IN THE UNITED STATES COURT OF FEDERAL CLAIMS

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FAIRHOLME FUNDS, INC, et al., :

Plaintiffs, :

v. : Case No. 13-465C

THE UNITED STATES, :

Defendant. :

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Washington, D.C.

Friday, May 15, 2015

CONFIDENTIAL - PROTECTED INFORMATION TO BE

DISCLOSED ONLY IN ACCORDANCE WITH PROTECTIVE ORDER

Videotaped Deposition of MARIO UGOLETTI, a witness herein, called for examination by counsel for Plaintiffs in the above-entitled matter, pursuant to notice, the witness being duly sworn by AMANDA BLOMSTROM, a Notary Public in and for the District of Columbia, taken at the offices of Cooper & Kirk, 1523 New Hampshire Avenue NW, Washington, D.C., at 9:34 a.m., Friday, May 15, 2015, and the proceedings being taken down by Stenotype by AMANDA BLOMSTROM, CRR/RMR/CLR/CSR, and transcribed under her direction.

Congress as a GSE.

Q. Okay.

A. And so that was, that was with Fannie Mae and Freddie Mac. And there were, of course, other GSEs: you have the Home Loan Bank System, the Farm Credit System, and one, Sallie Mae, which actually did go through a privatization which is exactly what they did they. They had a GSE charter by Congress, Sallie Mae, and they rescinded that charter and became what they are today, Sallie Mae, private corporate company, no GSE charter.

Q. And if the GSE charter had been revoked, was your -- did you look at: Well, what would that mean for their cost of borrowing?

A. Well, a lot of the whole report, and that's, that's been -- that was one of the issues all along and that's one of the main benefits of being a GSE, right, is that their cost of borrowing is generally much lower than it would be for another private company of similar capital and similar size and similar structure.

Q. Yes.

A. And it's, it's an interesting aspect of the whole GSE model in that Congress has granted all the GSEs various benefits through the charter --
Q. Yeah.
A. -- right, you have -- there, there was a -- with Fannie Mae and Freddie Mac, there's a small line of credit with treasury, a few billion dollars, but nothing near the size of their balance sheets, there's other benefits in terms of abusing the Fed as a fiscal agent, other various benefits that come with the GSE charter that can be enumerated, but those benefits are not that significant monetarily by themselves, but it's the whole sort of package of those benefits.
Congress created the GSEs to have a public purpose, resulted in and results today -- Fannie Mae and Freddie Mac are a little different now because they have explicit support from Treasury under the PSPAs, but even for the other GSEs, results in the market looking at them as being what most people would call implicitly backed by the government or -- or somehow supported by the government, that, that

they have less risk.
And so that results in borrowing costs being closer to Treasury than they would otherwise be if they were a fully private company.
Q. Okay. Yes.
A. Now, Sallie Mae looked at that potential calculus when they went private and said, Well, there's other things that we want to do that is not allowed by our charter, and so that is a benefit, and there was a whole lot of other issues going on in the student loan market where their basic charter business wasn't going to be nearly as profitable going forward, so they decided to rescind the charter.
Q. Now, what did your report that you were working on that first year, what did it conclude about privatization?
MS. HOSFORD: Objection. Mr. Thompson, I understand how you would want to cover Mr. Ugoletti's background, but at some point you're going to be extending into substance and time that's not within the Court's time frame, so I'd ask you to keep that

in mind.

THE WITNESS: Okay. A long time ago, it's almost 20 years ago, but, I mean, the, the general conclusion was we, we laid out, as I recall, the Treasury Department laid out, you know, the various issues associated with GSE status, raised questions of concerns about where there were risk exposures and -- and, and potential issues with risk exposure, raised issues of places where it looked like the market could step into the securitization business, there was a lot of securitization activity going on in other sectors of the economy, but did not come down with any conclusion on privatization or not. They're -- a very big issue. I mean, this is large companies. Completing the report was not an easy task.

BY MR. THOMPSON:

Q. All right. So what -- and you stayed at Treasury until 2009; is that right?

A. I did.

Q. Okay. And we'll get to the PSPA. Let, let's leave that to the side.

Q. Now, in those PSPAs, the common stockholders remained in place; is that right?

A. They did.

Q. And -- and there were warrants for 79.9 percent of the company, is that -- that were granted to Treasury with a nominal exercise price; is that right?

A. Yes. There were a number of types of compensation that were granted to Treasury as part of the PSPAs, and that was one of them.

Q. So --

A. Potential compensation.

Q. Yeah. So one of them was the warrants?

A. Yeah.

Q. A second one were dividends?

A. Yeah. There was a 10 percent dividend payment, yeah.

Q. Well, you say "10 percent dividend payment." That wasn't the only way the dividend could be paid.

A. That's true, but there was a dividend payment.

Q. Okay. So describe the dividend structure to me, the dividend payment.
A. The dividend payment was 10 percent in cash, right, based on the outstanding liquidation preference.
Q. Okay. Or?
A. Or it could be a deferred dividend that was paid at 12 percent and added to the liquidation preference.
Q. Okay. And that would be referred to as a "payment in kind"?
A. You could use that term.
Q. Okay. And you've used that term?
A. I've probably used that term.
Q. Okay. All right. Now, in terms of the warrants, the warrants made sense only if there was a view that they might have some value; is that right?
A. I'm not sure that's the only way to think about it. I mean, I think the warrants, I mean, what you're looking at with the PSPAs was trying to take what is -- would be considered a commercial contract, as best we could do it at the time, with Wachtel's

help, putting a commercial contract into this very unique situation.

So in any commer- -- if any investor was coming in in that situation, those are the types of terms you would want. You would want a dividend rate. This is a very troubled institution. You're putting a tremendous amount of funds at risk, a hundred billion initially, which is a big number, but we'll -- we'll see that that went up later, a hundred billion at risk. So you would want a significant dividend.

The pa- -- the, the deferred dividend, or I'll -- we'll use the "payment in kind" phrase, to me, that was a standard commercial contract term that I'm not sure, really, how much applicability it had in this situation.

I mean, that's -- that was put in place -- if some company is coming in to make this commitment or equity investment in another company and that other company now, for some reason, doesn't have any cash, doesn't have access to any funds, you want to continue to be able to increase your ownership stake not that you will be able to use them, then you undo the valuation allowance; is that right?

A. That is correct.

Q. Okay.

A. Those are the accounting rules that surround the marking of a deferred tax asset in general.

Q. Okay. Now, can deferred tax assets be monetized?

MS. HOSFORD: Objection. If you'd like to talk about deferred tax assets in the context of the topics that the Court has identified, I would -- I would be happy to let you do so; but you're, again, ask- -- you seem to be asking for some sort of expert testimony.

BY MR. THOMPSON:

Q. Can Fannie and -- could Fannie and Freddie monetize their deferred tax assets?

A. I am not the accountant expert here, but it's not clear to me how you monetize a deferred tax asset.

Q. Now, in the time leading up to the Net

Worth Sweep, FH- -- FHFA's projections were consistently overly pessimistic in the sense that they were below the actual operating results realized by the companies; is that right?

MS. HOSFORD: Objection; lack of foundation.

THE WITNESS: That is correct. And they were projections.

BY MR. THOMPSON:

Q. Yes.

A. And projections oftentimes are not correct.

Q. I understand.

A. Yeah. And in 2008, I had a lot of projections that I looked at from the companies and even our own projections at the first amendment that had losses of a certain level that were wildly incorrect the other way.

Q. A lot of the losses that ended up accruing were paper losses, right?

MS. HOSFORD: Objection; vague.

BY MR. THOMPSON:

Q. Like the loss of the deferred tax asset was a paper loss that was reversed?

A. Paper losses do not obviate the need to put a company in receivership. If you're balance sheet insolvent, whether it's paper losses or not, FHFA would have put the companies into receivership.

Q. And was there ever any discussion at FHFA in the second half of 2011 or first three months of 2012 saying, Gee, we should try to make our projections more accurate?

MS. HOSFORD: Objection; calls for speculation.

THE WITNESS: Again, just speculating, I mean, these are projections that were being done just to try to provide -- we had a lot of people that wanted to understand what the potential exposure of the enterprises might be.

So, in terms of your question, was there any way to make them more accurate --

BY MR. THOMPSON:

Q. Yeah.

A. -- yeah, you know, I mean, so what FHFA

Q. What do you mean by that?

A. The whole process I just went through. The whole process of initially putting the hundred in, adding another hundred, taking on unlimited exposure, that is the compensation for the full value of the commitment. Because if that wasn't put in, there wouldn't be any commitment to value.

Q. And what is your basis for saying that?

A. That's what I believe it should -- it would have been.

Q. Okay. Did --

A. I --

Q. Did you discuss that, this view, with anyone at FHFA?

A. No.

Q. Okay. Did you discuss that view with anyone at Treasury?

A. No. But if Treasury would have came to me with that position, that that's what they thought that meant, all the various commitment that they put in, I would find it very hard to argue against that.

Q. Have you ever attempted to calculate any

periodic commitment fee in any context?
A. I'm not aware of where that calculation would occur.
Q. So that's a no, you haven't done that?
MS. HOSFORD: Objection; confusing. Which commitment fee are you talking about?
BY MR. THOMPSON:
Q. Any commitment fee. Have you ever attempted to calculate what a com- -- any commitment fee should be in any context?
A. I'm not in the business of calculating commitment fees.
Q. And have you --
A. And I'm not aware of where they exist, so I guess the answer is no.
Q. You know, but you say in terms of where they exist. I mean, if you go and you get a line of credit, I mean, aren't there fees that people are charged for getting a line of credit?
A. Yeah, I, I agree. I'm --
Q. Yeah.
A. -- I'm not sure it's the same concept as

this, but there's a fee that you get for a line of credit, that's -- that's, that's true.

Q. Well, I understand the magnitude of this is bigger.

A. Yeah, that's what I'm saying, yeah. Sure, yeah, you, you charge a fee for somebody willing to provide you some amount of credit. Yeah, that's clearly one, yeah.

Q. Okay. Have you ever done such a valuation yourself of a commitment fee?

A. No.

Q. Okay. And have you ever read a valuation of a commitment?

A. Not that I recall.

Q. Okay. Isn't it true that commitment fees are calculated typically as a percentage of the amount that the borrower is willing to extend?

MS. HOSFORD: Objection; lack of foundation, calls for speculation.

THE WITNESS: Yeah, I can't, I can't speculate. I'm, I'm not the expert on commitment fees, so I can't speculate on how they're typically calculated.

BY MR. THOMPSON:

Q. Do you know of any commitment fee anywhere that's ever exceeded 10 percent of the value of the commitment?

A. I do not, but I also doubt that there is anyone that has this type of commitment in place.

Q. Do you know of any commitment fee that exceeds 1 percent of the face value of the commitment?

A. Again, I am not an expert on periodic commitment fees, but another factor of periodic commitment fees in the context of, you're talking about, in terms of lines of credits and, and issues like that, generally relate to companies making lines of credit available to creditworthy counterparties. I don't have creditworthy counterparties here.

Q. They paid back the money. What do you mean they're not creditworthy?

A. They have not paid back the money. There is 187.5 billion in liquidation preference still outstanding.

Q. Sure, I understand as a formal matter, but the United States government has taken in more than 187 billion --

A. It is a legal proceeding, that is a formal matter, they have not paid back 187.5 billion in, in liquidation preference.

Q. But the United States government has realized a positive return on its equity; is that right? They put in a hundred and 87 billion, and they got out more than a hundred and 87 billion, so that's --

A. So what --

MS. HOSFORD: Objection; argumentative.

BY MR. THOMPSON:

Q. -- is that a positive return on equity?

A. Only a positive return on equity if you consider the risk that's, that's out there.

Q. Well, it's positive, it's not negative?

A. It, it -- it's, it's not clear it's a positive return on equity.

Q. As of this moment, it's positive. Is the point you're making it might be negative someday in

Q. You did?
A. Yeah.
Q. Did -- did anyone else at FHFA provide input into his decision-making --
A. Well, it certainly was a --
Q. -- thoughts?
A. -- a legal issue, right?
Because this is a legal document, the General Counsel's office was involved.
Q. All right.
A. I do not recall if we had broader meetings within FHFA to discuss this or not at this point, but ...
Q. What was the legal issue?
MS. HOSFORD: Objection. To the extent it calls for your request for advice or advice given by Counsel in connection with this process, I will instruct -- instruct you not to answer.
BY MR. THOMPSON:
Q. So I'm not asking what your lawyer told you. I'm just asking what was the issue.
A. Right, well, what the issue was, as we

discussed earlier, the PSPAs is a contract and it's a legal contract. So if you're going to draft a legal contract, I need some lawyers to make sure they look at it.
Q. And now, you said there were some ideas for other structures.
A. Yeah.
Q. You know, what -- what were some of those ideas?
A. I went through them.
Other structures of?
Q. Give me -- I'm sorry to have a senior moment here, but just -- you said there were other structures you-all had talked about that might work.
A. Yeah, I mean --
Q. He's --
A. -- one structure could have been that as opposed to going straight from a 10 percent dividend to a Net Worth Sweep, I recall, well, maybe you could set it at -- you'd have to draw down to a hundred billion before you would go to a Net Worth Sweep.
Q. Was that something you floated --

A. Yeah.
Q. -- with Treasury?
A. I did.
Q. And what did they say?
A. They didn't like it because they -- they felt as -- that that would just be another place where any erosion of the capacity of a -- of the commitment -- you know, especially if you were in a -- in a -- in a downward situation is going to create more market problems than -- than it would -- would solve, and the market was going to test them if we put that type of structure in place, and so they did not react favorably to that suggestion.
Q. Were there other structures that were discussed with Treasury?
A. I wouldn't call them structures outside of the basic framework. There were discussions about what the buffer should be.
Q. And when you say "buffer," you mean how much retained capital --
A. Yeah --
Q. -- should be in the companies?

A. -- right, exactly. The -- right now, it started at three, goes down by 600 million every year until it hits zero. There was some discussion about whether the buffer should be ten or some other number within that range.

Q. Yeah. Who -- who wanted it lower? Did you want it higher and Treasury wanted it lower or --

A. We thought -- well, I think we both realized that it -- that it does provide some cushion. If the buffer is a little higher against quarterly fluctuations, it could cause a draw. So a higher buffer would protect against that.

But at the same time, given that the path was to reduce the risk of the companies, right, the portfolios were shrinking, that -- that's one of the main reasons, if you'd ever need a quarterly buffer to absorb some losses, we all -- very close, at least in Washington dollar terms, in the last couple quarters with the change in derivatives that I talked about, could have been a quarterly fluctuation that could have caused a draw.

Q. Because the buffer's going down to zero.

advisory bulletin on cyber security. That's a regulatory issue, but the conservator wants to have safe and sound operations and good protections against cyber security or good standards for counterparties. They did advisory bulletins on counterparties.

So if I would be reviewing that, what am I? Am I a regulator, or am I a conservator? I mean, both. They're -- they're both serving the same purpose of operating the companies in a safe and sound manner.

BY MR. THOMPSON:

Q. Okay. And because you did, you just referred in that answer to both groups, and isn't it true that at least you sometimes worked in each group?

MS. HOSFORD: Objection; lack of foundation.

BY MR. THOMPSON:

Q. Or on policies that related to each group?

A. Well -- well, right, so -- so if I got a -- if I got an advisory bulletin that came to my desk and it said, Here is an advisory bulletin that the Division of Enterprise Regulation wants to issue related to how they manage counterparty risk, right, I'm looking at -- am I going to look at that and say, Okay, I've got this hat on today, and this is why I want to look at that? No. I mean, it -- it serves both purposes, so ...

Q. Okay. Now, when you were assessing the future profitability of Fannie and Freddie in the first three-quarters of 2012, did you assume that there was a -- that FHFA had a mandate to preserve and conserve the assets of the companies?

MS. HOSFORD: Objection; lack of foundation.

You may answer.

THE WITNESS: That -- that's a fundamental part of conservatorship. That's one of the standards.

BY MR. THOMPSON:

Q. Okay. And what did -- what did you do to make sure that was -- what did you understand that mandate to include?

A. The mandate of preserving and conserving the assets?

Q. Yes, sir.

A. Right. Well, that mandate covers a number of things, all right. You'd want to be able to make sure that the companies are staying in place, because you have to preserve and conserve the assets of the companies so they're continuing to operate, so operationally there's a preserve-and-conserve aspect of that.

Q. Okay.

A. Trying to maintain some value in the companies that whenever a disposition is decided on the companies, there will be something there to dispose of.

Q. Okay.

A. So I would view it as an overall keeping the companies in place, and then there are particular preserve-and-conserve asset decisions on when you take particular actions.

Q. And when you were thinking about the future profitability of Fannie and Freddie in the

So under the 10 percent dividend, if that happened, there would be no companies to conserve, that's issue one. Under the strategic plan, where we were trying to de-risk, that would also help mitigate against the housing downturn that was going to decrease revenue; if we have decreasing revenue, that was going to call in question the ability to pay the 10 percent dividend and would further eat in the commitment. Those were the primary objectives from FHFA's perspective. This is Treasury's press release.

MR. THOMPSON: So the next one is going to be Ugoletti 36. Has a Bates number of FHFA 7767 through 7769.

(Exhibit No. 36 marked.)

BY MR. THOMPSON:

Q. Now, this is from Mr. Dickerson. Who was he?

A. I'm trying to think at that particular point in time where he worked. Right now he's, he's an assistant in the Division of Enterprise Regulation. At that time we had a small office of

Systemic Risk and Market Surveillance, so they kind of followed a lot of the -- that's why you see Bloomberg screens here, they followed a lot of this, where it was going on, some issues in the markets, whatever they were. Could be Treasury. They have people that follow the Treasury markets, things like that. So they send around little updates about what's going on.

Q. All right. So what is he referring to when he says "The 'no GSE reform is needed' trade worked for about a week"?

MS. HOSFORD: Objection; lack of foundation, calls for speculation.

THE WITNESS: Yeah, I don't know what he -- I don't know what he's talking about there.

BY MR. THOMPSON:

Q. Did it surprise you that the preferred stock got hammered the day the Net Worth Sweep was announced?

A. No. And it didn't surprise me in 2008 when the PSPAs were put in place that the preferred stock -- the market price of the preferred stock got hammered.

Q. Why did you expect the preferred stock to go down when the Net Worth Sweep was announced?

MS. HOSFORD: Objection; that misstates -- misstates prior testimony.

THE WITNESS: Well, evidently some people may have been speculating that there might be something there, but I would say that any investor that was speculating should have clearly read the agreement that said that there could be a periodic commitment fee set that could compensate Treasury for the full value of the commitment they're providing.

So I think you read that all with that set of caution in mind. So what's going on here, speculation on this that was going on all along. Look back in September.

BY MR. THOMPSON:

Q. If someone said to you on the day of the Net Worth Sweep that effectively it national- -- the Net Worth Sweep nationalized Fannie and Freddie, how would you respond to that?

MS. HOSFORD: Objection; calls for