UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF COLUMBIA

U.S. SECURITIES AND EXCHANGE COMMISSION, **100 F Street, NE** **Washington, D.C. 20549** **Plaintiff,** **v.** **DRAKE ASSET MANAGEMENT, LLC and OLIVER R. GRACE, JR.** **Defendants.**	Case: 1:11-cv-01905 Assigned To : Sullivan, Emmet G. Assign. Date : 10/31/2011 Description: General Civil **COMPLAINT**

Plaintiff, Securities and Exchange Commission ("Commission"), alleges:

SUMMARY

1. This matter involves a scheme to evade the group purchase limits of seven bank mutual-to-stock conversion offerings. From late-2003 to mid-2007, Oliver R. Grace, Jr. ("Grace"), an experienced conversion offering investor, along with his family and various entities under his control, on seven occasions acquired offering stock that exceeded the group purchase limits, in violation of banking regulations and offering terms. These entities included hedge funds (the "Drake Funds") managed by Drake Asset Management, LLC ("DAM"), an unregistered adviser in which Grace had a substantial ownership interest.

2. The scheme generated $610,781 in ill-gotten gains.

3. In the event that certain mutual banks would convert profitably to stock ownership, Grace opened accounts at a number of institutions for himself, his minor children, the Drake Funds (through their adviser, DAM), and several other affiliated entities in which he held a controlling interest or a senior position.

4. As experienced investors in mutual-to-stock conversion offerings, Grace and DAM (collectively, "Defendants") were well versed in conversion rules and had periodically obtained legal advice on group purchase limits. They understood specifically that, should these banks convert to stock ownership, they were required to treat Grace, the Drake Funds, and his other affiliated entities as "associates" or persons with whom they were "acting in concert," and to disclose them as such on their stock order forms.

5. Nevertheless, in seven offerings, and to evade their group limits, Grace certified and submitted stock order forms without disclosing his associations with these affiliated entities, resulting in false representations that the information he provided was true, correct, and complete.

6. Similarly, under Grace's oversight and supervision, DAM, in five offerings, certified and submitted stock order forms for the Drake Funds without disclosing Grace as an "associate" or person with whom they were "acting in concert."

7. To conceal their relationships and group activity from the converting banks and their underwriters, Defendants arranged for the Drake Funds to use addresses and/or signatories on their stock order forms that would prevent the banks from associating their orders with orders placed by Grace. Grace did the same for the order forms of his other affiliated entities.

8. Defendants' scheme harmed legitimate depositors of the seven converting banks. Had these banks known about Grace's association with the Drake Funds and his other affiliated entities, and vice versa, they would have been able to enforce the group limits and protect the rights of other legitimate depositors. Indeed, because these conversion offerings were oversubscribed, Defendants' scheme limited the shares available to otherwise eligible depositors.

9. By knowingly or recklessly engaging in the conduct described in this Complaint, Defendants violated, and unless restrained and enjoined will continue to violate, Section 10(b) of

the Securities Exchange Act of 1934 ("Exchange Act") [15 U.S.C. §78j(b)], and Rule 10b-5 thereunder [17 C.F.R § 240.10b-5].

JURISDICTION AND VENUE

10. This Court has jurisdiction over this action pursuant to Sections 21(d), 21(e), and 27 of the Exchange Act [15 U.S.C. §§ 78u(d), 78u(e), and 78aa].

11. Venue lies in the District of Columbia pursuant to Section 27 of the Exchange Act [15 U.S.C. § 78aa].

12. In connection with the conduct described herein, Defendants, directly or indirectly, made use of the mails or the means or instrumentalities of interstate commerce, or the facilities of a national securities exchange in connection with the acts, transactions, practices and courses of business alleged in this Complaint.

DEFENDANTS

13. **DAM**, a Delaware limited liability company, is headquartered in Glen Head, New York. At all relevant times, DAM was co-owned by Grace and his brother and operated alongside Grace's family office. DAM is the general partner of, and investment adviser to, certain hedge funds, including Drake Associates L.P. ("Drake") and Diversified Long-Term Growth Fund L.P. ("Diversified") (collectively, the "Drake Funds"). DAM is not registered with the Commission.

14. **Grace**, age 57, resided in Glen Head, New York during the relevant period. He is a private investor, philanthropist, and corporate board member. At all relevant times, Grace co-owned DAM and directed its activities from his family office.

OTHER RELEVANT ENTITIES

15. **Drake**, a Delaware limited partnership headquartered in Glen Head, New York, is a hedge fund formed by Grace and his brother in 1987 as an investment vehicle for friends and

family members. During the relevant period, Drake had over $175 million in assets. At all relevant times, Grace's ownership interest in Drake exceeded 10%. One of Drake's stated investment strategies was to participate in mutual-to-stock conversion offerings.

16. **Diversified**, a Delaware limited partnership headquartered in Glen Head, New York, is a hedge fund formed by Grace and his brother. At all relevant times, Grace's ownership interest in Diversified exceeded 10%. As with Drake, one of Diversified's stated investment strategies was to participate in mutual-to-stock conversion offerings.

FACTS

A. The Mutual-to-Stock Conversion Process

17. Savings and loan associations and savings banks are typically organized either as mutual associations or thrifts owned by depositors, or as capital stock companies owned by shareholders. When the conversion of a mutual thrift to stock ownership is approved, subscription rights to the stock offering are granted in tiers to defined groups of individuals with different levels of priority. The most typical tiers, in descending order of priority, are: (1) depositors who had accounts for at least a year before the offering; (2) bank employee benefit plans; (3) borrowers and others who held accounts for less than a year before the offering; and (4) if any shares remain available, members of the local community or, in a syndicated offering, other public investors.

18. Federal and state banking regulations limit the number of shares that can be acquired in conversion offerings by any one person, entity, or group of associated depositors. The purpose is to encourage broad participation in these offerings by eligible depositors and to prevent opportunities for manipulation or takeovers.

19. To ensure that depositors comply with the individual and group purchase limits, offering prospectuses and most stock order forms require depositors to affirmatively disclose the identities and orders of all "associates" or persons "acting in concert." Depositors are also

required to sign order forms and certify, under penalty of perjury, that the information provided on the form is true, correct, and complete.

20. Definitions of "associate" and "acting in concert" are provided explicitly in the offering materials and stock order forms. An "associate" of a depositor generally always means: (a) any entity of which a person is a senior officer or partner, or beneficially owns, directly or indirectly, ten percent or more of any class of equity securities of the entity; (b) any relative (by blood or marriage) who lives in the same house as the person; and (c) any person "acting in concert" with the persons or entities described above.

21. "Acting in concert" generally means, "knowing participation in a joint activity or interdependent conscious parallel action towards a common goal, whether or not pursuant to an express agreement."

22. Mutual-to-stock conversion offerings have proven to be lucrative investment opportunities, as the stocks often trade in the immediate aftermarket at prices that represent a substantial premium over the offering price. As a result, depositors as a whole often order more shares than the bank may issue. When a conversion offering is oversubscribed, some eligible depositors are allocated only a fraction of the shares they requested, and some depositors may receive none at all.

23. All of the offerings at issue were oversubscribed, and legitimate depositors were therefore deprived of their full opportunity to purchase stock as a result of Defendants' scheme.

B. <u>Defendants Were Experienced Bank Conversion Investors</u>

24. Grace began investing in mutual-to-stock conversion offerings over twenty-five years ago.

25. At all relevant times, Grace was well versed in conversion offering rules, particularly the group purchase limits, and was very familiar with the terms "associate" and

"acting in concert." Grace also periodically obtained legal advice concerning the application of these terms to his children and various entities.

26. At all relevant times, Grace was specifically aware that he was required to treat, for purposes of complying with the group limits of a conversion offering, his children living in his home, as well as the Drake Funds, and his other affiliated entities, as "associates," and to disclose them as such in stock order forms.

27. At all relevant times, the Drake Funds and these other affiliated entities qualified as "associates" of Grace within the meaning of the offering terms and stock order forms:

(a) Grace's limited partnership share in each of the Drake Funds exceeded 10%;

(b) Grace owned 49% of DAM, the general partner of the Drake Funds;

(c) Grace was the president and director of an affiliated entity; and

(d) Grace's limited partnership share in another affiliated entity exceeded 10% and he was the sole owner of its general partner.

28. DAM, like Grace, also had extensive experience with conversion offerings. DAM highlighted its expertise in these types of investments in marketing and promotional materials for the Drake Funds. DAM also periodically obtained legal advice from Grace's attorney on offering rules, including group limitations, and other conversion issues generally.

29. At all relevant times, Defendants were also aware that converting banks and their underwriters, to enforce group limits and ensure fair allocation of shares, carefully reviewed stock order forms and deposit account documentation in order to detect undisclosed relationships among depositors. Defendants knew that converting banks typically flagged order forms containing, for example, common addresses, common signatories, and the use of common service providers such as custodians, trustees, and law firms. Defendants understood that these

commonality indicators created a presumption of group activity that, absent a credible explanation, would likely result in a restriction on the amount of shares allocated to the depositors in question.

C. Defendants' Scheme

30. The misconduct at issue concerns the mutual-to-conversion offerings of seven banks between late-2003 through mid-2007: Northwest Bancorp, KNBT Bancorp, NewAlliance Bancshares, BankFinancial Corp., Investors Bancorp, Roma Financial Corp., and TFS Financial Corp.

31. Hoping that these banks would convert to stock ownership, Grace opened and funded savings accounts variously for himself, his children, and his affiliated entities. Under Grace's oversight and supervision, DAM caused the Drake Funds to open and fund savings accounts at five of the seven banks.

32. Defendants tracked their saving account activities and conversion offering participations using one database that was updated and monitored by Grace's employees at his family office in Glen Head, New York. DAM also operated from this office using some of the same employees.

33. When the seven banks initiated conversions, Grace, with the assistance of the employees he shared with DAM, completed and submitted stock order forms for himself, his children, the Drake Funds, and his other affiliated entities.

34. Grace correctly disclosed his association with his children who resided with him on his stock order forms. Likewise, Grace ensured that his children correctly disclosed their association with him on their order forms. In each conversion, Grace and his children ordered the maximum number of shares permitted for a group of associated depositors.

35. However, in an attempt to circumvent the group limits and prevent any reductions in the amount of shares allocated to him and his children, Grace knowingly or recklessly failed to treat the Drake Funds and his other affiliated entities as his "associates" or entities "acting in concert" with him, and to disclose them as such on his order forms. These order forms were thus materially false and misleading.

36. Moreover, Grace falsely certified that the information in his stock order forms was true, correct, and complete.

37. The Drake Funds and Grace's other affiliated entities also failed to disclose that they were "associated" or "acting in concert" with Grace on their stock order forms in connection with the conversion offerings in which they participated alongside Grace. These order forms were thus materially false and misleading.

38. Moreover, each of these entities falsely certified that the information in their stock order forms was true, correct, and complete.

39. To conceal their group activity from the converting banks and their underwriters, Defendants arranged for the Drake Funds and Grace's other affiliated entities to use either addresses on their forms that were not traceable back to Grace's family office where the entities were actually headquartered (or Grace's own residence), or different employees of the family office and DAM (other than Grace) to sign and certify stock order forms on behalf of these entities. As a result, Defendants intentionally misled the banks by submitting order forms for the group that were seemingly unrelated.

40. The scheme enabled Grace and his "associates" to order and receive conversion offering shares that exceeded the allowable group limits in seven offerings, five of which involved the Drake Funds.

D. Examples of Defendants' Scheme

41. The misconduct by Defendants in connection with two mutual-to-stock conversion offerings in particular illustrate in more detail how the scheme worked:

BankFinancial Corp.

42. In April 2005, BankFinancial, F.S.B., a federally-chartered savings bank in Illinois, mailed its account holders a package of information concerning its conversion from mutual to stock ownership. Under the conversion plan, a maximum of 24,466,250 shares of common stock were to be offered at $10.00 per share by BankFinancial Corp. ("BankFinancial"), a bank holding company formed to effect the conversion.

43. BankFinancial's common stock is currently registered with the Commission pursuant to Section 12(b) of the Exchange Act and is listed on the NASDAQ stock market under the symbol BFIN.

44. The package included prospectuses and stock order forms to be used by the account holders in subscribing to the offering. The account holders were required to complete the stock order forms, sign them, and submit them to the bank with payment for the full number of shares for which they subscribed.

45. As set forth in the prospectus and the stock order form, individual account holders could subscribe for a maximum of 50,000 shares (or $500,000) of common stock and no person, together with any "associates" or persons "acting in concert" could purchase more than 75,000 shares. The prospectus defined the term "associate" of a person to be:

> "(1) any corporation or organization . . . of which the person is a senior officer, partner or 10% beneficial stockholder;
>
> (2) any trust or other estate in which the person has a substantial beneficial interest or serves as a trustee or in a fiduciary capacity . .; and

(3) any blood or marriage relative of the person, who . . . lives in the same home as the person . . . ."

46. The front-side of the order form required purchasers to check a box titled in bold, "**Associates/Acting in Concert**," and to "complete the reverse side of this form, if you or any associates or persons acting in concert with you have submitted other orders for shares." On the reverse-side of the order form, there is a section titled in bold, "**Associates/Acting in Concert continued**" where the purchaser is required to "list . . . all other orders submitted by you or associates (as defined below) or by persons acting in concert with you (also defined below)" by disclosing the "name(s) listed on other stock order forms" and the corresponding "number of shares ordered." Directly below this section, the definition of "associate" from the prospectus was set forth.

47. Directly above the signature line on the front-side of the order form was an acknowledgment that stated: "Under penalty of perjury, I hereby certify that the Social Security or Tax ID Number and the information provided on this stock order form is true, correct and complete . . . ." The order form also listed a toll-free phone number if purchasers had any questions concerning the form.

48. Defendants submitted five order forms in May 2005 for Grace (47,400 shares), his two minority-aged children living with him (13,800 shares each), and two of the Drake Funds (50,000 shares for Drake; 25,000 shares for Diversified), for a total of 150,000 shares, 75,000 shares over the group purchase limit. Grace signed his order form.

49. While Grace and his two children disclosed their association with each other on their respective order forms, he knowingly or recklessly failed to disclose his association with Drake and Diversified on his form. Moreover, Grace falsely certified that the information provided in his order form was true, correct, and complete.

50. Similarly, while the Drake Funds disclosed their association with each other on their respective order forms, they each knowingly or recklessly failed to disclose their obvious association with Grace. Moreover, they falsely certified that the information provided in their respective order forms was true, correct, and complete.

51. Because the offering was oversubscribed and their savings account balances were not large enough to qualify for a full allocation, Grace and his two daughters received less than their full order – 37,598, 11,003, and 11,003 shares, respectively. Diversified also did not qualify for a full allocation and received 13,249 shares. Drake received the full amount of its order, 50,000 shares, because its account was large enough to qualify for a full allocation. Grace, his family, and the Drake Funds collectively received an aggregate of 122,853 shares, or 47,853 shares in excess of the group purchase limit, yielding ill-gotten gains of $172,270.

Roma Financial Corp.

52. In May 2006, Roma Financial Corp. ("Roma"), a federally-chartered stock holding company of Roma Bank, a federally-chartered savings bank in New Jersey, mailed account holders of the bank a package concerning an upcoming offering of stock in connection with Roma's conversion to stock form of ownership.

53. Roma's common stock is currently registered with the Commission pursuant to Section 12(b) of the Exchange Act and is listed on the NASDAQ stock market under the symbol ROMA.

54. The package included prospectuses and stock order forms for account holders to use to subscribe to the offering. The account holders were required to complete the order forms, sign them, and submit them to the bank with payment for the number of shares for which they subscribed.

55. As set forth in the prospectus and the stock order form, individual account holders could subscribe for a maximum of 30,000 shares of common stock and no person, together with any "associates" or persons "acting in concert" could purchase more than 30,000 shares. The prospectus defined the term "associate" of a person to be:

> "(1) any corporation or organization of which such person is a senior officer or partner or is, directly or indirectly, the beneficial owner of 10% or more of any class of equity securities;
>
> (2) any trust or other estate in which such person has a substantial beneficial interest or as to which such person serves as trustee or in a similar fiduciary capacity; and
>
> (3) any person who is related by blood or marriage to such person and . . . who lives in the same home as such person . . . ."

56. The prospectus also stated:

> "Each person purchasing shares of the common stock in the offering will be considered to have confirmed that his purchase does not conflict with the maximum purchase limitation. If the purchase limitation is violated by any person or any associate or group of persons affiliated or otherwise acting in concert with that person, we will have the right to purchase from that person at the $10.00 purchase price per share all shares acquired by that person in excess of that purchase limitation or, if the excess shares have been sold by that person, to receive the difference between the purchase price per share paid for the excess shares and the price at which the excess shares were sold by that person."

57. The front-side of the stock order form required purchasers to check a box titled in bold, "**Associates/Acting in Concert**," and to "complete the reverse side of this form, if you or any associates or persons acting in concert with you have submitted other orders for shares." On the reverse-side of the order form, there is a section titled in bold, "**Associates/Acting in Concert continued**" where the purchaser is required to "list . . . all other orders submitted by you or associates (as defined below) or by persons acting in concert with you (also defined below)" by disclosing the "name(s) listed on other stock order forms" and the corresponding

"number of shares ordered." Directly below this section, the definition of "associate" from the prospectus was set forth.

58. Directly above the signature line on the front-side of the order form was an acknowledgment that stated: "Under penalty of perjury, I hereby certify that the Social Security or Tax ID Number and the information provided on this stock order form is true, correct and complete . . . ." The order form also listed a toll-free phone number if purchasers had any questions concerning the form.

59. Defendants submitted six orders in June 2006 for Grace (4,800 shares), his three minor children who lived with him (8,400 shares each), and Drake (30,000 shares), for a total of 60,000 shares, 30,000 shares over the group purchase limit.

60. Grace signed his order form on which he disclosed his association with his children. Grace, as custodian, also signed his children's order forms, which disclosed their association with their father. However, Grace knowingly or recklessly failed to disclose his association with Drake as required and thus his order form was materially false and misleading. Moreover, Grace falsely certified that the information provided in his order form was true, correct, and complete

61. Similarly, Drake's order form was materially false and misleading as it did not disclose its association with Grace. Moreover, Drake falsely certified that the information provided in its order form was true, correct, and complete.

62. Because the offering was oversubscribed and their savings account balances were not large enough to qualify for a full allocation, Grace and his children did not receive the full amount of their orders – 4,457 for Grace, with each child receiving 8,104 shares. Drake received the full amount of its order, 30,000 shares, because its account was large enough to qualify for a full allocation. Grace, his three children, and Drake collectively received an aggregate of 58,769

shares, which was 28,769 shares in excess of the group purchase limit, yielding ill-gotten gains of $117,953.

CLAIMS FOR RELIEF

FIRST CLAIM

Violations of Section 10(b) and Rule 10b-5 of the Exchange Act by DAM

63. Paragraphs 1 through 62 are re-alleged and incorporated by reference.

64. DAM, by engaging in the conduct described above, knowingly or recklessly, in connection with the purchase or sale of securities, directly or indirectly, by use of the means or instrumentalities of interstate commerce, or the mails, or the facilities of a national securities exchange:

(a) employed devices, schemes and artifices to defraud;

(b) made untrue statements of material fact, or omitted to state material facts necessary in order to make statements made, in the light of the circumstances under which they were made, not misleading; and/or

(c) engaged in acts, practices and courses of business which operated or would have operated as a fraud or deceit upon any person in connection with the purchase or sale of any security.

65. By engaging in the forgoing conduct, DAM violated, and unless enjoined will continue to violate, Section 10(b) of the Exchange Act [15 U.S.C. §78j(b)], and Rule 10b-5 thereunder [17 C.F.R. § 240.10b-5].

SECOND CLAIM

Violations of Section 10(b) and Rule 10b-5 of the Exchange Act by Grace

66. Paragraphs 1 through 62 are re-alleged and incorporated by reference.

67. Grace, by engaging in the conduct described above, knowingly or recklessly, in connection with the purchase or sale of securities, directly or indirectly, by use of the means or instrumentalities of interstate commerce, or the mails, or the facilities of a national securities exchange:

(a) employed devices, schemes and artifices to defraud;

(b) made untrue statements of material fact, or omitted to state material facts necessary in order to make statements made, in the light of the circumstances under which they were made, not misleading; and/or

(c) engaged in acts, practices and courses of business which operated or would have operated as a fraud or deceit upon any person in connection with the purchase or sale of any security.

68. By engaging in the forgoing conduct, Grace violated, and unless enjoined will continue to violate, Section 10(b) of the Exchange Act [15 U.S.C. §78j(b)], and Rule 10b-5 thereunder [17 C.F.R. § 240.10b-5].

PRAYER FOR RELIEF

WHEREFORE, the Commission respectfully requests that this Court enter a judgment:

A. Permanently restraining and enjoining DAM from violating, directly or indirectly, Section 10(b) of the Exchange Act [15 U.S.C. § 78j(b)], and Rule 10b-5 thereunder [17 C.F.R. § 240.10b-5];

B. Permanently restraining and enjoining Grace from violating, directly or indirectly, Section 10(b) of the Exchange Act [15 U.S.C. § 78j(b)], and Rule 10b-5 thereunder [17 C.F.R. § 240.10b-5];

C. Ordering Grace to disgorge all ill-gotten gains derived from the violations alleged herein, and to pay prejudgment interest thereon;

D. Ordering DAM to pay civil monetary penalties pursuant to Section 21(d)(3) of the Exchange Act [15 U.S.C. § 78u(d)(3)];

E. Ordering Grace to pay civil monetary penalties pursuant to Section 21(d)(3) of the Exchange Act [15 U.S.C. § 78u(d)(3)]; and

F. Granting such further relief as the Court may deem just and appropriate.

*****

Dated: October 31, 2011

Respectfully Submitted,

Frederick L. Block (DC Bar No. 492358)
Robert B. Kaplan
Scott F. Weisman
Paul E. Kim

Attorneys for Plaintiff
U.S. Securities and Exchange Commission
100 F Street, N.E.
Washington, D.C. 20549
(202) 551-4919 (Block) – Phone
(202) 772-9245 (Block) – Fax