, review and analyze the loans being made by Cooperative. Instead, the Bank's Credit Manual ("Loan Policy") set forth 9 levels of loan approval authority within the Bank. Five of those levels of authority are relevant to the damages claimed herein: Authority Level 3 - \$100,000: Bridger; Level 7- \$1.5 million: Willetts or Burrell; Level 8-25% of the Bank's legal lending limit: any three officers with Level 5, 6 or 7 authority, one of which had to be Willetts, Burrell or the Senior Credit Risk Manager; Level 9 - 50% of the Bank's legal lending limit: Willetts and two directors; above 9 – up to the Bank's legal lending limit: full Board approval.

17. State and federal regulators repeatedly warned Cooperative's management and Board about the risks associated with its high concentration in speculative loans and weaknesses in its lending function. Beginning with the NCCB June 20, 2005 Report of Examination ("RoE"), examiners questioned the Bank's goal of reaching \$1 billion in assets and raised concerns about the Bank's liquidity and loan concentrations in real estate construction, development loans and beach resort properties.

18. In the FDIC July 24, 2006, RoE examiners noted deficiencies in Cooperative's underwriting and credit administration and advised the Board that the loan portfolio was subject to undue risks with respect to credit administration, underwriting, and monitoring practices. The RoE identified specific underwriting weaknesses - loans were made with little or no hard borrower equity required; analysis of the borrower's or guarantor's contingent liabilities was not performed; and stale financials and credit memoranda were relied upon to approve loans. The examiners admonished the Defendants that previously identified underwriting and administration weaknesses were not being resolved. The FDIC examiners also warned that oversight and

organizational weakness in the lending area were contributing to credit administration and underwriting deficiencies. The Director Defendants took no action in response to these warnings to improve Bank operations.

19. In the September 10, 2007, NCCB RoE examiners' criticisms continued, and the Board was specifically told that deficiencies identified in previous examinations had not been adequately corrected, and that weaknesses in credit administration continued. These warnings were not heeded either. The Defendants persisted in their aggressive growth strategy without implementing sufficient policy or operation changes to improve either underwriting or credit administration.

20. From 2005 to 2008, regulators consistently warned the Board about Cooperative's commercial real estate concentrations. In February 2008, two state banking examiners advised the Board that Cooperative's commercial real estate concentration was the highest percentage in North Carolina - nevertheless, in clear conflict with the best interest of the Bank, the Board permitted and approved Cooperative's continued focus on commercial real estate lending, even though the Board had known since at least early 2007 that the real estate market was slowing.

21. Cooperative received a composite CAMELS 5 rating in the November 10, 2008, Joint FDIC and NCCB RoE. The examiners observed that recommendations for enhancing credit administration and underwriting practices had previously been made, but that these recommendations were not implemented or were ignored. The examiners identified significant weaknesses, including liberal renewal and extension practices; inadequate analysis of the borrower's repayment capacity; inadequate borrower equity in real estate projects; over-reliance on collateral as the primary source of repayment; renewing credits without sufficient current

financial information; inadequate real estate appraisals and the residential lot loan program.

22. The Defendants recklessly failed to ensure that Cooperative identified, measured, monitored and controlled the risk associated with its rapid growth. The Bank's growth was fueled by its risky and uncontrolled increase in residential development and commercial real estate ("CRE") loans, many of which were poorly underwritten and made in violation of laws, regulations and the Loan Policy. The negligence, gross negligence and reckless conduct of the Defendants, as officers and directors of the Bank, ultimately led to the Bank's failure. The failure was caused, in part, by losses on loans for which the FDIC now seeks recovery (the "Loss Loans"), as set forth below.

#### **IV. LOSS LOANS**

##### **A. Lot Loans**

23. In October 2006, Willetts and Bridger proposed a Lot Loan Program to the Bank's Asset Liability Committee ("ALCO"), a committee of officers whose purpose was to advise the Board on risks and suitability of new loan and other financial products. The Lot Loan Program provided credit to borrowers to buy vacant lots for the purported purpose of eventually building vacation homes in developments along the North Carolina coast. Willetts and Bridger acknowledged that the Lot Loans would not be moneymakers, but they contended that the program would lead to new customers who were more likely to obtain their construction loans from Cooperative when they started to build. The ALCO, which included as members the CFO and Vice-President of Internal Audit, responded that FDIC examiners were concerned about the large number of interest only and no-equity loans in the Bank's portfolio. Willetts and Bridger represented to the ALCO that the Lot Loans would be limited to a 90% loan-to-value ("LTV")

ratio and payments would not be interest only. A 90% LTV for the Lot Loans would violate the Bank's Loan Policy, which allowed only a 65% LTV limit for raw land and a 75% LTV limit for land development.

24. Cooperative made Lot Loans in 12 different developments beginning in late 2006. By September 30, 2008, Lot Loans comprised 52% of Cooperative's Tier One Capital and 45% of its Total Risk Based Capital. Moreover, the Lot Loans were not made as Willetts and Bridger represented to the ALCO. Instead, the loans were exactly what the ALCO and FDIC examiners were concerned about. The loans were no-equity loans with interest only payments. While there were some differences in how the Lot Loan Program worked in the various subdivisions, typically the Program operated so that a third-party, such as Total Realty Management, LLC ("TRM"), would present seminars to individuals from other states, suggesting that these individuals could buy these water-view lots, hold them for a few years, then obtain a significant return on their investment selling their lots. TRM would gather buyers, and then would buy the lots from the developer and turn around and sell them to the buyer on the same day or week often for twice as much as TRM paid for the lots. Appraisers (selected by the mortgage broker to which TRM referred prospective buyers) would appraise the lots based on similar transactions, thus resulting in grossly inflated appraisals. TRM would take a note and second mortgage for 20% of the purchase price in lieu of a "downpayment," pay all the closing costs, and advance the interest payments for up to 24 months. Thus, Cooperative granted many loans secured by vacant lots in which the borrower paid nothing as a downpayment, paid no closing costs, and paid no interest – all based on lots that had been flipped to raise the prices.

25. In addition, contrary to the representations by Willetts and Bridger, a majority of



the loans were stated income loans, and were “no document loans,” meaning that the Bank did not require the borrower to provide financial statements or tax returns. This was a violation of the Loan Policy, which required that borrowers submit 2 years of complete tax returns and recent financial statements for all loans over \$100,000. The primary purchasers of the lots through the Lot Loan Program were people who lived outside of North Carolina. Of the 78 Lot Loans upon which this claim is based, 76 of the borrowers were from out-of-state.

26. One of the subdivisions where Cooperative made Lot Loans was the Summerhouse subdivision. In Summerhouse, 26 lots were sold to TRM in a one-month period. One lot, #244, was sold to TRM on June 20, 2007, for \$226,000. The next day, TRM sold it to Mr. T.T. of Virginia Beach, Virginia, for \$425,000. The appraisal of \$425,000 relied upon other recently TRM-flipped properties. The Bank’s loan to Mr. T.T. was an interest-only \$340,000 loan (which showed an 80% LTV ratio). Mr. T.T. did not make the \$85,000 down payment, TRM did by “only” taking \$114,000 out of the \$199,000 equity gain at closing, leaving “paper equity” of \$85,000 in the property which it “loaned” to Mr. T.T. The loan to Mr. T.T. was a stated-income, no-document loan in violation of the Loan Policy.

27. Bridger approved all of the Lot Loans upon which this claim is based, even though his approval authority of \$100,000 was insufficient. Bridger was grossly negligent in approving the Lot Loans in violation of the Loan Policy, in part because he knew that the majority of the loans were stated-income, no-document loans; the borrowers had no equity in the property; the borrowers paid no closing costs or interest; and the borrowers typically had insufficient cash flow to service the loans and were depending on speculative increases in lot values to repay them. Willetts was grossly negligent in supervising the Lot Loan Program

because Willetts was likewise aware of the violations of the Loan Policy presented by that program as well as the highly speculative nature of the program. Indeed, by June 2007, both Willetts and Bridger knew that some loan officers and even an appraiser had questioned the values of the lots upon which Cooperative was making loans. On July 5, 2007, Bridger informed the ALCO, including Willetts, that he had a second appraisal performed on one of the lots that Cooperative financed, and the second appraisal was for nearly \$100,000 less than the appraisal used to support the loan. However, Bridger and Willetts were undeterred by the mounting evidence that the Bank was financing lots at grossly inflated values.

28. The Director Defendants learned about the high-risk Lot Loan Program no later than the July 17, 2007, Board Meeting when Bridger informed them that the Lot Loans did not comply with the Loan Policy. The Director Defendants also knew that Bridger's loan approval authority was only \$100,000, because during the 12-month period before the July 17, 2007, meeting, the Board approved the lending authority matrix seven times, and each time Bridger had a maximum lending authority of \$100,000. All 78 of the Lot Loans within this claim were for more than \$100,000.

29. Even following the July 17, 2007, meeting, the Board took no corrective action with respect to the Lot Loan Program, which was clearly in conflict with the best interests of the Bank. Despite repeated regulatory warnings and Bridger's report to the Board of systematic Loan Policy violations, in a complete abdication of its responsibilities, the Board continually failed to supervise the Bank's Lot Loan lending function. An additional \$4.4 million in losses was incurred on Lot Loans approved after the July 17, 2007, Board meeting, as a result of the Director Defendants' gross negligence in failing to monitor, direct and supervise the Lot Loan

program.

30. The following table lists the Lot Loans upon which the FDIC seeks recovery from the various Defendants. The FDIC seeks a judgment against Willetts and Bridger for all of the losses resulting from Lot Loans, and from the Director Defendants for all of the losses relating to Lot Loans approved after July 17, 2007.

**LOT LOANS MADE BEFORE JULY 17, 2007, BOARD MEETING**

<b>Borrower</b>	<b>Loan #</b>	<b>Date of Origination</b>	<b>Original Loan Amount</b>	<b>Loss to FDIC</b>
RWH <sup>1</sup>	190001300	1/5/2007	999,000.00	328,117.60
KW	190001308	4/26/2007	341,991.00	232,424.59
LKM	190001311	5/3/2007	296,991.00	190,114.07
FMH	1690000195	5/18/2007	279,200.00	208,531.44
SM	1690000196	5/18/2007	295,200.00	221,607.61
SP	1690000197	5/18/2007	221,600.00	161,457.25
MDF	1690000198	5/18/2007	303,200.00	233,185.62
SOW	1690000199	5/18/2007	311,200.00	234,683.77
KMT	1690000200	5/18/2007	295,200.00	221,607.61
KMT	1690000201	5/18/2007	295,200.00	242,445.79
MAR	1690000205	5/18/2007	345,600.00	228,237.48
LD	190001314	5/22/2007	349,191.00	241,998.44
TAE	1690000204	5/24/2007	355,200.00	247,567.67
ABS	190001316	5/30/2007	309,992.00	202,617.35
JKB	1690000207	6/1/2007	295,200.00	225,207.68
TM	1690000210	6/1/2007	287,200.00	215,069.52
BJV	2090000079	6/5/2007	319,200.00	203,561.94
PPB	1690000208	6/8/2007	287,200.00	211,469.46
JKD	1690000214	6/8/2007	303,200.00	224,545.62
BBG	1690000215	6/8/2007	263,000.00	202,491.97
GMG	1690000216	6/8/2007	340,000.00	258,220.86
JB	1690000217	6/8/2007	303,200.00	228,145.69
SF	1690000220	6/8/2007	303,200.00	217,346.27
SDE	1690000221	6/8/2007	303,200.00	228,145.69
AKR	1690000222	6/8/2007	287,200.00	211,469.46

<sup>1</sup> All of the individual borrowers referenced herein are identified by initials to protect the confidential financial information of the borrowers. The loan files for all borrowers referenced herein have previously been provided to the Defendants; thus the Defendants are aware of the full identity of the borrowers on the loans in question.

<b>Borrower</b>	<b>Loan #</b>	<b>Date of Origination</b>	<b>Original Loan Amount</b>	<b>Loss to FDIC</b>
HR	190001321	6/13/2007	271,192.00	174,833.48
KK	1690000224	6/13/2007	303,200.00	224,545.62
BCC	1690000225	6/13/2007	303,200.00	230,207.29
MS	1690000226	6/13/2007	303,200.00	228,145.69
BH	2090000078	6/13/2007	283,200.00	174,100.57
JS	2090000080	6/15/2007	327,200.00	273,069.56
MJS	2090000082	6/15/2007	319,200.00	205,130.52
JLH	1690000229	6/20/2007	324,000.00	245,144.70
WC	1690000231	6/20/2007	303,200.00	231,496.00
DEJ	1690000233	6/20/2007	355,200.00	249,043.59
TAT	1690000234	6/25/2007	340,000.00	243,821.38
RDC	1690000235	6/25/2007	324,000.00	245,168.00
KGF	2090000084	6/25/2007	319,200.00	203,502.40
BHS	190001322	7/2/2007	353,691.00	243,807.18
JAB	2090000081	7/2/2007	355,200.00	229,344.04
RB	190001324	7/5/2007	350,991.00	246,303.60
CD	1690000242	7/11/2007	328,000.00	263,732.82
LC	1690000243	7/11/2007	308,000.00	228,468.46
DAK	2090000091	7/11/2007	319,200.00	207,162.01
			<b>SUBTOTAL</b>	<b>9,967,297.36</b>

**LOT LOANS MADE AFTER JULY 17, 2007, BOARD MEETING**

<b>Borrower</b>	<b>Loan #</b>	<b>Date of Origination</b>	<b>Original Loan Amount</b>	<b>Loss to FDIC</b>
LAC	190001329	7/25/2007	307,700.00	184,114.52
DB	1690000247	7/26/2007	311,200.00	230,003.43
ML	1690000248	7/26/2007	287,200.00	211,469.46
MVR	1690000254	8/2/2007	287,200.00	208,778.40
ALK	1490000107	8/3/2007	143,910.00	102,411.20
JP	1690000251	8/3/2007	324,000.00	244,080.00
JSP	1690000252	8/3/2007	340,000.00	249,859.90
RJB	1690000253	8/3/2007	340,000.00	270,488.72
CAL	190001330	8/22/2007	287,991.00	6,087.94
JLC	190001331	8/23/2007	311,992.00	213,162.40
CAP	1490000105	8/24/2007	143,910.00	92,954.40
AM	1490000106	8/24/2007	314,910.00	199,487.20
AM	1490000109	8/30/2007	114,210.00	74,533.95
SMR	1490000110	9/4/2007	114,210.00	66,287.55

<b>Borrower</b>	<b>Loan #</b>	<b>Date of Origination</b>	<b>Original Loan Amount</b>	<b>Loss to FDIC</b>
AAN	1490000114	9/5/2007	119,610.00	72,444.52
DKR	2090000090	9/7/2007	319,200.00	205,051.20
JAM	1490000112	9/14/2007	116,910.00	68,227.84
JC	2090000092	9/14/2007	319,200.00	203,660.00
NJW	1490000120	9/18/2007	154,710.00	55,020.00
VJV	1490000123	9/21/2007	154,710.00	51,403.20
TWT	190001338	10/11/2007	280,491.00	186,138.66
MFB	190001340	10/22/2007	289,800.00	129,363.06
SJS	1490000132	10/25/2007	144,810.00	47,135.20
CWL	190001341	11/9/2007	328,140.00	170,294.08
VJV	1490000140	11/14/2007	109,710.00	78,495.20
BMD	1490000139	11/15/2007	119,610.00	86,392.00
JMT	1490000143	11/20/2007	106,110.00	68,178.40
PRB	1490000144	11/26/2007	122,310.00	88,578.40
CL	1490000145	12/4/2007	125,910.00	86,504.00
MAM	1490000158	1/22/2008	125,910.00	83,264.00
SJZ	1490000160	1/22/2008	126,810.00	91,646.40
LR	190001350	2/27/2008	325,800.00	144,303.77
CHF	190001353	3/25/2008	324,360.00	150,412.80
XRR	1490000170	4/10/2008	101,900.00	62,361.18
			<b>SUBTOTAL</b>	<b>4,482,592.98</b>

**TOTAL LOSSES ON LOT LOANS                                      \$14,449,890.34**

**B.      Commercial Real Estate Loans**

31.      In addition to the losses incurred on the Lot Loans, the FDIC has also been damaged by losses incurred on CRE loans which contain serious flaws from the deficient underwriting and imprudent credit administration about which the regulators had repeatedly cautioned the Director Defendants.

32.      Because there was no formal loan committee at Cooperative during the relevant time, approval for CRE Loans was typically obtained by Willetts (or his designee) calling individual directors on the telephone, one at a time until he had enough votes for approval. Prior

to approving loans, the Director Defendants did not meet to discuss the loans and did not have copies of the loan files or any other presentations to evaluate the loans other than what they were told on the telephone. The telephonic discussions of the loans were too brief and cursory to enable the approvers to identify the serious underwriting deficiencies in these CRE Loans. The approvals were “reported” at the next Board meeting. The CRE Loans upon which the FDIC’s claim is based are included in the chart below and described in further detail in the paragraphs that follow:

<b>Borrower</b>	<b>Date</b>	<b>Original Amount</b>	<b>Loss to FDIC</b>	<b>Approved By</b>
Bluewater Beach, LLC	06/05/07	\$10,605,700	\$5,473,021.23	1,2,4,6,7
Palmetto Pointe Building Company, LLC	04/17/07	\$5,570,000	\$1,378,912.02	1,2,3,5,6
Mill Creek Holdings, LLC	03/06/07	\$8,198,000	\$2,126,056.01	1,2,3,4,5,7
Mill Creek Holdings, LLC	10/17/07	\$1,500,000	\$777,149.00	1,7
BBN Mercer, LLC	03/06/07	\$6,343,500	\$3,025,214.37	1,2,3,4,5,7
BBN Mercer, LLC	10/17/07	\$1,500,000	\$1,103,977.34	1,7
RWM/PRM	06/08/07	\$3,700,000	\$1,370,220.28	1,2,3,4
Richmond Hills Residential Partners, LLC	07/30/07	\$7,750,000	\$3,570,082.06	1,2,4,6,7
Crossover Enterprises, LLC	04/08/08	\$2,700,000	\$1,196,347.98	7

**TOTAL LOSS ON CRE LOANS** **\$20,020,980.29**

Approvers: 1-Willetts; 2-Fensel; 3-King; 4-Rippy; 5-Wright; 6-Burton; 7-Burrell

**Bluewater Beach, LLC**

33. On or before June 5, 2007, Willetts, Fensel, Rippy, Burton and Burrell approved a

\$10,605,700 loan to Bluewater Beach, LLC (“Bluewater Beach”). The purpose of the loan was to develop 105 acres in a subdivision in Leland, North Carolina. The terms of the loan called for interest only monthly payments, with an 18-month maturity. The loan was secured by roughly 105 acres of the Bluewater Beach Subdivision in Leland. The purpose of the loan was to refinance the acquisition costs of the land, to complete the infrastructure of Phase I (50 residential lots), and land clearing and site preparation for Phases II and III. A glaring problem with the Bluewater Beach loan is that the purchase price for the property was just over \$3 million, yet \$7,190,516 of the loan was used to payoff a prior loan from SunTrust Bank. There is no explanation in the loan file, and none was provided to the Directors, as to how the other \$4,093,516 of the Suntrust loan proceeds had been spent. In June 2007, when Cooperative approved the loan, there were no structures or infrastructure anywhere on the property. Another deficiency in the Bank’s underwriting was that the only repayment source noted for the loan was the sale of collateral, a significant deficiency given that neither the newly-formed borrower, Bluewater Beach, nor the guarantors had sufficient cash flow to make monthly interest payments. Moreover, interest costs were not included in the project budget.

34. The Bluewater Beach loan was improperly structured in an effort to avoid legal lending limit violations due to the existing high level of indebtedness to Cooperative already owed by the guarantors on the loan (LB and KP) and their related entities. Even though LB and KP were each 50% owners in Bluewater Beach, the guaranties were structured such that LB was a 55% guarantor and KP was a 45% guarantor. In addition, there was no adequate basis for repayment of the loan. Significantly, KP, one of the guarantors, had a below-average credit score, which was explained away by noting that the low credit score was “mostly due to the high

revolving debt for [KP's construction business]". Further, the guarantors lacked sufficient surplus cash flow to service the debt. In fact, the principals collectively did not have sufficient surplus cash flow to pay the monthly interest charges on the loan. Nevertheless, the loan was approved even though none of the Bank's cash flow analysis included debt service for this loan. Approval of this loan was grossly negligent and clearly in conflict with the best interest of the Bank. To date, the FDIC's loss on the Bluewater Beach loan is \$5,473,021.23.

**Palmetto Pointe Building Company, LLC**

35. On or before April 7, 2007, Willetts, Fensel, King, Wright and Burton approved a \$5,570,000 loan to Palmetto Pointe Building Company, LLC ("Palmetto Pointe"). The purpose of the loan was to provide a construction line of credit to acquire 15 residential lots in the Palmetto Pointe Subdivision and build 3 single family spec homes. The loan was an 18-month loan with interest only payments payable monthly with all principal due at maturity. The only repayment source noted for the loan was the sale of homes and lots. However, none of the spec homes were under contract and the 15 lots were undeveloped at the time the loan closed. The financial statements of the guarantors of the loan reflected that the guarantors had limited liquidity to satisfy this loan if the sale of the spec homes and lots did not come to fruition as anticipated. At the time the loan was underwritten, the guarantors had a combined liquidity of only \$142,000, and both guarantors' net worth was derived primarily from long-term real estate holdings.

36. The loan to Palmetto Pointe was supported by inadequate or wrongly valued security. The comparable lot sales used in the March 7, 2007 appraisal were sales in 2005 and 2006. Those sales showed that the 2006 sales were 30% lower than the 2005 lot sales, however,



the appraiser applied an average upward time adjustment to each respective lot sale of 6.2%, which was clearly unwarranted given the historical data reflecting declining values for the lots. The foregoing Defendants were grossly negligent in approving this loan which was clearly in conflict with the best interest of the Bank, given the lack of financial strength of the borrower and guarantors as well as the wrongly valued collateral security. The FDIC's loss to date on the Palmetto Pointe loan is \$1,378,912.02.

**BBN Mercer, LLC/Mill Creek Holdings, LLC**

37. On March 6, 2007, Cooperative extended two loans to two special purpose entities, Mill Creek Holdings, LLC ("Mill Creek") and BBN Mercer, LLC ("BBN"). Mill Creek and BBN were owned by the same principals. The loan to Mill Creek was a construction line of credit for \$6,343,500, of which \$2,427,000 was new money and \$3,916,480 was a consolidation of existing debt. The loan to BBN was a construction line of credit for \$8,198,000, of which \$3,985,000 was new money, and \$4,242,379 was a consolidation of existing debt. Mill Creek and BBN were formed in 2005 to acquire 167.77 acres in Boliva, North Carolina and to develop residential lots in the Mill Creek subdivision. BBN and Mill Creek acquired the subject property in two separate purchase transactions in 2005, where each purchased a one-half undivided interest in the property for a total combined purchase price of \$5,250,000. The stated purpose of the Mill Creek loan was to complete the infrastructure for 55 remaining residential lots in Phase II, Section 2 and Phase III of Mill Creek Cove subdivision, and the stated purpose of the BBN loan was to complete the infrastructure for the remaining 60 residential lots in Phase I, Section 2, the community clubhouse and pool. Both of these loans were approved by Willetts, Fensel, King, Rippey, Wright and Burrell. These two loans resulted in a total of \$14,541,500 in

qualifying commitments to lend to the common enterprise of Mill Creek and BBN, exceeding Cooperative's legal lending limit of \$11,940,600 at the time these loans were originated. As such, the Defendants who approved this loan approved it in violation of N.C.G.S.A. §53-48.

38. On October 17, 2007, Cooperative extended two new loans to Mill Creek and BBN, each in the amount of \$1.5 million which were purportedly business lines of credit for additional land development expenses. These two loans were approved only by Willetts and Burrell, even though the Loan Policy required the Board's majority approval because the aggregate indebtedness of Mill Creek and BBN exceeded 50% of the Bank's legal lending limit. Moreover, as of October 17, 2007, the Bank had total loans and extensions of credit to the common enterprise of Mill Creek and BBN of \$17,541,500, when the Bank's legal lending limit was only \$12,610,650. This again was a violation of N.C.G.S.A. §53-48.

39. In September 2008, the Bank renewed the four loans to Mill Creek and BBN with an aggregate balance of \$11,036,997, which was 87.9% of the Bank's legal lending limit. The Loan Policy provided that the Bank's president and two directors could approve loans up to 50% of the Bank's legal lending limit, but anything above 50% of the Bank's legal lending limit required the Board's majority approval. All of the September 2008, renewals were approved only by Burrell and Willetts in violation of the Bank's Loan Policy. The renewals also violated the Loan Policy requirement of a new appraisal for any renewal, refinancing or modification of an existing loan when there had been a material change in market condition or when new money was advanced, both of which were present at the time of the renewal. Moreover, with the four renewals, the Bank increased its overall exposure by over \$1 million.

40. The FDIC's losses to date on the loans to Mill Creek are \$2,126,056 and

\$777,149, and the losses on the two loans to BBN are \$3,025,214 and \$1,103,977. The approval of the original four loans to Mill Creek and BBN was grossly negligent and clearly in conflict with the best interest of the Bank because, among other things, the loans violated the Bank's legal lending limits. The approval of the renewals of the four loans, which included extending additional monies to Mill Creek and BBN, was grossly negligent and clearly in conflict with the best interest of the Bank because, among other things, the loans were approved in violation of the Loan Policy and no explanation was given for the increase in exposure of over \$1 million.

### **RWM/PRM**

41. On June 8, 2007, Cooperative made a loan of \$3,700,000 to RWM and PRM to provide funds for the purchase of an interest in a land development company which would own and develop a marina in North Carolina. The loan covered 100% of the purchase price for the acquisition of the interest in the company, and also funds for interest carry and project expenses. The loan had a two-year term, which was modified on June 11, 2007, by extending the maturity another year until June 8, 2010, as had been approved at loan origination. The primary repayment source was anticipated to be a land development and construction loan for the marina, however, the take-out loan never occurred. The collateral for the loan was five residential lots owned by the borrowers. This loan was approved by Willetts, Fensel, King, Rippy and Burrell.

42. The RWM/PRM loan, which was an interest-only, fixed rate, 3-year term loan, violated Cooperative's Loan Policy requirement of amortization with regular monthly or quarterly payments for business term loans with an original maturity of more than one year. Cooperative's files do not reflect that any feasibility study for the proposed marina was obtained or considered, nor is there any indication that the purchase agreement for the borrowers'

investment in the land development company was obtained or considered. The appraisal for the five lots that were offered as collateral relied on comparable sales that were over 12 months old, and the appraisal did not include market information to support the values that were suggested. As such, the approval of this loan was grossly negligent and clearly contrary to the best interest of the Bank in allowing the 100% financing of the speculative purchase in the land development company. The FDIC's loss on this loan is \$1,370,220.

**Richmond Hills Residential Partners, LLC**

43. On July 30, 2007, Cooperative extended a \$7,750,000 loan to Richmond Hills Residential Partners, LLC ("Richmond Hills"). The purpose of the loan was to payoff existing loans held by SunTrust and Cooperative, to provide funding to pay already incurred development expenses, and to establish an interest reserve to carry the loan for eight months. The loan was for 18 months, with monthly interest-only payments and the principal due at maturity. The primary repayment source was noted to be revenue from lot sales as stated in a purchase contract with St. Lawrence Homes ("SLH"). There was no second or third repayment source noted. At the time of the Cooperative loan, a contract was in place for SLH to purchase all 167 lots of the Richmond Hills Subdivision, only 40 of which were developed and an additional 47 lots were 95% completed. There were no funds in the loan to cover the cost of development of additional lots. Therefore, as the loan was set up, Richmond Hills would only have 72 lots available to sell to SLH, which would not generate sufficient funds to repay Cooperative's loan. As such, this debt could not be retired without the borrower securing additional financing to complete the development of the remainder of the lots.

44. The loan officer overstated the collateral value. He presented the loan using an

appraised value of \$105,000 per lot pursuant to an appraisal obtained by SunTrust and recertified to Cooperative prior to the loan closing. However, he should have used the actual contracted for purchase price for the lots which was far less than the per lot value assigned by the appraiser. Instead of the \$105,000 per lot the appraiser assigned, the contract prices ranged from \$73,000 to \$90,000, considerably less than the per lot value in the appraisal. Moreover, neither the borrower nor the guarantors possessed the ability to repay this loan in the event the SLH contract fell through, which indeed happened.

45. The FDIC's loss on the Richmond Hills loan is \$3,570,082. Approval of this loan was grossly negligent and clearly in conflict with the best interest of the Bank given the improper valuation of the collateral and the lack of financial support for the loan by the borrower and guarantors.

**Crossover Enterprises, LLC**

46. On April 9, 2008, the Bank extended a \$2,700,000 loan to Crossover Enterprises, LLC ("Crossover"). The purpose of the loan was to refinance three outside construction loans and to provide \$700,000 cash-out for investment in another project. The loan was an 18-month, interest only, loan which required a borrower funded interest reserve of \$182,250. The collateral for the loan was 28 condominium units located within 4 buildings in Little River, South Carolina (2 one-bedroom units, 11 two-bedroom units and 15 three-bedroom units). This loan was approved by Burrell.

47. Burrell approved this loan notwithstanding the stale financial statement submitted by the borrower and a financial statement by one of the guarantors that did not comply with the Loan Policy; moreover, the debt coverage ratios for both the borrower and the guarantors were

inadequate and in violation of the Loan Policy. Further, the appraisal used to support the loan valued the two-bedroom units at \$185,000 and the three-bedroom units at \$215,000 which values relied, in part, on sales of condominium units 10 miles from the subject property. The appraisals ignored the actual previous sales of two- and three-bedroom units within the subject buildings, which reflected that two-bedroom units sale prices ranged from \$139,900 to \$149,900 and three-bedroom units sold for \$179,900 to \$189,900. The borrower had been unable to sell additional units at that price point, therefore, it was wholly unfeasible that the units were valued at prices higher than the previous sales.

48. The underwriting of this loan was woefully deficit. The borrower had negative book equity and negative cash flow, thus, lacked capacity to service the debt on the loan. The owners of Crossover, who were the guarantors on the loan, were withdrawing more money from the company as dividends and distributions than the company was earning after taxes. Further, in calculating the debt service on the loan, the Bank failed to consider the \$15,000 interest payment per month which was due, even though the interest reserve account set up for the loan would only carry the payments for the first 12 months of the 18-month term. The financial analysis showed that neither the borrower nor the guarantors could service the loan without the interest reserve so no consideration was given to how the loan would be paid once the 12-month interest reserve was depleted. In addition, while the loan approval required the borrower to fund the interest reserve, the interest reserve was actually funded from Cooperative's loan proceeds.

49. Burrell approved this loan notwithstanding the financial inability of the borrower and guarantors to service the debt and the wrongly valued collateral offered in support of the loan. Burrell's actions in this regard were negligent and grossly negligent. To date, the FDIC's

loss on the Crossover loan is \$1,196,347.

## **V. CLAIMS FOR RELIEF**

### **COUNT I - NEGLIGENCE AND GROSS NEGLIGENCE**

50. The allegations of Paragraphs 1 through 49 of this Complaint are incorporated herein by reference.

51. As directors and officers of Cooperative, the Defendants owed a duty of care to discharge their duties in good faith, with the care an ordinarily prudent person in a like position would exercise under similar circumstances and in a manner in which they reasonably believed to be in the best interest of Cooperative. This duty of care included, but was not limited to, the following:

- (a) To adopt such careful, reasonable and prudent policies and procedures, including those relating to lending and underwriting, as required to insure that the Bank did not engage in unsafe and unsound banking practices, and to insure that the affairs of the Bank were conducted in accordance with these policies and procedures;
- (b) To timely acknowledge and adequately respond to changes in economic conditions that create additional risks with respect to certain types of products or transactions;
- (c) To review Reports of Examinations and other directives of regulatory agencies, to carry out the instructions and orders contained in those Reports, to investigate and cure problems noted therein, and to prevent any repetition of such problems and deficiencies;
- (d) To take such action as necessary to insure that Cooperative's loans were underwritten, approved, disbursed and collected in accordance with the law, regulations, and Loan Policy applicable thereto and in accordance with sound and prudent banking practices;
- (e) To exercise reasonable control and supervision over the employees of Cooperative; and
- (f) To faithfully and diligently perform their duties as officers and directors of Cooperative.

52. In disregard of their duties to Cooperative, the Defendants failed to exercise that degree of diligence, care, judgment, skill and good faith which an ordinarily prudent person would have exercised under similar circumstances in like positions in managing, conducting, supervising and directing Cooperative's making, supervising and administering of loans. The Defendants' failures to exercise reasonable care, skill, diligence, loyalty and good faith in the discharge of their responsibilities include, but are not limited to:

- (a) A complete failure to manage the risks associated with the Bank's aggressive real estate lending, particularly in the area of ADC and CRE loans;
- (b) Inadequate analysis of borrower repayment capabilities (eg., a lack of cash flow analysis, inaccurate computations of cash flow and debt service coverage ratios);
- (c) Requiring little or no borrower equity in real estate loans and reliance on collateral (such as the sale of real estate) as a primary source of repayment;
- (d) Instances in which loans were made for residential lots with little or no documentation or verification of borrower income, employment, or repayment capability;
- (e) Liberal loan renewals and extensions, including renewal of interest-only loans;
- (f) Failure to establish and enforce appropriate loan repayment programs;
- (g) Renewing credits without sufficient or current financial information;
- (h) Failing to order and/or analyze real estate appraisals independent from the lending function;
- (i) Operating the Bank in a high-risk manner with an excessive risk exposure to the Bank;
- (j) Failing to develop or maintain a safe and sound strategy for the operation of the Bank, resulting in excessive credit concentrations in higher risk loans, excessive loan delinquencies, excessive problem assets, violations of law and regulations, resulting in insufficient capital to operate the Bank;
- (k) Failing to exercise independent judgment and to act in the best interest of



Cooperative in entering, approving and ratifying loans;

- (l) Failing to exercise due diligence and care in the supervision of Cooperative's officers and employees in the discharge of their duties;
- (m) Permitting loans to be made on the basis of grossly inadequate or inaccurate information regarding the finances of the borrower, the value of the collateral, and/or the sources of repayment;
- (n) Permitting loans to be made on an undersecured basis, contrary to prudent banking practice and in conflict with the best interest of the Bank;
- (o) Failing to establish or adhere to policies responsive to the numerous and repeated warnings and criticisms of federal and state banking regulators;
- (p) Permitting loans to be made in excess of the legal lending limits established by North Carolina law;
- (q) Failing to utilize a formal loan committee to analyze, review, discuss and approve loans; and
- (r) Permitting loans in excess of 100% financing for speculative ventures.

53. The acts and omissions of the Defendants are so imprudent, reckless and represent such an extreme deviation from the standard of care so as to amount to not only negligence but also gross negligence on the part of the Defendants.

54. As a direct and proximate result of the foregoing and other breaches, acts and omissions of the Defendants, Cooperative suffered serious financial losses in excess of \$33 million on 78 Lot Loans and 9 CRE Loans, referred to herein as the Loss Loans.

55. Pursuant to 12 U.S.C.A. §1821(k), N.C.G.S.A. §55-8-30 and N.C.G.S.A. §55-8-42, the FDIC is entitled to recover from the Defendants all damages sustained as a result of their negligence and gross negligence alleged herein.

## **COUNT II - BREACH OF FIDUCIARY DUTIES**

56. The allegations of Paragraphs 1 through 55 of this Complaint are incorporated herein by reference.

57. Pursuant to applicable federal statutes, regulations and North Carolina law, directors and officers of insured financial institutions, such as Cooperative, stand in a fiduciary relationship to the institutions they serve, and are obligated to discharge the duties of their respective positions in accordance with the standards imposed by those laws.

58. The Defendants owed fiduciary duties, individually and collectively, to exercise the highest degree of loyalty, care, diligence and fair dealing in the management, conduct and direction of the business of Cooperative. The Defendants duties included, but were not limited to, those set forth in Paragraph 51 of this Complaint.

59. The Defendants, individually and collectively, breached their fiduciary duties to Cooperative, its depositors and shareholders, by not discharging their duties in good faith, and by failing to exercise that degree of diligence, care, loyalty, judgment and skill required of them in the conduct, direction, supervision and control of Cooperative's business and affairs.

60. The Defendants committed or permitted acts and omissions which resulted in great damage to Cooperative, including, but not limited to, those act and omissions listed in Paragraph 52 of this Complaint.

61. As a direct and proximate result of the breaches of fiduciary duty by the Defendants, Cooperative sustained losses in excess of \$33 million.

62. Pursuant to provisions of applicable law, the FDIC is entitled to recover from the

Defendants all damages sustained as a result of the breaches of fiduciary duty alleged herein.

WHEREFORE, THE FDIC PRAYS for judgments against the Defendants as follows:

1. Against Willetts for:

\$14,449,890 on losses from loss Lot Loans  
\$5,473,021 on the Bluewater Beach loan  
\$1,378,912 on the Palmetto Pointe loan  
\$2,903,205 on the Mill Creek loans  
\$4,129,191 on the BBN loans  
\$1,370,220 on the RWM/PRM loan  
\$3,570,082 on the Richmond Hills loan

For a total of \$33,274,520

2. Against Burton for:

\$4,482,593 on loss Lot Loans made after July 17, 2007  
\$1,378,912 on the Palmetto Pointe loan  
\$3,570,082 on the Richmond Hills loan

For a total of \$9,431,587

3. Against Hundley for:

\$4,482,593 on loss Lot Loans made after July 17, 2007

For a total of \$4,482.593

4. Against King for:

\$4,482,593 on loss Lot Loans made after July 17, 2007  
\$1,378,912 on the Palmetto Pointe loan  
\$2,126,056 on the Mill Creek loans  
\$3,025,214 on the BBN loan  
\$1,370,220 on the RWM/PRM loan

For a total of \$12,382,995

5. Again Wright for:

\$4,482,593 on loss Lot Loans made after July 17, 2007  
\$1,378,912 on the Palmetto Pointe loan

\$2,126,056 on the Mill Creek loans  
\$3,025,214 on the BBN loan

For a total of \$11,012,775

6. Against Rippy for:
- \$4,482,593 on loss Lot Loans made after July 17, 2007
  - \$5,473,021 on the Bluewater Beach loan
  - \$2,126,056 on the Mill Creek loans
  - \$3,025,214 on the BBN loan
  - \$1,370,220 on the RWM/PRM loan
  - \$3,570,082 on the Richmond Hills loan

For a total of \$20,047,186

7. Against Fensel for:
- \$4,482,593 on loss Lot Loans made after July 17, 2007
  - \$5,473,021 on the Bluewater Beach loan
  - \$1,378,912 on the Palmetto Pointe loan
  - \$2,126,056 on the Mill Creek loans
  - \$3,025,214 on the BBN loan
  - \$1,370,220 on the RWM/PRM loan
  - \$3,570,082 on the Richmond Hills loan

For a total of \$21,426,098

8. Against Bridger for:
- \$14,449,890 on losses from loss Lot Loans

For a total of \$14,449,890

9. Against Burrell for:
- \$5,473,021 on the Bluewater Beach loan
  - \$2,903,205 on the Mill Creek loans
  - \$4,129,191 on the BBN loans
  - \$1,370,220 on the RWM/PRM loan
  - \$3,570,082 on the Richmond Hills loan
  - \$1,196,348 on the Crossover loan

For a total of \$18,642,067

10. For prejudgment interest against all Defendants on amounts for which they are liable.
11. For the FDIC's recoverable costs and expenses incurred in connection with this matter.
12. For a trial by jury and for any other relief as the Court may deem just, equitable or proper.

Respectfully submitted,

/s/ Ruth Allen

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