#2009-253
Terminates **#N06-001**

UNITED STATES OF AMERICA
DEPARTMENT OF THE TREASURY
OFFICE OF THE COMPTROLLER OF THE CURRENCY

In the Matter of:	)	
	)	**FINAL DECISION AND ORDER**
Carlos Loumiet, Esq.	)	**OCC-AA-EC-06-102**
Former Counsel to	)	
Hamilton Bank, N.A. (Closed)	)	
Miami, Florida	)	

JOHN C. DUGAN, Comptroller of the Currency

INTRODUCTION

In November 2006, Enforcement & Compliance ("E&C"), pursuant to 12 U.S.C. §§ 1818(b) and (i), served a notice of charges against Mr. Carlos Loumiet, then a partner in the law firm of Greenberg & Taurig LLP ("Greenberg"), seeking a cease-and-desist order ("C&D") and an assessment of a $250,000 civil money penalty ("CMP"). Greenberg had been retained by the audit committee of Hamilton Bank, N.A. ("Hamilton" or "bank") to investigate whether senior management of the bank had knowingly concealed their participation in "adjusted price trades" in connection with the sale in 1998 of four Russian loans with a collective par value of approximately $20 million and the contemporaneous purchase of replacement debt. After Greenberg collected evidence clearly supporting the conclusion that the bank had knowingly participated in adjusted price trades, Mr. Loumiet wrote two reports in which he concluded that the evidence did not support the finding that the simultaneous trades had been knowingly made or that bank management had mislead the bank's auditors regarding their knowledge of the transactions as adjusted price trades.

Under 12 U.S.C. § 1813(u)(4), in order to find that an independent contractor like Mr. Loumiet is an institution affiliated party ("IAP") and, therefore, subject to the agency's authority to impose a sanction, the agency must establish three elements: There must be a certain form of **Misconduct** (here, breach of fiduciary duty), a certain form of **Culpability** (the independent contractor must "knowingly or recklessly" participate in the misconduct), and a certain form of **Effect** (the misconduct "caused or is likely to cause more than a minimal financial loss to, or a significant adverse effect on, the insured depository institution").

Because the conclusion reached by Mr. Loumiet in the reports (that there was no convincing evidence showing that bank officers had knowingly engaged in the adjusted price trades) departed so strikingly from the evidence included in the reports, E&C

charged that Mr. Loumiet in providing his services satisfied each of the elements necessary to find him to be an IAP under 12 U.S.C. § 1813(u)(4)(B). E&C sought to impose a C&D under 12 U.S.C. § 1818(b)(1) contending that Mr. Loumiet's preparation of the clearly inaccurate reports for use by the bank's audit committee constituted an unsafe or unsound practice in conducting the business of the bank. E&C also assessed a CMP under 12 U.S.C. §§ 1818(i)(2)(B)(i)(II), and (III) contending that Mr. Loumiet recklessly engaged in an unsafe or unsound practice in conducting the affairs of the bank and recklessly breached his fiduciary duties to the bank by preparing the inaccurate reports for the bank's audit committee. Following a hearing, Administrative Law Judge ("ALJ") Ann Z. Cook issued a recommended decision ("RD") finding that the charges should be dismissed because, among other reasons, E&C failed to establish any of the required elements of IAP status.

After carefully reviewing the exceptions filed by the parties to the RD and the entire record, the Comptroller finds that many of the findings and conclusions of the RD should be rejected. The record establishes that Mr. Loumiet could have breached his fiduciary duty of care and candor and met the **culpability** requirement for IAP status by *recklessly* breaching those two duties. However, consideration of these issues was materially hindered by the ALJ's abuse of discretion in precluding E&C's expert, Professor James P. Fleissner, from testifying. His testimony would have provided a context for judging whether or not Mr. Loumiet breached his duties of care and candor and, if so, whether these breaches were reckless. Nevertheless, on this record, for reasons explained below, the Comptroller finds insufficient evidence concerning the **effect** of Mr. Loumiet's conduct to establish this element necessary to hold him responsible as an IAP. Accordingly, all of the elements of IAP status have not been satisfied.

The ALJ's abuse of discretion in precluding the testimony of a key witness normally would counsel for remand of the case with instructions to permit the proffered testimony and to issue a new recommendation in light of that testimony. However, because the record does not establish the "effect" element of IAP status, this case will not be remanded and the charges against Mr. Loumiet are dismissed.

FACTS

The Adjusted Price Trades

In September 1999, OCC examiners discovered what appeared to be "adjusted price trades" involving the bank's sale in September 1998 of four Russian loans and the purchase at the same time of Latin American and other debt obligations. Adjusted price trades are trades in which one asset is sold for a price above its fair market value and replaced by another asset purchased for a price above fair market value. The economic result of the trades is a sale and purchase of assets at their fair market values, net transaction costs, but the loss on the sold asset is obscured by the adjusted prices. Such knowing trades are not illegal or fraudulent *per se*. However, under GAAP, the exchanges must be recorded as related transactions with any resulting losses recognized at the time of the exchange.

The bank's adjusted price trades uncovered by the OCC examiners involved the following transactions: On September 16, 1998, the bank sold a City of Moscow loan with a par value of $6 million. On September 18, 1998, the bank sold a Gazprombank loan with a par value of $5 million. On September 21, 1998, the bank sold a Vneshtorgbank loan with a par value of $1.5 million. And, on September 28, 1998, the bank sold a Mezhcombank loan with a par value of $7.5 million. For the first three sales, the bank sold the loans to West Merchant Bank, Ltd. ("WM Bank") and bought contemporaneously from WM Bank, through an intermediary, Morgan, Grenfell & Co. ("MGC"), debt securities primarily from Latin America. In connection with the last transaction, the bank sold the Mezhcombank loan to Standard Bank of London, Ltd. ("Standard Bank") and bought Latin American debt securities from Standard at the same time. In all, the bank overpaid for the debt purchased in these transactions by approximately $22 million. The aggregate face value of the Russian loans was approximately $20 million and prior to their sale the OCC had required reserves for loss on The City of Moscow, Gazprombank, and Vneshtorgbank loans equal to approximately $3 million. At the time of these transactions, neither Hamilton nor its holding company recognized the losses on the sale of the Russian loans as required by GAAP.

The OCC Temporary C&D and Deloitte's Reaction to OCC Provided Evidence

Focusing on these transactions, in April 2000, the OCC issued a temporary cease-and-desist order to the bank requiring that the bank take certain remedial actions. On September 8, 2000, the bank, based upon legal advice provided by Mr. Loumiet and others, entered into a consent order with the OCC in which the bank, without admitting wrongdoing, agreed to adopt procedures needed to prevent future adjusted price trades. The OCC also required the bank to amend its Call Reports to reflect that it had overpaid for the assets acquired in the adjusted price trades. The bank's holding company, however, disagreed with the OCC's position and did not restate its 1998 financial statements at that time to reflect the losses.

In connection with the OCC's enforcement action against the bank, the OCC had obtained counterparty documents on the trade transactions. After entry of the above consent order, the OCC provided those documents, called the "box of records," to the bank with the express direction that the bank share the box of records with Deloitte & Touche ("Deloitte"), the outside auditor for the bank and holding company. In July 2000, Deloitte reviewed the box of records and its previous accounting for the transactions. In subsequent discussions, the OCC told Deloitte that it believed the bank knowingly sold the Russian loans in excess of their market value and knowingly overpaid for the debt securities they purchased. In the OCC's view, "the Bank had knowledge of what the counterparties' pricing was and what the counterparties ultimately did with those securities and the buy/sells were in fact the same parties in all cases." JX 6 at 4.

In Deloitte's view, the "concerns expressed by the OCC and the documents obtained from the counterparties raised both potential accounting issues ***and*** potential integrity issues with respect to individuals who may have been involved in the transactions."[1] *Id.* (emphasis added). In early August 2000, Mr. Joseph Echevarria, the Deloitte partner overseeing the Hamilton audit, consulted with the Deloitte national office. *Id.* That consultation led to a request by Deloitte to the Hamilton audit committee that the committee retain a law firm to conduct an independent investigation "in order to (1) review the Bank's understanding and involvement with respect to the structure and pricing of the transactions it entered into and (2) determine whether any oral or written misrepresentations had been made to Deloitte in the course of conducting the audits of the Bank's financial statements." *Id.* at 4-5. In the meantime, Deloitte ceased providing accounting services to the bank.

In a memorandum to file in August 2000, Mr. Echevarria memorialized his discussion with the audit committee about the dual purpose of the investigation:

> We discussed at length [with bank officials], why we were asking them to engage an independent counsel and not an accounting firm. We reiterated that we were not only looking for an accounting conclusion but for information and documentation of the transactions to understand whether (1) the individuals involved in the transactions had misrepresented their understanding of the transactions to the Bank, and/or us; or (2) the individuals involved in the transactions misunderstood the agreement or the understanding of the counter parties, which may have resulted in a different accounting conclusion at the time.

JX 65 at 1.

In that same August 2000 memorandum, Mr. Echevarria stated that he told bank management that, if the investigation concluded that misrepresentations had been made, Deloitte would need to consider what remedial actions needed to be taken by the bank's board or audit committee before Deloitte would make a decision about whether it would resume providing audit services to the bank:

> I discussed very clearly [with bank officials], the potential consequences, should it turn out any misrepresentations by individuals involved in the transactions were made. I indicated that if the investigation concluded there were misrepresentations, we would need to consider the Board

[1] The following bank officers were involved in the transactions: Eduardo Masferrer, Hamilton's Chairman and Chief Executive Officer ("CEO"), Juan Carlos Bernace, the bank's President, and John Jacobs, the bank's Chief Financial Officer ("CFO") (collectively "senior officers"). These senior officers were also officers at the holding company.

> and the Audit Committee's remedial actions. [Describe in detail what consequences discussed].

Id. at 1 (bracketed material in original); *see also* Tr. 1437 (Echevarria) (testifying that the suspension of audit services "put the audit committee and the board of directors on notice that it was a severe matter and, until it was resolved, we would not reengage"). Despite the notation "Describe in detail what consequences discussed," there is no documentary or testimonial evidence in the record stating what those consequences would have been. Mr. Echevarria was not asked at the hearing about the remedial actions Deloitte would have requested or demanded if the investigation determined that the senior officers had lied to Deloitte and to the audit committee, and no member of the audit committee testified.

Greenberg Taurig Engaged to Conduct Investigation

The audit committee retained Greenberg to conduct the investigation, which began in September 2000.[2] Mr. Loumiet, a partner at Greenberg, did not participate in the investigation initially but became increasingly involved and ultimately was the principal author of the two reports submitted to the bank's audit committee. At the commencement of Greenberg's investigation, the OCC provided Greenberg with the same box of records the OCC had provided to the bank and Deloitte.

Loumiet's November Report Finding No Agreement and No Convincing Evidence Officers Intentionally Misled Audit Committee or Deloitte

On November 15, 2000, Greenberg presented its first report ("November Report"), written by Mr. Loumiet, to the audit committee. The November Report concluded that there had been no agreement "certainly in any legal sense of the word" regarding a swap or exchange of assets, and that there was no "convincing evidence" indicating that the senior officers had "intentionally misled" Deloitte or the audit committee in connection with the adjusted price trades. JX 3 at 18. The report, however, discussed documents found in the bank's files (generated both by the bank and WM Bank) concerning the first transaction; copies of these documents were included in an appendix to the report. Those documents indicated that the sale of the Moscow loan and the contemporaneous acquisition of Latin American debt instruments were adjusted price trades.

The November Report also discussed and quoted Standard Bank documents related to the sale of the Mezhcombank loan that plainly indicated that the sale and purchases were orchestrated swaps. Specifically, the report stated: "To begin with, the memorandum dated September 28, 1998 . . . says that it 'summarize(s) the proposal [that Standard

---

[2] Greenberg was retained even though it acted as the bank's counsel for SEC matters and the investigation raised potential liability issues for the bank, Deloitte, and Greenberg under federal securities law. JX 5. Greenberg was subsequently retained by the holding company and the senior officers to represent them in a class action suit brought by the holding company's preferred and common stockholders alleging securities and banking law violations relating to the transactions.

Bank] . . . put to Hamilton last week . . .'" The November Report then quoted at length from this Standard Bank memorandum:

> Hamilton buys a package of illiquid Latin American assets presently held by SBL [Standard Bank]. (Such assets will be mainly bonds trading at a discount to face value . . . . These bonds will be purchased by Hamilton at face value . . . .
>
> The discount between the face value and the market value will be used by SBL to purchase Hamilton's US$7,500,000 participation in the Mezhcombank US$20,000,000 syndicated credit.
>
> If there is a shortfall between the discount on the face value and the 'adjusted' market value of assets held by SBL, our Emerging Markets desk will go into the market and buy deeply discounted Latin American bonds, on Hamilton's behalf, to raise the shortfall. SBL will only buy such bonds in the market when Hamilton has remitted sufficient funds to us to cover this shortfall.
>
> Only when we have cleared funds for the package of Latin American assets we are selling will we proceed with the purchase of the Mezhcombank US $7,500,000.

JX 3 at 13-14. The November Report then stated that "two other internal memoranda from [Standard Bank] . . . indicate that the Latin American loans purchased by Hamilton from Standard Bank were purchased on September 30, 1998 and settled on October 5, 1998, and that Standard Bank did not intend to purchase the Mezhcombank loan until the Latin American loans settled." *Id.* at 14.

This evidence demonstrated the necessity of Hamilton's active involvement in coordinating the sale and contemporaneous purchases of replacement debt. Nevertheless, the report concluded that there was no "convincing" evidence that Hamilton or its senior officers had knowingly participated in orchestrating the adjusted price trades. *Id.* at 23. In reaching this conclusion, Mr. Loumiet accepted the representations of the senior officers that the bank always bought and sold at par value loans intended to be held to maturity and that the sale of the Russian debt at par and the purchase of the replacement debt was consistent with the bank's historical practice. There is no evidence that Mr. Loumiet ever saw, or requested to see, the bank's policies and records regarding the purchases and sales of various debt instruments that would have shown that the bank typically made purchases at market value even where the bank intended to hold the debt to maturity, which would have demonstrated that the representations of the senior officers were false.

Loumiet's November Report Questioned, the Holding Company Amends Financial Statements to Account for Transactions as Adjusted Price Trades, and Jacobs Relieved of his CFO Duties

On November 28, 2000, Deloitte met with Mr. Loumiet to discuss the November Report, at which time Deloitte gave Mr. Loumiet a list of sixteen questions it had about the basis of the conclusions in the report. Mr. Loumiet answered these questions in December 2000 and continued to stand by his conclusion.[3] Despite Mr. Loumiet's conclusion that there was no "convincing" evidence that senior management knowingly entered into adjusted price trades, the audit committee, with the concurrence of Deloitte, determined that for accounting purposes the trades should be treated as such. JX at 6. Accordingly, in December 2000, the bank's holding company restated its financial statements to reflect the loss on the sales of the Russian debt and filed an amended 10-K with the Securities and Exchange Commission for the year ended December 31, 1998. After the restatement, the holding company's financial statements were consistent with the amended Call Reports the OCC had required the bank to file eight months earlier in April 2000. Also in response to the November Report, the Audit Committee concluded that CFO Jacobs should be barred from participating in any activities related to financial reporting, controls and significant business issues "because both the OCC and Greenberg had separately indicated Mr. Jacobs's statements were at times inconsistent." JX 61 at 2. Given Mr. Jacob's removal from his duties as CFO, the Audit Committee concluded, based on the November Report, that there was "no immediate need nor any evidence to support taking any other immediate action." *Id.*

The OCC Questions the Conclusion in the November Report

In mid-January 2001, OCC Deputy Comptroller Ann F. Jaedicke informed Mr. Loumiet about sworn testimony obtained by the OCC in connection with its enforcement action from the point of contact at WM Bank, Mr. Ian Tweedley. JX at 2. WM Bank was the counterparty for three of the trades along with another firm used as an intermediary, MGC. In her letter, Ms. Jaedicke informed Mr. Loumiet that Mr. Tweedley's testimony indicated that Hamilton's senior officers intended to execute the adjusted price trades and that Mr. Tweedley had engaged in extended conversations with bank CFO Jacobs to that effect. *Id*. According to Ms. Jaedicke's letter, Mr. Tweedley testified that he discussed with Mr. Jacobs the assets to be purchased by the bank, including their pricing, ratios, and market value.

Also, on February 8, 2001, the OCC met with Mr. Loumiet and questioned his conclusion in the November report that the bank customarily bought and sold assets at par. *Id.* The OCC also read the deposition transcript of Mr. Tweedley to Mr. Loumiet at this meeting. *Id*. at 7. In addition, the OCC gave Mr. Loumiet a list of six "red flags" indicating that the exchanges had been adjusted price trades. *Id.*

---

[3] A memorandum to file, dated December 21, 2000, by Deloitte's lead auditor, Mr. Echevarria, restated the sixteen questions Deloitte had posed to Greenberg and Greenberg's answers. JX 5.

Greenberg Taurig Engaged to Defend Bank and Executive Officers in Shareholder Class Action

During February 2001, Greenberg was retained by the bank's holding company and the senior officers to represent them in a class action suit brought by holding company investors concerning the same trades that formed the basis of the November Report. The bank's general counsel and members of the bank's board of directors, including the chair of the bank's audit committee, were ware of, and comfortable with, the situation presented by Greenberg's dual engagement, although no written waiver of the conflict of interest was obtained as required by Greenberg's conflicts policy.

Loumiet's March 2001 Report and Closing of Investigation

Mr. Loumiet responded to Deputy Comptroller Jaedicke's letter and the OCC's six "red flags" in his second report to the audit committee, dated March 14, 2001 ("March Report"). JX 2. In his March Report, he restated his conclusions in the November Report. With respect to the OCC's red flag that the bank would not have paid more for the assets than they were worth on the market unless they were part of a "swap" for the Russian loans, the March Report stated only that: "To us, this is by far the most troubling of the OCC's 'red flags.'" JX 2 at 11 (March Report). The March Report concluded:

> We do not mean to condone the way this entire process was handled within Hamilton Bank.
>
> To date, the "evidence" available to us in this investigation that Hamilton Bank intentionally entered into a disguised "swap" or "exchange" of assets with WLB [WM Bank] and DMG [MGC] can be summarized as consisting of (1) excerpted hearsay from Mr. Tweedley, subject to the limitations noted [primarily no chance to cross-exam], (2) various documents internal to WLB [WM Bank] which reflect the fact that WLB [WM Bank] itself treated these transactions as a "swap" or "exchange", and (3) a handful of circumstances that *could*, but do not necessarily, or even probably, support the conclusion that Hamilton Bank intended such a "swap" or "exchange". Noticeably, what we have not seen is *any* "evidence" *whatsoever* from within Hamilton Bank showing any intention within the bank to engage in such a "swap" or "exchange."
>
> We find that when viewed in its totality, the "evidence" available to us is not convincing that Hamilton Bank intentionally engaged with WLB [WM Bank] in a disguised "swap" or "exchange" in connection with the sale of Russian loans and purchase of Latin American assets, nor is such "evidence" convincing that management at Hamilton

> Bank intentionally misled Deloitte & Touche or your Committee (or has demonstrated a lack of integrity) about these matters.

Id. at 14 (emphasis original). The conclusion added a footnote about the Standard Bank transaction, stating that it was already discussed in the November Report, and that CFO Jacobs had denied statements made by a representative of Standard Bank about conversations he had with Mr. Jacobs. The March Report did not address the fact that the Standard Bank documentation, as described and quoted in the November Report, shows that the transactions were necessarily adjusted price trades.

In April 2001, Deloitte met with Mr. Loumiet about the status of his investigation. He informed Deloitte that no reports or investigative activities had occurred since the March Report. At that point, Deloitte concluded that, given the investigation and "remedial actions" already in place, Deloitte was "willing to rely on management's representations and to proceed in performing audit services." JX 68 at 2.

Aftermath

On January 11, 2002, the OCC determined that the bank had been operating in an unsafe or unsound manner, closed the bank, and appointed the Federal Deposit Insurance Corporation as its receiver.

In October and December 2003, the bank's CEO, Mr. Masferrer, and the bank's President, Mr. Bernace, without admitting or denying liability, entered into consent orders with the OCC regarding the adjusted price trades. E&C Notice at 8. The orders bar them from participating in the affairs of any insured depository institution.[4] In 2005, Mr. Jacobs agreed to be prohibited from participating in the affairs of any insured depository institution. *Id*. at 9. In October 2006, Greenberg entered into a settlement agreement and consent order with the OCC that related to the investigation. The consent order required Greenberg to pay a CMP of $750,000. *Id*. at 11.

[4] In June 2004, the senior officers were indicted by a grand jury in the U.S. District Court for the Southern District of Florida for bank and securities fraud concerning the September 1998 adjusted price trades, among other things. E&C Notice at 8-9. In 2005, Messrs. Bernace and Jacobs pled guilty to lesser charges. *Id.* In May 2006, a jury convicted Mr. Masferrer of sixteen counts relating to the adjusted price trades and their concealment. Mr. Masferrer was sentenced to thirty years in prison. *Id.* Messrs. Bernace and Jacobs were sentenced to twenty-eight months in prison. In October 2006, the district court ordered Mr. Masferrer to pay criminal restitution in the amount of $17.2 million and held Messrs. Bernace and Jacobs jointly and severally liable for $14.5 million in criminal restitution. The court found that the adjusted price trades caused a net loss of $22.2 million to the bank, subsequently reduced to $14.5 million by principal reductions and increases in asset values. *Id.* at 9. In June 2008, the U.S. Court of Appeals for the Eleventh Circuit affirmed the conviction of Mr. Masferrer. *United States v. Masferrer*, 514 F.3d 1158 (11th Cir. 2008).

THIS ENFORCEMENT PROCEEDING

In November 2006, E&C served a notice of charges upon Mr. Loumiet, as an IAP, seeking the issuance of a C&D barring Mr. Loumiet from providing legal services to any insured depository institution or its affiliates and the imposition of a CMP of $250,000. As pertinent here, E&C asserted that the bank engaged Mr. Loumiet as an independent contractor to provide services to the audit committee and that his conduct met all elements necessary to establish his status as an IAP. Specifically, the notice alleged:

(1) ***Misconduct:*** Mr. Loumiet breached his fiduciary duty to the bank's audit committee in three ways: (a) he breached his fiduciary duty of care by not reviewing the bank's policies, practices, and records relating to the purchase and sale of debt instruments of the type involved, including failure to verify in the bank's books and records that such loans were, in fact, purchased and sold at par value as the senior officers had claimed (had he done so, E&C asserted, he would have discovered that the senior officers' representations were untrue); (b) he breached his fiduciary duty of candor by misrepresenting the results of the evidence in his possession (the preponderance of the evidence, E&C asserted, indicated that the bank's officers, in fact, knowingly engaged in adjusted price swaps); and (c) he breached his fiduciary duty of loyalty because of his conflict of interest related to Greenberg's retention in February 2001 to defend the bank and its senior officers in the class action suit brought by bank investors;

(2) ***Culpability*****:** Mr. Loumiet's alleged misconduct was undertaken knowingly or recklessly; and

(3) ***Effect/Causation:*** Mr. Loumiet's alleged misconduct caused the requisite harm to the bank by: (a) exonerating senior officers engaged in felonious activity; (b) facilitating the continued material overstatements of the bank's capital and income in the holding company's financial statements; and (c) depriving the bank of the value of the $210,000 it paid for Loumiet's reports.

Based upon its assertion that Mr. Loumiet acted as an IAP, E&C sought: (1) a C&D under 12 U.S.C. § 1818(b)(1) alleging that he engaged in an unsafe or unsound practice in conducting the business of the bank; and (2) a CMP under 12 U.S.C. § 1818(i)(2)(B) alleging that he recklessly breached his fiduciary duty to the bank.

The enforcement action was tried before ALJ Cook in October 2007. On June 17, 2008, ALJ Cook issued the RD concluding that the charges should be dismissed because E&C had failed to establish ***any*** of the three necessary elements of IAP status. ALJ Cook also concluded, relying upon *Grant Thornton LLP v. OCC*, 514 F.3d 1328 (D.C. Cir. 2008), that Mr. Loumiet provided legal services only and, therefore, did not participate in an "unsafe or unsound practice" for IAP purposes, 12 U.S.C. § 1813(u)(4), or engage in an "unsafe or unsound practice" in conducting the business of the bank for purposes of a C&D, 12 U.S.C. § 1818(b)(1).

On September 19, 2008, pursuant to 12 C.F.R. § 19.39, both E&C and Mr. Loumiet filed exceptions to the RD. E&C does not challenge the ALJ's conclusions based upon *Grant Thornton* that the provision of legal services is not a banking practice and, therefore, cannot form the basis for an allegation that Mr. Loumiet participated or engaged in an "unsafe or unsound [banking] practice" in providing those services for purposes of the IAP or C&D statutes. In its exceptions, however, E&C, for the first time, asserts with respect to its request for a C&D that Mr. Loumiet engaged in an unsafe or unsound practice in conducting the business of the bank "through his advisory role in the Bank's unsafe or unsound decision not to dismiss or discipline its 'corrupt' senior officers."[5] E&C Exc. at 40.

On October 30, 2008, the Comptroller, pursuant to 12 C.F.R. § 19.40(a), issued an order notifying the parties that the proceeding had been submitted to the Comptroller for final decision. The ninety-day time period for issuing a final decision, 12 C.F.R. § 19.40(c)(2), has been extended to and including July 28, 2009.

DISCUSSION

Under 12 C.F.R. § 19.40, the Comptroller renders a final decision based upon a review of the entire record of the proceeding including the exceptions filed by the parties. In doing so, the Comptroller is not bound by the RD of ALJ Cook or the exceptions submitted by the parties. 12 C.F.R. § 19.40(c).

In its exceptions, E&C challenges the ALJ's conclusions that Mr. Loumiet did not breach his fiduciary duties, did not act with the requisite recklessness, and did not cause the requisite actual or potential harm to become an IAP. Mr. Loumiet's exceptions assert that the investigations and reports constituted protected speech under the First Amendment to the Constitution of the United States.

A. ***Misconduct and Culpability***

E&C charged that Mr. Loumiet satisfied the misconduct and culpability requirements for IAP status under 12 U.S.C. § 1813(u)(4)(2) by recklessly breaching his fiduciary duties of care, loyalty, and candor to the bank. Regarding substantive standards, there is no dispute between Mr. Loumiet and E&C about what the fiduciary duties of care, candor, and loyalty generally require. "Recklessly," as used in the IAP statute, calls for an objective standard. In *In the Matter of Augustus I. Cavallari*, OCC–AA–EC–92–115 (1994), the Comptroller applied an objective standard for "reckless" conduct, stating that in the non-criminal context, "'[t]he usual meaning assigned to . . . . 'reckless' . . . is that the actor has intentionally done an act of an unreasonable character in disregard of a

[5] This Final Decision does not address the applicability of *Grant Thornton* or whether E&C is precluded from raising this new articulation regarding Mr. Loumiet's alleged "unsafe or unsound practice." Regardless of any impact that *Grant Thornton* would or would not have had on the imposition of a C&D here, it would not have affected the imposition of a CMP because the CMP statute permits the imposition of a penalty based upon the breach of a fiduciary duty and, in that context, does not require that the breach of duty occur in "conducting the affairs" of the bank.

known or obvious risk so great as to make it highly probable that harm would follow, and which thus is usually accompanied by a conscious indifference to the consequences.'" *Id.* (citing, at 10, Liability of Attorneys, Accountants, Appraisers and Other Independent Contractors under the Financial Institutions Reform, Recovery, and Enforcement Act of 1989, 42 Hastings L. J. 249, 274 n.157 (1990) (*quoting* W. Prosser & W. Keeton, The Law of Torts 213 (5th Ed. 1984) for the civil standard)). Under the bank regulatory statutes, conduct is reckless if it is undertaken in disregard of a known or obvious risk of substantial harm. *Id.*; *Cavallari v. Office of the Comptroller of the Currency*, 57 F.3d 137, 142 (2nd Cir. 1995) (citing the Comptroller's final decision in *Cavallari* in defining reckless conduct in this context). It does not require that actors subjectively know or intend that their conduct will result in harm, only that an objective observer in the circumstances would recognize the obvious risk of substantial harm and take required steps to avoid it. *Id.* Thus, the standard precludes the necessity of finding "intent" or "scienter" to conclude that an IAP acted "recklessly." *Id.*

At the hearing, however, ALJ Cook precluded E&C's expert, Professor Fleissner, from testifying about what duties are required of an attorney retained to conduct an investigation of the type undertaken here. His proffered testimony indicates that he would have opined that Mr. Loumiet recklessly violated his fiduciary duty of care by failing to request and examine readily accessible documentation of the bank's investment policy and trading history, which would have revealed that the bank was not following its usual practice when it engaged in the adjusted price trades. Expert Report of James P. Fleissner at 12-15 (Exhibit A to E&C's Resp. in Opp. to Motion in Limine) ("Expert Report").[6] He also would have opined that Mr. Loumiet breached his fiduciary duty of candor by misframing the issue of whether there was an agreement concerning linked trades in terms of a documented and legally enforceable agreement and that this misframing seriously undermined the accuracy of the November report. In Professor Fleissner's view, by defining "agreement" as having indicia of a legitimate, enforceable contract, the November report "dodged" the central question that Mr. Loumiet was retained to investigate, namely whether illicit trades knowingly took place that caused material losses to the bank that were not recognized on the bank's financial statements. *Id*.

The Comptroller finds that the ALJ abused her discretion in not permitting Professor Fleissner to testify. Under 12 C.F.R. § 19.36, the standard applicable to the admission of evidence is a liberal one. Evidence that might be inadmissible under the Federal Rules of Evidence may not be ruled inadmissible so long as such evidence is relevant, material, reliable, and not unduly repetitive. *Id.* There is no credible argument that Professor Fleissner's testimony would have been irrelevant, immaterial, unreliable, and unduly repetitive. Professor Fleissner's testimony would have been relevant to whether Mr. Loumiet breached his fiduciary duty of care and, if so, whether that breach was reckless under the circumstances. And, there is no doubt that the testimony would not

[6] Professor Fleissner also would have testified that, although the audit committee and Deloitte were free to draw their own conclusions, the failure to state in the Reports the standard of proof by which he weighed the evidence was a breach of the duty of care by Mr. Loumiet, because Deloitte and the audit committee were not lawyers.

have been repetitive inasmuch as the ALJ concluded that E&C failed to present expert testimony or other evidence on what the fiduciary duty of care required in this circumstance.

1. The Duty of Care

The fiduciary duty of care requires that a lawyer provide legal services with competence and diligence. RD at 11 (citing Restatement of the Law (Third), the Law Governing Lawyers § 16). E&C asserts that had Mr. Loumiet conducted his investigation with the competence and diligence required under this circumstance, he would have discovered the bank's policy to buy and sell debt instruments at their fair market value and he would have discovered that the bank, in fact, usually bought and sold such instruments at fair market value – not par value as the senior officers had claimed. In this regard, E&C contends that Professor Fleissner would have established what the fiduciary duty of care required in this circumstance and that Mr. Loumiet breached that duty by failing to review the bank's investment policy and trading history.

With respect to culpability, Professor Fleissner concluded that, in his view, Mr. Loumiet's:

> failure to fulfill his duties to investigate and report were, at least, reckless in that Mr. Loumiet must have consciously disregarded an obvious risk that his investigation was incomplete and his reports inaccurate. The breach of fiduciary duty is fundamental and obvious because important information was not discovered and disclosed and the reports as written did not completely and accurately report information that had not only the potential to influence the Bank's decisions, but a real possibility of altering the decision-making of the Bank on matters of great significance to the Bank.

Expert Report at 19-20.

The obvious risk of substantial harm (relevant to recklessness) here, according to E&C, was that a failure to conclude that the senior officers misrepresented the nature of the trades, as dictated by the evidence, would enable dishonest officers involved in felonious conduct to continue to run the bank, engage in other illegal or unsafe or unsound practices, cause continuing misstatement of the financial statements of the bank or its holding company, and deprive the bank of the benefit of its engagement of Greenberg.

The ALJ's ruling on the motion in limine was prejudicial error. Where the truth of the senior officers' representations was a principal focus of the investigation Mr. Loumiet was engaged to conduct, and where so much of the evidence collected demonstrated that the bank had engaged in adjusted price trades, an ALJ and the Comptroller, with the assistance provided by Professor Fleissner's testimony regarding an attorney's fiduciary

duties when conducting an investigation of the type Mr. Loumiet was hired to perform, would be in a much better position to assess whether Mr. Loumiet participated in reckless misconduct by continuing to accept the senior officers' representations at face value and by failing to request access to the bank's investment policy and trading history in order to corroborate their explanation.

2. Duty of Candor

The fiduciary duty of candor requires truthfulness and honesty. RD at 11 (citing Restatement of the Law (Third), the Law Governing Lawyers § 16). In his proffered testimony, Professor Fleissner opined that Mr. Loumiet mischaracterized the nature of the inquiry in order to protect the senior officers. In his opinion, Mr. Loumiet consistently misframed the issue as whether the documents and witness accounts establish a "legal" agreement and that in doing so Mr. Loumiet "improperly limit[ed] the scope of the investigation and the [November] report." Expert Report at 14.

Professor Fleissner's testimony would have provided a context for judging whether or not Mr. Loumiet breached his fiduciary duty of candor and assisted the ALJ and the Comptroller in determining whether Mr. Loumiet recklessly breached that fiduciary duty in the context of the investigation he was conducting.

3. Duty of Loyalty

The duty of loyalty requires that an attorney avoid conflicts of interests. RD at 11 (citing Restatement of the Law (Third), the Law Governing Lawyers § 16). The ALJ recognized that Mr. Loumiet had a conflict of interest as a result of his duty to independently investigate the senior officers while his law firm, Greenberg, at the same time undertook to defend the bank's holding company and the senior officers in a class action suit based upon securities and banking law fraud brought by the holding company's shareholders based upon the bank's sale of the Russian debt. The ALJ recognized that Greenberg's defense team in the class action suit had a strong incentive to find that the senior officers had not engaged in adjusted price trades. RD at 14. At the same time, Mr. Loumiet's investigation had to be free of bias with respect to whether the senior officers had misrepresented the trades. *Id.* Nevertheless, the RD concluded that Mr. Loumiet was not required by his duty of loyalty to withdraw his representation despite the obvious conflict of interest. *Id.*

E&C in its exceptions argues that there is no support for this conclusion because the Florida Rules of Professional Conduct do not recognize any exception that would permit a lawyer to continue representation where a conflict exists absent a waiver. E&C further maintains that the Florida Rules of Professional Conduct provide that in situations where the attorney (or his firm) has a conflict and the attorney (or his firm) has a policy of obtaining waivers in writing, the attorney (or his firm) must withdraw or obtain a *written* waiver in order to proceed with the representation. Here, although a clear conflict existed, no written waiver was obtained.

This record, however, does not support a conclusion that the breach was reckless. The record evidence indicates that an unwritten waiver was obtained, that the audit committee considered the conflict, and that both the audit committee and the board of directors were "comfortable" with the double engagement. Tr. 2957-59 (Alfieri); *see also* Tr. 1657 (Moore) (testifying that the bank's general counsel was aware of the issue). Under these circumstances, the record does not support the conclusion that Mr. Loumiet disregarded a known or obvious risk of harm by failing to assure that Greenberg had obtained a written waiver.

B. ***Effect/Causation***

In order to be an IAP, an independent contractor's wrongful conduct must have "caused or [be] likely to cause more than a minimal financial loss to, or a significant adverse effect on," the bank. E&C maintains that the conclusions reached in Mr. Loumiet's reports (which are the embodiment of his alleged misconduct): (1) deprived the bank of the value of the $210,000 it paid for the reports; (2) enabled senior officers engaged in felonious activity to remain at the bank longer than they would have otherwise; and (3) caused the continued material overstatements of the bank's capital and income in the holding company's financial statements. E&C also asserts in its post-hearing brief and in its exceptions to the RD that Mr. Loumiet's misconduct enabled dishonest management to approve, between the time the November Report was issued and the issuance of the March Report, an unsafe or unsound $15 million loan that was never repaid. The ALJ rejected E&C's contentions.

With respect to E&C's contention that the "effects" prong of IAP status is satisfied because the bank did not receive value for the $210,000 it paid for the reports, the record does not support the conclusion that the actual injury or potential harm to which the bank was exposed is of the type or severity contemplated by the IAP statute. The most natural reading of the "effects" language as used in 12 U.S.C. § 1813(u)(4) is that it normally encompasses harm that includes elements other than whether the bank received full value for the amount the bank paid for services.

To establish that the reports caused or were likely to cause harm to the bank by enabling senior officers engaged in felonious activity to remain at the bank, it was necessary to demonstrate that the bank or the OCC likely would have removed the officers had the reports concluded that that one or more of the officers of the bank had knowingly misrepresented the nature of the transactions at issue. However, there was no testimony from members of the audit committee, members of the board of directors, Deloitte, or an OCC official concerning what remedial steps would have been taken had the reports concluded that the senior officers misrepresented their knowledge about the linked nature of the trades. Removal would have been one option available, but there were a range of other outcomes. For example, the holding company or the bank may have taken the same type of actions as those taken in response to the November Report, *i.e.*, restatement of the holding company's financial statements, removal of Mr. Jacobs from his responsibilities as CFO and similar restrictions for other officers who were shown to have been involved

in the misrepresentations. Although the OCC presumably could have removed the senior officers under these circumstances, there is no evidence in the record to that effect.

E&C further maintains that the "effect" element of IAP status is established because the conclusions in Mr. Loumiet's November Report caused the holding company to continue to materially misstate its financial statements. On this record, however, the evidence is insufficient to establish that the conclusions in the November Report caused or were likely to cause requisite harmful effect to the bank. First, the report had no effect on the bank's financial statements because the record reflects that, at the OCC's request, it had amended its income and capital statements eight months prior to the issuance of the November Report. Moreover, despite the report's conclusions, evidence of the linked transactions as well as Mr. Loumiet's detailed discussion of that evidence was included in the November Report. The evidence discussed in the report led the bank's audit committee, with the concurrence of Deloitte, to conclude promptly that the linked transactions should be treated as adjusted price trades for accounting purposes, which, in turn, prompted the holding company to restate its financial statements shortly thereafter. Notwithstanding Mr. Loumiet's conclusions, the record evidence of the November Report shows that it likely would have led to a restatement of the holding company's financial statements, which, in fact, is what occurred. Thus, the record fails to establish that the report's conclusions, which were at odds with the detailed evidence contained in the report, likely would have caused actual or potential harm to the bank.

Finally, E&C relies for proof of "effect" upon the unchallenged statement by an OCC examiner that, in the period between the November and March reports,[7] Mr. Masferrer approved a $15 million loan to an offshore entity that had been created either the same day the loan was made or the day before and that the loan was unsafe or unsound because there was no source of repayment or stated purpose for the loan. Tr. 916-17 (Rardin). Because there was no repayment capacity, the OCC required that the bank write off the loan and, after the bank was closed, the FDIC, as receiver, was unable to recover any of the proceeds. *Id*.

There are several problems with E&C's reliance on this event to satisfy the "effect" element for IAP status. None of the transaction documents nor any specific details regarding this loan are in the record. The first reference to this loan was during the cross-examination of NBE Rardin and he acknowledged that he had not reviewed the transaction documents in connection with this case and provided few details related to the loan. Consequently, from the record, it is impossible to determine the precise date the loan was made or that the bank necessarily would have taken any action prior to the date the loan was made to prevent the senior officers from engaging in that transaction. Also, as discussed above, without evidence of the remedial action that the bank's board would have taken had Mr. Loumiet's report concluded that one or more officers had knowingly participated in the adjusted price trades and misrepresented their knowledge concerning the transactions, the record simply does not demonstrate how the November Report would have kept the loan from being made. The record is particularly lacking in

[7] Because this event occurred before the March Report was issued, any harm to the bank can only be attributed to effect of the conclusions in the November Report.

evidence that the board necessarily would have taken action to prevent Mr. Masferrer from engaging in the $15 million loan. While the record shows that Mr. Loumiet had evidence of Mr. Jacobs's direct involvement in the trades prior to the issuance of the November Report, the record does not show that Mr. Loumiet had similar evidence of the direct involvement of Mr. Masferrer, and the board's action may have been limited to removal of Mr. Jacobs or greater restrictions on his authority at the bank.[8] In short, although it is possible that the board could have taken action to prevent Mr. Masferrer from making the $15 million loan had Mr. Loumiet's November Report reached conclusions that are more consistent with the evidence included in that report, the record lacks evidence of the actions that they would have taken.

CONCLUSION

For all of the foregoing reasons, the RD is largely rejected for the reasons set forth in this decision. Moreover, the ALJ abused her discretion in precluding the testimony of E&C's expert witness on the fiduciary duties of care and candor in the context of the investigation Mr. Loumiet was engaged to perform on behalf of the bank's audit committee. This case will not be remanded, however, because the record lacks sufficient evidence that the two reports prepared by Mr. Loumiet caused, or were likely to cause, harm to the bank that satisfies the "effect" requirement to hold Mr. Loumiet responsible as an IAP. Accordingly, the charges against Mr. Loumiet are dismissed.

_____/s/_________________________ Dated: July 27, 2009
John C. Dugan
Comptroller of the Currency

[8] On this record, had Loumiet stated in the November Report that the evidence supported the conclusion that Mr. Jacobs had knowingly engaged in the adjusted price trades and misrepresented the transactions, Mr. Loumiet may not have acted recklessly in failing to identify Mr. Masferrer as complicit in the misconduct, even if his failure to develop more evidence regarding the participation of Mr. Masferrer may have breached his fiduciary duty of care.