IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF PUERTO RICO

FEDERAL DEPOSIT INSURANCE CORPORATION, as Receiver for Eurobank,

Plaintiff,

v.

RAFAEL ARRILLAGA-TORRÉNS, JR.; WILLIAM TORRES-TORRES; LUIS HERNÁNDEZ-SANTANA, his spouse NORA LOPEZ-RODRIGUEZ, and the HERNÁNDEZ-LOPEZ CONJUGAL PARTNERSHIP; RICARDO LEVY-ECHEANDÍA, his spouse LOURDES ARCE-RIVERA, and the LEVY-ARCE CONJUGAL PARTNERSHIP; ANTONIO PAVÍA-BIBILONI, his spouse JUDITH VIDAL-GÓMEZ, and the PAVÍA-VIDAL CONJUGAL PARTNERSHIP; PEDRO FELICIANO-BENÍTEZ; PLÁCIDO GONZALEZ-CORDOVA; JUAN GÓMEZ-CUÉTARA, his spouse ROCIO GIL-GÓMEZ, and the GÓMEZ-GIL CONJUGAL PARTNERSHIP; DIANA LOPEZ-FELICIANO; LIBERTY MUTUAL INSURANCE COMPANY; ACE INSURANCE COMPANY; and XL INSURANCE COMPANY;

Defendants.

Case No. 13-01328

<u>Gross Negligence, Declaratory Judgment, Damages</u>

<u>Plaintiff Demands Trial by Jury</u>

<u>COMPLAINT AND DEMAND FOR JURY TRIAL</u>

TO THE HONORABLE COURT:

Plaintiff, the Federal Deposit Insurance Corporation ("FDIC"), as Receiver for Eurobank of San Juan, Puerto Rico ("Eurobank" or "the Bank"), files the following Complaint and shows the Court as follows:

I. PRELIMINARY STATEMENT

The FDIC brings this lawsuit to recover over $55 million in losses the Bank suffered on twelve (12) commercial real estate and business loans approved by the defendants named herein that were directors of the Bank ("Director Defendants") between March 6, 2006, and December 22, 2008 ("Loss Loans"). The Director Defendants approved these loans in violation of the Bank's Loan Policy ("Loan Policy"), in contravention of safe and sound banking practices, and without any reasonably probable chance of repayment based upon the information before them. The approval of these loans badly diminished the Bank's capital which thereby threatened the Bank's continued existence. The Director Defendants approved these loans despite numerous warnings from multiple sources about serious problems in the Bank's commercial credit function and their construction loan department. In approving the Loss Loans in the face of obvious deficiencies, the Director Defendants acted outside the bounds of reason and were grossly negligent. Their conduct demonstrated a reckless indifference to or deliberate disregard of the welfare of the Bank and its depositors, and an absolute lack of care, or exercise of a degree of diligence so small as to justify the belief that there was a complete disinterest for the interests of the Bank and its depositors.

The FDIC covered all of the legally qualified deposits at Eurobank and currently estimates the loss to the Deposit Insurance Fund to be $647 million for the Eurobank failure. Absent the FDIC's deposit insurance, when Eurobank failed, the depositors of Eurobank, citizens of Puerto Rico and elsewhere, would have lost over $600 million of their savings. The FDIC seeks to recover only a portion of its losses.

II. INTRODUCTION

1. On April 30, 2010, the Office of the Commissioner of Financial Institutions ("OCFI") of Puerto Rico closed Eurobank and appointed the FDIC as Receiver. Pursuant to that

appointment, the FDIC succeeded to all rights, titles, powers, and privileges of Eurobank and its stockholders, depositors, account holders and others with respect to the assets of the institution. 12 U.S.C. § 1821(d)(2)(A)(i). As Receiver, the FDIC is charged with collecting money owed to Eurobank and distributing the funds to its creditors. 12 U.S.C. § 1821(d)(2)(B)(ii) and § 1821(d)(11). The FDIC is authorized to pursue claims against directors and officers of failed banks for breaches of the applicable duty of care. 12 U.S.C. § 1821(k). Pursuant to that authority, the FDIC files this suit against nine former directors of Eurobank (the Director Defendants), the named related spouses and conjugal partnerships, and the named insurance companies for the acts of gross negligence and breach of fiduciary duty detailed herein.

2. Despite having ultimate responsibility for all aspects of Eurobank's lending activity, the Director Defendants failed to properly oversee Eurobank's lending practices and approved 12 high-risk loans with glaring underwriting deficiencies that violated prudent lending standards as well as the Bank's own credit risk management policy. These deficiencies included loan-to-value ("LTV") ratio violations, lack of required borrower equity, outdated real estate appraisals, insufficient collateral, no analyses of project viability, insufficient borrower and guarantor financial information, inadequate sources of repayment, loans to one borrower violations, and lending to borrowers in default, among others. The Director Defendants knew or should have known that the likelihood of the Loss Loans being repaid was remote and that the risk of loss to the Bank was unreasonably large, especially in light of the economic environment in which Eurobank was operating.

3. The Loss Loans were a product of the Director Defendants' failure to use safe and sound banking practices and implementation of a reckless and unsustainable business strategy of pursuing rapid asset growth concentrated in high-risk real estate loans, without putting in place adequate credit administration and loan underwriting policies and practices to manage the risk.

As a result of the Director Defendants' gross negligence in connection with the Loss Loans, Eurobank sustained losses in excess of $55 million. The FDIC seeks to recover these losses.

III. PARTIES

4. Plaintiff FDIC is a corporation organized and existing under the laws of the United States of America, specifically 12 U.S.C. § 1811 *et seq.*, and is an instrumentality of the United States of America charged with, among other duties, the orderly liquidation of failed banks. 12 U.S.C. § 1821(d).

5. Defendant Rafael Arrillaga-Torréns, Jr. ("Arrillaga") was Chairman of the Board, President and CEO of Eurobank from 1993 until the Bank failed.

6. Defendant William Torres-Torres ("Torres") was a director from July 15, 1999, until the Bank failed.

7. Defendant Luis Hernández-Santana ("Hernández") was a director from May 22, 2006, until the Bank failed. Hernández's spouse is Nora Lopez-Rodriguez, with whom he has a conjugal partnership. Both Nora Lopez-Rodriguez and the conjugal partnership are also included as defendants.

8. Defendant Ricardo Levy-Echeandía ("Levy") was a director from February 25, 2002, until the Bank failed. Levy's spouse is Lourdes Arce-Rivera, with whom he has a conjugal partnership. Both Lourdes Arce-Rivera and the conjugal partnership are also included as defendants.

9. Defendant Antonio Pavía-Bibiloni ("Pavía") was a director from November 18, 1997, until the Bank failed. Pavía's spouse is Judith Vidal-Gómez, with whom he has a conjugal partnership. Both Judith Vidal-Gómez and the conjugal partnership are also included as defendants.

10. Defendant Pedro Feliciano-Benítez ("Feliciano") was a director from October 21, 1999, until the Bank failed.

11. Defendant Placído Gonzalez-Cordova ("Gonzalez") was a director from November 18, 1997, until his resignation on November 16, 2009.

12. Defendant Juan Gómez-Cuétara ("Gómez") was a director from January 26, 2004, until May 22, 2006, and then from March 26, 2007, until the Bank failed. Gómez's spouse is Rocio Gil-Gómez de Liaño, with whom he has a conjugal partnership. Both Rocio Gil-Gómez de Liaño and the conjugal partnership are also included as defendants.

13. Defendant Diana Lopez-Feliciano ("Lopez") was a director from July 30, 2001, until her resignation on December 31, 2007.

14. Defendant Liberty Mutual Insurance Company ("Liberty") is a corporation organized and based in Massachusetts and licensed and authorized to do business in Puerto Rico. Liberty issued Policy No. D04N494486004 to EuroBancshares, Inc. covering the period from September 29, 2009, through September 29, 2010, which provides coverage for the claims asserted herein against the Director Defendants. Liberty is subject to suit in this action pursuant to Puerto Rico's Direct Action Statute, P.R. Laws Ann. tit. 26, §§ 2001, 2003 ("the Direct Action Statute").

15. ACE Insurance Company ("ACE") is a corporation organized and based in Puerto Rico, and operates as a subsidiary of ACE INA International Holdings, Ltd. ACE is licensed and authorized to do business in Puerto Rico. ACE issued Policy No. DO1466 to EuroBancshares, Inc. covering the period from September 29, 2009, through September 29, 2010, which provides coverage for the claims asserted herein against the Director Defendants. ACE is subject to suit in this action pursuant to the Direct Action Statute.

16. XL Specialty Insurance Company ("XL") is a corporation organized under the laws of Delaware that is licensed and authorized to do business in Puerto Rico. XL issued Policy No. ELU114018-09 to EuroBancshares, Inc. covering the period from September 29, 2009, through September 29, 2010, which provides coverage for the claims asserted herein against the Director Defendants. XL is subject to suit in this action pursuant to the Direct Action Statute.

IV. JURISDICTION AND VENUE

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

18. The Court has personal jurisdiction over the Director Defendants, their spouses and related conjugal partnerships, because the Director Defendants at all relevant times were residents of, and conducted the business of the Bank in, the Commonwealth of Puerto Rico.

19. Venue in this district is proper under 28 U.S.C. § 1391 because the events giving rise to the claims asserted in this Complaint occurred in this district.

V. FACTUAL BACKGROUND

20. Eurobank was established in 1980 as an uninsured trust company named Española De Finanzas Trust Company. It became an FDIC-insured state nonmember bank in 1987 and assumed its current name in 1993. In 2001, Eurobank became a wholly-owned subsidiary of EuroBancshares, Inc., a one-bank holding company. Eurobank had, at all relevant times, a Loan Policy ("Loan Policy"), approved by the Board, which set forth Eurobank's minimum requirements for loans to be approved.

A. Eurobank's Rapid Growth and Aggressive Lending

21. Eurobank sought to develop a niche market by serving small and mid-sized businesses as well as their owners, executives, and employees. In the early to mid-2000s, Eurobank began aggressively growing its commercial real estate ("CRE") portfolio – including acquisition, development, and construction ("ADC") loans – despite recognition that these loans carried a higher risk for the Bank. From June 30, 2005, to June 30, 2009, the ADC portfolio grew by 240% – over six times the growth rate of its peer group for the same period.

22. The growth of the CRE and ADC portfolios was largely responsible for the Bank's assets growing from $1.3 billion as of December 31, 2003, to $2.9 billion by December 31, 2008. Unfortunately, Eurobank's desire for rapid growth caused the Bank to abandon sound underwriting, resulting in numerous collateral-dependent loans with no alternate source of repayment to borrowers who had no equity in the projects and no demonstrated ability to repay the loans.

B. Eurobank's Dangerous Lending Environment

23. To make matters worse, this growth occurred in the midst of an increasingly dangerous economic environment. Puerto Rico's economy has been in the midst of a recession for a number of years. The negative impact of the economic downturn on the Bank was magnified by the Director Defendants' decision to increase the Bank's exposure to construction loans as the economy soured, rather than restricting high-risk lending and preserving the Bank's capital. Furthermore, the Director Defendants took actions that masked the Bank's growing problems and further exposed the Bank to risk by funding or extending loans with large interest reserves that would keep the loan current for a time although no funds were coming into the Bank.

24. The Director Defendants were well aware of the precarious lending environment in which the Bank was operating. Appraisals that the Board reviewed in 2005, a year before the first of the Loss Loans, indicated that the Puerto Rico economy had been in a recessive trough since 2001 and that recovery would be slow and stated that the total value of building permits had fallen 11 percent from the previous year. The following year, appraisals noted that the value of new building permits had dropped an additional 23 percent. Despite their awareness of the need for extra diligence and caution in light of the worsening lending environment, the Director Defendants continued to approve loans that violated the Bank's Loan Policy, laws or regulations, and safe and sound banking principles, and thus did not adequately adjust the Bank's risk management practices.

C. The Director Defendants' Awareness of the Bank's Problems

25. The Director Defendants were repeatedly warned that the Bank's commercial credit function was performing poorly and needed immediate attention. In 2004, an internal audit found that there were numerous commercial loans that had deficiencies and failed to have sufficient credit reporting and rated the Bank's Construction Loan Department with its lowest rating of "needs improvement."

26. In the March 31, 2005, Joint FDIC-OCFI Report of Examination ("RoE"), the examiners cautioned the Bank and reported that the dollar value of adversely classified assets had increased, and that the commercial credit area accounted for 56 percent of adversely classified loans. Examiners further noted that management needed to address weaknesses in internal loan review, including lack of documentation.

27. The June 30, 2006 Joint FDIC-OCFI RoE downgraded Eurobank's management rating, noting numerous oversight deficiencies, including failure to implement promised corrective action for Bank Secrecy Act-related deficiencies, numerous apparent violations of

laws and regulations, weaknesses in internal audit and management succession planning, and weaknesses in risk management practices, including funds management, asset/liability management, internal loan review, and internal controls. Examiners again reported weaknesses in the internal loan review process and grading system, which did not properly identify losses in the commercial loan portfolio. Internal loan review reports needed to be enhanced to include a narrative analysis of the borrower's background, the adequacy of the collateral coverage, identification of all of the credit weaknesses, policy exceptions, if any, review of the borrower's compliance with outstanding loan covenants, and the obligor's current financial condition. Adversely classified loans and delinquencies continued to increase and the classifications were concentrated in the commercial credits. The examiners also found that the Bank did not have a comprehensive list of the Bank's largest credit relationships in order to determine whether or not any particular loan violated legal lending limits.

28. In 2006 and 2007, the Director Defendants also had their own indicators that the Bank was in trouble. From 2004 to 2007, the Bank's income had plummeted 80 percent, charge-offs had increased 250 percent, and the provision for ALLL had increased 500 percent. Monthly reports to the board of directors indicated that in 2006 the ratio of charge-offs to total loans averaged seven percent and in 2007 increased as high as 11.96 percent. In 2007 the Bank hired an outside auditor to review its construction loan department's loan applications, loan approvals, and loan administration. The report, dated December 28, 2007, gave the Construction Loan Department the worst available rating of "5." The report stated that the department was not in compliance with safe and sound banking practices due to numerous loans being recommended that violated laws, regulations, or the Bank's loan policy.

29. The September 30, 2007 Joint FDIC-OCFI RoE lowered the Bank's overall composite CAMELS rating to a "3", and examiners stated that the deterioration of the Bank was

a reflection on management and the board of directors' less than satisfactory performance. The examiners said there were multiple weaknesses in risk management, including internal loan review and grading. They warned that prompt corrective action was needed. The examiners found the volume of adversely classified items had significantly increased since the last examination and repeated their criticism of the internal loan review process. Classifications continued to be concentrated in the commercial credits, and some loan classifications again were not properly identified internally and were not accurately classified. Examiners told management to proactively review and monitor its construction loan portfolio in view of the adverse impact that economic conditions could have on this loan category.

30. The September 30, 2008 Joint FDIC-OCFI RoE further lowered the Bank's overall rating and criticized the board's and management's oversight as being inadequate. The RoE stated that the board consistently approved extensions of credit on troubled ADC loans and advanced additional interest reserves with no tangible support from guarantors or developers and without current appraisals, which led examiners to identify the underwriting deficiencies as "pervasive." Examiners found many cases where extensions were made without an updated appraisal, despite a material change in market conditions. The examiners stated that the board and management had not implemented effective credit risk management systems, especially in light of the weak local economy. Examiner review disclosed lax underwriting and credit administration that had substantially contributed to the Bank's troubled condition.

31. As noted in previous examinations, the volume of adversely classified items continued to increase dramatically, and again the examiners identified more adversely classified loans than those recognized by the Bank's internal loan review. And as in the previous RoE, the examiners cited management for its failure to implement risk management procedures stated in

the Joint Guidance and in the board's failure to approve an overall CRE lending strategy with established policy guidelines.

32. Finally, on or about September 1, 2009, after examiners had noted repeated violations by the Bank, the Director Defendants (with the exception of Lopez who had previously resigned) consented to the entry of a Cease and Desist Order which required the Bank to cease and desist from certain unsafe and unsound banking practices and violations of law including:

- operating with inadequate management whose policies and practices were detrimental to the Bank;
- operating with inadequate oversight by the board of directors to prevent unsafe and unsound banking practices and violations of laws and regulations;
- operating with lax underwriting, poor credit administration practices, and ineffective loan review practices;
- operating with an excessive level of adversely classified loans and/or delinquent loans;
- operating with inadequate capital and reserves in relation to the kind and quality of assets held by the Bank; and
- operating with inadequate internal controls.

33. The serious underwriting deficiencies at the Bank were not lost on the Director Defendants. In correspondence to an FDIC examiner in December 2008, the Director Defendants admitted that they were "certain that mistakes have been made in our underwriting." The underwriting deficiencies in the Loss Loans were obvious and avoidable, and the Director Defendants' conscious decision to turn a blind eye toward them directly and proximately caused significant losses to the Bank.

VI. THE LOSS LOANS

34. The following table lists the Loss Loans at issue in this suit and indicates which of the Director Defendants approved each loan. The FDIC is only seeking damages from each Director Defendant for the loans that he or she approved:

Borrower	**Loan Amount (millions)**	**Approval Date**	**Loss (millions)**	**Loan Approval Votes**								
				Arillaga	**Torres**	**Hernández**	**Levy**	**Pavía**	**Feliciano**	**Gonzalez**	**Gómez**	**Lopez**
1. Skylofts	$4.3	Mar. 6, 2006	$4.73	x	x		x	x	x	x	x	x
Skylofts	$1.0	Jun. 27, 2007		x	x	x	x	x	x	x		
2. La Ciudadela	$20.00	Apr. 24, 2006	$19.51	x	x	x	x	x	x	x	x	x
3. Hillstone	$4.10	Sept. 27, 2006	$4.13	x	x	x	x	x	x	x		x
Hillstone	$0.30	Sept. 29, 2008		x	x	x	x	x	x	x	x	
4. Acor Se	$9.8	Mar 19, 2007	$6.22	x	x	x	x	x	x	x		x
Acor Se	$2.56	Mar. 25, 2008		x	x	x	x	x	x	x	x	
Acor Se	$0.69	Feb. 19, 2009		x	x	x	x	x	x	x	x	
5. Jocar Inc.	$5	Dec. 21, 2007	$4.69	x	x	x	x	x	x	x	x	x
6. City Walk	$5.2	Dec. 28, 2007	$4.81	x	x	x	x	x	x	x	x	x
7. Marat LLC	$13.3	Nov. 24, 2008	$11.38	x	x	x	x	x	x	x	x	
Marat LLC	1.9	Dec. 22, 2008		x	x	x	x	x	x	x	x	
TOTAL	**$68.15**		**$55.47**									

35. In connection with the Loss Loans, the Director Defendants routinely overlooked extreme and obvious departures from sound underwriting practices and the Bank's own lending policies, and by all appearances approved the loans based on little more than hope. The Loss Loans violated the underwriting standards set forth in 12 C.F.R. § 364.101, Appendix A, and the real estate lending standards in 12 C.F.R. § 365.2, Appendix A. Thus, the Director Defendants breached their fiduciary duty of care to the Bank when failing to exercise due care or any business judgment while ignoring the obvious risks posed by these specific loans.

36. The indiscriminate use of interest reserves funded by loan proceeds for certain of the Loss Loans gave the false appearance to stockholders and regulators that the loans were performing and the Bank was making income from these loans when, in fact, the funds were simply recycled within the Bank. Generally, the borrowers had little or no equity in the project. The risk with these transactions was borne almost entirely by the Bank and, as noted, came at a time when the economic environment should have inspired the Director Defendants to exercise greater caution in subjecting the Bank to credit risk. The Loss Loans are summarized below.

Skylofts

37. On February 27, 2006, the Director Defendants approved a $4.3 million loan to Skylofts, Inc. to assist in the acquisition and development of land in Miramar, San Juan, PR, for the Skylofts project, a 120-unit residential complex. The source of repayment was to be the proceeds of an interim loan that would be procured at a later date for the construction of the units. There was no commitment for a construction loan on file in violation of the Loan Policy. There was no evidence that the Bank inquired or had discussion with the principals regarding their ability to obtain such financing. The secondary source of repayment was identified as the sale of the property or from the guarantors' own resources.

38. The loan was secured by 1,782 square meters at the development site and supported by the personal guarantees of Francisco Pujol, Zoila Levis and Caridad Fernandez. Complete and current financial statements and tax returns were not provided for each guarantor in violation of the Bank's Policy. Despite the lack of complete financial information, the guarantors were evaluated based on their net worth rather than their capacity to repay the loan in the event of default. Their real estate holdings constituted the majority of their assets and net worth, yet there was no analysis or verification of these holdings. There were no credit reports on file for the guarantors. As Skylofts, Inc. was a recently-formed corporation, there were no

financial reports for analysis, and audited financial statements for the companies owned by the principals were not obtained and analyzed.

39. The appraisal used to value the collateral property was commissioned by one of the guarantors and not the Bank in violation of the Loan Policy and federal regulations. The appraiser's value was based upon the hypothetical condition that all government permits were in place rather than on the lower "as is" value. Therefore, the loan was approved with a 97 percent LTV ratio in violation of the Loan Policy. The appraisal also indicated that the purchase price of the land was $3.2 million and therefore the Bank financed 100 percent of the property cost and required no equity from the borrower in this transaction.

40. On June 25, 2007, the loan was increased to $5.3 million for the purpose of increasing the interest reserve and defraying additional costs. The increase was supported by an appraisal showing a 25 percent increase in the market value of the property from February 2006 despite deterioration in the real estate market. There were several extensions of the loan's maturity date with no diligent review of the loan, the guarantors' financial condition and the real estate market decline.

41. The Bank suffered a loss on this loan in an amount to be determined by the jury, but at this time estimated to be approximately $4.73 million. Such loss was proximately caused by the conduct alleged herein.

La Ciudadela de Santurce, Inc.

42. On April 24, 2006, the Director Defendants approved a $20 million participation in a $140 million loan led by Banco Popular for the development and construction of a three phase mixed use construction project known as La Ciudadela de Santurce consisting of 518 residential units, 150,000 square feet of commercial space and over 2,000 parking spaces. The source of repayment was from the sale of the individual and commercial units to be built. The

Bank entered into this participation loan without performing an independent evaluation of the overall transaction and the risks involved in violation of the Loan Policy.

43. The loan was secured by participation in a first mortgage note in the amount of $140 million and assignment of all tax credits and supported by the personal guarantee of the sponsor and developer, Carlos Lopez de Azua, and a corporate guaranty of Miramar Real Estate Management, Inc. Interest payments were to be made from an interest reserve account, and the principal was payable beginning on the 24th month to be fully paid on or before May 31, 2010. Financial and credit analysis of the sponsors and guarantors were not conducted in accordance with Loan Policy. The little financial information provided indicated that the guarantors were evaluated on their net worth rather than on their capacity to repay the debt in the event of default, and there were no credit reports for the guarantors. The Bank's reliance on any tax credits was speculative in that there were no work papers to support the estimate, and the application for the credits had not been approved. In fact, the application was approved 14 months after the Director Defendants approved the loan, but there was still no verification of the amounts or timing of any of the tax benefits.

44. The appraisal used to value the subject property was over two years old in violation of Loan Policy and federal regulations. The appraisal had questionable and incomplete information to support the collateral requirements of the loan. The appraisal also indicated that the Bank exceeded its LTV ratio limits as set forth in Loan Policy as well as its loan-to-cost ("LTC") Policy limits. There was no equity cash contribution required of the borrower or guarantors. The original term of the loan was 48 months in violation of the Loan Policy.

45. The Bank suffered a loss on this loan in an amount to be determined by the jury, but at this time estimated to be approximately $19.51 million. Such loss was proximately caused by the conduct alleged herein.

Hillstone

46. On August 30, 2006, the Director Defendants approved a $4.1 million loan to Hillstone Builders, Inc. to finance the purchase of land for future development of 350 residential units in Bayamon, PR. The source of repayment was to be the proceeds of an interim loan that would be procured at a later date for the construction of the units. There was no commitment for a construction loan on file in violation of Bank Loan Policy. There was no evidence that the Bank inquired or had discussion with the principals regarding their ability to obtain such financing, nor was there any analysis of the viability of the project. The secondary source of repayment was identified as the sale of the property or from the guarantors' own resources.

47. The loan was secured by first and second mortgages on 22 cuerdas in Bayamon and supported by personal guarantees of Elberto Berdut and Peregrine Development, Inc. In violation of the Bank's Policy, the capacity of the guarantors was not analyzed and verified, there were no credit reports on file for the guarantors, and there were no financial statements for Peregrine Development, Inc.

48. The appraisal used to value the collateral property was commissioned by guarantor Berdut and not the Bank, and was actually a Certificate of Value rather than a formal appraisal, all in violation of the Loan Policy and federal regulations. The Certificate was deficient in the selection of comparable properties, unexplained adjusting factors, the vagueness of highest and best use and the use of hypothetical conditions that approvals and permits were in place. A later review of the appraisal/Certificate by the Bank determined that it was not adequately supported. Based on the appraised value, the LTV was 67 percent in violation of the Loan Policy maximum of 50 percent for raw land.

49. The original term of the loan was one year, but it was renewed for an additional year on August 20, 2007. On September 22, 2008, the Director Defendants approved an increase

of the loan to $4.4 million and extended it until April 30, 2009. The loan extensions and increases were approved without obtaining current appraisals despite a significant decline in the real estate market in violation of the Loan Policy and federal regulations. The Bank failed to monitor the loan and permitted interest payments dependent upon interest reserves and the principal repayment was dependent on an unconfirmed construction loan.

50. The Bank suffered a loss on this loan in an amount to be determined by the jury, but at this time estimated to be approximately $4.13 million. Such loss was proximately caused by the conduct alleged herein.

Acor, SE

51. On January 22, 2007, the Director Defendants approved an amendment to a loan to Acor, SE in the amount of $9.8 million to construct 192 walk-up apartments located in Bayamon with the project name of Villas de Hato Tejas. The primary source of repayment was based on the sale of the units. There was no secondary source of repayment identified as required by the Loan Policy.

52. The loan was secured by mortgages on the subject property and supported by personal guarantees. The financial analysis lacked the due diligence required by the Loan Policy and the guarantors were evaluated based on their net worth rather than on creditworthiness and the capacity to repay the loan in the event of default. There were no credit reports for the guarantors.

53. The appraisal used in the approval of this amendment was from the original loan and outdated by over six years in violation of Loan Policy and federal regulations. Thus the estimates used for repayment of the loan were based upon the units pending to be sold at the average selling price and not on an updated market value. Additionally, there was no showing that a thorough review of the current state of the project was done with an updated cost to

complete, despite the Bank's awareness of situations of soil instability that had increased costs and caused delays in the construction process. There was no calculation of a LTV ratio of this loan to make a determination if the loan amendment request was compliant with the Loan Policy.

54. The loan was amended again in both 2008 and 2009 increasing it to $13.05 million. These increases were made without the benefit of current financial statements of the guarantors, without receipt of additional collateral, and with the Bank's source of repayment based upon a sale of units in a weakened and depressed economy. All of these factors violated various Loan Policy provisions.

55. The Bank suffered a loss on this loan in an amount to be determined by the jury, but at this time estimated to be approximately $6.22 million. Such loss was proximately caused by the conduct alleged herein.

Jocar

56. On September 17, 2007, the Director Defendants approved a $5 million line of credit to Nova Infusion & Compounding Pharmacy ("Nova"), a subsidiary of HIMA San Pablo ("HIMA"). The loan was for working capital to pay suppliers. The source of repayment of the loan was the cash flow of the borrower. There was no identified secondary source of repayment. The collateral was to be an assignment of accounts receivable and inventory. HIMA was a guarantor.

57. The loan was funded on December 27, 2007, and was fully drawn by January 2, 2008. At some time between the approval of the loan and funding, Nova was acquired by another HIMA subsidiary, Jocar, Inc. ("Jocar"), and the borrower on the loan was changed to Jocar.

58. There was significant lack of financial analysis on this loan. The primary source of repayment was the earnings of the borrower or HIMA, but there was no review of adequate

financial data for at least the two most recent years and/or even a current interim statement for the borrower and guarantors, and no cash flow projections. Furthermore, the latest financial information on HIMA provided to the Bank was from 2005, and it showed minimal capacity to service the debt. At the time of the loan, Nova had an overdraft in its operating account of more than $400,000. Most importantly, there was no financial analysis of Jocar, the actual borrower on the loan.

59. The collateral on the loan was intended to be secured by 80 percent of eligible accounts receivables up to 180 days and inventory up to 50 percent of cost. However, there was no review of the accounts receivables and inventory, no aging reports were available, and there was no determination of the outstanding balance of the inventory or mention of how to treat obsolete inventory and work-in-process. In summary, the required controls of accounts receivables and inventory collateral were not documented. Not only was there a failure to verify the collateral prior to advancing funds on the loan, no formal assignment or perfected interest of the collateral was made at the origination date and thus, this became an unsecured loan.

60. Despite the lack of due diligence and the violation of Loan Policy regarding Undesirable Loans, Bank management ignored the clear signs of distress and, instead, extended the loan nine times from 2008 to 2009. There was no effort made to put any type of workout plan in place. In January 2010 the loan was converted to a three-year term loan and classified as sub-standard.

61. The Bank suffered a loss on this loan in an amount to be determined by the jury, but at this time estimated to be approximately $4.69 million. Such loss was proximately caused by the conduct alleged herein.

City Walk

62. On November 26, 2007, the Director Defendants approved a $5.2 million loan to City Walk Development Corporation ("City Walk") to purchase and develop a commercial land lot consisting of 3,780 square meters located at Marginal 6 of Muñoz Rivera Expressway at Miramar, Santurce, PR.

63. City Walk was to buy the property from an entity called Hogares, S.A. ("Hogares"). Although City Walk and Hogares were separate companies with different ownership, both City Walk, Hogares and a third entity, Sunrise Partners II, S.E. had Joseph McCloskey as one of the principal owners and/or managing agent. (Joseph McCloskey has been recently convicted of a bank crime involving Sunrise Partners II and another bank.) The purchase price was used to pay off a non-performing Hogares loan with the Bank secured by a lien on the property, and to pay off another non- performing loan to Sunrise Partners II, S. E. The extension of a loan to an affiliate of a non-performing or delinquent borrower violated the Bank's Loan Policy. Additionally, this loan gave the false appearance to stockholders and regulators that the number of non-performing loans had decreased while performing loans had increased.

64. There was no primary or secondary source of repayment noted in the loan request. In fact, the loan request made to the Director Defendants was a simple email that recommended the pay-off of an existing non-accrual loan and to make an interest payment on another non-accrual loan. There is no evidence that the Bank carried out appropriate due diligence or underwriting of the loan in violation of Loan Policy. As such, the Director Defendants further violated Loan Policy in that the loan increased exposure to a borrower who had other troubled loans with the Bank.

65. The loan was secured by a first demand mortgage over the subject 3,780 square meter property. The guarantors on the loan were not evaluated at loan origination in violation of Loan Policy. There are no financial statements or credit reports on file for any of the guarantors. There was no appraisal used to value the collateral property at loan origination in violation of Loan Policy and federal regulations. One year after the loan originated, the Bank received an appraisal from McCloskey, Mulet & Bonnin Appraisers that was performed during December 2007. This appraisal shows a conflict in interest as appraiser Robert McCloskey is the brother of Joseph McCloskey, and also demonstrates, based upon the market value of the raw land, that the Bank had exceeded its LTV limits as set forth in Loan Policy.

66. The Bank suffered a loss on this loan in an amount to be determined by the jury, but at this time estimated to be approximately $4.81 million. Such loss was proximately caused by the conduct alleged herein.

Marat

67. On October 24, 2008, the Director Defendants approved a $13.3 million loan to Clema Development Corporation ("Clema") for the purpose of developing 33 detached residential units on approximately 29 cuerdas in the Villas del Golf II development in Caguas PR. The sole source of intended repayment was the Bank receiving 93 percent of the selling price of each unit. There was no secondary source of repayment as required by the Loan Policy. The term of the loan was 30 months, which also violated the Bank's Loan Policy maximum term of 24 months.

68. The borrower was initially required to inject $3 million in cash equity. The borrower was unable to meet this requirement or a lower requirement of $2 million. One month later, the Bank waived the requirement entirely and the loan was amended to raise the loan amount to $15.2 million.

69. Prior to the closing of the loan, Clema indicated to the Bank that it would be transferring the realty to its affiliate, Marat, LLC (Marat) and title would pass to Marat at the closing of the loan. This change was not approved by the Board of Directors.

70. The loan was secured by first, second, and third mortgages in the principal amounts of $6 million, $2.15 million, and $7.05 million, respectively, over the property to be developed. The loan was guaranteed by Clema and Cleofe Rubi and his wife, Moraima Cintron. The Bank violated its Loan Policy and prudent banking standards in its failure to conduct a diligent review of the borrower and guarantors' ability to repay the loan. Clema was unable to meet the cash equity requirement. The Bank did not have information on the true borrower, Marat, a recently formed LLC. The Bank had incomplete and unaudited financial information on the guarantors. With the incomplete information, the Bank's evaluation was based upon the guarantors' net worth and not on the ability to repay the loan in the event of default. The Bank failed to note that the financial statements indicated that a guarantor was considerably overdrawn on their bank account and current liabilities significantly exceeded current and liquid assets.

71. At the time of loan origination, Clema had other loans from the Bank that were matured and/or with interest past due. There was no reference in the loan application that over half of the proceeds would be diverted to pay off the Clema debt and not used to complete the Marat development. The extension of a loan to an affiliate of a non-performing or delinquent borrower violated the Bank's Loan Policy. On information and belief, the Plaintiff alleges that the Director Defendants either knew that Clema had non-performing loans and approved this loan in an attempt to give a false appearance to regulators and stockholders that performing loans had increased and non-performing loans had decreased, or in the alternative, that the Director Defendants did not even realize that the guarantor of a major loan had three non-performing loans with the Bank. Additionally, the Bank failed to calculate the total risk that this loan

represented to the Bank because it did not take into consideration the aggregate number of loans to this one borrower. Moreover, the issuance of this loan violated the Bank's legal lending limit to one borrower.

72. The appraisal used to evaluate the collateral was over four years old and not prepared specifically for the Bank in violation of Loan Policy and federal regulations. As the economic condition and real estate market had changed since the appraisal was completed, the Bank did not take these factors into account at the time this loan. As a result, the 101 percent LTV ratio far exceeded the Bank's Loan Policy and Interagency Guidelines. There was no evidence of property inspection, insurance, presales/lease commitments, review of the project and site, permits and studies, and evaluation of the contractor as required by the Loan Policy.

73. The Bank suffered a loss on this loan in an amount to be determined by the jury, but at this time estimated to be approximately $11.38 million. Such loss was proximately caused by the conduct alleged herein.

VII. OVERALL INJURY TO THE BANK

74. The approval of each of the Loss Loans demonstrates the Director Defendants' reckless disregard of sound underwriting practices. This reckless disregard happened not only in these loans but in other lending and general banking decisions made by the Director Defendants which injured the Bank, its stockholders, its depositors, and creditors. The Director Defendants were repeatedly warned of the problems at the Bank by internal and external auditors and by regulators, but the Director Defendants did not take sufficient actions to save the Bank from the harm of their decisions and inactions. The Bank's underwriting deficiency with respect to securing valid, current appraisals was particularly pronounced. The Bank did not even have an appraisal policy until 2006 when its new Chief Lending Officer implemented one. And an independent consulting firm that reviewed the Bank's reserve allocations in January 2010

observed that the Bank had "only recently" begun to follow industry best practices for appraisal ordering and review, and noted an immediate need for the Bank to order newer, more credible appraisals that could be used to establish a realistic fair value of the Bank's collateral.

75. In approving, increasing, renewing and extending the Loss Loans in the face of the foregoing gross and obvious deficiencies which were apparent from the information presented to them before approval, the Director Defendants acted outside the bounds of reason and were grossly negligent. Their conduct demonstrated a reckless indifference to or deliberate disregard of the welfare of the Bank and its depositors, and an absolute lack of care, or exercise of a degree of diligence so small as to justify the belief that there was a complete disinterest for the interests of the Bank and its depositors.

76. Not only did the Director Defendants approve loans with extreme underwriting flaws, but also they failed to implement an adequate internal loan review function. During the 2007 and 2008 examinations, examiners identified significantly more adversely classified loans than recognized by the Bank's internal loan review. During the 2007 examination, eight commercial loans aggregating $43.2 million had not been properly classified by management, of which $32.1 million or 74 percent were adversely classified construction loans. Examiners also identified construction loans that warranted a substandard classification that were not adversely classified, or included on the Bank's watch list as special mention.

<u>Adverse Domination/Delayed Discovery</u>

77. The Director Defendants adversely controlled and dominated Eurobank at all times relevant to this action and took actions that concealed the damaging effect of their loan approvals, thereby preventing the Bank or anyone with legal authority to act on behalf of the Bank from discovering and taking legal action against the Director Defendants prior to the failure of the Bank and appointment of the FDIC as Receiver.

VIII. CLAIMS FOR RELIEF

Count 1 – Gross Negligence against the Director Defendants

78. The FDIC incorporates by reference Paragraphs 1-77 into this Claim.

79. As directors and/or officers of Eurobank, the Director Defendants owed a fiduciary duty of care and diligence and fair dealing in the management, conduct and direction of the business of Eurobank and in the approval of loans. The Director Defendants' duties included, but were not limited to, the following:

a. To manage, conduct and direct the business and affairs of Eurobank in accordance with and to ensure compliance with applicable laws, regulations, bylaws, policies, and sound and prudent banking practices;

b. To adopt and follow loan policies to ensure lending in accordance with safe and sound banking practices;

c. To review carefully each report of examination of Eurobank's affairs as made by the regulatory authorities and internal or external audits and to respond in a manner to correct any deficiencies contained in such reports and to establish and maintain procedures to ensure no recurrence of any deficiencies set forth therein;

d. To attend the regular meetings of the Board and actively to review and approve or disapprove each loan and/or investment in accordance with the Loan Policy and safe and sound banking practices;

e. To take such action as necessary to ensure that Eurobank's loans and investments were underwritten, approved, disbursed and collected in accordance with the law, regulations, bylaws and policies applicable thereto and in accordance with sound and prudent banking practices;

f. To take such action as necessary to ensure that the officers, employees, and agents of the institution complied with the instructions and directions of the Board;

g. To exercise independent judgment in the best interest of Eurobank in the conduct of its business and affairs;

h. To ensure that Eurobank did not engage in any unsafe or unsound practices; and

i. To perform faithfully and diligently their duties as members of Eurobank's Board committees.

If the Director Defendants had adhered to these duties, they would not have approved the Loss Loans, and the resulted losses would have been avoided.

80. In disregard of their duties to Eurobank, the Director Defendants demonstrated a reckless indifference to or deliberate disregard of the welfare of the Bank and its depositors, and an absolute lack of care, or exercise of a degree of diligence so small as to justify the belief that there was a complete disinterest for the interests of the Bank and its depositors. This misconduct included but was not limited to the following acts and omissions:

a. Pursuing an aggressive and reckless growth and lending strategy that placed short term income and profits ahead of the safety and soundness of the federally insured depositor funds entrusted to the Director Defendants;

b. Permitting the Bank's commercial loan portfolio to deteriorate due to continued approvals, increases, extensions, and renewals of poorly underwritten, high risk commercial loans in violation of Bank policies, procedures, federal regulations, and prudent banking practices, thereby jeopardizing the Bank's financial health and causing it significant losses;

c. Approving the Loss Loans in violation of the Bank's Loan Policy, federal safety and soundness regulations, and prudent banking practices;

d. Approving multiple increases, extensions and/or renewals of delinquent and defaulted Loss Loans in order to fund interest reserves and continue to derive short term income and profits at the expense of the safety and soundness of federally insured depositor funds, and in order to give the false appearance that the Bank was performing better than it was; and

e. Failing to heed examiner and auditor warnings of deficiencies in lending and loan administration, failing to correct those deficiencies, and approving, increasing, extending, and/or renewing Loss Loans despite those warnings.

f. Failing to inform themselves and each other of the true condition of the assets and liabilities of Eurobank and the nature of its loan portfolio, or to review and inquire adequately into Eurobank's loan transactions;

g. Failing to adhere to the Bank's Loan Policy prescribing the conditions and limitations under which loans could be made and the underwriting and record-keeping which should be undertaken on loans, resulting in hazardous lending;

h. Causing or permitting approval of loans with excessive LTV ratios that exceeded allowable LTV ratios pursuant to Loan Policy and Interagency Guidelines and/or relying upon deficient, outdated, incomplete, or non-existent appraisals;

i. Failing to establish or adhere to policies responsive to the numerous and repeated warnings and criticisms of federal and state banking authorities and regulators;

j. Failing to inform themselves and each other of the nature, viability, legality and prudence of loans presented for their review, analysis, approval or ratification;

k. Failing to require adequate loan documentation;

l. Failing to exercise independent judgment and to act in the best interest of Eurobank in approving and ratifying loans;

m. Violating or permitting violation of prudent banking practices by making or permitting loans in which the sale or liquidation of collateral security was the only method by which the loan could be repaid;

n. Causing or permitting loans to be made to borrowers who were known or should have been known to be poor credit risks, or who were in obvious financial difficulty;

o. Causing or permitting loans to be made on the basis of grossly inadequate or inaccurate information regarding the finances of the borrower, the value of the collateral, and/or the sources of repayment;

p. Causing or permitting loans to be made on an under-secured basis, contrary to prudent banking practice;

q. Failing to make or cause to be made appropriate investigations into borrowers' creditworthiness, representations of values contained in the borrowers' financial statements, and the actual value of collateral given to secure loans;

r. Causing or permitting loans to be made to borrowers or their related interests after loans made previously to these borrowers had already become nonperforming, were in default, or were classified by regulatory authorities; and

s. Causing or permitting in excess of 100% financing for speculative ventures.

81. The Director Defendants were grossly negligent in their failure to exercise any due care or any business judgment in approving obviously risky and deficiently underwritten loans. When approving these loans –object of the instant complaint-, which they knew or should have known were extremely unlikely to be paid back, the Director Defendants ignored blatant risks of injury to the Bank. These grossly negligent acts and omissions directly and proximately caused at least $55.47 million in damages to Eurobank.

82. The named defendant spouses and conjugal partnerships are liable to the extent that the related Director Defendant is liable for damages.

Count 2 – Direct Action against Liberty, ACE, and XL

83. The FDIC incorporates by reference Paragraphs 1-82 into this Count.

84. Defendants Liberty, ACE, and XL issued policies of insurance covering the losses caused by the Director Defendants as alleged in this Complaint. The Director Defendants and the FDIC timely notified the insurers of the claims within the claim reporting periods under the policies, and any conditions precedent have been met. Pursuant to the Direct Action Statute, the FDIC is entitled to assert a claim directly against Liberty, ACE, and XL and to receive compensation for the losses caused by the Director Defendants' gross negligence up to the full amount of the policies.

Count 3 – Declaratory Judgment against ACE and XL

85. The FDIC incorporates by reference Paragraphs 1-84 into this Count.

86. With respect to ACE and XL, the FDIC seeks in the alternative a declaratory judgment that under the policies issued by them, ACE and XL are obligated to the FDIC to the extent that losses alleged in this Complaint exceed and/or exhaust the limits of underlying policies.

87. To date, ACE and XL have not agreed to indemnify the FDIC for losses relating to the wrongful acts of the Director Defendants as set forth above, and thus an actual controversy presently exists between the FDIC and ACE and XL concerning the rights and obligations of the parties under the insurance policies. Declaratory relief from this Court will resolve and terminate the controversy and is thus necessary to determine the FDIC's rights and ACE's and XL's obligations with respect to coverage for the claims under the insurance policies.

IX. JURY DEMAND

88. The FDIC respectfully demands a trial by jury.

X. PRAYER FOR RELIEF

For these reasons the FDIC requests that upon final hearing the Court award the FDIC judgment for compensatory and consequential damages as follows:

1. Against each Director Defendant, their spouse and conjugal partnership, if any, for the losses caused by that Director Defendant's gross negligence in approving the Loss Loans which he or she approved as set forth in the chart in paragraph 34;

2. Against Liberty, ACE, and XL up to the amount of their respective policies for any judgment obtained against the Director Defendants for their gross negligence;

3. Declaratory relief against ACE and XL declaring that they are obligated to the FDIC to the extent the losses alleged herein exceed and/or exhaust the limits of the underlying policies.

4. Against all Defendants for reasonable attorneys' fees, costs, and prejudgment and postjudgment interest as allowed by law; and

5. All other relief to which the FDIC may be entitled.

Respectfully submitted in San Juan, Puerto Rico, on April 26, 2013

/s/ *Jairo Mellado-Villarreal*
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