IN THE UNITED STATES COURT OF FEDERAL CLAIMS
NO. 13-465 C
(FILED FEBRUARY 26, 2014)

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FAIRHOLME FUNDS, INC., ET AL

VS. RCFC 12(b); RCFC 12(b)(6); RCFC 56(d)

THE UNITED STATES
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PROTECTED INFORMATION ONLY TO BE DISCLOSED

IN ACCORDANCE WITH PROTECTIVE ORDER

ORAL DEPOSITION OF MS. SUSAN MCFARLAND

HOUSTON, TEXAS

JULY 15TH, 2015

10:01 A.M.

Reported By:
SAMANTHA DOWNING, CSR
JOB NO. 39652

different in time.

And it -- Grant Thornton is projecting that Fannie is going to lose 13 billion dollars in 2012. Your shop was projecting a loss of 2.1 billion dollars.

Do you think Grant Thornton's number was overly pessimistic?

MR. LAUFGRABEN: Objection to the form of the question; lack of foundation, lack of personal knowledge, speculation.

A. It would be difficult for me. I haven't read the document. I haven't assessed what assumptions they were using. So I don't think I can answer that question.

Certainly their number was more negative in that year than the number we were projecting. There were other years out from that that they were more positive. I mean, there were differences in our projections clearly.

Q. (BY Mr. THOMPSON) And if someone had come to you on the eve of the net worth sweep and said to you, "I think Fannie Mae is going to lose 13 billion dollars in 2012," do you think that would have been an unreasonable statement of future profitability as of August 2012?

MR. LAUFGRABEN: Object to the form of

the question; calls for speculation, calls for an expert opinion.

A. In the first quarter -- here's where my numbers recollection comes in versus names recollection -- I believe we made 2 to 3 billion in the first quarter of '12. I think Fannie Mae was 6 billion dollars in the second quarter of 2012. I am sure we can go look at publically-available documents to determine whether I was right or not.

So let's say the total profit to date after June 30th was 8 to 9 billion dollars. So if someone said, "We're going to lose 13 billion," that would mean we would have to have a pretty big loss, a substantial loss during the latter part of the year that would have had to have been greater than the loss we had for all of 2011.

I -- certainly that was not what we were expecting. That's not anywhere close to what our projections were showing. They -- that was not in any way, shape, or form, what we had reviewed with Treasury and FHFA at that point in time.

So if somebody had come to me, I would say, "Okay. Tell me what I missed. What is it that you think is going to happen in the last few months of the year that's going to completely wipe out the profits that we've already posted, and then, you know, take it a further 13 billion in the red?"

I would have a hard time -- I can't think of situations that could happen that would cause that outcome to be so.

Q. (BY MR. THOMPSON) Okay. If you were making an important financial decision for Fannie Mae's future on the date of the net worth sweep, would you have relied on projections from September 30, 2011?

MR. LAUFGRABEN: Object to the form of the questions; calls for speculation, lack of foundation.

A. The reason we did updates to the forecast quarterly were so that we could have, you know, fairly current perspectives from which to make decisions on.

Q. (BY MR. THOMPSON) Why was it important to have a fairly current perspective?

MR. LAUFGRABEN: Objection; form.

A. The situation was very fluid. A lot of things were changing and quickly, and so things could become very dated very quickly in that particular environment at that particular time.

So it was very important to ensure -- we were picking up goods and bad that were happening as quick as we could -- we recognized them and could consume them into our projections.

MR. LAUFGRABEN: David, I am sorry.

If you have a couple of more questions, let's go, but can we go for a break?

MR. THOMPSON: Just another minute or two, and then we'll move away from this document.

Q. (BY MR. THOMPSON) So -- but you said there were goods and bad.

If we look at the period from September 30, 2011 to the date of the net worth sweep, the goods outweighed the bad insofar as, you know, these projections that Fannie put together in McFarland 4 showed a projected loss of 2 billion or so for 2012, and yet you had -- any had made almost 8 billion halfway through the year; is that right?

MR. LAUFGRABEN: Object to the form of the question.

MR. BARTOLOMUCCI: Objection; form.

A. There were a lot of things that moved in a positive direction between September of 2011 and late July, early August 2012.

You can look at publically-available information, look at the Home Price Index as it was published out there and how much those changed during that period of time.

Fannie does produce its own Home Price Index. But you can look at non-published information, and you can see improvements in projections coming from third parties during that period of time. You can look at average loss statistics on different work-out situations. You can look at how much G fees changed during that period of time.

If you look at what existed September 11, and you compared that to what existed in mid, late summer 2012, there's a number of key factors that moved in a positive direction during that period.

Q. Okay. And those positive developments outweighed any negative developments in that time period on balance?

MR. LAUFGRABEN: Object to the form of the question.

A. Our forecasts attempted to incorporate all of those changes good and bad, and the outcomes, you can see, improved.

So the collective -- so if you said if we added up all the puts and takes in a quantifiable fashion, then the net benefits outweighed the net negatives.

MR. THOMPSON: Let's take a break.

THE REPORTER: It's 11:37.

(Recess from 11:37 a.m. to 11:48 a.m.)

THE REPORTER: It's 11:48.

Q. (BY MR. THOMPSON) I would like to ask the court reporter to mark as McFarland 6 a document that bears a Bates number FM3075 through 3091.

(McFarland Exhibit No. 6 was marked.)

Q. (BY MR. THOMPSON) All right. So these are minutes of a meeting of the Board of Directors of Fannie Mae on November 18th, 2011. We can see that in the third paragraph that Jeff Spohn of the FHFA was there, and we can see in that same paragraph that you were there. And if you would be kind enough to turn to page 3087, it's the carry-over paragraph, and it's four lines from the bottom of that carry-over paragraph. It says, "The Board discussed longer-term forecasting and key sensitivities, as well as the ability to utilize net operating losses for tax purposes."

Is this a reflection of the fact that the Board was briefed on the ability of the companies to use their NOLs?

MR. LAUFGRABEN: Object to the form of the question.

A. Yeah.

It's reference to under what conditions might some or all of the DTABs be good.

Q. (BY MR. THOMPSON) Okay.

A. And I don't remember the specifics that we discussed at that point in time, other than it was a -- it's a material item for the company. So it is something that we would periodically, you know, review and discuss in normal course.

And then obviously as we got closer to, you know, the potential to release the allowance, those discussions picked up.

Q. Okay. When you said might be to the good, that's a way of saying that the valuation allowance might be reversed?

A. Correct.

MR. LAUFGRABEN: Object to the form of the question.

Also, for the record, can you please wait a second for me to interpose my objection before answering?

MR. THOMPSON: Just to be clear -- I am fine with that, but we're not going to take, you know -- that's fine.

Q. (BY MR. THOMPSON) In any event, now, you said, "periodically."

Was the DTVA, when you first got there, being reviewed on at least a quarterly basis?

A. It would be -- from an accounting perspective, we reviewed it every quarter, because we have to make a determination every quarter whether or not the allowance should stay on or be released.

Q. And who on your team was advising you on that issue?

MR. LAUFGRABEN: Object to the form of the question; vague.

A. Well -- so Vickie Lyons was head of Tax at the time we really started -- you know, later in my time there. I can't remember if she was head of Tax at the start, okay?

She worked under Krissa [phonetic] Haley. Krissa Haley was a Senior Accounting Manager reporting directly to me. Krissa had significant tax experience herself, and so she was heavily involved in all of the discussions around the DTVA. And most of my conversations around the DTVA involved Greg Fink as Controller; Krissa Haley; sometimes Kirk Silva, who is the Accounting Policy Manager; and then Vickie Lyons, who was head of Tax.

Q. And how is Ms. Haley's last name spelled?

A. H-a-l-e-y, I think.

Q. Okay. So -- and then would they -- someone then brief the Board on this issue?

in compliance with those covenants. We did so on a quarterly basis.

So we had a process whereby we got -- I got a variety of attestations from various executives across the company that the component parts of these statements that were relevant to them and what they and their team did, that to the best of their knowledge, we were in compliance with.

And legal -- internal legal counsel at Fannie Mae assisted me in this process so that I then, on behalf of Fannie Mae, could certify to Director DeMarco that we indeed were in compliance.

So this is just one of the provisions that we were acquired to make that certification.

Q. (BY MR. THOMPSON) So Fannie Mae has -- I think it was your words -- no capital essentially on its Balance Sheet in 2011, and, yet, they're making dividend payments, is that right, to the Government?

MR. LAUFGRABEN: Object to the form of the question.

A. Yes.

Q. (BY MR. THOMPSON) And was there ever any discussion at Fannie Mae that, "We don't have any capital, and, yet, we're being forced to make dividend payments"?

Did anyone ever discuss that somewhat anomalous state of affairs?

MR. LAUFGRABEN: Object to the form of the question; leading.

MR. BARTOLOMUCCI: Objection; form.

A. There was conversation about the -- our irony in the fact that we had to draw money to pay it right back to Treasury. So we had to borrow money from Treasury to pay them their dividends for a period of time while the company was not profitable.

Q. (BY MR. THOMPSON) And the agreements provided for a payment-in-kind option; is that right?

MR. LAUFGRABEN: Object to the form of the question.

Q. (BY MR. THOMPSON) In other words, it was 10 percent if paid in cash or 12 percent if paid in increased liquidation preference?

MR. LAUFGRABEN: Same objection.

A. Yeah. That's incorporated into the Preferred Stock Purchase Agreement.

Q. (BY MR. THOMPSON) Was there ever any discussion at Fannie of rather than drawing down on the line of commitment and, by the way, not being able to repay this 10 percent money, we should do a payment in kind?

MR. LAUFGRABEN: Object to the form of the question.

A. I was not involved in any conversation that discussed that option.

Q. (BY MR. THOMPSON) Okay. Did that thought ever cross your mind?

MR. LAUFGRABEN: Same objection.

A. The -- in my mind, what form of payment we would make and what we were able to do was what Treasury would allow us to do.

Q. (BY MR. THOMPSON) Okay. So if we --

A. And let me add to that.

In other words, if I thought I could make a case that they would agree to letting us use the liquidation preference, then go for it, right? So in my mind, I had to be realistic about that, that we would be able to affect their influence.

Q. I understand that.

Now, let's put that document to the side.

Although, you did say there was -- you mentioned there an irony. What were those discussions?

Who did you have those discussions with, Tim Mayopoulos?

MR. LAUFGRABEN: Object to the form of the question; misstates previous testimony.

A. I mean, what I would call those was kind of hallway-conversation types of things that -- and it wasn't just a single conversation. It could be relatively junior people at the company. You know, anybody that was sort of familiar with the mechanics of how it worked.

There's certainly a number of individuals that kind of took notice of the fact that there was this sort of, you know, like a hamster on a wheel. You borrow to pay to borrow to pay.

And the more we borrowed to pay, the more we had to pay in dividend because the more the amount we drew on went up, and the more dividend -- you know, so it had compounded dividend implications.

Q. (BY MR. THOMPSON) And at the time of the net worth sweep, did you feel that Fannie Mae was in a death spiral?

MR. LAUFGRABEN: Object to the form of the question.

A. No, I did not think Fannie Mae was in a death spiral in mid August of 2012.

Q. (BY MR. THOMPSON) Why not?

A. The company was making money. The projections that I had been involved in and reviewed and felt comfortable with seemed to indicate that there was a good chance that the company would continue to make money. There were a lot of things that were improving within the company, and I felt the company was on a positive trajectory.

Q. Okay. So our next one is going to be McFarland 8, and it has a Bates number of FHFA25815 through 25816.

(McFarland Exhibit No. 8 was marked.)

Q. (BY MR. THOMPSON) So this is an e-mail from Mary Miller to Ed DeMarco on January 4, 2012. And if we turn to the next page, it says, "Agenda for Discussion With FHFA."

And it says in the very first sentence, "FHFA and Treasury share common goals to promote a strong housing market, reduce Government involvement in the housing market over time, and to provide the public and financial markets with a clear plan to wind down the GSEs."

Now, when you were at Fannie Mae in 2011 and 2012, did you see any manifestations of this common goal of trying to wind down the GSEs?

MR. LAUFGRABEN: Objection; form, foundation, vague.

A. The reestablished goals -- performance goals for the company in agreement with FHFA -- and I actually oversaw that process -- we want to -- FHFA and ourselves

MR. LAUFGRABEN: Object to the form of the question.

Q. (BY MR. THOMPSON) The sweep was the 17th, I will represent to you.

A. Yeah.

This is August 6th?

Q. Yeah.

A. So as of this meeting, no, I did not know that the Third Amendment was going to be put in place.

Q. And do you recall what Tim Mayopoulos' reaction was to the Third Amendment?

MR. LAUFGRABEN: Object to the form of the question; lack of foundation.

A. I can tell you the logistics of the communication of the Third Amendment. That might be helpful.

Q. (BY MR. THOMPSON) Sure.

A. I was on vacation in Mexico and was contacted, I believe it was Tuesday of that week -- I may be off a day -- that Secretary Geithner would like to meet with the CEOs and CFOs of the two GSEs the next morning. I inquired into flight arrangements that could get me back in time for the meeting, only to discover there were no commercial arrangements to make that happen.

So I let Tim know that I couldn't find a way to get back in time. And apparently there were some other individuals -- I don't know if it was the CEO or CFO of Freddie. I was not the only one logistically challenged to make the meeting at 8:00 the next morning.

The decision was then made that Secretary Geithner would not then meet. Instead, they set up a meeting with Mary Miller that I know Tim attended in person, and she communicated the -- that they were going to put the Third Amendment in place.

Tim subsequently had a briefing call with myself and a few other executives at Fannie Mae after that to inform us. So I was still in Mexico on vacation on the phone receiving -- being informed of the Third Amendment.

So I say that only in the context of, you know, I have to assess it based on what I heard. I wasn't in the room. I couldn't, you know, get a sense from body language or any of the other things.

I think -- you know, the sense I got was maybe not that dissimilar from my reaction. When you're in the unique situation that the GS Es were in, you're never shocked at anything. But I -- there was a little bit of surprise and yet not surprise, in the sense that the chance that they -- we didn't believe that Treasury would be too fond of a significant amount of capital buildup inside the enterprises.

Q. Why not.

They had mortgaged 79.9 percent of the economy.

MR. LAUFGRABEN: Objection to the form of the question; calls for speculation.

A. There was a desire to reach a more wholistic solution for housing finance reform.

So as time passed and the companies continued to operate and things happened through the operation of those companies, you had -- all of the parties involved, whether that's Treasury or FHFA or Fannie, had to deal with the outcomes of those in the absence of a more wholistic solution.

Some of those outcomes could start taking things down a certain path that might affect or make the ultimate solution, if there ever is one, more difficult to deal with.

And I don't know. I am just saying that if you start allowing capital to accumulate up in the enterprises, then that creates an additional variable or factor that has to be taken into account if and when perhaps a more wholistic solution is put in place.

You know, again, I am giving you sort of my perspective on why, you know, there might be a reason to prefer that not to happen -- you know, capital accumulation to happen at that point in time.

Q. And what did Mr. Mayopoulos say during this conference call when you were in Mexico?

A. Well, he was very factual providing the information that was provided to him by Treasury.

Q. Yeah.

A. Kind of discussing, okay, what does this mean? What do we need to do?

You know, there were communication issues, there's logistical issues, different things that had to be -- you know, we had to be prepared to deal with it. And so what do we as a company need to do and by when and who is on point for different things. So there was a little bit of a call to action.

And, you know, we needed to communicate to the Board. We also ultimately needed to communicate to the employees. But you -- you know, the timing of when and how you did that was very important because we couldn't get out in front of, you know, the communications that Treasury needed to make. So we needed to make sure that we were clear on that -- you know, that type of thing --

Q. Okay.

A. -- and working through that.

it's talking about potential value creation opportunities.

And my question, Ms. McFarland, is, have you ever seen this document before?

A. No.

Q. Okay. We can put it to the side, then.

Okay. The next document is going to be McFarland 27. It's got a Bates number of FHLMC96 through 171.

(McFarland Exhibit No. 27 was marked.)

Q. (BY MR. THOMPSON) So this is a Freddie Mac document. I understand it's not your document. It does say, "May 22, 2012, Corporate Forecast Three-Year Outlook."

I would like to direct your attention to page 27 of this document. And the final bullet point says, "Our sensitivity to a commitment fee based on remaining commitment available beginning in 2013 of 149 billion dollars shows that a 25 basis point fee results in a 400,000,000 annual impact on stockholders' equity."

Does that strike you as a reasonable estimate of an appropriate fee for the commitment from the Government?

MR. LAUFGRABEN: Object to the form of the question; calls for speculation, lack of foundation, lack of personal knowledge.

MR. BARTOLOMUCCI: Same objections.

A. I -- the only comment I would have is that's not dissimilar to pricing you might see, say, for a letter of credit, which was the comparison I made earlier.

Q. (BY MR. THOMPSON) Okay. Very good. Let's see.

Now, if we -- for loan loss reserves, did the company have a -- did it have a model to project, you know, future losses and, therefore, to make its loan loss provisions?

MR. LAUFGRABEN: Object to the form of the question.

A. Yes, we had a model.

Q. (BY MR. THOMPSON) Who maintained that model?

A. Leslie Deich and her team.

Q. Okay. Were those models shared with FHFA; do you recall?

A. Yes, and they were -- their regulatory arm did regular exams, examinations of that group and the models that they used.

Q. Okay. Now, we've talked a lot about deferred tax assets today.

And if I wanted to find all the