

**PART B**

**THE RELATIONSHIP OF MADISON GUARANTY, CMS,  
JIM McDOUGAL, THE ROSE LAW FIRM, HILLARY  
RODHAM CLINTON AND WILLIAM J. CLINTON**

**Chapter 1:**

**The Final Fifteen Months of Jim McDougal's Involvement at Madison Guaranty  
(1985 to Summer 1986)**

## I. INTRODUCTION

This Chapter details evidence about the relationship between three individuals (Jim McDougal, Hillary Rodham Clinton, and William J. Clinton) and four entities (Capital Management Services, Whitewater Development Company, the Rose Law Firm, and Madison Guaranty Savings & Loan) in 1985 and 1986.

First, both Jim McDougal and Mrs. Clinton had a direct relationship with Madison Guaranty. McDougal, the thrift's owner and operator, hired the Rose Law Firm ("Rose") where Mrs. Clinton was a partner. Mrs. Clinton performed legal services for Madison Guaranty including work before various state agencies operating under Governor Clinton.

Second, McDougal, Mrs. Clinton, Madison Guaranty, and Rose were all connected to a real estate development called Castle Grande. McDougal purchased the land and buildings from Industrial Development Corporation ("IDC") by using the resources of Madison Guaranty and its subsidiary, Madison Financial Corporation. To evade regulatory limitations on the amount Madison Guaranty could invest in real estate transactions of its service corporation, McDougal arranged for some of the land and a sewer and water utility located thereon to be purchased by Seth Ward, Rose partner Webster Hubbell's father-in-law and a Madison Financial employee. Hubbell, Mrs. Clinton, and Rose provided legal services related to Madison Financial's purchase and development of the property, including conferences with "straw purchaser" Seth Ward. Portions of Castle Grande were sold to insiders (including Jim Guy Tucker) at fraudulently inflated prices so that Madison Financial could book a "profit."

The Castle Grande transactions were scrutinized by federal thrift examiners, who

concluded that the transactions rendered Madison Guaranty insolvent. To conceal Ward's compensation from the Castle Grande transaction, Ward and Madison Guaranty insiders created fraudulent loan documents and an option agreement that deceived regulators. Mrs. Clinton performed legal services for Madison Guaranty and Ward to create these deceptive documents, though the evidence is insufficient to prove she knew the fraudulent nature or purpose of the documents.

Third, McDougal and Madison Guaranty had a substantial relationship with David Hale, who owned CMS, a federally licensed and regulated small business investment company that was supposed to loan money to disadvantaged small businesses. Between 1985 and 1986, McDougal, Hale, and others (including Mrs. McDougal and former Arkansas Governor Jim Guy Tucker) engaged in a financially complex fraud scheme. The scheme's central focus, described more fully in Volume I, Appendix 5, was a fraudulent loan from Madison Guaranty to a straw purchaser named Dean Paul. Paul used this loan to purchase property from Hale at inflated prices, allowing Hale to book a "profit," which Hale shifted to CMS so he could get three dollars in federal funds for every dollar he had invested in CMS.

Hale and CMS made four fraudulent loans to people or businesses designated by McDougal, including Larry Kuca, Steve Smith, Susan McDougal, and a corporation controlled by Jim Guy Tucker. Tucker's corporation used his CMS money for a down payment on the sewer and water system at McDougal's Castle Grande development. As detailed in Volume II, Part A of this Report, the proceeds from some of the CMS loan to Susan McDougal were used to make payments that benefited the Whitewater Development Company, then jointly owned by the

Clintons and McDougals. Some evidence suggests Governor Clinton knew about the CMS loan to Mrs. McDougal and its intended use to benefit Whitewater, but that evidence was insufficient to prove Governor Clinton's knowing participation in a fraudulent scheme. As set forth in this Chapter, some evidence also suggests that Mrs. Clinton did legal work that may have been related to Castle Sewer and Water's purchase of the utilities from Ward and Madison Financial.

This Chapter focuses exclusively on evidence of events during 1985 and 1986. A detailed explanation of these historical events serves two functions:

- James McDougal ran Madison Guaranty (and its subsidiary, Madison Financial) in a corrupt and fraudulent fashion that involved numerous significant federal criminal offenses. The Independent Counsel's investigation established that fact, and determined that insufficient evidence existed to prove beyond a reasonable doubt that either Governor Clinton or Mrs. Clinton knowingly participated in that criminal conduct in 1985 and 1986.
- Fraudulent activity conducted at Madison Guaranty quickly came under scrutiny by federal regulators and federal investigators. When it became apparent that McDougal's activities had caused the thrift's failure, many individuals associated with the thrift took steps to conceal or minimize their connection.

## **II. FINDINGS AND ANALYSIS**

The Independent Counsel reports the following findings and conclusions:

About Rose's initial representation of Madison Guaranty:

- Madison Guaranty's principal law firm was Mitchell, Williams, Selig, Jackson & Tucker.
- Rose first did work for McDougal when it represented the Bank of Kingston/Madison Bank in the early 1980s. Rose's bill for an appeal remained unpaid for over two years.
- In October 1984, Madison Bank & Trust paid Rose's outstanding bill.
- From 1985 to 1986, Rose performed legal services for Madison Guaranty on regulatory matters before the Arkansas Securities Department. These included:

- Seeking authorization to issue preferred stock; and
  - Seeking to open a limited partnership/broker-dealer.
- Madison Guaranty wanted to issue preferred stock to increase its net worth and satisfy regulators about the institution's financial status.
  - Mrs. Clinton was the Rose billing partner on Madison Guaranty matters. She performed work on the matters involving the ASD, and her name appeared in some of the correspondence between Rose and the agency.

About the Castle Grande real estate transaction:

- Seth Ward and Jim McDougal engaged in a fraud designed to purchase property from IDC while evading regulatory limitations.
- Ward acted as a straw purchaser of some of the IDC property. Although the title was in Ward's name and there was a loan taken out in Ward's name, he had no other indicia of ownership: Ward was not personally liable to pay the loan. His compensation for his role in the purchase was to be paid certain "commissions" on future sales of the property - - whether he had a hand in the sales or not -- rather than being compensated for the capital gains on the land.
- Webb Hubbell did legal work for Ward on Ward's purchase and subsequent disposition of the Castle Grande property.
- Between the date the property was purchased (October 4, 1985) and sold (February 28, 1986), Mrs. Clinton billed Madison Guaranty for fourteen conferences with Seth Ward.
- Portions of the property were resold to insiders -- Jim Guy Tucker, Larry Kuca, and Davis Fitzhugh -- at inflated prices. The purchases were financed primarily by loans from Madison Guaranty.
- Rose also performed legal work related to proposed uses of Castle Grande requiring approval from state agencies:
  - An examination of whether a brewery could be constructed at the property, which involved the Arkansas Alcohol Beverage Commission; and
  - An examination of whether the utility on the property could sell services outside of Castle Grande, which involved the Arkansas Public Service

Commission, the Arkansas Pollution Control Board, and the Arkansas Board of Health.

- In early March 1986, Madison Guaranty was subject to an extensive examination by federal examiners from the Federal Home Loan Bank Board, which oversaw thrifts.
- To conceal the compensation Ward was paid for his role as straw man, Madison Guaranty created fictitious records of two "cross loans."
- When federal examiners questioned the propriety and relationship of the two cross loans, Madison Guaranty falsely told examiners the two cross loans were unrelated.
- To conceal the relationship between the two cross loans, Ward and Madison Guaranty used an option agreement. Mrs. Clinton was involved in drafting the option agreement for Madison Guaranty and Ward.
- The evidence is insufficient to prove beyond a reasonable doubt that Mrs. Clinton knew Madison Guaranty and Seth Ward intended to use the option agreement to deceive regulators.

About Jim McDougal's relationship with Hale's Capital Management Services and related transactions as detailed in this Chapter; Volume I, Appendix 5, and Volume II, Part A of this Report:

- Jim McDougal, Jim Guy Tucker, and David Hale, engaged in a fraudulent plan to induce the Small Business Administration to provide additional federal funds to Capital Management Services for their own benefit.
- Part of the plan involved Madison Guaranty loaning money to a straw purchaser, Dean Paul. Paul purchased three parcels of property from David Hale at prices created with falsely inflated appraisals. Hale used profits from these fraudulent sales to provide money to CMS. CMS's increase in capital was matched three-for-one with federal funds by the Small Business Administration.
- CMS made fraudulent loans to Tucker's corporation, Mrs. McDougal, Stephen Smith, and Larry Kuca. These loans were not used for purposes specified in loan application documents.
- Mrs. Clinton did legal work for Seth Ward that appears to be connected to the utilities which were the subject of loans to Tucker's corporation.

- Some of Mrs. McDougal's loan proceeds went to pay Whitewater Development Company obligations; the McDougals and Clintons were equal owners of Whitewater Development.
- There was some evidence that Governor Clinton may have known about the loan to Mrs. McDougal, but there was insufficient evidence to prove beyond a reasonable doubt that Governor Clinton knew the loan was illegally obtained.

The Independent Counsel's findings resolve several previously disputed questions of historical fact. Four aspects of these findings and conclusions warrant brief elaboration here.

The topics addressed include: 1) the retention of the Rose Law Firm by Madison Guaranty, and an old bill for the prior representation by Rose for McDougal Madison Bank and Trust; 2) Seth Ward's role as a straw purchaser of the Castle Grande; 3) Mrs. Clinton's role in drafting an option agreement in the Castle Grande transaction; and 4) the option agreement's deceptive effect on the federal bank examination of Madison Guaranty.

**A. Madison Bank and Trust Bill.**

The Office's investigation was able to establish that when Madison Guaranty retained Rose in April 1985, Madison Bank & Trust did not have an unpaid bill for Rose's services from the early 1980s. That Madison Bank & Trust bill was paid in October 1984. This conclusion is significant because Mrs. Clinton testified that the retention of the Rose Firm by Madison Guaranty began in April 1985 when she met with Jim McDougal to demand payment of this (already paid) bill.

The Rose bill for services to Madison Bank & Trust on July 30, 1982, amounted to \$5,000 in legal fees, and \$893.63 in costs and expenses. Documentary evidence showed that in July 1982, when Rose's work for Madison Bank & Trust was complete, McDougal was unhappy

with the result and told his staff not to pay the bill. Documentary evidence also showed that in October 1983, Mrs. Clinton unsuccessfully tried to collect payment on this bill from McDougal.

Documentary evidence also established that in September 1984, Madison Bank & Trust board authorized the Bank's president to negotiate settlement of the disputed bill with Rose. Rose engaged in a discussion with Madison Bank & Trust, hoping to obtain payment, memorialized in correspondence between Vince Foster and the Bank. On October 22, 1984, the Bank paid Rose \$5,000. The next day, Rose stamped the Bank of Kingston bill "paid" and credited attorneys who had worked on the matter with their portion of the collected fees, which were adjusted to reflect that Rose had "written off" the costs. The Bank considered the matter settled; Rose never made any effort to collect the written off \$893.63.

**B. Castle Grande.**

Three aspects of the fraudulent Castle Grande transaction warrant elaboration: Seth Ward's role; Mrs. Clinton's role drafting the option agreement; and the deceptive effect the option agreement had on federal bank examiners.

Seth Ward and Castle Grande -- Evidence established that Seth Ward was the straw purchaser of some of the IDC property, later known as Castle Grande. Ward enabled McDougal and Madison Financial to buy the land by circumventing the regulatory six percent limit on investments that a thrift could make in its subsidiary. The six percent limit restricted what Madison Guaranty could lend Madison Financial; it did not limit what Madison Guaranty could lend to a private party such as Ward.

Ward wanted assurance that he had no personal financial risk for acting as nominee.



McDougal agreed Madison Guaranty would lend Ward the entire amount of the purchase price on a nonrecourse basis. Madison Guaranty would rely only on the value of the property itself for repayment if Ward failed to repay the loan. In return, Ward agreed to grant Madison Financial an option for at least 270 days to purchase any part of the property from him at a price equal to the nonrecourse loan plus all accrued interest. Madison Financial could purchase portions of Ward's property as needed, and sell them to third parties. Ward received "commissions" on subsequent sales of the property to third parties -- even when he had nothing to do with arranging sales. Ward served as a "warehouse" for the property, and never put in any of his own money.

When Ward and his accountant, Mike Schaufele, met with McDougal in late August 1985, Ward specifically sought reassurance about the tax implications of the transaction. Madison Financial agreed to reimburse Seth Ward for any additional taxes he owed by virtue of his holding the property. Madison Financial also agreed to handle all administrative duties associated with the property, such as collecting rents and sewer and water fees.

Ward received significant compensation with no risk or responsibility, making clear Ward was Madison Financial's straw purchaser using Madison Guaranty's money. Ward did nothing to earn his "commissions," and had none of the traditional indicia of property ownership, like the burden of paying taxes and collecting rents. Moreover, Ward's only source of compensation was his "commission," having relinquished any rights to appreciation in the property's value.

Mrs. Clinton and the Option Agreement -- Mrs. Clinton testified that she did not remember doing any legal work on the May 1, 1986 option agreement, nor did she think she

drafted it "from scratch." Evidence showed that Mrs. Clinton helped draft the option agreement.

Mrs. Clinton billed Madison Guaranty for her work, and there was no evidence that this bill was in error. The option agreement bore Mrs. Clinton's unique Rose computer code, designed by Rose to identify the attorney who drafted a particular document. Finally, Mrs. Clinton once had a file labeled "Ward Option," which she had destroyed in July 1988, along with her other Madison Guaranty files.

The Regulators and the Option Agreement -- Federal examiners said the existence of the option hindered their investigation of Madison Guaranty. Although the examiners were suspicious of the cross loans and option, the existence of the option provided documentary support for Madison Guaranty's claim that two unfunded April 7, 1986 cross loans were intended to document Madison Financial's intention to purchase Holman Acres from Ward, and were not related to the original September 24, 1985 Castle Grande land purchase agreement.

The option successfully deceived the examiners. Ward was paid over \$380,000 for his role as straw man in the IDC transaction at the same time examiners were attempting to shed light on such fraudulent transactions. The option concealed the true nature of Ward's payments from examiners, who accepted Madison Guaranty's claim that the loans to Ward were unrelated to his commissions.

### **III. FACTUAL SUMMARY**

This section summarizes evidence found by the Independent Counsel's investigation about the final fifteen months of the Madison Guaranty operation. It discusses evidence about:

- Madison Guaranty's retention of Mrs. Clinton and Rose, and work Rose did for Madison Guaranty in front of Arkansas state agencies under her husband's authority;
- transactions involving the Castle Grande development, including a summary of legal work done by Rose and Mrs. Clinton;
- the examination of Madison Guaranty conducted by federal regulators and efforts of the Madison Guaranty insiders to conceal their misconduct; and

The section also briefly discusses relevant aspects of the evidence relating to an \$825,000 loan made by Madison Guaranty to Dean Paul so that Paul could buy property at falsely inflated prices from David Hale, which Hale used to get more federal funds for CMS. CMS made fraudulent loans to Jim Guy Tucker's corporation, Susan McDougal, Larry Kuca, and Steve Smith. Mrs. McDougal's CMS loan was used to benefit Whitewater Development Company and its partners, the McDougals and Governor and Mrs. Clinton.<sup>465</sup>

**A. The Rose Law Firm's Representation of a McDougal-Controlled Financial Institution before 1985.**

Beginning in 1992, Madison Guaranty's retention of Rose, where Mrs. Clinton was a partner, and Rose's work for the savings and loan, received considerable attention. Public reports disclosed that Governor and Mrs. Clinton had a business relationship with Jim McDougal, owner of the failed savings and loan, and that Mrs. Clinton and Rose had represented the thrift during its most troubled period. McDougal publicly stated that Governor Clinton had asked him to hire

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<sup>465</sup> Much of the information relating to the \$825,000 loan to Dean Paul and the subsequent fraudulent loans to Kuca and Smith are detailed in Vol. I, Appendix 5. The subsequent fraudulent \$300,000 loan to Susan McDougal (d/b/a Master Marketing) and the use of the proceeds of that loan to benefit the Whitewater Corporation are detailed in Vol. II, Part A of this Report. This Chapter details the evidence relating to the subsequent fraudulent loan to Castle Sewer and Water, a corporation controlled by Jim Guy Tucker.

Mrs. Clinton. Journalists and then federal investigators questioned President and Mrs. Clinton about Rose's Madison Guaranty representation.

Numerous conflicting stories were told by those involved about how Madison Guaranty came to hire Rose. While Jim McDougal claimed that Madison Guaranty hired Rose because Governor Clinton asked him to hire his wife, Mrs. Clinton said Governor Clinton had nothing to do with it. Mrs. Clinton further said Madison Guaranty hired Rose because a young associate at Rose knew the president of Madison Guaranty, John Latham, and asked Latham to hire them. Mrs. Clinton's statements on this subject are addressed in Part B, Chapter 3 of this Report. This section addresses only known facts about the retention and the early work Rose did for Madison Guaranty.

**1. Rose Represented the McDougals' Bank of Kingston (Madison Bank & Trust) in a Regulatory Matter and Litigation.**

Rose's first representation of a McDougal-controlled financial institution began in April 1981, when Rose represented the Bank of Kingston in its effort to move its principal office to a different town in Arkansas.<sup>466</sup> Jim McDougal hired Charles Joseph "Joe" Giroir Jr., then chief operating officer of Rose.<sup>467</sup> Mrs. Clinton apparently had nothing to do with Rose's hiring and,

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<sup>466</sup> Letter from E.J. Ball, Ball & Mourton attorney, to Don Denton, Senior Vice-President, Madison Guaranty (Oct. 20, 1980) (Doc. Nos. 1171-00000376 through 380). Jim and Susan McDougal purchased a controlling interest in the Bank of Kingston in October 1980. Other investors included Steve Smith, Julie Baldrige (Smith's wife), and Jim Guy Tucker. Statement from Ball & Mourton to Bank of Kingston and James B. McDougal (Oct. 20, 1980) (Doc. No. GG-00000065).

<sup>467</sup> J. McDougal 8/96-6/97 Int. at 8; J. McDougal 4/2/97 GJ at 76; see also Giroir 7/18/96 GJ at 18 ("I think [the business] came because of my reputation . . . in the commercial banking

although she was allocated a small portion of the fee for Rose's handling of the matter, she did no substantive work on the case.<sup>468</sup>

Rose initially represented the bank in petitioning the Arkansas Bank Department to move the bank's principal office to Huntsville, Arkansas. The prior owners of the Bank of Kingston also owned the nearby First National Bank of Huntsville. When they sold their stock to the McDougals and the others, the contract contained a clause prohibiting a move to that location. First National Bank of Huntsville learned of the Bank of Kingston's proposal, and sued to enforce the non-competition clause.<sup>469</sup>

The litigation was handled primarily by Vincent W. Foster Jr., a partner in Rose's litigation section.<sup>470</sup> The Chancery Court ruled against Bank of Kingston on November 6, 1981, and prohibited the move.<sup>471</sup> Foster prepared a letter to the bank's board "provid[ing] an estimate of the cost of an appeal, and provid[ing] a recommendation concerning an appeal."<sup>472</sup> Madison

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area").

<sup>468</sup> See Rose Billing Records (Dec. 21, 1981) (Doc. No. DEK014941) (Mrs. Clinton was allocated \$21.25 on fees of more than \$13,000 billed in December 1981).

<sup>469</sup> Complaint, First Nat'l Bank of Huntsville v. Bank of Kingston, (Ch. Ct. of Madison County, Ark Aug. 4, 1981) (Doc. Nos. 1171-00000316 through 319).

<sup>470</sup> Rose allocations show that Foster was allocated fees of \$8,436 of the total fee amount of \$13,060.50 before the appeal. Rose Billing Records (Dec. 21, 1981) (Doc. No. DEK014941).

<sup>471</sup> Findings of Fact, Conclusions of Law and Order of the Court, First Nat'l Bank of Huntsville v. Bank of Kingston, No. E-81-112 (Ch. Ct., Madison County, Ark.) (Doc. Nos. GG-00000156 through 161).

<sup>472</sup> Letter from Vincent Foster, Rose Attorney, to Mr. and Mrs. James B. McDougal, stockholders of Madison Bank & Trust, Steve Smith, stockholder of Madison Bank & Trust, Austin Smith, board member of Madison Bank & Trust and Steve Smith's father, Gary Easterling, board member of Madison Bank & Trust, Jim Guy Tucker, board member and

Bank & Trust (Bank of Kingston's new name) decided to appeal at a fixed rate of \$5,000 plus costs.<sup>473</sup> The appeal was unsuccessful.<sup>474</sup> Rose's fees totaled the agreed \$5,000 plus \$893.63 in expenses, and on July 30, 1982, Giroir mailed McDougal a bill.<sup>475</sup> McDougal wrote on the outside of the envelope: "Carla: DO NOT PAY. KEEP IN FILE. Jim."<sup>476</sup>

Rose's July 1982 bill remained unpaid for more than two years. McDougal said he refused to pay the bill because he was "vastly overcharged"<sup>477</sup> because Rose billed him for a senior attorney like Foster, but sent a junior attorney to argue the appeal.<sup>478</sup> In the fall of 1983, Mrs. Clinton contacted McDougal to try to get the bill paid.<sup>479</sup> Giroir later said he may have

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attorney at Mitchell Williams and James Vaughn, board member of Madison Bank & Trust, at 1 (Nov. 16, 1981) (Doc. Nos. GG-00000146 through 148).

<sup>473</sup> See Letter from Vincent Foster, Rose attorney, to Gary Bunch, President, Madison Guaranty (cc: James McDougal, Senior Vice-President, Madison Guaranty, Joe Giroir, Rose attorney) (Oct. 9, 1984) (stating that \$5,000 fee limit was agreement between Jim McDougal and Joe Giroir).

<sup>474</sup> Madison Bank & Trust v. First Nat'l Bank of Huntsville, 276 Ark. 405, 635 S.W.2d 268 (1982).

<sup>475</sup> Letter from C.J. Giroir Jr., Rose attorney, to James B. McDougal, Chairman of the Board for the Bank of Kingston (July 30, 1982).

<sup>476</sup> Letter from C.J. Giroir Jr., Rose attorney, to James B. McDougal, Chairman of the Board for the Bank of Kingston with attached envelope (July 30, 1982) (uppercase in original).

<sup>477</sup> J. McDougal 4/2/97 GJ at 77-78, 105-06.

<sup>478</sup> J. McDougal 8/96-6/97 Int. at 8; J. McDougal 4/2/97 GJ at 77; 114. Board Minutes from Madison Bank & Trust corroborate some discussion about a "new lawyer" who was assigned to the appeal. Madison Bank & Trust Board Minutes at 2 (Sept. 25, 1984); see also Letter from Vincent Foster, partner of Rose, to Gary Bunch, President, Madison Guaranty, (cc: James McDougal, Senior Vice President, Madison Guaranty, Joe Giroir, Rose Attorney) (Oct. 9, 1984).

<sup>479</sup> See Letter from C.J. Giroir, Rose Attorney, to James B. McDougal, Chairman of the Board for Bank of Kingston (Oct. 10, 1983) (Doc. No. 56-00064693) ("Pursuant to your discussion with Hillary Rodham Clinton, I am enclosing herewith a copy of our firm statement,

asked Mrs. Clinton to intercede because she knew Jim McDougal and Steve Smith.<sup>480</sup> After Mrs. Clinton's conversation with McDougal, Giroir sent another copy of the July 1982 bill on October 10, 1983.<sup>481</sup> The bank did not pay.

The Madison Bank Board Minutes for September 25, 1984, reflected that the board concluded that Gary Bunch, the bank's president, "will negotiate settlement" with Rose about the bill.<sup>482</sup> Bunch later testified that McDougal had asked him to settle the outstanding bill with Rose.<sup>483</sup>

Bunch negotiated settlement with Vince Foster, who wrote Bunch on October 9, 1984, threatening to sue unless the bill was paid by October 22, 1984:

In accordance with our telephone conversation last week, I am enclosing another copy of the statement for our services rendered in connection with the appeal of

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dated December 23, 1981. . . "). The statement was actually dated July 30, 1982. McDougal was shown a copy of Giroir's letter and did not remember speaking to Mrs. Clinton about the outstanding bill. J. McDougal 8/96-6/97 Int. at 12. Notes of John Podesta (May 18, 1994) (Doc. No. 2139-00000158) (Mrs. Clinton had "some recollection" of talking to Giroir: "This is a 10-year letter. She has some recollection of Giroir talking to her about the unpaid bill and may have talked to McDougal about it").

<sup>480</sup> Giroir 7/18/96 GJ at 21-22. Both Jim McDougal and Smith had served under Governor Clinton in his first administration in 1979-1980. Tr. at 4806, United States v. McDougal, Tucker, and McDougal, No. LR-CR-95-173 (E.D. Ark.) (testimony of S. Smith); Tr. at 6970, United States v. McDougal, Tucker, and McDougal, No. LR-CR-95-173 (E.D. Ark.) (testimony of J. McDougal).

<sup>481</sup> Letter from C.J. Giroir, Rose attorney, to James B. McDougal, Chairman of the Board for the Bank of Kingston (Oct. 10, 1983) (Doc. No. 56-00064693).

<sup>482</sup> Minutes of the Madison Bank & Trust Board Meeting at 2 (Sept. 25, 1984) (GJ Exh. 1634).

<sup>483</sup> Senate Whitewater Comm. Hearing, supra note 147, at 17 (May 16, 1996) (testimony of G. Bunch); Bunch 1/20/98 GJ at 29-30. Bunch initially said he could not remember why payment of the old bill had come up in the fall of 1984. Bunch 2/28/96 GJ at 27.

the referenced litigation. As I mentioned to you the \$5,000.00 fee limitation was established by agreement between Joe Giroir and Jim McDougal before we began work on the appeal. The agreement turned out to be to the benefit of the Bank since our actual time spent exceeded the amount charged.

You mentioned something about a "girl" lawyer doing the work on appeal. I was assisted on the appeal briefs and abstracting of the record by Carol Arnold, then a 40-year-old trial lawyer, who had already done some of the basic legal research for trial. According to our records approximately 75% of the attorney time on the appeal was spent by me.

We are totally baffled by the continued delay in the payment of this statement, but are willing to allow you an extension until October 22 in which to satisfy this statement. Otherwise, I am directed by the Firm to file suit.<sup>484</sup>

On October 22, 1984, Madison Bank & Trust paid the bill by a check to Rose for \$5,000 for "Legal Fee."<sup>485</sup> Rose credited attorneys who worked on the appeal with earning fees of \$4,106.37, which equates to the \$5,000 Madison Bank & Trust paid minus expenses Rose incurred, totaling \$893.63.<sup>486</sup> Allocating the earning of fees, less the expenses, indicates that Rose wrote off the lost expenses against the lawyers who earned the fees. After all relevant documents were located, Bunch testified that the \$5,000 payment was a final settlement of the

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<sup>484</sup> Letter from Vincent Foster, partner of Rose to Gary Bunch, President of Madison Guaranty (cc: James McDougal, Joe Giroir) (Oct. 9, 1984).

<sup>485</sup> Records from Madison Bank show that on October 23, 1984, a debit of \$5,000 was made from its general ledger for legal fees. Debit General Ledger for Account No. 16011, Legal Fees Account for \$5,000 (Oct. 23, 1984) (Doc. No. MGSL-FR-00000009). A Rose invoice confirmed a credit of \$5,000 on Madison Bank & Trust's account one day later on October 24, 1984 (July 30, 1982) (Doc. No. 1180-00000249). Letter from Alden Atkins, Vinson & Elkins attorney, to W. Hickman Ewing Jr., Deputy Independent Counsel (Apr. 17, 1996) ("[Records from Worthen Bank] show that Rose deposited a check for \$5,000 on October 24, 1984. We are told by the bank's representatives that the identification number for that check shows that it was written on an account at Madison Bank & Trust in Kingston, Arkansas").

<sup>486</sup> Letter from Ronald M. Clark, Rose attorney, to Amy St. Eve, Associate Independent



bill, and that Rose made no further efforts to collect any balance.<sup>487</sup>

In July 1997, a set of Rose's Madison Guaranty billing records from 1985-87 were found in a briefcase in the attic of Vince Foster's home.<sup>488</sup> The briefcase also contained two documents bearing on the payment of the Bank of Kingston bill. The first document was a copy of Rose's bill to the Bank of Kingston dated July 30, 1982. The copy found in Foster's briefcase was marked "paid" on October 23, 1984.<sup>489</sup> The second document found in the briefcase was a five-page chronology of Rose's representation of Madison Guaranty.<sup>490</sup> The chronology included the following:

07/30/82      Final bill of Rose Law Firm to Bank of Kingston (a/k/a Madison Bank & Trust) of \$5,000 fees and \$893 in costs (contains note in Giroir's hand: "Have Hillary bill with letter to McDougal -- will pay.")

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Counsel (May 31, 1995).

<sup>487</sup> Bunch 1/20/98 GJ at 30.

<sup>488</sup> See Evidence Report OIC-35063-1B-1212 (Aug. 1, 1997) (showed property acquired July 31, 1997); Rose Billing Records produced from Vince Foster's attic (run off date Feb. 12, 1992) (Doc. Nos. 1180-00000250 through 364); L. Foster 8/12/97 Int. at 1-2 (Vince Foster's daughter discussing how she found the documents in her family's attic on July 23, 1997).

<sup>489</sup> Rose bill to the Bank of Kingston (July 30, 1982) (Doc. No. 1180-00000249).

<sup>490</sup> Foster Chronology of the Rose Law Firm Representation of Madison Guaranty Savings & Loan (Mar. 26, 1992) (Doc. Nos. 1180-00000236 through 240). Ronald Clark, Chief Operating Officer of Rose, said the document originated on Foster's computer at Rose, with a print date of March 26, 1992. Clark 12/2/97 GJ at 135-37. Clark identified the numbers that appear on the second page, "RLL1860.WP5" as a document number under the firm's computer system. With knowledge of these identification numbers Clark was able to call up the document on the system and determine that secretary Lorraine Cline created the document for Foster. Clark 12/2/97 at 136. The numbers on the second page, 3-26-92, reflect the date the document was printed, and change every time it is printed. Clark was able to de-archive the document and print it off the system. His printed version had a date of 12-01-97. *Id.* at 135-37.

1983            Bank of Kingston final bill written off

10/23/84       \$5,000 paid on Bank of Kingston bill<sup>491</sup>

Rose made no additional attempts to collect on the bill.<sup>492</sup>

**2.        Madison Guaranty Was Principally Represented by the Mitchell Williams Firm.**

In 1982, the McDougals and five other partners purchased Woodruff County Savings and Loan Association.<sup>493</sup> Woodruff Guaranty was soon renamed Madison Guaranty Savings & Loan. Madison Guaranty's primary counsel and "lead firm" was Mitchell, Williams, Selig, Jackson & Tucker ("Mitchell Williams").<sup>494</sup> McDougal hired Mitchell Williams because of his relationship with Jim Guy Tucker, who had been a friend and business partner of his for years.<sup>495</sup>

Madison Guaranty relied almost exclusively on Mitchell Williams for legal advice. The firm provided a wide range of legal services, including regulatory work before the Arkansas Securities Department, Arkansas Bank Department, Federal Home Loan Bank Board, and other agencies.<sup>496</sup> Mitchell Williams also helped with real estate matters (some involving David Hale

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<sup>491</sup> Foster Chronology of the Rose Law Firm Representation of Madison Guaranty Savings & Loan (Mar. 26, 1992) (Doc. Nos. 1180-00000236 through 237).

<sup>492</sup> Clark 12/2/97 GJ at 135 (no evidence in Rose's files of any more collection efforts); Bunch 1/20/98 GJ at 30 (no other bills sent).

<sup>493</sup> The McDougals purchased Woodruff County Savings and Loan on January 26, 1982, with Steve Smith, C.E. Ransom, and Julie Baldrige. Memo from Lornea Wells, Legal Assistant at Mitchell Williams, to John Selig, Partner with Mitchell, Williams, about Madison Guaranty Savings & Loan/McDougal Group (Oct. 23, 1987) (Doc. No. 174-00012956).

<sup>494</sup> J. McDougal 4/2/97 GJ at 134-35; but see J. McDougal 8/96-6/97 Int. at 12.

<sup>495</sup> J. McDougal 8/96-6/97 Int. at 7, 33.

<sup>496</sup> See Tucker 9/23/81 Depo. at 13-14, First Nat'l Bank of Huntsville v. Bank of

and Dean Paul) and other general legal representation.<sup>497</sup> McDougal later testified that he was satisfied with Mitchell Williams throughout its representation and, until his conversation with Governor Clinton, had no intention of hiring Rose.<sup>498</sup>

**B. Madison Guaranty Initially Retained Rose on Two Issues before State Regulators.**

Rose's representation of Madison Guaranty began April 23, 1985, with two matters; one a preferred stock offering and the other a limited partnership/broker-dealer matter. The stock offering was Madison Guaranty's attempt to raise money and increase its net worth by issuing a new class of preferred stock. Both the Arkansas Securities Department ("ASD") and the Federal Home Loan Bank Board ("FHLBB") had directed Madison Guaranty to increase its net worth to meet state and federal requirements. Madison Guaranty wanted to increase its net worth with the stock offering, but needed approval from the ASD, and Arkansas law was unclear whether a thrift could issue a non-voting, preferred class of stock. Rose was hired to get the ASD's approval. The limited partnership matter, also called the broker-dealer matter, was Madison Guaranty's effort to establish a subsidiary investment broker-dealer to sell real estate limited partnerships. Like the preferred stock, the limited partnership/broker-dealer required ASD

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Kingston No. E-81-112 (Ch. Ct. Madison County, Ark.) (Doc. Nos. 1171-00000125 through 126).

<sup>497</sup> Information about the scope of Mitchell Williams's representation of Madison Guaranty is found in the voluminous billing records produced by Mitchell Williams to the OIC under subpoena. Grand Jury Subpoena No. 155 (E.D. Ark. May 3, 1994). See Response Letters from Mitchell Williams, Selig, Gates and Woodyard Law Offices to Office of the Independent Counsel (Doc. Nos. 155-00006309; 155-00039041; 155-00039043; 155-00054759 through 54760; 155-00056160; 155-00057157 through 57159). That firm also later defended Madison Guaranty in Seth Ward's breach of contract action against it in 1987-1988.

approval. Rose associate Richard Massey billed more hours than any other Rose attorney on these two ASD matters; Mrs. Clinton billed more time than any other Rose partner.

### **1. Arkansas Securities Department.**

The ASD was a cabinet state level agency that regulated state-chartered thrifts,<sup>499</sup> ensuring they operated soundly and complied with Arkansas regulations.<sup>500</sup> The head of the ASD was the Arkansas Securities Commissioner, who was nominated by the Governor and confirmed by the state senate,<sup>501</sup> and who also served as Arkansas Savings and Loan Supervisor.<sup>502</sup> Beverly Bassett served as Securities Commissioner from January 1985 through January 1991.<sup>503</sup> The Commissioners who preceded Bassett were Lee Thalheimer, Harvey Bell, and John Selig.<sup>504</sup> Beverly Bassett had worked on Madison Guaranty matters while an associate at Mitchell Williams. She left Mitchell Williams in January 1985 when she was appointed by Governor

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<sup>498</sup> J. McDougal 4/2/97 GJ at 134-35.

<sup>499</sup> Other responsibilities of the ASD included the regulation of securities (e.g. stocks and bonds), credit unions, mortgage companies, loan brokers, and check issuers (e.g. those who issue money orders, travelers checks, etc.). C. Handley 10/3/95 GJ at 5. The ASD did not regulate banks. The regulation of banks was the responsibility of a separate agency, the Arkansas Bank Department. Id. at 13-14.

<sup>500</sup> Id. at 19. The ASD was responsible for enforcing the Arkansas Savings and Loan Act and the Arkansas Building and Loan Act. Id. at 13-14.

<sup>501</sup> Bassett 11/8/95 GJ at 52.

<sup>502</sup> C. Handley 10/3/95 GJ at 25.

<sup>503</sup> Beverly Bassett married in 1990 at which time she changed her name to Beverly Bassett Schaffer. She was later known as Beverly Schaffer. Throughout this report, she will be referred to by the name she had for the period being discussed.

<sup>504</sup> Governor Frank White, a Republican, appointed Thalheimer. Governor Clinton, who succeeded White in 1983, permitted Thalheimer to continue as Commissioner until Thalheimer resigned in late 1984.

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<sup>505</sup> Letter from Bill Clinton, Governor of Arkansas, to Beverly Bassett, Wright, Lindsey, and Jennings attorney (Jan. 22, 1985) (Doc. No. DEK219149). The Governor's Office issued a press release announcing Bassett's appointment (Jan. 18, 1985) (Doc. No. 319-00028649). Bassett's brother, Woody Bassett, was "a long time close friend and supporter of Bill Clinton's [who] ha[d] been active in Democratic Party matters for years." Memo from Beverly Bassett Schaffer, Wright, Lindsey and Jennings attorney, to Jeff Gerth, New York Times Reporter at 2 (Feb. 25, 1992) (Doc. No. 174-00022194). Sometime in mid-1984, Bassett learned that Thalheimer, who was a friend of Bassett's and a law school classmate of her brother, was considering stepping down as Arkansas Securities Commissioner. Memo from Beverly Bassett Schaffer, Wright, Lindsey, and Jennings attorney, to Jeff Gerth, New York Times Reporter at 2 (Feb. 25, 1992) (Doc. No. 174-00022194). After confirming Thalheimer's intent to leave, Bassett and her brother spoke informally to Governor Clinton about her interest in becoming the new Securities Commissioner, and was soon formally appointed as of January 21, 1985. Bassett 11/8/95 GJ at 43-45; Letter from Governor Bill Clinton to Beverly Bassett (Jan. 22, 1985) (Doc. Nos. DEK219149, DEK219147). Woody Bassett also wrote several letters to Clinton commending his sister. See, e.g., Letter from Woody Bassett, Bassett Law Firm attorney, to Governor Bill Clinton (Nov. 26, 1984) (Doc. Nos. DEK218783 through 218785); Letter from Woody Bassett, Bassett Law Firm attorney, to Governor Bill Clinton (Dec. 19, 1984) (Doc. Nos. DEK218786 through 218787); Letter from Woody Bassett, Bassett Law Firm attorney, to Governor Bill Clinton (Dec. 7, 1984) (Doc. Nos. DEK218788 through 218789). At Selig's request, Jim McDougal, who knew Bassett, recommended Bassett to Governor Clinton. J. McDougal 8/96-6/97 Int. at 8. McDougal called Governor Clinton on December 22, 1984, to recommend Bassett. Message slip (Dec. 22, 1984) (Doc. No. DEK218791); see J. McDougal 4/2/97 GJ at 117. Bassett said she did not know McDougal recommended her, and she did not and would not have asked McDougal to recommend her. Senate Whitewater Comm. Hearing, supra note 147, at 72 (Jan. 25, 1996) (testimony of B. Schaffer). Bassett specifically asked members of her firm to stay out of the nomination process so she would not feel obligated to the firm or any of its clients. Id. at 148-149. Bassett testified she would not have wanted a recommendation from anyone in the thrift industry. Id. at 151. President Clinton said he did not remember whether McDougal recommended Bassett. W. Clinton 4/22/95 Depo. at 77.

## 2. Madison Guaranty's Net Worth Problems.

After the McDougals purchased Madison Guaranty in 1982, its deposits grew rapidly.<sup>506</sup> This growth made its pre-existing financial problems worse.<sup>507</sup> Deposits are liabilities for a savings and loan -- money owed to others -- while loans were assets -- money owed to it by others. Madison Guaranty's liabilities were nearly equal to and sometimes exceeded its assets, leaving it little net worth.<sup>508</sup> Federal regulations required thrifts like Madison Guaranty to maintain a three percent net worth.<sup>509</sup> Throughout the McDougals' ownership, this regulation was a substantial problem.

The FHLBB first examined Madison Guaranty under the McDougals' ownership in January 1984.<sup>510</sup> Its Report of Examination criticized Madison Guaranty's asset growth and net

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<sup>506</sup> Madison Guaranty's assets were \$6.6 million in 1982, \$17 million in 1983, \$49 million in 1984, and \$110 million in 1985. Pillsbury Madison & Sutro LLP, General Report on the Investigation of Madison Guaranty Savings & Loan and Related Entities: Prepared for Resolution Trust Corporation 10 (Dec. 28, 1995).

<sup>507</sup> See Memo from John Mitchell, Supervisory Analyst, Federal Home Loan Bank of Dallas, to File (Nov. 20, 1984) (Doc. Nos. 99-00005396 through 5399). Madison Guaranty's problems preceded McDougal. When McDougal purchased Madison Guaranty, "[i]t was broke. It had a negative net worth. It was in imminent danger of being closed by the regulators." J. McDougal 4/2/97 GJ at 23.

<sup>508</sup> Pillsbury Madison & Sutro LLP, General Report on the Investigation of Madison Guaranty Savings & Loan and Related Entities: Prepared for Resolution Trust Corporation 6 -14 (Dec. 28, 1995).

<sup>509</sup> FHLBB Regulation 563.13

<sup>510</sup> Report of Special Limited Examination (Jan. 20, 1984) (Doc. Nos. 212-00001601 through 1619). Madison Guaranty was also the subject of a "Special Limited Examination" in Apr. 1982, which noted a substantial decline in net worth. Memo from John Mitchell, Supervisory Analyst, Federal Home Loan Bank of Dallas, to File (Nov. 20, 1984) (Doc. Nos. 99-00005396 through 5399).

worth, indicating that if Madison Guaranty properly recognized sales of real estate from its real estate investment corporation (Madison Financial), Madison Guaranty would have shown a negative net worth of \$70,000.<sup>511</sup> The Report of Examination concluded that Madison Guaranty was in trouble because of real estate projects.<sup>512</sup> In July 1984, Jim McDougal executed a "Supervisory Agreement" with the FHLBB's parent agency, the Federal Savings and Loan Insurance Corporation ("FSLIC"). Madison Guaranty agreed to try to increase net worth.<sup>513</sup> The ASD received the FHLBB Report of Examination and FSLIC's Supervisory Agreement, and knew all about Madison Guaranty's net worth problems.<sup>514</sup> John Latham conceded the problems in a January 14, 1985 letter to the FHLBB's supervisory agent: "We recognize that the Association's total assets have been growing at a faster rate than its net worth has . . . . We are very cognizant of our net worth position and monitor it very closely on a daily basis."<sup>515</sup>

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<sup>511</sup> FHLBB Report of Special Limited Examination at 6 (Jan. 20, 1984) (Doc. No. 212-00001606).

<sup>512</sup> Id. at 2 (Doc. No. 212-00001602).

<sup>513</sup> FHLBB Supervisory Agreement (July 19, 1984) (Doc. Nos. 54-00361839 through 361844). FHLBB regulation 563.13 required a federally insured thrift to have a net worth of at least 3 percent of assets.

<sup>514</sup> Bassett testified the FHLBB directed Madison Guaranty to raise money to improve its net worth. Bassett 4/14/94 FDIC Aff. at 1. She also said the ASD worked closely with the FHLBB to remedy Madison Guaranty's problems. Bassett 1/12/94 Int. at 2.

<sup>515</sup> Letter from John Latham, Chairman of Madison Guaranty, to Carol Ondrake, Supervisory Agent, Federal Home Loan Bank (Jan. 14, 1985) (Doc. Nos. 99-00031540 through 31542).

### **3. Preferred Stock Idea: After Madison Guaranty Employees Worked on the Proposal, Regulators Denied the Application.**

Madison Guaranty proposed to raise money by issuing a new class of preferred stock.<sup>516</sup> No state-chartered thrift in Arkansas had asked to issue preferred stock before Madison Guaranty's request;<sup>517</sup> whether it could do so under state law was an open question. Mitchell Williams opened a file on the preferred stock issue on February 6, 1985; it was entitled, "Sale of Stock."<sup>518</sup> The file remained empty and Mitchell Williams billed no fees.<sup>519</sup> On February 27, 1985, Madison Guaranty filed its business plan with the FHLBB,<sup>520</sup> but did not mention issuing preferred stock as a method of raising money.<sup>521</sup>

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<sup>516</sup> Bassett testified the federal regulators commonly recommended that small thrifts with net worth problems issue preferred stock as a way to raise money for the institution. Senate Whitewater Comm. Hearing, supra note 147, at 54-55 (Jan. 25, 1996) (testimony of B. Schaffer); see also J. McDougal 4/2/97 GJ at 29 (stock idea was in response to regulators' demand to raise money); C. Handley 10/3/95 GJ at 50-52.

<sup>517</sup> Senate Whitewater Comm. Hearing, supra note 147, at 240-41 (Jan. 25, 1996) (testimony of C. Handley).

<sup>518</sup> Letter from Mitchell, Williams, Selig, Jackson & Tucker Law Offices to Sarah Hawkins, Senior Vice-President, Madison Guaranty, enclosing a Preliminary Offering Circular (Dec. 3, 1985) (Doc. Nos. 155-00001504 through 1506). More than one month later, Mitchell Williams opened another matter on Madison Guaranty's account, entitled "Broker-Dealer." (Doc. Nos. 155-00001507 through 1509). The broker-dealer file was also empty. These were the ninth and tenth matters opened by Mitchell Williams for Madison Guaranty.

<sup>519</sup> John Selig, a partner at Mitchell Williams who handled most of Madison Guaranty's regulatory work, said he did not remember doing any work or opening a file for Madison Guaranty on the preferred stock matter and speculated "[i]t may be that [Madison Guaranty] asked us initially about it and then decided not to use us." Selig 7/18/96 GJ at 19-20.

<sup>520</sup> Business Plan with FHLBB (Feb. 27, 1985) (Doc. Nos. 99-00031549 through 31567).

<sup>521</sup> See id.



On April 3, 1985, Madison Guaranty executives met with FHLBB officials.<sup>522</sup> Madison Guaranty asked for the meeting so its management could get acquainted with the FHLBB's regulatory personnel and "discuss the business plan previously submitted by Madison."<sup>523</sup> Madison Guaranty officials told the FHLBB that they planned to raise money by issuing preferred stock, and that they already had a buyer.<sup>524</sup>

That same day, Madison Guaranty employee Davis Fitzhugh called the ASD to obtain the forms required to issue preferred stock.<sup>525</sup> Fitzhugh's request was referred to ASD supervisor Charles Handley.<sup>526</sup> Handley researched whether Arkansas law permitted a state-chartered thrift to issue preferred stock, and called Fitzhugh back to tell him that Arkansas law did not permit a

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<sup>522</sup> John Latham, Madison Guaranty's CEO; Greg Young, Madison Guaranty's CFO; and Sarah Worsham-Hawkins, formerly an examiner with the FHLBB and then a Sr. Vice-President of Madison Guaranty, attended the meeting for Madison Guaranty. Memo from John Mitchell, Supervisory Analyst, Federal Home Loan Bank of Dallas to File. Three analysts and a supervisory agent from the FHLBB also attended the meeting. Memo from John Mitchell, Supervisory Analyst, Federal Home Loan Bank of Dallas, to File (Apr. 3, 1985) (Doc. No. 99-00005342). This meeting may have happened on April 2, 1985. An apparent sign-in sheet for the meeting is dated "4-2-85." (Doc. No. 99-00031589).

<sup>523</sup> Memo from John Mitchell, Supervisory Analyst, Federal Home Loan Bank of Dallas, to File about Madison Guaranty S&LA ("Madison"), Little Rock, Arkansas, FHLBB No. 7601 (Apr. 3, 1985) (Doc. No. 99-00005342).

<sup>524</sup> Id.

<sup>525</sup> See Memo from Charles [Handley], Supervisor, Arkansas Securities Department, to Beverly [Bassett], Arkansas Securities Department Commissioner (Apr. 3, 1985) (Doc. Nos. 105-00009527 through 9529). Fitzhugh was a lawyer with a Masters Degree in Business Administration. Fitzhugh 2/9/95 Int. at 1-2.

<sup>526</sup> See Memo from Charles [Handley], Supervisor, Arkansas Securities Department, to Beverly [Bassett], Arkansas Securities Department Commissioner (Apr. 3, 1985) (Doc. Nos. 105-00009527 through 9529).

state-chartered thrift to issue preferred stock.<sup>527</sup> Handley said Madison Guaranty's attorneys could submit a legal opinion on the issue.<sup>528</sup>

On April 16, 1985, Fitzhugh sent a memorandum to Latham, concluding that it was permissible for a state-chartered thrift to issue a preferred class of stock.<sup>529</sup> On April 18, 1985, McDougal sent Latham a memorandum stating there was a buyer lined up, later identified by McDougal as Senator William Fulbright,<sup>530</sup> and urged Latham to promptly issue the new stock.<sup>531</sup> Five days after McDougal's memorandum, McDougal and Latham met with Mrs. Clinton, and Rose's formal representation of Madison Guaranty on the stock offering began.<sup>532</sup>

#### **4. Limited Partnership/Broker-Dealer Matter.**

The limited partnership proposal was Jim McDougal's idea and apparently not directly related to Madison Guaranty's net worth problems. McDougal's concept was to develop real estate projects and syndicate investments in the projects through limited partnerships.<sup>533</sup> The

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<sup>527</sup> See id.

<sup>528</sup> Handley sent copies of his memo and copies of the cited statutes and opinions to Beverly Bassett, Arkansas Securities Department Commissioner and Davis Fitzhugh, Real Estate Attorney and then Vice-President of Madison Guaranty and Loan (Doc. No. 105-00009528).

<sup>529</sup> Memo from Davis Fitzhugh, Vice-President Madison Guaranty, to John Latham, Madison Guaranty Executive Vice President, about Statutes on Issuance of Preferred Stock (Apr. 16, 1985) (Doc. Nos. 105-00009511 through 512).

<sup>530</sup> J. McDougal 4/2/97 GJ at 120.

<sup>531</sup> Memo from Jim McDougal to John Latham, Madison Guaranty Executive Vice President (Apr. 18, 1985) (Doc. No. 174-00033162). McDougal later said Senator Fulbright said he would have interest in buying the preferred stock. J. McDougal 4/2/97 GJ at 119-120.

<sup>532</sup> Statement written by Mrs. Clinton re: Rose Law Firm's representation of Madison Guaranty (1992) (Doc. Nos. DEK200962 through 200963).

<sup>533</sup> Fitzhugh 6/4/96 Int. at 4; Fitzhugh 10/22/96 Int. at 6; Fitzhugh 1/31/96 Senate

limited partnerships would be offered through a newly formed, Madison Guaranty-controlled broker/dealer.<sup>534</sup> Arkansas regulations required a thrift to get approval from the ASD before establishing the subsidiary. Davis Fitzhugh was hired by McDougal and Latham in March 1985 primarily to set-up the broker/dealer to sell securities and real estate limited partnerships.<sup>535</sup>

#### **5. Madison Guaranty Retained Rose in April 1985.**

On Tuesday, April 23, 1985, Rose's representation of Madison Guaranty began when Mrs. Clinton met with Jim McDougal and John Latham at Madison Guaranty. The first entry on Rose billing records for Madison Guaranty was recorded by Mrs. Clinton, who billed two hours for 1) a conference with Jim McDougal and John Latham; 2) a conference with Rick Massey; and 3) a conference with her law partner Watt Gregory.<sup>536</sup> Massey's entries for that day show that he had a conference with Mrs. Clinton; a conference with John Latham; a conference with Rose associate Les Baledge; and research on a "preferred stock offering."<sup>537</sup>

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Whitewater Comm. Depo at 101.

<sup>534</sup> Fitzhugh 6/4/96 Int. at 4; Fitzhugh 10/22/96 Int. at 6. Contemporaneous with Fitzhugh's employment at Madison Guaranty, Madison Guaranty purchased Thorpe & Company, a dormant broker/dealer. Fitzhugh 10/22/96 Int. at 6; Fitzhugh 1/15/96 Senate Whitewater Comm. Depo. at 41-42.

<sup>535</sup> Fitzhugh 1/15/96 Senate Whitewater Comm. Depo. at 29-31; Senate Whitewater Comm. Hearing, supra note 147, at 4 (Jan. 31, 1996) (testimony of D. Fitzhugh). Fitzhugh said he worked on at least two real estate projects which were to be, but were not, sold in parcels by limited partnerships. Fitzhugh 6/4/96 Int. at 1-4. One of the projects was the syndication of the Levi Strauss building, and the other project was the development and syndication of property located at 12th and Main Streets in Little Rock. Fitzhugh 6/4/96 Int. at 1-4.

<sup>536</sup> Rose Billing Records (May, 9, 1985) (Doc. No. DEK014950). The morning portion of Mrs. Clinton's personal calendar for April 23 says: "9 -- McDougal." Hillary Clinton's personal calendar (Apr. 23, 1985) (Doc. No. 319-00034730).

<sup>537</sup> Rose Billing Records (May 2, 1985) (Doc. No. DEK014947). Mrs. Clinton

On April 24, an internal Madison Guaranty memorandum from Latham to Greg Young, Madison Guaranty's comptroller, announced Madison Guaranty's retention of Rose.<sup>538</sup> Madison Guaranty sent its first retainer check to Rose on May 2, 1985, for \$2,000.<sup>539</sup> For all but two of the next fifteen months -- through July 1, 1986 -- Madison Guaranty sent Rose a monthly \$2,000 retainer check.<sup>540</sup>

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"review[ed] draft documents" and had "conferences" with Massey, Latham, and Davis Fitzhugh. Massey and Sharon Grimes, a paralegal at Rose, conducted legal research and "draft[ed] documents." Rose Billing Records (May 2, 1985) (Doc. No. DEK014947).

<sup>538</sup> Memo from John Latham, Chairman of the Board, Madison Guaranty and Loan, to Greg Young, CPA, Madison Guaranty (Apr. 24, 1985) (Doc. No. 54-00266226) ("Greg, we have retained the Rose law firm. We will be paying them a retainer of \$2,000 per month. Please go ahead and send the first \$2,000 check to the firm, in care of Hillary Clinton").

<sup>539</sup> Check No. 2340 from the account of Madison Guaranty signed by Greg Young payable to Rose for \$2,000 (May 2, 1985) (Doc. No. 54-00231271).

<sup>540</sup> The Independent Counsel discovered no evidence of a written engagement agreement between Madison Guaranty and Rose. Rose billed Madison Guaranty its usual hourly rates and used the monthly retainer as a prepayment against fees actually incurred by Rose. The "retainer" was not a monthly payment made without regard to actual work performed. McDougal stated that he had never paid a retainer to a law firm before. McDougal 8/1/96-6/9/97 Int. at 10. Latham stated that Rose was the only law firm Madison Guaranty ever had on retainer. Latham 2/14/95 Int. at 3. Internal Madison Guaranty documents refer to the monthly retainer payments to Rose as "prepaid legal fees." See, e.g., Check No. 2340 from Madison Guaranty to Rose for \$2,000 (May 2, 1985) (Doc. No. 54-00266225); Check No. 3370 from Madison Guaranty to Rose for \$2,000 (Oct. 31, 1985) (Doc. No. 54-00264667); Check No. 5153 from Madison Guaranty to Rose for \$2,000 (Nov. 29, 1985) (Doc. No. 054-00264668); Check No. 5294 from Madison Guaranty to Rose for \$2,000 (Dec. 27, 1985) (Doc. No. 054-00264669); Check No. 5494 from Madison Guaranty to Rose for \$2,000 (Jan. 31, 1986) (Doc. No. 54-00260954); Voucher No. 135 about Rose January 1, 1986 billing (Feb. 19, 1986) (Doc. No. 54-00260973); Voucher No. 4372 about Rose January 1986 billing (Feb. 19, 1986) (Doc. No. 54-00260974); Check No. 6069 from Madison Guaranty to Rose for \$2,000 (Mar. 28, 1986) (Doc. No. 54-00260956); Check No. 6612 from Madison Guaranty to Rose for \$2,000 (July 1, 1986) (Doc. No. 54-00282220).

The second and third checks to Rose dated May 17, 1985 and July 22, 1985 were for \$2,018.00 and \$3,023.20, respectively. Check No. 2431 from Madison Guaranty to Rose for

In 1985, the decision whether to require pre-payment on a retainer fee from a client was up to the responsible attorney.<sup>541</sup> Ronald Clark, Rose's Chief Operating Officer, testified, "back in those days, it was a little bit unusual for [Rose] to get a retainer. . . . [E]ven to this day [1994], it's very seldom -- except for large clients, maybe . . . ."<sup>542</sup> Webster Hubbell, Chief Operating Officer at Rose from 1985 through 1988, said retainers were unusual, and did not remember any client other than Madison Guaranty on retainer.<sup>543</sup> But Mrs. Clinton said retainer agreements were not unusual:

I can't recall their name to you right now, but it was not unusual to ask a client, a new client or a client that perhaps there had been some billing problems with in the past, to make a deposit against fees and expenses.<sup>544</sup>

As billing attorney, almost all of Madison Guaranty's retainer checks were addressed to Mrs. Clinton.<sup>545</sup>

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\$2,018 (May 17, 1985) (Doc. No. 54-00231446); Check No. 2802 from Madison Guaranty to Rose for \$43,023.20 (July 22, 1985) (Doc. No. 54-00232199). The difference represents fees incurred in excess of the \$2,000 retainer.

<sup>541</sup> Letter from Alden L. Atkins, Vinson & Elkins attorney, to Bruce A. Ericson, Pillsbury, Madison, & Sutro, Counsel to RTC, at 6 (Oct. 31, 1995) ("In 1985, Rose Law Firm did not have any policy about retainers or client advances. The decision about whether a retainer or client advance would be requested was left to the discretion of each lawyer depending on the circumstances of the particular matter"); see also Giroir 7/18/96 GJ at 11-12.

<sup>542</sup> Clark 3/30/94 GJ at 58.

<sup>543</sup> Hubbell 12/19/95 GJ at 187-88.

<sup>544</sup> H. Clinton 4/22/95 Depo. at 14.

<sup>545</sup> Check Nos. 2431, 2991, 3201, 3370, 5153, 5294, 5494, 6069, 6196, 6612, 6760, 7154 from the account of Madison Guaranty signed by Lisa McEntire payable to "Rose Law Firm, Attn: Hillary Clinton." for amounts ranging from \$2,000 to \$2,018 (May 1985 -- Oct. 1986) (Doc. Nos. 54-00231446, 54-00232674, 54-00233116, 54-00233456, 54-00234001, 54-00234265, 54-00211033; 54-00212147, 54-00212393, 54-00214419, 54-00215014, 54-

## 6. Rose Worked on the Preferred Stock Matter.

Before Madison Guaranty could issue its preferred stock, Rose had to convince the ASD that Arkansas law allowed a savings and loan to issue a preferred class of stock. In addition to Mrs. Clinton's conferences on April 23 with McDougal, Latham, Massey, and Gregory, Massey billed 2.8 hours for conferences and "research on preferred stock offering."<sup>546</sup> The next day, April 24, Massey billed 2.2 hours for "research" and "drafting documents," and Sharon Grimes, a paralegal at Rose, billed 6.5 hours for drafting corporate documents and "related research."<sup>547</sup> Mrs. Clinton billed 1.5 hours on April 24 for "telephone conferences with R. Massey, John Latham, Davis Fitzhugh," and for "review[ing] draft documents."<sup>548</sup>

On Thursday, April 25, Massey billed 2.2 hours for "drafting & revis[ing] documents" and conferences with Latham and Mrs. Clinton.<sup>549</sup> Mrs. Clinton billed one half hour for

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00216137). How Mrs. Clinton came to be billing attorney on the Madison Guaranty account is disputed, and conflicting statements on this are discussed in Chapter 3 of this Part. The billing attorney was responsible for assigning and supervising legal work in addition to reviewing and sending bills to the client. Giroir 7/18/96 GJ at 13. An April 29, 1985 Rose document called "The Daily Briefs" announced Madison Guaranty as a new client and identified Mrs. Clinton as "attorney" for the account. Rose Daily Briefs (Apr. 29, 1985) (Doc. No. 105-00008011). "The Daily Briefs" the next day announces another Madison Guaranty matter -- the broker/dealer -- and Mrs. Clinton again as the attorney. Rose Daily Briefs (Apr. 30, 1985) (Doc. No. 105-00008012).

<sup>546</sup> Rose Billing Records (May 1985) (Doc. No. DEK014950). Les Baledge, an associate at Rose, also billed 1.1 hour for a "conference" with Massey. Id.

<sup>547</sup> Id. The documents drafted appeared to be corporate minutes and resolutions to amend Madison Guaranty's certificate of incorporation to create a preferred class of stock.

<sup>548</sup> Id.

<sup>549</sup> Id.

"review[ing] subscription agreement" and a conference with Massey.<sup>550</sup> On Friday, April 26, Massey continued his research and drafting, billing 2.3 hours.<sup>551</sup> Watt Gregory billed one hour for a conference with Massey and "review of consent on draft subscription agreement."<sup>552</sup>

Research and document drafting culminated between Monday, April 29, and Tuesday, April 30, with Mrs. Clinton billing one hour for a "telephone conference" with Beverly Bassett and a "telephone conference" with Massey on the preferred stock matter.<sup>553</sup>

The day after Mrs. Clinton's conference with Bassett, Rose sent a two-page opinion letter to the ASD arguing that, contrary to Handley's opinion, Arkansas law allowed a thrift to issue a preferred class of stock.<sup>554</sup> The letter was addressed to Handley and copied to Beverly Bassett.<sup>555</sup>

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<sup>550</sup> Id.

<sup>551</sup> Id.

<sup>552</sup> Id. The billing records also showed that on Friday, April 26, Mrs. Clinton and Massey began their first work on the limited partnership/broker-dealer matter. Id.

<sup>553</sup> Id. ("telephone conference with B. Bassett, Securities Commissioner; telephone conference with R. Massey").

<sup>554</sup> Letter from Rose to Charles Han[d]ley, Supervisor, Arkansas Securities Department, cc: Hon. Beverly Bassett, Arkansas Securities Department Commissioner (Apr. 30, 1985) (Doc. Nos. RFL1 03182 through 3183) :

Madison Guaranty, a Savings and Loan chartered under the laws of the State of Arkansas, contemplates a capitalization plan whereby it would authorize and issue a class of nonvoting preferred stock which would have preference as to dividends and amounts paid in liquidation. The question has arisen as to whether an Arkansas chartered Savings and Loan Association may under Arkansas law create, authorize and issue a class of preferred stock. For the reasons stated below, we are of the opinion that a state chartered savings and loan may do so.

Because the Arkansas statutes expressly give to an Arkansas chartered savings and loan all of the powers possessed by a corporation under the Arkansas Business Corporations Act, which powers include the power to create and issue a class of preferred capital stock, and because we find no express prohibition in Act

The letter closed, "Should you require further information or assistance, please advise Hillary Rodham Clinton or Richard Massey of this firm" and was signed "Rose Law Firm."<sup>556</sup> Massey later testified that he had drafted the letter and included Mrs. Clinton's name as a contact because "she was the billing partner."<sup>557</sup> Massey also said that he did not think Mrs. Clinton told him who to send the letter to, though, "she could have."<sup>558</sup> Massey said it was the securities section's practice at Rose to sign "Rose Law Firm" to all correspondence stating a legal conclusion.<sup>559</sup> Massey also said Rose would "always copy" the Securities Commissioner on such a letter "as a matter of protocol."<sup>560</sup>

Mrs. Clinton later testified that she was not involved in drafting the letter to Bassett, and did not remember whether she saw or approved the letter before it was sent.<sup>561</sup> Mrs. Clinton has

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227 against the creation or issuance of such a class of preferred stock, we have concluded that Madison Guaranty Guaranty's proposed capitalization plan is not inconsistent with Arkansas law. Should you require further information or assistance, please advise Hillary Rodham Clinton or Richard Massey of this firm.

<sup>555</sup> Id.

<sup>556</sup> Id.

<sup>557</sup> Senate Whitewater Comm. Hearing, supra note 147, at 109 (Jan. 11, 1996) (testimony of R. Massey). Massey testified he "would have routinely included the billing partner's name on the first letter written on the first engagement for this client, and without regard to who that partner was." Id.

<sup>558</sup> Id. at 113-14.

<sup>559</sup> Massey 11/7/95 GJ at 26.

<sup>560</sup> Id. at 30-31.

<sup>561</sup> H. Clinton 4/22/95 Depo. at 23 ("I did not have anything to do with preparation of the letter. Whether I saw it before it went out or not, I cannot tell you").



said her name was used because she was the billing partner.<sup>562</sup> Asked whether she authorized Massey to use her name on ASD correspondence, Mrs. Clinton testified, "Not that I recall . . .

"<sup>563</sup>

In response to Rose's letter, Handley reiterated his contrary position in a May 6, 1985 memorandum to Bassett and Nancy Jones, the Assistant Securities Commissioner.<sup>564</sup> Jones agreed in part and disagreed in part with Handley's analysis, concluding that it might have been possible for Madison Guaranty to issue preferred stock.<sup>565</sup>

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<sup>562</sup> H. Clinton Whitewater Press Conference (Apr. 22, 1994) ("But because I was what you call the billing attorney, in other words I had to send the bill to get the payment made, my name was put at the bottom of the letter"); see also H. Clinton 1992 Draft Campaign Statement at 2 (1992) (Doc. Nos. DEK009889 through 9890) ("Massey has stated he does not know why he included my name in the letter to the Securities Commissioner, and I do not know either and do not recall ever seeing it before it was sent. . . . Massey has said his secretary may have included my name in error").

<sup>563</sup> H. Clinton 4/22/95 Depo. at 28.

<sup>564</sup> Routing Slip to Beverly [Bassett] and Nancy [Jones] from Charles [Handley] (May 6, 1985) (Doc. No. RLF1 03185); C. Handley 10/3/95 GJ at 52 ("I, as the supervisor, was the initial one to review that application, and I had some concerns about that because our act only speaks of one class of stock, permanent capital stock, which would be common stock, not preferred"). Jones was a CPA. Jones 11/1/95 GJ at 3.

<sup>565</sup> Memo from NJ [Nancy Jones] (May 6, 1985) (Doc. No. RLF1 03186):

- 1). I agree with Charles that this must be permanent capital stock payable in liquidation after savings accounts. I believe it would be.
- 2). I disagree w/ Charles that it has to be done under the wild card statute. I believe the Rose firm's analysis regarding ordinary business corporations is correct.
- 3). The problem, not addressed by the Rose firm, is the NON VOTING portion. I don't know if "capital notes" authorized under federal statute is non-voting, but the preferred stock is a similar debt/equity instrument.
- 4). They have to get through our regulation section & FSLIC too!

Bassett reviewed the materials and wrote a note to staff attorney Bill Brady at the top of Jones' memorandum to "please review and draft response to Hillary."<sup>566</sup> Brady subsequently sent a memorandum to Bassett disagreeing with Rose's analysis and suggesting that Bassett refer the matter to the Arkansas Attorney General for an opinion.<sup>567</sup> Brady later testified that he had not seen the memorandum since giving it to Bassett, which indicated to him that she disagreed with his conclusion.<sup>568</sup>

Bassett later stated that there were "conflicting impressions and opinions" among ASD staff<sup>569</sup> and that she had meetings with Handley and Jones, and ultimately all agreed with Rose's interpretation.<sup>570</sup> Bassett said she did not refer the matter to the Attorney General for an opinion because that office did not have the necessary expertise and it was the ASD's job to render such an opinion.<sup>571</sup>

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<sup>566</sup> Id.

<sup>567</sup> Brady 5/18/94 RTC Aff. at 1 ("My research revealed that the issuance of preferred stock by an Arkansas chartered savings and loan had never been approved before this request. . . . [I] did not agree with the Rose Law Firm interpretation of the Arkansas statute"); see also Senate Whitewater Comm. Hearing, supra note 147, at 84-85 (Jan. 25, 1996) (testimony of W. Brady) (advising to seek the Attorney General's opinion).

<sup>568</sup> Brady 5/18/94 RTC Aff. at 1; Senate Whitewater Comm. Hearing, supra note 147, at 85-86 (Jan. 25, 1996) (testimony of W. Brady). No such Memo was produced to the OIC or identified by any other witness.

<sup>569</sup> Senate Whitewater Comm. Hearing, supra note 147, at 94-95 (Jan. 25, 1996) (testimony of B. Schaffer).

<sup>570</sup> Bassett 4/14/94 FDIC Aff. at 2. Handley agreed that he, Bassett, and Jones met to discuss the issue and that he changed his opinion. C. Handley 10/3/95 GJ at 59. Jones does not remember meeting, but said she may have done so. Jones 5/12/94 RTC Aff. at 3-4.

<sup>571</sup> Senate Whitewater Comm. Hearing, supra note 147, at 277 (Jan. 25, 1996) (testimony of B. Schaffer).

On May 14, 1985, Bassett sent a response to Mrs. Clinton.<sup>572</sup> Bassett wrote:

Dear Hillary:

. . .

I agree with your analysis and conclusion of the question whether an Arkansas chartered savings and loan association may under Arkansas law create, authorize and issue a class of preferred stock. . . . Accordingly, as the Savings and Loan Supervisor, I concur in your opinion that Madison's proposed capitalization plan is not inconsistent with Arkansas law.<sup>573</sup>

Bassett said she addressed the letter to Mrs. Clinton because Mrs. Clinton was the partner identified in Rose's letter as a contact and because she had spoken to Mrs. Clinton about the issue.<sup>574</sup> Mrs. Clinton testified that she "assume[d]" she received the letter because "it came to me," though she would have sent it to Massey.<sup>575</sup>

On May 23, 1985, Mrs. Clinton wrote McDougal, forwarding Bassett's letter:

Dear Jim:

Enclosed is a letter for your files from Beverly Bassett, approving the proposed authorization and issuance of a class of non-voting preferred stock. We appreciate the opportunity to work for you and look forward to continuing success in resolving whatever questions arise as you continue your plan for growth.<sup>576</sup>

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<sup>572</sup> Letter from Beverly Bassett, Arkansas Securities Department Commissioner, to Hillary Clinton (May 14, 1985) (Doc. No. RLF1 03184).

<sup>573</sup> Letter from Beverly Bassett, Arkansas Securities Department Commissioner to Hillary Clinton (May 14, 1985) (Doc. No. RLF1 03184). The Independent Counsel agreed Bassett's analysis and opinion appeared to be in accord with Arkansas law.

<sup>574</sup> Bassett 11/8/95 GJ at 76-77.

<sup>575</sup> H. Clinton 4/22/95 Depo. at 24; see also H. Clinton 1992 Draft Campaign Statement at 2 (1992) (Doc. Nos. DEK009889 through 9890) ("I also do not recall receiving the letter addressed to me from the Commissioner, because if I had seen it I would have immediately sent it to Massey").

<sup>576</sup> Letter from Hillary Rodham Clinton to Jim McDougal (May 23, 1985) (Doc. No. 0000084). Copies of the letter went to Latham and Massey.

Mrs. Clinton could not remember why she, rather than Massey, forwarded Bassett's letter to McDougal.<sup>577</sup>

McDougal wrote a note to Latham at the top of Bassett's letter: "John: Be sure we keep their \$2,000 a month retainer paid. Jim."<sup>578</sup> In the first week of Rose's representation, it billed more than twenty-three hours on the preferred stock matter,<sup>579</sup> and in the next eight months -- May through December 1985 -- Rose billed only twenty-seven additional hours.<sup>580</sup> The ASD had given Madison Guaranty until the end of December 1985 to meet its net worth requirements before it could issue the stock, but Madison Guaranty never met them. By December 1985, Madison Financial had acquired the IDC property. Madison Guaranty was able to fraudulently increase its net worth through those transactions by making it appear on paper the IDC property was being re-sold for substantial profits; those fraudulent sales all being made to insiders almost wholly financed by Madison Guaranty. The fraudulent Castle Grande transactions achieved the same result the stock offering was intended to achieve -- increasing Madison Guaranty's net worth to comply with regulatory requirements.<sup>581</sup>

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<sup>577</sup> H. Clinton 2/14/96 FDIC Int. at 35-36.

<sup>578</sup> McDougal 4/2/97 GJ at 121. McDougal later acknowledged the note to Latham was in his handwriting, but he did not remember receiving the letter. J. McDougal 8/96-6/97 Int. at 13-14; Letter from Hillary Rodham Clinton to Jim McDougal (May 23, 1985) (Doc. No. RTC KC 39624).

<sup>579</sup> See Rose Billing Records (May 1985) (Doc. No. DEK014950).

<sup>580</sup> See Rose Billing Records (May through Dec. 1985) (Doc. Nos. DEK014960, 014971, 014976, 014985, 015009 through 15010).

<sup>581</sup> J. McDougal 4/2/97 GJ at 88-90.

## 7. **Rose Worked on the Limited Partnership/Broker-Dealer Matter.**

Rose attorneys first worked on the limited partnership/broker-dealer matter on April 26, 1985, when Mrs. Clinton billed two hours for a conference with Latham, Fitzhugh, and Massey.<sup>582</sup> Massey subsequently consulted with various Madison Guaranty personnel and conducted legal research culminating, on May 14, 1985, in a nine-page application to the ASD for Madison Guaranty to engage in "certain brokerage services through a second-tier service corporation."<sup>583</sup> Charles Handley again reviewed Madison Guaranty's application.<sup>584</sup> Handley's primary concern was Madison Guaranty's inability to sustain a viable, wholly-owned subsidiary because Madison Guaranty "d[id] not meet the minimum net worth requirements . . . of the [FHLBB]'s Regulations."<sup>585</sup>

Massey responded to Handley's May 22, 1985 memorandum with an amended application on June 17, 1985.<sup>586</sup> Again, Handley prepared a memorandum the next day for Bassett and Jones

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<sup>582</sup> Rose Billing Records (May 1985) (Doc. No. DEK014952). Massey's corresponding entry was 1.2 hours for a conference with Latham and Fitzhugh. Rose Billing Records (May 1985) (Doc. No. DEK014952).

<sup>583</sup> See Letter from Richard N. Massey, Rose attorney, to Charles Handley, Arkansas Securities Department Supervisor, enclosing an application to the Arkansas Savings and Loan Supervisory Board (May 14, 1985) (Doc. Nos. 105-00009456 through 9467).

<sup>584</sup> C. Handley 3/27/95 Int. at 3-4.

<sup>585</sup> Memo from Charles Handley, Arkansas Securities Department Supervisor, to Beverly Bassett, Arkansas Securities Department Commissioner and Nancy Jones, Arkansas Securities Department Assistant Commissioner, at 2 (May 22, 1985) (Doc. Nos. RLF2 03583 through 3584). Handley forwarded copies of each of his internal memoranda to Rose.

<sup>586</sup> Letter from Richard N. Massey, Rose attorney, to Beverly Bassett, Supervisor, Arkansas Securities Department Nancy Jones, Assistant Arkansas Securities Department Commissioner, and Charles Handley, Supervisor, Arkansas Securities Department (June 17, 1985) (Doc. Nos. RIC039285 through 39286).

recommending denial.<sup>587</sup> Massey responded to Handley's second memorandum with a letter on July 10, 1985,<sup>588</sup> attaching documents containing various financial information about Madison Guaranty. Massey's response closed: "Should you have any questions, please call Hillary Rodham Clinton or me . . ."<sup>589</sup>

On July 17, 1985, Handley prepared another memorandum in response to Massey's letter, and again recommended that approval of the application be conditioned on Madison Guaranty's meeting net worth requirements.<sup>590</sup> This time Latham replied by sending a three-page letter to the ASD addressing Handley's financial concerns, attaching related financial information prepared by Madison Guaranty's accountants, Frost & Company.<sup>591</sup> On July 25, 1985, Massey also replied to

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<sup>587</sup> Memo from Charles F. Handley, Arkansas Securities Department Supervisor, to Beverly Bassett, Arkansas Securities Department Commissioner, and Nancy Jones, Arkansas Securities Department Assistant Commissioner (June 18, 1985) (Doc. Nos. 174-000096750 through 96751).

<sup>588</sup> Letter with enclosures from Richard N. Massey, Rose attorney, to Beverly Bassett, Arkansas Securities Department Commissioner, Nancy Jones, Arkansas Securities Department Assistant Commissioner, and Charles Handley, Arkansas Securities Department Supervisor (July 10, 1985) (Doc. Nos. 105-00009326 through 9354).

<sup>589</sup> Letter with enclosures from Richard N. Massey, Rose attorney, to Beverly Bassett, Arkansas Securities Department Commissioner, Nancy Jones, Arkansas Securities Department Assistant Commissioner, and Charles Handley, Arkansas Securities Department Supervisor at 2 (July 10, 1985) (Doc. No. 105-00009327).

<sup>590</sup> Memo from Charles F. Handley, Supervisor, Arkansas Securities Department, to Beverly Bassett, Arkansas Securities Department Commissioner, and Nancy Jones, Arkansas Securities Department Assistant Commissioner (July 17, 1985) (Doc. Nos. 5000213 through 214).

<sup>591</sup> Letter with enclosures from John Latham, President, Madison Guaranty, to Beverly Bassett, Arkansas Securities Department Commissioner, Nancy Jones, Assistant Commission, Arkansas Securities Department, and Charles Handley, Supervisor, Arkansas Securities Department, (July 24, 1985) (Doc. Nos. 105-00009224 through 9245).

Handley's memorandum, relying on Madison Guaranty's accounting firm's (Frost & Company's) financial information to support Madison Guaranty's contention that its financial condition was sound.<sup>592</sup> Handley responded to Latham and Massey on July 27, 1985:

I am still of the opinion that the approval of this application be conditioned on the Association meeting the net worth requirements of the FHLBB or at a minimum the Association filing a detailed and reasonable plan which reflects that these net worth requirements will be met within a very short time.<sup>593</sup>

On August 27, 1985, Latham, Massey, Handley, and Bassett met to discuss the application<sup>594</sup> and determined that "Madison's application to engage in brokerage activities would be approved on condition that Madison submit timetables of proposed activities which would serve to bring Madison in compliance with the minimum net worth requirements . . . by December 31, 1985."<sup>595</sup> On September 9, 1985, Massey sent a letter to the ASD memorializing the meeting and proposing that Madison Guaranty offer \$3,000,000 of preferred stock as well as anticipated profit from a new limited partnership. He claimed this would produce sufficient

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<sup>592</sup> Letter from Richard N. Massey, Rose attorney, to Beverly Bassett, Arkansas Securities Department Commissioner, Nancy Jones, Assistant Arkansas Securities Department Commissioner, and Charles Handley, Supervisor, Arkansas Securities Department (July 25, 1985) (Doc. Nos. 105-00009246 through 9247).

<sup>593</sup> Memo from Charles F. Handley, Supervisor, Arkansas Securities Department, to Beverly Bassett, Arkansas Securities Department Commissioner, and Nancy Jones, Assistant Arkansas Securities Department Commissioner (July 27, 1985) (Doc. Nos. 105-00023391- 93).

<sup>594</sup> See Letter from Rick Massey, Rose attorney, to Beverly Bassett, Commissioner, Arkansas Securities Department (Sept. 9, 1985) (Doc. Nos. RLF2 03492-93); Rose Billing Records (Oct. 25, 1985) (Doc. No. DEK014999).

<sup>595</sup> Letter from Rick Massey, Rose attorney, to Beverly Bassett, Arkansas Securities Department Commissioner (Sept. 9, 1985) (Doc. Nos. RLF2 03492-93).

revenue to bring Madison Guaranty in compliance with the net worth requirements.<sup>596</sup>

The ASD approved Madison Guaranty's application to engage in brokerage activities conditioned on Madison Guaranty's meeting necessary requirements by December 31, 1985.<sup>597</sup> On December 9, 1985, Handley asked Massey for the status of Madison Guaranty's progress<sup>598</sup> and on December 19, Massey sent Latham a proposed response to Handley's letter.<sup>599</sup> Massey proposed delaying the preferred stock offering, but offered additional funding through a subordinated debt offering.<sup>600</sup> On December 23, Latham went to see Handley and told him that a debenture application would be filed in mid-January, putting Madison Guaranty in compliance with net worth requirements.<sup>601</sup> Handley told Latham not to engage in brokerage activities until debentures were issued and Madison Guaranty came into compliance.<sup>602</sup> Madison Guaranty never did meet the minimum net worth requirements, and hence never created the broker-

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<sup>596</sup> Id.

<sup>597</sup> Letter from Beverly Bassett, Arkansas Securities Department Commissioner, to Richard Massey, Rose attorney (Oct. 17, 1985) (Doc. No. RLF1 03178).

<sup>598</sup> Letter from Beverly Bassett, Arkansas Securities Department Commissioner, written by Charles Handley, Supervisor, Arkansas Securities Department, to Richard Massey, Rose attorney (Dec. 9, 1985) (Doc. No. 105-00009474).

<sup>599</sup> Letter from Richard N. Massey, Rose attorney, to John Latham, President, Madison Guaranty (Dec. 19, 1985) (Doc. Nos. 105-00009471 through 9473).

<sup>600</sup> Id.

<sup>601</sup> Handley 12/19/95 Senate Whitewater Comm. Depo. at 113-115; Handley 3/27/95 Int. at 6.

<sup>602</sup> See Handwritten Memo from Charles [Handley], Supervisor, Arkansas Security Department, to Beverly [Bassett], Arkansas Securities Department Commissioner and file (Dec. 23, 1985) (Doc. Nos. 5000246 through 5000249).



dealer.<sup>603</sup>

**C. Castle Grande Transactions (Fall 1985 through Spring 1986).**

The second connection between the McDougals, Madison Guaranty, the Clintons, and CMS was a real estate development originally purchased from the Industrial Development Corporation ("IDC"), later known as the 145th Street Property or Castle Grande. Using financing from Madison Guaranty, Jim McDougal purchased property in the name of Madison Financial and Seth Ward. To avoid regulatory scrutiny, Seth Ward (Webster Hubbell's father-in-law) was used as straw purchaser for some of the property. Rose did legal work on the initial purchase. Rose and Mrs. Clinton did legal work on the proposed development of the property.

**1. The Relationship of Rose Partner Webster Hubbell and Madison Financial Employee Seth Ward.**

The relationship of Seth Ward and Webster Hubbell began in 1971, when Hubbell married Suzanna Ward, Seth Ward's daughter.<sup>604</sup> Seth Ward, a successful Little Rock businessman, helped pay Hubbell's law school tuition and bought a house for them in Fayetteville (the location of the University of Arkansas).<sup>605</sup> Hubbell graduated from the University of Arkansas Law School in 1973, and joined Rose immediately on graduating.<sup>606</sup>

Seth Ward loaned or gave Hubbell money and property throughout the 1970s, 1980s, and

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<sup>603</sup> See Memo from [Beverly Bassett, Arkansas Securities Department Commissioner] to File (undated) (Doc. No. 105-00023442).

<sup>604</sup> Hubbell 12/27/95 Int. at 4; Hubbell 8/22/96 GJ at 3, 8.

<sup>605</sup> Seth "Skeeter" Ward II 1/21/98 GJ at 5-6; Letter from Webb Hubbell to Mr. and Mrs. Seth Ward (June 1, 1981) (Doc. No. 491-00000169); Hubbell 8/22/96 GJ at 3, 15-16.

1990s.<sup>607</sup> Ward also provided Webb and Suzy with ownership interests in various businesses, including a Datsun dealership and a parking meter manufacturer, POM, Inc.<sup>608</sup> Ward often gave the Hubbells expensive gifts, including property.<sup>609</sup>

Hubbell provided legal services to Seth Ward and his businesses,<sup>610</sup> as did other Rose attorneys.<sup>611</sup> One of the companies Hubbell incorporated for Seth Ward was Deta, Incorporated. Ward formed Deta to buy POM,<sup>612</sup> and once Ward incorporated Deta, he gave the Hubbells five percent of the stock.<sup>613</sup> When POM was purchased, Seth Ward's son, Seth "Skeeter" Ward II, began running the company.<sup>614</sup>

Hubbell did legal work for POM without charging, although Rose charged for any work done by its other attorneys. Hubbell was POM's corporate secretary from 1981 to 1987, and chief legal counsel from 1981 until January 1993, when Hubbell joined the Department of Justice in Washington, D.C.<sup>615</sup> Hubbell owned stock in POM from 1981 until October 1989, when he

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<sup>606</sup> Hubbell 4/20/95 RTC-OIG/OIC Int. at 1; Hubbell 12/27/95 Telephone Int. at 3.

<sup>607</sup> Seth "Skeeter" Ward II 1/21/98 GJ at 4-7; Hubbell 8/22/96 GJ at 13-14.

<sup>608</sup> Hubbell 8/22/96 GJ at 11-13.

<sup>609</sup> Seth "Skeeter" Ward II 1/21/98 GJ at 4-7.

<sup>610</sup> Hubbell 3/16/95 FDIC-OIG Int. at 5-6; Seth "Skeeter" Ward II 1/21/98 GJ at 8; see also Hubbell 8/22/96 GJ at 6, 17-18, 28-32 (discussing Hubbell's legal work for and involvement with Ward's companies).

<sup>611</sup> Hubbell 3/16/95 FDIC-OIG Int. at 5-6.

<sup>612</sup> Id. at 6.

<sup>613</sup> Hubbell 8/22/96 GJ at 11; see also id. at 11-13 (discussing POM).

<sup>614</sup> Id. at 119-20.

<sup>615</sup> Hubbell 3/16/95 FDIC-OIG Int. at 6; Seth "Skeeter" Ward II 1/21/98 GJ at 13-15; Seth "Skeeter" Ward II RTC-OIG Int. at 1-7.

transferred the stock to Skeeter Ward.<sup>616</sup> Rose typically sent POM monthly bills of \$5,000, although after May 1990 that amount increased enormously because Rose handled a large lawsuit for POM against another company.<sup>617</sup> Skeeter Ward was unhappy with what he viewed as unnecessarily high legal bills from Rose: "I never really made an issue of it because I didn't want -- you know, I was trying to keep the peace in the family," he said. "That would raise -- somebody would raise hell over that."<sup>618</sup>

Skeeter Ward said Hubbell and Little Rock accountant Mike Schaufele "handled all of th[e] corporate mumbo jumbo stuff" for POM.<sup>619</sup> This "stuff" included Hubbell's service as POM's incorporator, "resident agent," and "the agent upon whom process against POM may be served."<sup>620</sup> Hubbell also did the legal work to amend POM's corporate bylaws.<sup>621</sup>

In 1995, Hubbell described his relationship with Seth Ward as "close."<sup>622</sup> Hubbell later wrote that their relationship disintegrated when Hubbell went to prison for fraud in 1995.<sup>623</sup> Early in 1995, the Independent Counsel granted Seth Ward, by then in his 70's, informal immunity from prosecution.

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<sup>616</sup> Hubbell 4/20/95 RTC-OIG/OIC Int. at 22; Seth "Skeeter" Ward II 1/21/98 GJ at 13.

<sup>617</sup> Seth "Skeeter" Ward II 1/21/98 GJ at 15, 18-24.

<sup>618</sup> Id. at 15.

<sup>619</sup> Id. at 31.

<sup>620</sup> Id. at 34-35.

<sup>621</sup> Id. at 43-44.

<sup>622</sup> Presentence Investigation Report for Webster Hubbell at Part C, ¶ 27 (June 21, 1995).

<sup>623</sup> Webb Hubbell, Friends in High Places 326 (1997). The November 1997 publication of Hubbell's book, Friends In High Places, deepened the Ward-Hubbell division. Seth "Skeeter" Ward II GJ 1/21/98 at 27

**2. Acquisition of the IDC Property (August through October 1985).**

**a. Madison Guaranty Hired Harry Don Denton and Seth Ward.**

In April 1985, Jim McDougal hired Harry Don Denton, formerly senior lending officer at Union National Bank, to be Madison Guaranty's Chief Lending Officer in April 1985.<sup>624</sup> Denton was responsible for all Madison Guaranty loans.<sup>625</sup> Denton said Madison Guaranty was acquiring deposits (liabilities) much faster than it was lending them (assets). McDougal hired him to increase the number of Madison Guaranty commercial loans.<sup>626</sup>

Seth Ward was one of Denton's close friends and a customer at Union National. Ward "was known in the business community," Don Denton said.<sup>627</sup> "He had been successful. He was recognized as a business player and also happened to have a . . . real estate broker's license."<sup>628</sup> Denton thought Ward would be a valuable asset to Madison Guaranty because of his experience

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<sup>624</sup> Denton 8/20/96 GJ at 4; Denton 8/19/94 FDIC-OIG Aff. at 2.

<sup>625</sup> Latham 3/28/95 GJ at 15.

<sup>626</sup> Denton 8/20/96 GJ at 12. In simple terms, an increase in the number of loans made by a financial institution increases its assets, because the loans are viewed as collectible assets (whereas deposits are, conversely, obligations to repay and thus, debts). All other things being equal, an increase in assets will result in an increase in net worth.

<sup>627</sup> Denton 8/20/96 GJ at 12.

<sup>628</sup> Id. Denton later remembered that Hubbell "served as Seth Ward's legal counsel on most, if not all, of his business arrangements." Id. at 15. Denton said of perhaps 50 business deals he was involved in with Seth Ward, dating back to 1975, Hubbell had provided legal advice to Ward in all 50. Id. at 15. When Ward first began his work at Madison Guaranty, he spoke with Webb Hubbell about it, and both went to Madison Guaranty's offices to meet Jim McDougal. Hubbell 8/22/96 GJ at 64, 75-76. Hubbell later described Ward's work for Madison Guaranty: "He was supposed to locate property and put McDougal together -- I use 'McDougal' as the savings and loan -- put McDougal together with the purchaser and help develop parcels of property, similar to his Maple Creek Farm property." Id. at 75.

and contacts in the local business community. Denton put Ward in touch with Jim McDougal in mid-1985, and McDougal hired Ward almost immediately.<sup>629</sup> Madison Guaranty's service corporation, Madison Financial, employed Ward and paid him a yearly salary of \$25,000 plus commissions on land sales.<sup>630</sup> Ward did public relations work and looked for land to develop,<sup>631</sup> but kept only sporadic office hours.<sup>632</sup>

**b. Ward Began Work on the IDC Purchase.**

Soon after Ward started at Madison Financial, Jim McDougal told him he was interested in purchasing landlocked property from International Paper Company, north of the Maple Creek Farm development. McDougal wanted Ward to help obtain an easement to the property.<sup>633</sup>

Ward approached Everett Tucker, president of the Industrial Development Corporation ("IDC"), which owned adjacent property just north of the International Paper land, about selling

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<sup>629</sup> *Id.* at 11-12. See Letter from James B. McDougal, President, Madison Guaranty, to Seth Ward (May 5, 1985) (Doc. No. 396-00000482) (about Ward's "remuneration relating to [Ward's] employment by Madison Guaranty Financial Corporation" and advising Ward of Madison Guaranty's "expectations in the matter of transportation").

<sup>630</sup> Denton 8/20/96 GJ at 16; Ward 11/29/94 GJ at 7.

<sup>631</sup> Denton 8/20/96 GJ at 12-13 (A. "[I]t was my understanding that he would be doing public relations work and looking for and developing real estate." Q. Did he do that? A. Yes"); Latham 3/28/95 GJ at 31-32; Hubbell 8/22/96 GJ at 75-76.

<sup>632</sup> Denton said although Ward worked at Madison Financial, "[h]e certainly was not there regularly. He didn't come in at 8 and leave at 5. But he would be in and out. Some days, some weeks, he may not be there at all. I'd say his hours were unusual." Denton 8/20/96 GJ at 14. "I didn't want to punch a clock," Ward later testified. Ward 11/29/94 GJ at 7. "So I agreed, provided I could come and go as I pleased." *Id.*

<sup>633</sup> Ward 1/17/96 GJ at 13-14; Ward 2/12/96 Senate Whitewater Comm. Depo at 10-11; J. McDougal 8/96-6/97 Int. at 17.

Madison Financial an easement.<sup>634</sup> Tucker declined, but said he would sell the entire 1,050-acre IDC parcel for \$3.5 million.<sup>635</sup>

McDougal said a \$3.5 million deal was too large for Madison Financial.<sup>636</sup> But IDC was under pressure from its lenders to sell the property<sup>637</sup> because IDC had not been successful developing the land as an industrial park causing loans on the property to default.<sup>638</sup> IDC reduced its asking price by late July 1985 to \$1.75 million.<sup>639</sup>

Though McDougal was interested in purchasing the IDC property at this price, Madison Financial did not have sufficient funds to finance the entire \$1.75 million purchase.<sup>640</sup> More prohibitive was a state regulation limiting the investment that Madison Guaranty could make in its service corporation to six percent of its assets.<sup>641</sup> Because Madison Guaranty was already

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<sup>634</sup> Ward 1/17/96 GJ at 14.

<sup>635</sup> Id.; Ward 2/12/96 Senate Whitewater Comm. Depo at 9-11, 27; Handwritten listing of all real and personal property owned by IDC including but not limited to the IDC property (Doc. No. 396-00000482).

<sup>636</sup> Ward 1/17/96 GJ at 14; Ward 2/12/96 Senate Whitewater Comm. Depo at 12-13, 36.

<sup>637</sup> Denton 8/20/96 GJ at 16-20.

<sup>638</sup> Cook 7/19/96 Int.; Dover 7/18/96 Int; see also Denton 8/20/96 GJ at 22 ("it was generally known around town that IDC, Industrial Development Company, was heavily indebted to the three largest Little Rock banks and that the loans were non-performing").

<sup>639</sup> Memo from Charles Cook, First Communication Bank, to Gordon Parker, spokesperson, First Commercial Bank, Bob Wilson, Union National Bank, and Robert Taylor, President, Boatmen's Bank (July 30, 1985) (Doc. No. 2035-00000038).

<sup>640</sup> J. McDougal 4/2/97 GJ at 84-87. Don Denton later remembered that Madison Financial became interested in the IDC property "because it was dirt cheap. It was close to town and it had a water and sewer system already in place." Denton 8/20/96 GJ at 20.

<sup>641</sup> J. McDougal 8/96-6/97 Int. at 17; Denton 8/20/96 GJ at 10; J. McDougal 4/2/97 GJ at 87.

close to this six percent limit, Madison Guaranty could not lend Madison Financial the entire purchase price.<sup>642</sup>

**c. Negotiations between McDougal and Ward: Ward Agreed to Take Title to Part of the IDC Property.**

**i. Ward and McDougal Agreed That Ward Would "Purchase" Part of the IDC Property with No Risk to Himself.**

To circumvent the six percent limit, McDougal and Ward agreed that Ward would personally take title to all of the IDC property north of 145th Street.<sup>643</sup> Although the six percent limit restricted amounts Madison Guaranty could lend Madison Financial, that limitation did not apply to a private party such as Ward. Ward and his accountant, Mike Schaufele, met with McDougal in late August 1985 to discuss the terms.<sup>644</sup> Ward was concerned about the tax

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<sup>642</sup> J. McDougal 8/96-6/97 Int. at 17; Tr. at 96, Ward v. Madison Guaranty, No. 87-7580 (E.D. Ark.) (testimony of Latham) (Doc. Nos. 341-00004128 through 4129).

<sup>643</sup> Memo from Jim McDougal to Seth Ward (Sept. 3, 1985) (Doc. No. 396-00001130); J. McDougal 4/2/97 GJ at 87-88. Schaufele 1/30/96 GJ at 14 ("[Seth Ward] explained to me that it was his understanding that the bank could only own so much real estate and -- or one of its subsidiaries could only own so much real estate. And therefore, when they bought this property, which they were buying from the IDC, that it was more than they could acquire in their name, in the bank's name. And so therefore, Mr. Ward was buying part of it. And then as they could acquire it, based upon their regulations, which I'm not familiar with, they were going to acquire it back from Mr. Ward"); see also Denton 8/20/96 GJ at 26-27.

<sup>644</sup> Schaufele 5/27/88 Depo. at 5, Ward v. Madison Guaranty, No. 87-7580 (E.D. Ark.); Ward 8/30/88 Depo. at 128-30, Ward v. Madison Guaranty, No. 87-7580 (E.D. Ark.) (Doc. Nos. 341-00004039 through 4041); Schaufele 1/30/96 GJ at 9. As discussed later, the September 3, 1985 memo memorializing the meeting refers to "our conversation of last Friday . . ." This would establish the exact date of the meeting as Friday, August 30, 1985. This is also consistent with Schaufele's testimony the meeting was around Jim McDougal's birthday, which is August 25; see also Ward 2/12/96 Senate Whitewater Comm. Depo at 91 (indicating that Schaufele was Ward's accountant "at that time" in 1985 and 1986).

implications.<sup>645</sup> They agreed Madison Guaranty would lend Ward the entire amount of the purchase price on a nonrecourse basis.<sup>646</sup> If Ward did not repay the loan, Ward had no personal liability if selling the land did not bring enough money to pay off the loan.<sup>647</sup> Ward agreed the nonrecourse financing was a good deal: "Now, I'll be honest with you, somebody offers me a non-recourse note, I'm not going to try to make them change their mind."<sup>648</sup> When Ward was asked why Madison Guaranty had him purchase the property north of 145th Street when Madison Guaranty financed the purchase at 100 percent, Ward answered, "I do not know."<sup>649</sup> Denton said Ward wanted no risk in the deal.<sup>650</sup> Madison Guaranty accommodated Seth Ward's wish: Ward put up no money, and made no down payment, and the non-recourse loan meant that Madison Guaranty could not recover from him if Ward made no payments.<sup>651</sup>

Ward granted Madison Financial an option lasting up to 270 days to purchase the IDC

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<sup>645</sup> Hubbell 8/22/96 GJ at 90.

<sup>646</sup> Denton 8/20/96 GJ at 28-29; Hubbell 8/22/96 GJ at 79-82.

<sup>647</sup> Denton 8/20/96 GJ at 28-29 ("Madison [Guaranty] let Ward buy the note, buy the property, gave him the \$1.15 million to do it and said, we won't hold you personally liable. The only thing we'll do is we'll take the land back if you fail to pay").

<sup>648</sup> Ward 2/12/96 Senate Whitewater Comm. Depo. at 33.

<sup>649</sup> Id. at 113.

<sup>650</sup> Denton 8/20/96 GJ at 28-29, 33. Ward claimed that he "offered to" put up money for the IDC transaction, but that McDougal refused because "it was such a good deal." Ward 2/12/96 Senate Whitewater Comm. Depo. at 111; see also Ward 2/12/96 Senate Whitewater Comm. Depo at 117 (indicating that McDougal offered Ward a nonrecourse note because the IDC purchase was "such a good deal").

<sup>651</sup> Denton 8/20/96 GJ at 29. "His purchase price was \$1,150,000, and Madison [Guaranty] loaned him \$1,150,000." Denton 8/20/96 GJ at 29. Ward later said he had not planned on being without risk, but the offer was too good to pass up. Ward 2/12/96 Senate Whitewater Comm. Depo at 112.



property from him for the amount of the non-recourse loan plus all accrued interest.<sup>652</sup> This allowed Madison Financial to "purchase" portions of Ward's property as needed to sell them to third parties. The property remained in Ward's name until Madison Financial sold it to someone else.<sup>653</sup>

Madison Financial agreed to reimburse Seth Ward for any additional taxes he may have had to pay by virtue of his holding the property<sup>654</sup> and also agreed to handle all administrative duties associated with the property such as collecting rents.<sup>655</sup> In return for "warehousing" the property for Madison Financial, Ward was entitled to receive commissions on subsequent sales of the property to third parties -- even if he had nothing to do with arranging sales.<sup>656</sup> Mike Schaufele, Ward's accountant, said the transaction was unusual, because Ward had no risk.<sup>657</sup> Ward's significant compensation with no risk or responsibility led the FDIC and others to

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<sup>652</sup> Memo from Jim McDougal to Seth Ward (Sept. 3, 1985) (Doc. No. 396-00001130); Letter from Seth Ward to Jim McDougal at 1 (Sept. 24, 1985) (Doc. Nos. 99-00035000 through 35001).

<sup>653</sup> The option was also significant because it was inconsistent with Madison Financial's eventual "purchase" of a second option from Ward. As discussed below, in May 1986, Mrs. Clinton drafted another option agreement between Ward and Madison Financial that was used to deceive the bank regulators. That agreement gave Madison Financial an option to purchase certain land for \$400,000. That same land was already subject to the first option agreement discussed in text, which, as of May 1986, allowed Madison Financial to purchase the land for \$70,000.

<sup>654</sup> Denton 8/20/96 GJ at 33-34.

<sup>655</sup> Id. at 34.

<sup>656</sup> Id. at 54-55.

<sup>657</sup> Schaufele 1/30/96 GJ at 13; see also Denton 8/20/96 GJ at 28 ("Mr. Ward had no risk").

characterize Ward as a "straw man" or "nominee" purchaser.<sup>658</sup> Ward did not have to do anything to earn his "commissions" and he had none of the traditional indicia of ownership of the property such as responsibility for taxes and collecting rents.

**ii. The Incomplete September 3, 1985 Memorandum.**

Seth Ward and Jim McDougal, for Madison Financial, tried to memorialize their agreement in a September 3, 1985 memorandum from McDougal to Ward:

The following is a summary of our conversation of last Friday [August 30, 1985]:

1. You will purchase all land north of 145th Street and the utility plants for \$1,150,000.
2. Madison Guaranty will take an option for 270 days to purchase those properties for \$1,187,000 . . . . If any tax consequences should arise for you from the transaction, Madison Guaranty will pay those taxes.
3. You will have the present IDC manager collect the rent and utility payments and forward the net proceeds monthly to Greg Young here. Greg will then apply this monthly income to the accruing interest on your loan.
4. Madison Guaranty will provide you with a letter requiring that you drive a prestigious automobile while you are in charge of this project.<sup>659</sup>

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<sup>658</sup> See FDIC-OIG Supplemental Report on Rose Law Firm Conflicts of Interest, WA-94-0016 at ii-vi (Sept. 20, 1996); Report on Crimes arising from the Castle Grande transactions from William K. Black to Independent Counsel's Office at 2-4 (Sept. 4, 1998).

<sup>659</sup> Memo from Jim McDougal, President Madison Guaranty to Seth Ward (Sept. 3, 1985) (Doc. No. 341-00004360). The September 3, 1985 memorandum addressed tax concerns expressed by Ward and Schaufele in their meeting with McDougal but the memorandum failed to address the amount of financial compensation owed to Ward, so the memorandum was not a full recital of the terms of the agreement. See, e.g., Latham 8/20/96 GJ at 14-15 (discussing the September 3, 1985 memo and indicating that it summarized "[i]n general" John Latham's understanding of Ward's agreement with McDougal).

**iii. The Unexecuted September 23, 1985 Letter.**

Ward and McDougal drafted additional documents detailing other terms of their agreement. With Hubbell's help, Ward drafted a letter dated September 23, 1985, explaining the compensation due Ward:

I have agreed to take title to all of the assets and property north of 145th Street, the water and sewer improvements, and for the water and sewage treatment ponds south of 145th Street. Madison Guaranty Savings & Loan Association will agree to lend me on a non-recourse basis the purchase price secured only by a mortgage of those parcels and the sewer and waterworks.

Madison Guaranty will have an option for at least 270 days to purchase the property from me at any time for the amount of the note plus all accrued interest. It is the intention of both Madison and myself to attempt to develop the property and sell it as quickly as possible. If there is any purchase of the property or any portion thereof during the 270-day period, the purchase price must be approved by me and Madison Guaranty. The proceeds of any sale will be applied toward the promissory note, less a ten percent commission to be paid to me, if the property is sold by me. If it is sold by anyone else, then the proceeds will go to Madison Guaranty, less the commission to the other seller, and a four percent commission to me.

. . . .

[O]n all property sold either by me or by Madison Guaranty after the exercise of Madison's option, I shall receive a ten percent commission on said property, if it is sold by me, and a four percent commission if it is sold by anyone else.<sup>660</sup>

The parties never executed this letter.

The letter's terms conformed to Jim McDougal's recollection of his agreement with Seth Ward.<sup>661</sup> In addition, the drafting of the letter reflects Webb Hubbell's involvement in this

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<sup>660</sup> Letter from Seth Ward to Jim McDougal at 1 (Sept. 23, 1985).

<sup>661</sup> J. McDougal 8/96-6/97 Int. at 19.

transaction. Martha Patton, Hubbell's secretary, typed the September 23, 1985 draft letter at Hubbell's direction.<sup>662</sup> Hubbell said generally Ward would show him the letters Hubbell's secretary typed for him before they were mailed and Ward would not mail them if Hubbell disapproved of their language.<sup>663</sup> Hubbell also acknowledged that he and Ward discussed the terms of Ward's employment with Madison Financial.<sup>664</sup>

**iv. The Original September 24, 1985 Agreement.**

The September 23, 1985 letter was never executed; rather, the parties executed a second letter dated September 24, 1985,<sup>665</sup> typed by Sue Strayhorn, McDougal's secretary.<sup>666</sup> Eventually in July 1986, Ward and McDougal would execute a second agreement backdated to September

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<sup>662</sup> Patton 3/17/98 GJ at 13-14 (indicating in reference to Seth Ward's IDC/Castle Grande letter agreements and correspondence with Madison Guaranty and Madison Financial that "I can say with certainty that I typed those letters" and that "I would have gotten that [information that went into the letter] from Webb Hubbell"). Martha Patton's testimony contradicted Hubbell. She said she typed Ward's IDC/Castle Grande letters and other documents from information she received from Hubbell, not Ward, and she had no memory of ever typing Ward's notes. Additionally, she said she did not recognize Seth Ward's handwriting. Id.

<sup>663</sup> Hubbell 8/22/96 GJ at 44. Seth Ward claimed that Hubbell did not participate in the drafting of Ward's IDC/Castle Grande documents, including the September 23, 1985 draft. Ward 2/12/96 Senate Whitewater Comm. Depo. at 18-19. Both Patton and Hubbell contradicted Ward's testimony. The documentary evidence also contradicted Ward's testimony.

<sup>664</sup> Hubbell 8/22/96 GJ at 76-77. Hubbell said he would have told Seth Ward to have a written employment contract -- "to get it in writing" -- but that he did not remember providing that advice. Id. at 76.

<sup>665</sup> Letter from Seth Ward to Jim McDougal (Sept. 24, 1985) (Doc. Nos. 396-00000698 through 699).

<sup>666</sup> The letter had Strayhorn's "ss" initials at the bottom, and Seth Ward said Sue Strayhorn "wrote the agreement." Ward 2/12/96 Senate Whitewater Comm. Depo. at 19-20.

24, 1985,<sup>667</sup> which had materially different terms. That backdated agreement, and Ward's subsequent suit against Madison Guaranty based upon it, is discussed below. The original September 24, 1985 agreement from Ward to McDougal said:

Dear Jim:

This letter is to set forth our agreement concerning the property commonly referred to as all the land owned by the Industrial Development Company of Little Rock.

On or about the 13th day of September, 1985, Madison Guaranty Savings & Loan Association agreed to acquire all of Industrial Development Company of Little Rock's property except the Timex building. In the agreement, Madison has the right to assign its rights to that agreement to any entity or individual. As part of our agreement, I have agreed to take title to all of the assets and property north of 145th Street, the water and sewer improvements, and the water and sewage treatment ponds south of 145th Street. Madison Guaranty Savings & Loan Association will agree to lend me on a non-recourse basis the purchase price secured only by a mortgage of those parcels and the sewer and waterworks.

Madison Guaranty will have an option for at least 270 days to purchase the property from me at any time for the amount of the note plus all accrued interest. It is the intention of both Madison Guaranty and myself to attempt to develop all of the property acquired from I.D.C., and sell it as quickly as possible. If there is any purchase of the property or any portion thereof during the 270-day period, the sale price will be mutually approved by me and Madison Financial Corporation. The proceeds of any sale will be applied toward the promissory note, less a ten percent commission to be paid to me if the property is sold by me, or at Madison's discretion, the particular piece of property may be deeded back to Madison prior to the execution of the sales transaction. If it is sold by anyone else, then the proceeds will go to Madison Guaranty, less the commission to the other seller, and a four percent commission to me.

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<sup>667</sup> In 1986, with regulators likely to question the Ward-Castle Grande transactions, Don Denton and Seth Ward created a document intended to disguise Madison Guaranty's right under original agreements to buy all of the IDC property originally titled to Ward. The disguise would only work if they created a document backdated to appear as if it had been agreed to by Ward and Madison Guaranty on September 24, 1985, which is what they did.

It is also agreed, in addition to the salary I am receiving from Madison Guaranty, on all property acquired from I.D.C. sold either by me or by Madison Guaranty after the exercise of Madison's option, or on that portion of the property already acquired by Madison from I.D.C., I shall receive a ten percent commission on said sale if it is sold by me, and four percent commission if it is sold by anyone else.

During the term of the option period, all of the net revenues of the waterworks and sewer department shall be forwarded directly to Madison Guaranty for application toward the note.

I would appreciate your acknowledging and agreeing to the terms of this letter agreement.

Sincerely,  
/s/ Seth Ward

SW:ss

Acknowledged and accepted:

/s/ Jim McDougal  
Jim McDougal, President  
Madison Financial Corporation<sup>668</sup>

Thus, Ward and McDougal agreed that:

- Seth Ward would take title to some of the property owned by IDC;
- Madison Guaranty would lend Seth Ward the purchase price on a non-recourse basis;
- Madison Financial would have an option for at least 270 days to purchase the IDC property from Seth Ward at any time for the amount of the non-recourse loan plus all accrued interest; and
- Seth Ward would receive payment of "commissions" from Madison Financial when the IDC property was resold.

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<sup>668</sup> Letter from Seth Ward to Jim McDougal (Sept. 24, 1985) (Doc. Nos. 99-00035000-01).

McDougal later said he thought the letter was Hubbell's idea.<sup>669</sup>

**d. Rose's Work and Negotiations between Madison Financial and IDC.**

As soon as Jim McDougal indicated interest in the IDC property at the \$1.75 million price, negotiations began between Madison Financial (represented by Seth Ward) and IDC on the specific terms of the deal. Attorneys from Rose represented Madison Financial (and Seth Ward) in the purchase.

**i. Webster Hubbell Opened a New Matter at Rose.**

Substantial evidence showed that Webster Hubbell was involved in Rose's representation of Madison Guaranty in the acquisition of the IDC property from the beginning. On August 2, 1985, a New Client Master Form was circulated at Rose.<sup>670</sup> The form listed the matter as "I.D.C." and the originating attorney as Hubbell.<sup>671</sup> The August 5, 1985 Rose Law Firm Daily Brief, a

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<sup>669</sup> McDougal also said the size of the "c" in McDougal's signature on the letter led him to think he was in a manic condition when he initialed the document, and had no specific recollection of it. J. McDougal 8/1/96-6/9/97 at 19.

<sup>670</sup> Rose New Client Master Form, (Aug. 2, 1985) (Doc. No. 105-00008017). This was the fifth "matter" opened by Rose for Madison Guaranty. Matter 1 was "Preferred Stock Offerings," Matter 2 was "Broker-Dealer," Matter 3 was "Bibler Golden," and Matter 4 was titled "General." Mrs. Clinton was the billing partner on all of these matters.

<sup>671</sup> Hubbell later claimed the New Client Master Form might have been mistakenly filled out by a Rose employee who assumed Hubbell was responsible attorney because the matter involved Seth Ward. Hubbell 8/22/96 GJ at 47. Hubbell's explanation was inconsistent with the form's contents, which listed Madison Guaranty as the client, not Ward. Anyone who assumed Hubbell was the responsible attorney would have to have known this particular Madison Guaranty matter also involved Ward. Additionally, Martha Patton, then Hubbell's secretary, said handwriting on the form was hers and that she would have received information for completing the form from Hubbell. Patton 9/26/96 Int. at 2. Denton also said Hubbell represented Ward in the IDC transaction. Denton 8/20/96 GJ at 77. Jim McDougal said Webb Hubbell was Seth

daily internal firm memorandum, also listed Hubbell as responsible attorney for a new matter entitled "I.D.C."<sup>672</sup>

Seth Ward's accountant, Mike Schaufele, testified in 1988 that he spoke with Hubbell about the IDC/Castle Grande transactions when they were being done:

Q. Have you had any discussions with anyone other than Seth Ward concerning Mr. Ward's commissions?

A. At the time of the original transaction, I discussed it with Mr. Ward's attorney, Web[b] Hubbell.<sup>673</sup>

But, in 1996, Schaufele claimed Hubbell did not represent Ward in the original purchase of the IDC property and Schaufele had not discussed the transactions with him:

Q. Who generally represented Mr. Ward in his previous land deals?

A. His son-in-law, Webb Hubbell.

Q. And do you know if he -- he, Mr. Hubbell -- represented Mr. Ward in this transaction?

A. He didn't. I do know that after the meeting with Mr. McDougal [in late August 1985] we placed a call to Webb to talk about this. And Webb informed us that because the firm was representing Madison Guaranty, that he could not represent Mr. Ward and Mr. Ward needed to find other

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Ward's attorney on the IDC/Castle Grande matter. J. McDougal 4/3/97 GJ at 39-40.

<sup>672</sup> Rose Daily Briefs (Aug. 5, 1985) (Doc. No. 105-00008015). Hubbell never billed any time to any of the Madison Guaranty matters handled by Rose. Hubbell's name does appear twice on the billing records. On November 20, 1985, Mrs. Clinton billed Madison Guaranty Matter 4 ("General") 1 hour for "Conference with Seth Ward; conference with W. Hubbell." Rose Billing Records (Jan. 21, 1986) (Doc. No. DEK015014). On November 26, 1985 Clinton billed Madison Guaranty Matter 1 ("Stock Offering") 1 hour for "Conference with S. Ward; conference with T. Thrash; conference with W. Hubbell." Rose Billing Records (Jan. 21, 1986) (Doc. No. DEK015009).

<sup>673</sup> Schaufele 5/27/88 Depo. at 13, Ward v. Madison Guaranty, No. 87-7580 (E.D. Ark.).



counsel.

Q. And that conversation with Mr. Hubbell, was it about contemporaneous with the date of the meeting that you and Mr. Ward had with Mr. McDougal, the first meeting?

A. I think it was -- actually, I really do think it was that afternoon.<sup>674</sup>

Hubbell corroborated Schaufele's original, not revised, version:

Q. You note in here that he [Schaufele] has identified you as Mr. Ward's attorney.

A. Right.

Q. Were you Mr. Ward's attorney?

A. I think everybody thought I was Mr. Ward's attorney, including me, yes.

Q. At the time of the original transaction that is the cause -- or was the basis of Mr. Ward's commissions, did you give legal advice to your father-in-law?

A. I think under your definition of "legal advice," absolutely.<sup>675</sup>

Martha Patton, Hubbell's secretary at Rose in 1985 and 1986, said Hubbell represented Ward "on matters that related to Madison Guaranty Savings & Loan Association," although she

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<sup>674</sup> Schaufele 1/30/96 GJ at 16.

<sup>675</sup> Hubbell 8/22/96 GJ at 40. Hubbell's reference to "your definition of 'legal advice'" referred to the questioner's earlier statement:

But for my purposes, when I ask you, did you perform legal services, I don't mean were you his lawyer, meaning the only lawyer Seth Ward had and the only lawyer that gave advice to Seth Ward on a particular issue. I am asking you a question I'd like you to answer as to whether you performed any legal services, gave him any legal advice with regard to that matter, whether you billed or not, okay?

Id. at 29.

"could not recall any special issues related to Madison [Guaranty]."<sup>676</sup> Patton also remembered that Ward visited Hubbell frequently at Rose during the IDC/Castle Grande transactions, sometimes as often as five times a week.<sup>677</sup> Hubbell acknowledged that he represented Seth Ward in most of his transactions in 1985 and 1986, including real estate transactions.<sup>678</sup> "But I didn't consider myself as his lawyer," Hubbell later claimed.<sup>679</sup> "[B]ut I was more of his son-in-law who was a lawyer, who he used a lot for free legal advice."<sup>680</sup>

**ii. Rose Law Firm Attorneys Began Work on the IDC Matter.**

The first time Rose billed on the IDC matter was August 6, 1985, when Rose attorney Tom Thrash billed for "Review contract for sale."<sup>681</sup> In the next weeks, Thrash and Rose attorney R. Davis Thomas billed for numerous telephone conferences with Seth Ward and IDC attorney Darrell Dover, as well as tasks like "make changes in documents," "review changes in agreement," "attend IDC Board meeting," and "prepare corporate resolutions."<sup>682</sup> The parties exchanged numerous drafts of a purchase agreement, which was signed on September 13, 1985.<sup>683</sup> Both the draft (September 23, 1985) agreement between Ward and McDougal and the

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<sup>676</sup> Patton 3/17/98 GJ at 5.

<sup>677</sup> Patton 3/17/98 GJ at 8.

<sup>678</sup> Hubbell 8/22/96 GJ at 27.

<sup>679</sup> Id. at 29.

<sup>680</sup> Id.

<sup>681</sup> Rose Billing Records (Nov. 20, 1985) (Doc. No. DEK014986).

<sup>682</sup> Rose Billing Records (Nov. 20, 1985, Dec. 5, 1985 and Nov. 12, 1985) (Doc. Nos. DEK014986, DEK015004, and DEK015007).

<sup>683</sup> Draft purchase agreements by and between Madison Financial and IDC (undated) (Doc. Nos. 2035-00000071 through 77 and 2040-00000442 through 448); Signed purchase

original (September 24, 1985) agreement refer to that September 13, 1985 purchase agreement.<sup>684</sup>

One specific change to the purchase agreement requested by Rose attorneys was to the definition of "Madison Financial Corporation." IDC's original draft defined the purchasing entity as Madison Financial, including "any of its affiliates to whom Madison might elect to assign its rights hereunder."<sup>685</sup> Rose attorneys changed the language to define Madison Financial as "any entity or individual to whom Madison might elect to assign its rights hereunder."<sup>686</sup> This enabled Madison Financial to assign its rights to over half the property to Ward, which it did on September 13, 1985, the same day it signed the purchase agreement with IDC.<sup>687</sup> Don Denton, whose signature appeared on the assignment, said it "was executed some time after the closing in

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agreement by and between Madison Financial and IDC (Sept. 13, 1985) (Doc. Nos. KI-00000001 through 6); see also Denton 8/20/96 GJ at 31 (indicating the purchase agreement was signed about September 13, 1985).

<sup>684</sup> There was an error in the September 23, 1985 draft, which said the date as the "13th day of December, 1985." Letter from Seth Ward to Jim McDougal (Sept. 23, 1985). The original September 24, 1985 agreement stated the correct month. Letter from Seth Ward to Jim McDougal (Sept. 24, 1985) (Doc. Nos. 99-00035000 through 35001).

<sup>685</sup> Draft purchase agreement between Madison Financial and IDC (undated) (Doc. No. 2040-00000442).

<sup>686</sup> Signed purchase agreement by and between Madison Financial and IDC (Sept. 13, 1985) (Doc. Nos. KI-00000001 through 6).

<sup>687</sup> Assignment from John Latham, Madison Financial, to Seth Ward, Madison Guaranty employee (Sept. 13, 1985) (Doc. No. 99-00042705 and FDICHRC 0081). Madison Financial specifically assigned to Ward all land north of 145th Street including the sewer and water utilities. Ward was assigned all property lying north of 145th Street with the exception of a small 6.6-acre parcel leased by Levi Strauss and eventually purchased by Davis Fitzhugh. Assignment from John Latham, Madison Financial, to Seth Ward (Sept. 13, 1985) (Doc. Nos. 99-00042705 and FDICHRC 0081); see also Denton 8/20/96 GJ at 31 (discussing the assignment); and J. McDougal 4/2/97 GJ at 90 (discussing the Levi Strauss warehouse).

October [of 1985]."<sup>688</sup>

**iii. Sale of the IDC Property to Madison Financial and Ward Closed.**

Sale of the IDC property, "the largest purchase that Madison ever made,"<sup>689</sup> closed on October 4, 1985.<sup>690</sup> Madison Financial paid \$600,000 of the purchase price and took title to the part of the property located south of 145th Street. Ward paid \$1.15 million for the portion of the property assigned to his name, disbursed in two checks: approximately \$750,000 for the land north of 145th Street and \$400,000 for the sewer and water utilities.<sup>691</sup> Madison Guaranty loaned Ward the entire amount with a \$1.15 million nonrecourse loan.<sup>692</sup>

Although the proceeds of the loan to Ward were paid on October 4, the day of the closing,

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<sup>688</sup> Denton 8/20/96 GJ at 32.

<sup>689</sup> Id. at 35.

<sup>690</sup> Id. at 25.

<sup>691</sup> Check Nos. 160574 and 160575 from the account of Beach Abstract & Guaranty Co. signature illegible payable to First Commercial Bank, N. A. for \$400,000 and \$750,000 (Oct. 4, 1985) (Doc. Nos. 99-00042794 and 99-00042796); see also Beach Abstract invoice to Mr. Don Denton, Madison Guaranty Savings & Loan for a recording fee of \$438.08 (undated) (Doc. No. 396-00000252); see also Check Nos. 4575, 4577, and 4673 from the account of Madison Guaranty Savings & Loan Association signature illegible payable to Beach Abstract Company for \$398,106.93, \$748,844.93, and \$438.08 (Oct. 4, 1985 and Oct. 18, 1995) (Doc. Nos. 396-00000252 through 255).

<sup>692</sup> Copies of the \$1.15 million loan from Madison Guaranty to Seth Ward (Oct. 15, 1985) (Doc. Nos. 396-00000248 through 251). John Latham approved the loan. Latham 8/20/96 GJ at 19-20. Funds were disbursed to Ward on the day of the closing (October 4, 1985), but the loan documentation (including Ward's note evidencing the loan) bore the date October 15, 1985, eleven days after closing. Madison Guaranty Savings & Loan Assn. Loan No. 2962-50 for \$1,150,000 (Oct. 14, 1986) (Doc. No. 105-00046395); Loan Documentation from Madison Guaranty to Seth Ward (Oct. 15, 1985) (Doc. Nos. 396-00000248 through 251). Consistent with Ward's status as a nominee for Madison Guaranty, Ward received the proceeds of his loan before he filled out a loan application.

the loan documents were not prepared for 11 days thereafter. Don Denton had the October 15, 1985 note prepared at the direction of Jim McDougal and John Latham.<sup>693</sup> Denton said Webster Hubbell authored the nonrecourse language on Ward's \$1.15 million note on a plain 8 1/2" x 11" piece of paper.<sup>694</sup> Hubbell later stated that he did not "recognize that language at all as being anything I drafted or advised [Ward] on."<sup>695</sup>

**3. October 1985 - February 1986: The IDC Property Is Developed and Sold to Insiders.**

**a. Development of the Property -- Initial Sales to Insiders.**

After the October 4, 1985 purchase of the IDC property, Madison Financial began developing it. Jim McDougal was the primary person involved in this effort. Ward was involved

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<sup>693</sup> Denton 8/20/96 GJ at 35; see also Ward 2/12/96 Senate Whitewater Comm. Depo. at 90 (indicating that Denton "handled the notes on all of" Ward's Madison Guaranty loans).

<sup>694</sup> Denton 8/20/96 GJ at 37. In contrast, Denton had said in 1994:

In response to the issue of Webb Hubbell's involvement in Seth Ward's business dealings, I know from my friendship with Ward that Hubbell is his son-in-law. I know that because of their relationship and my observations, that Ward discusses his business dealings with Hubbell, and I recall discussing Ward's financing with Hubbell when I worked at Union National Bank. In particular, I understand that it was reported in the Washington Post that I purportedly said Hubbell drafted the language on the \$1.15 million loan from Madison to Ward used to finance the Castle Grande deal. I have no personal knowledge of Hubbell drafting any such language, although the language on the promissory note was not the standard language I used at Madison. Further, based on my familiarity with Ward's writing through the years I have dealt with him, I do not believe Seth Ward drafted the language in this note. I have no person[al] recollection of where the language came from that was used on this note and I do not know who authored that language.

Denton 8/19/94 FDIC-OIG Aff. at 3.

<sup>695</sup> Hubbell 8/22/96 GJ at 84-85.

in the development in a more limited way. This development included a series of quick sales of parcels to Madison Guaranty insiders, efforts to develop the property south of 145th Street, and the sale of the property north of 145th Street and the utilities. The property became known as the 145th Street property or "Castle Grande,"<sup>696</sup> apparently derived from the name of the company that was to provide mobile homes for a proposed residential community to be the development's centerpiece, called "Castle Grande Estates."

In October and November 1985, Madison Financial sold portions of the property to employees or other Madison Guaranty-related parties. These insider sales falsely inflated Madison Financial's profits, relieving some of Madison Guaranty's financial burden.<sup>697</sup> Typically, Madison Guaranty fully financed the subsequent sales of the Castle Grande property, and the down payments often came from proceeds of loans or commissions paid by Madison Financial. Because arbitrarily low cost allocations were used in calculating the cost of sales, these transactions generated \$1,451,000 in inflated profits for Madison Financial.<sup>698</sup>

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<sup>696</sup> Denton 8/20/96 GJ at 36. Seth Ward said Jim McDougal renamed only some of the IDC property "Castle Grande." Ward 2/12/96 Senate Whitewater Comm. Depo. at 9.

<sup>697</sup> Madison Guaranty was criticized in a 1984 Supervisory Agreement for inadequate capitalization. Federal regulations required Madison Guaranty to maintain a certain net worth to protect the safety of its deposits. See 12 CFR 563.13 (1981). Cf. Latham 8/20/96 GJ at 6-7 (discussing the 1984 Supervisory Agreement).

<sup>698</sup> When the FHLBB exam began in March 1986, the federal examiners quickly discovered the profits were improper. Interim Report of James Clark at 2 (Apr. 2, 1986) (Doc. No. 99-00038847):

recognition of this income does not appear to be valid. The portion of project costs allocated to these sales is very low and does not appear to reflect the true cost of real estate sold. As a result of the low cost, high profits have been recognized.

**i. Jim Guy Tucker.**

On October 25, 1985, Jim Guy Tucker, a long-time friend, lawyer, and business partner of Jim McDougal, purchased a thirty-four acre parcel of undeveloped land, located at the extreme west side of Castle Grande, from Madison Financial for \$125,000. But Madison Guaranty lent Tucker \$260,000<sup>699</sup> in two checks: one sent to Tucker for \$135,000, and one to Madison Financial for \$125,000. Madison Guaranty's internal documents reflect that the \$135,000 of loan proceeds over the purchase price was to be used for property improvements, but there was no loan application to support this.<sup>700</sup> Madison Financial claimed a paper profit on the sale of \$93,620.00.<sup>701</sup> Tucker eventually repaid this loan to the RTC in 1992 through his attorney, John

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See also id. at 3 (Doc. No. 99-00038895):

Greg Young stated that James McDougal told him to use a [cost] basis of \$1,000 per acre for the land purchases by Madison Financial. Greg Young stated that McDougal did not have any documented support for this amount, but that it was calculated in McDougal's head.

Id. at 11 (Doc. No. 99-00038874):

Sales of the large parcels in Castle Grande have resulted in the recognition of \$1,451,000 of fictitious income by Madison Guaranty and Madison Financial, thus inflating net worth by this amount. This income was recognized despite the fact that almost all sales were to affiliated persons and were fully financed by Madison Guaranty.

<sup>699</sup> This was purchase money mortgage loan no. 3004. See J. McDougal 4/2/97 GJ at 89-90 (indicating that Tucker bought the 34 acre parcel "[r]ight by the freeway exit there, this lower half" and that Madison Guaranty loaned Tucker the money to buy the property).

<sup>700</sup> Tucker used the \$135,000 excess proceeds of the loan to repay a loan for Irene Garner, of which he was a guarantor. Patkus 7/19/95 GJ at 9-11.

<sup>701</sup> Federal Home Loan Bank Board Report of Examination ("as of" date Mar. 4, 1986) (Doc. No. 99-00038823).

Haley, and a corporation called Ikansa Realty.<sup>702</sup>

**ii. Davis Fitzhugh.**

On October 25, 1985, Davis Fitzhugh purchased (the Levi Strauss warehouse) from Madison Financial for \$525,000.<sup>703</sup> Fitzhugh was a salesman for Madison Financial, earning a ten percent commission, so Madison Financial paid Fitzhugh \$50,000 in commissions for selling to himself. Fitzhugh made his "down payment" by signing over his commission check.<sup>704</sup> Madison Financial claimed \$389,000.00 in paper profit on the sale.<sup>705</sup> In 1990, John Latham pleaded guilty to falsifying Madison Guaranty's records for this loan.<sup>706</sup>

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<sup>702</sup> This loan was the subject of RTC Crim. Ref. No. 190, dated September 24, 1993, and was listed as one of the overt acts in Count 1 of the indictment returned in the 1996 trial and conviction of Jim McDougal, Susan McDougal, and Jim Guy Tucker. Jim McDougal and Tucker were convicted on the conspiracy count focusing on this loan. This loan was also referenced in Counts 20 and 21 on which Tucker was acquitted. Verdict at 25-26, United States v. McDougal, Tucker, McDougal, No. LR-CR-95-173 (E.D. Ark May 28, 1996).

<sup>703</sup> This transaction was one of the subjects of the 1989 indictment of Jim McDougal, from which he was acquitted after a jury trial in 1990. See Indictment at 1-3, United States v. McDougal, et. al., No. LR-CR-89-161 (E.D. Ark. Nov. 20, 1989); see also J. McDougal 4/2/97 GJ at 90 (indicating the Levi Strauss warehouse "was sold for \$550,000, I believe").

<sup>704</sup> Federal Home Loan Bank Board Report of Examination (Mar. 4, 1986) (Doc. No. 99-00038824).

<sup>705</sup> The cost basis used was only \$61,000.00. Greg Young said James McDougal told him to use a basis of \$1,000.00 per acre for the land purchases by Madison Financial. Greg Young said McDougal did not have documented support for this amount, but that it was calculated in McDougal's head. Federal Home Loan Bank Board Report of Examination (Mar. 4, 1986) (Doc. No. 99-00038824). The title documentation for this sale became significant: the legal description for this property was mistakenly used in the first version of the May 1, 1986 option agreement drafted by Mrs. Clinton.

<sup>706</sup> Latham 3/28/95 GJ at 48-50. That criminal case was United States v. Latham, No. CR-LR-89-29 (E.D. Ark.). Latham pleaded guilty to one count of violating 18 U.S.C. §1006.



**iii. Larry Kuca.**

On November 20, 1985, Larry Kuca, a business partner of Jim McDougal and the general manager of Campobello Properties Ventures, purchased an undeveloped parcel from Madison Financial for \$120,000. Madison Guaranty loaned Kuca \$108,000 in the form of a check sent to Madison Financial.<sup>707</sup> Kuca provided a \$12,000 down payment from a \$15,000 bonus received from Campobello Properties Ventures. Madison Financial claimed a paper profit of \$99,000 on the sale.<sup>708</sup>

**b. Madison Financial and Ward Developed Property South of 145th Street, and Hillary Rodham Clinton and Rose Provided Legal Work.**

Jim McDougal generated many ideas to develop Castle Grande, including opening a brewery and expanding the customer base of the sewer and water utilities. This led to more legal work for Hillary Rodham Clinton and Rose.

**i. An Overview of Hillary Rodham Clinton's Billings for November 1985 through January 1986.**

Hillary Rodham Clinton billed Madison Guaranty for work on the "IDC" matter (matter 5) for Madison Guaranty between November 14, 1985, and June 10, 1986.<sup>709</sup> The greatest number of billing entries for Mrs. Clinton occurred between November 14, 1985, and January 7,

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<sup>707</sup> Cashier's Check No. 3468 from the account of Madison Guaranty payable to Madison Financial Corp. for \$108,000.00 noted "Loan 3134-50 Larry Kuca" (Dec. 4, 1985) (Doc. No. 99-00042906).

<sup>708</sup> Federal Home Loan Bank Board Report of Examination (Mar. 4, 1986) (Doc. Nos. 99-00038824 through 38825).

<sup>709</sup> Rose Billing Records (Jan. 1986 through June 1986) (Doc. Nos. DEK015016 through 15019, DEK015021 through 15022, DEK015029 through 15032, and DEK015038).

1986,<sup>710</sup> when Mrs. Clinton billed for twelve conferences with Seth Ward,<sup>711</sup> and two conferences in November 1985 with Webb Hubbell.<sup>712</sup> Billing entries for these conferences did not describe the subjects discussed.

In April 1995, before Mrs. Clinton's attorneys produced the Rose/Madison Guaranty billing records, Mrs. Clinton testified that when Madison Guaranty hired Rose, she was to be the billing partner, but have no substantive role in Rose's work for Madison Guaranty.<sup>713</sup> Besides matters with the Arkansas Securities Department, Mrs. Clinton testified that she did not remember doing work on any other matters.<sup>714</sup>

A Rose fee allocation recap prepared by Ronald Clark of the Rose Law Firm in 1993 showed that Mrs. Clinton received a \$2,731.25 fee allocation for "Madison Guaranty/Stock Offering and IDC" in January 1986 (by several times the largest fee allocation she received on Madison Guaranty matters).<sup>715</sup> Mrs. Clinton testified that she did not remember what the IDC matter was or what work she may have done.<sup>716</sup> After billing records were produced in January

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<sup>710</sup> Id.

<sup>711</sup> Rose Billing Records (Nov. 1985 through Jan. 1986) (Doc. Nos. DEK014991, DEK015012, DEK015014, and DEK015016 through 15019).

<sup>712</sup> Rose Billing Records (Jan. 1986) (Doc. Nos. DEK015014 and DEK015008 through 15009).

<sup>713</sup> H. Clinton 4/22/95 Depo. at 15.

<sup>714</sup> Id. at 30-31.

<sup>715</sup> Recap of fees from Madison Guaranty Savings & Loan Final Recap at 2 (for period 1983 through Sept. 1987) (Doc. No. 105-00083353 through 354). H. Clinton 4/22/95 Depo. at 41. When discovered, the billing records listed that in fact the entire \$2,731.25 was for the IDC matter. Rose Law Firm Billing Records (Jan. 21, 1986) (Doc. No. DEK015017).

<sup>716</sup> H. Clinton 4/22/95 Depo. at 41-43.

1996, Mrs. Clinton testified that she still did not remember the specifics of conferences shown in the billing records, but the billing records led her to believe they were part of legal research Rose performed for Madison Guaranty on the brewery and the sewer and water utilities.<sup>717</sup>

Seth Ward testified that he did not remember any discussions with Mrs. Clinton.<sup>718</sup> Webb Hubbell testified in 1996 that he remembered talking to Rick Massey, Mrs. Clinton, and Ward about the work being done.<sup>719</sup>

In addition to her work reflected on Rose's billing memoranda, Mrs. Clinton charged Madison Guaranty for an additional 14.5 hours of undocumented legal work on the IDC matter, performed prior to January 30, 1986. On January 30, 1986, Rose (through Mrs. Clinton as billing partner) sent Madison Guaranty five bills for legal services, one for each open matter.<sup>720</sup> On the draft bill for the IDC matter, the computerized billing memorandum said Mrs. Clinton had performed \$912.50 worth of legal work on IDC.<sup>721</sup> Mrs. Clinton made a handwritten change to the billing memorandum to increase her own billings to \$2,731.25.<sup>722</sup> She did not indicate on the billing memorandum what additional work justified this increase. No supporting information for this work was ever entered into the Rose billing computer. Significantly, Mrs. Clinton's

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<sup>717</sup> H. Clinton 4/25/98 Depo. at 74.

<sup>718</sup> Ward 1/17/96 GJ at 62.

<sup>719</sup> Hubbell 8/22/96 GJ at 21.

<sup>720</sup> Rose Billing Records (Jan. 1986) (Doc. Nos. DEK015008, 015011, 015013 and 015016).

<sup>721</sup> Rose Billing Records (Jan. 1986) (Doc. No. DEK015017).

<sup>722</sup> Id.

timesheets for the 1985 to 1986 time period were never found or produced.<sup>723</sup>

**ii. The Brewery Proposal and the "Wet/Dry Issue."**

On November 14, 1985, Mrs. Clinton billed Madison Guaranty a half hour for a "Conference with Seth Ward regarding purchase from Brick Lile."<sup>724</sup> On November 20, 1985, Jim McDougal sent Ward a memorandum about the Castle Grande property sales and a proposal, involving Bill Lyon, for a brewery on the property.<sup>725</sup> Ward spoke with Hubbell about the brewery, and Ward told Hubbell that "McDougal had a potential purchaser for part of the property that was going to put a brewery in, a beer brewery, that was also going to have kind of an open-air, where you sit and drink beer at the brewery."<sup>726</sup>

The November 20, 1985 memorandum from McDougal to Seth Ward said:

Subject to approval by the ABC [the Alcoholic Beverage Commission], Bill will place his brewery in the shell building, along with a tasting room. I have spoken with the Governor on this matter and expect that it will be approved. We must be very careful to not mention that there will be a "tavern" in the location, as word is

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<sup>723</sup> The only Rose Firm timesheets that the Independent Counsel obtained for Mrs. Clinton were her 1987-1989 timesheets produced on January 23, 1996 by Webster Hubbell. As discussed in detail in Part D of this Report, in 1992, during the Presidential campaign Mrs. Clinton's secretary, Millie Alston, requested Mrs. Clinton's timesheets for the period 1985-86 from Rose storage. Those timesheets have never been located by this or any other investigation.

<sup>724</sup> This entry was actually billed to the "General" matter number, but the reference to the "purchase from Brick Lile" clearly refers to the IDC matter. Lile was involved in the IDC sale to MFC and Ward. Rose Billing Records (Jan. 1986) (Doc. Nos. DEK015014 and 015016).

<sup>725</sup> Memo from Jim McDougal to Seth Ward (Nov. 20, 1985) (Doc. No. 105-00050190).

<sup>726</sup> Hubbell 8/22/96 GJ at 59. McDougal said the brewery was his idea. J. McDougal 8/96-6/97 Int. at 15. Bill Lyon denied the brewery was his idea. Lyon already operated a brewery in Little Rock. He said McDougal pressed him to move his operation to the Castle Grande site. Lyon said he humored McDougal because he had several outstanding loans from Madison Guaranty, but he never seriously considered moving his brewery operation. Lyon 12/14/95 Senate Whitewater Comm. Depo. at 38; Lyon 1/23/96 Senate Whitewater Comm. Depo. at 62.

already out to that effect and it is causing us problems in the area. Bill's operation must be sold to both the state regulators and to the public as a tourist attraction.<sup>727</sup>

Also on November 20, 1985, Mrs. Clinton billed the IDC matter one hour for

"Conference with Seth Ward; conference with W. Hubbell."<sup>728</sup> Mrs. Clinton later testified about her November 1985 entries in the billing records:

Q. . . [L]et me direct your attention to page DEK015014 in the billing records.

There is, it appears that that is the first, well, this is under Matter: General. And there is an entry HRC 11/14/85, conference with Seth Ward regarding purchase from Brick Lile. Do you know who Brick Lile was?

A. I do. I do know who Brick Lile was.

Q. Is he a lawyer or a businessman?

A. I thought he was a businessman. He's deceased now, I believe.

Q. And then the next, on the 20th, conference with S. Ward; conference with W. Hubbell. Then there is a, if you look at page DEK015009, which is five pages before that, there is an entry on 11/26/85, conference with S. Ward; conference with T. Thrash; conference with W. Hubbell. Did you talk with Mr. Hubbell about this property that had been bought by Madison Financial and by Seth Ward?

A. I may very well have, if that's what the billing records reflect. I know that there were a number of conversations with many people about the uses that the property would be put to. So, that's all I can tell you, based on the billing records.

Q. Did you talk with Mr. Ward about how it came about that he was an owner of some of the property down there?

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<sup>727</sup> Memo from Jim McDougal to Seth Ward (Nov. 20, 1985) (Doc. No. 105-00050190).

<sup>728</sup> Rose Billing Records (Jan. 1986) (Doc. No. DEK015014).

A. No, I did not.

Q. Did you know that Mr. Ward was an owner of part of that property?

A. I did not know that.

Q. What did you know about Mr. Ward? Why were you billing Madison Guaranty Savings & Loan for a conference with Seth Ward?

A. Because I believed that Mr. Ward worked for Madison Guaranty, that he was an employee or a contract agent, and that part of his duties for Madison was to find land that Madison could purchase, and then find uses for land that Madison could purchase, or had purchased.

So, my understanding during this period and my review of the documents is that Mr. Ward was very interested in trying to figure out how Madison Guaranty could make use of this property that they had just purchased, known as IDC. And that's what I worked on with the wet/dry issue and some of the other matters that I discussed with Mr. Ward and others during this two or three-month period.<sup>729</sup>

After the November 20, 1985 memorandum from McDougal to Ward there arose an issue about whether the proposed brewery site was located in a "dry" township (one that prohibited sales of alcoholic beverages). McDougal later stated that he had called Mrs. Clinton to have research done, and -- if the site was located in a "dry" township -- on how to make it a "wet" township.<sup>730</sup> McDougal remembered calling Mrs. Clinton to handle this because: 1) he did not know Webb Hubbell personally; and 2) he wanted Mrs. Clinton to work on it because it involved a state agency and he thought she would have more influence with the state agency.<sup>731</sup>

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<sup>729</sup> H. Clinton 4/25/98 Depo. at 65-67.

<sup>730</sup> J. McDougal 8/96-6/97 Int. at 15.

<sup>731</sup> J. McDougal 8/96-6/97 Int. at 15. Jim Guy Tucker later said he had frequently thought that Mrs. Clinton's position at Rose gave it an unfair advantage when dealing with

McDougal continued to meet with Ward, Jim Guy Tucker, and others to discuss development of the property. On November 21, 1985, for example, McDougal met with Ward, Tucker, Bill Lyon, and an engineer named James Castin, to discuss joint efforts to develop the Castle Grande property. As confirmed in November 25, 1985 letters from Castin to Tucker and McDougal, the parties discussed various residential and commercial development ideas and the possibility of Castin doing a Master Development Plan for the property.<sup>732</sup>

On November 26, 1985, the day after the Castin letters were sent, Mrs. Clinton billed IDC for one hour for "Conference with S. Ward; conference T. Thrash; conference with Webb Hubbell."<sup>733</sup>

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agencies whose members were appointed by Governor Clinton. See Tucker 3/18/98 GJ at 72-81. In describing an action involving the Arkansas Public Services Commission, in which the other party was represented by Rose, Tucker said, "But this was another instance of at least my client and I feeling that this was a totally improper role for the Rose Law Firm to have. Again, you have a state commission which, in this case, is paying state funds to the law firm in which the wife of the governor is located, and the governor has appointed the members of the commission involved and we were directly adversarial." Id. at 73-74. Tucker also contended that other lawyers in Little Rock were angry about the situation. Id. at 74.

<sup>732</sup> Letter from John A. Castin, engineer, Manes, Castin, Massey, McGetrick, to Jim McDougal (Nov. 25, 1985) (Doc. Nos. 99-00042721 through 42725); Letter from John A. Castin, engineer, Manes, Castin, Massey, McGetrick, to Jim Guy Tucker, attorney (Nov. 25, 1985) (Doc. Nos. 199-00206234 through 206235).

<sup>733</sup> Rose Billing Records (Jan. 1986) (Doc. No. DEK015009). Thrash did not remember this conference. Thrash 3/20/96 GJ at 40. Mrs. Clinton's calendar for November 27, 1985 said, "10 Seth Ward" along with some illegible notes that include the name "Hubbell." Mrs. Clinton's calendar (Nov. 27, 1985) (Doc. No. DEK212935). There is no corresponding entry in the billing records for this calendar entry.

### iii. Mrs. Clinton's December 1985 Activities.

December 1985 was Mrs. Clinton's most active month on the IDC matter, with ten separate billing entries on ten different days.<sup>734</sup> On December 6, 1985, Mrs. Clinton billed .3 hours for "Telephone conference with S. Ward; D. Dover."<sup>735</sup> On December 10, Mrs. Clinton billed .5 hours for "Telephone conference with S. Ward; telephone conference with D. Dover."<sup>736</sup> On December 11, 1985, Mrs. Clinton billed another 0.5 hours to the IDC matter for "Telephone conference with S. Ward."<sup>737</sup>

On December 17, 1985, Bill Lyon left a message for McDougal at Madison Guaranty: "Called and wanted Davis to take a map of [illegible] property to ABC. The building Lyon is looking at is in a dry township."<sup>738</sup> Two days later, on December 19, Jack Castin left a message for McDougal at Madison Guaranty: "Needs plat of 145th St. property showing pieces that have been sold or an option has been given. Also, needs appt to see you early next week or immediate after Christmas."<sup>739</sup> That same day, Mrs. Clinton billed 0.5 hours to the IDC matter for

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<sup>734</sup> Rose Billing Records (Jan. 1986) (Doc. Nos. DEK015012, DEK015014, and DEK015017).

<sup>735</sup> Rose Billing Records (Jan. 1986) (Doc. No. DEK015017). Dover was IDC's attorney, and he later remembered receiving a phone call from Mrs. Clinton about "liquor laws." Dover 7/18/96 Int. at 2.

<sup>736</sup> Rose Billing Records (Jan. 1986) (Doc. No. DEK015017).

<sup>737</sup> Id.

<sup>738</sup> Madison Guaranty Phone Logs (Dec. 17, 1985) (Doc. No. 56-00114362). It was proposed the brewery would be located in a "shell" building already on the property. J. McDougal 4/2/97 GJ at 125. "ABC" was the Alcohol Beverage Commission, which was the state agency regulating such issues.

<sup>739</sup> Madison Guaranty Phone Logs (Dec. 19, 1985) (Doc. No. 56-00114366).



"Telephone conference with S. Ward."<sup>740</sup> The next day, December 20, 1985, Mrs. Clinton billed one hour to IDC for "telephone conference with S. Ward; search for map."<sup>741</sup> Mrs. Clinton then billed IDC one hour on December 23, for "Telephone conference with to and from S. Ward's office."<sup>742</sup> Mrs. Clinton's frequent conferences with Ward continued, billing one hour for "Telephone conference with Seth Ward" on Christmas Eve December 24,<sup>743</sup> and 0.5 hours for "Conference [in person] with S. Ward telephone conference with election commission on December 26."<sup>744</sup>

In 1998 Mrs. Clinton discussed her work for Madison Guaranty during this period:

Q. Now, tell us, based on the backup billing memoranda there, what you -- did you -- did you do some of that work?

A. Yes, I did.

Q. And what were some of the things that you did as represented by your entries there?

A. Telephone conferences and conferences primarily.

Q. And are they primarily with Seth Ward?

A. They are primarily with Seth Ward.

Q. And based on well, what did they relate to?

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<sup>740</sup> Rose Billing Records (Jan. 1986) (Doc. No. DEK015017).

<sup>741</sup> Id.

<sup>742</sup> Id.

<sup>743</sup> Id.

<sup>744</sup> Id. This was billed to Matter 2 -- Limited Partnership, but the description of services indicated that it was related to IDC. Id.

- A. Well, again, based on not my memory because I don't have a memory, but based on my review of the billing records and the work that was going on in the firm at that time, they concerned Mr. Ward's questions on behalf of Madison about uses that could be worked on for the IDC property.

The two that we spent the most time on were an idea of a brewery with a tasting room, and that engendered a great deal of research and discussion. And then an issue related to whether or not the sewer and water system that was on the IDC property either could be expanded or could sell water off of the property. And that also engendered a good bit of research and work.<sup>745</sup>

**iv. Rose Began Legal Research.**

Jim McDougal spoke with Mrs. Clinton about legal research for a brewery at the Castle Grande property.<sup>746</sup> Rose performed legal research on the brewery-related issues. On December 30, 1985, Rose attorney Rick Donovan billed the IDC file for researching "county court local option election records."<sup>747</sup> Over the next week, Donovan billed Madison Guaranty:

December 31, 1985: "Conference with ABC [Alcoholic Beverage Commission] regarding wet-dry precincts; townships south of the river; researched local option law;"

January 2, 1986: "Completed research on 'wet-dry' issue; drafted memo";

January 3, 1986: "Went back to county clerk to check for order of court regarding township wet-dry deletion; revised memo."<sup>748</sup>

The memorandum discussed in Donovan's billing entries is a separate memorandum he wrote addressed to Mrs. Clinton dated January 3, 1986 "Re: Madison Guaranty Savings & Loan-

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<sup>745</sup> H. Clinton 4/25/98 Depo. at 74.

<sup>746</sup> J. McDougal 4/2/97 GJ at 126.

<sup>747</sup> Rose Billing Records (Jan. 1986) (Doc. No. DEK015017).

<sup>748</sup> Rose Billing Records (Jan. 1986) (Doc. No. DEK015017).

'Wet'-'Dry' Issue." It concluded the proposed brewery location was in a township that probably retained its dry status after being annexed by a wet township. Donovan concluded that Madison Guaranty could build the brewery on the proposed site only if:

- (1) it convinced the state Alcoholic Beverage Commission that the proposed site was not located in the old township; or
- (2) it convinced the Alcoholic Beverage Commission, and eventually the courts, that a dry township loses its dry status when such a dry township becomes annexed by a wet township.<sup>749</sup>

On April 22, 1995, Mrs. Clinton testified that she had no specific recollection of working on the wet/dry issue:

Q. And there is actually a memo from Rick Donovan to you. Do you recall anything what that was about?

A. I don't recall specifically, but there was some property that Madison Guaranty either owned or was trying to develop that was partially in a township that was dry and they were curious about how to make it wet, or something like that. That's all I remember right now.

.....

Q. If you understand where I'm coming from, there is an allegation that they are putting you on retainer and then and/or the Rose Law Firm on retainer to take care of money problems. And the question I have is, that's why I'm saying, what work did you do or was there any system whereby if you're the one that brought the business in, you get an allocation even though you weren't actually doing work?

A. Well, I did work. I just can't remember ten years from the work exactly what the work was.<sup>750</sup>

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<sup>749</sup> Memo from Rick Donovan, Rose attorney, to Hillary Rodham Clinton (Jan. 3, 1986) (Doc. Nos. 105-0003691 through 3696).

<sup>750</sup> H. Clinton 4/22/95 Depo. at 42-43. As discussed elsewhere in this Report, in 1992 Mrs. Clinton reviewed the Rose billing records for Madison Guaranty legal work.

In 1998, Mrs. Clinton testified that she and Ward talked about liquor issues and a possible brewery or tasting room.<sup>751</sup>

Mrs. Clinton discussed Donovan's memorandum with Seth Ward and Ken Shemin, another Rose partner.<sup>752</sup> In a handwritten note to Donovan, Mrs. Clinton said she had "visited with Seth Ward and gave him a copy of your memo."<sup>753</sup> In the note, Mrs. Clinton also said she discussed the memorandum with Ken Shemin and that she wanted Donovan to meet with Shemin "about a strategy to approach the ABC to argue the 'dissolved township' theory."<sup>754</sup> Donovan met with Shemin and Mrs. Clinton, then resumed his research, resulting in another memorandum to Mrs. Clinton, dated January 23, 1986, on the dissolved township theory.<sup>755</sup>

On February 7, 1986, McDougal sent a memorandum to Jim Guy Tucker attaching a copy of the first Donovan memorandum to Mrs. Clinton, stating: "Here is a copy of a legal opinion

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<sup>751</sup> H. Clinton 4/25/98 Depo. at 88 ("Q. And so, Mr. Ward is talking to you, you've already said, about liquor issues having to do with a possible brewery or tasting room, have you not? A. That's right"), and at 102-03 ("I talked to Mr. Ward about the plans for the brewery. Mr. Ward's questions, as reflected in Mr. Donovan's memos, was whether this particular water and sewer company could extend services. And one of the places they were thinking of extending it, according to Mr. Donovan's memo, was Maple Creek").

<sup>752</sup> Rose Billing Records (Jan. 1986) (Doc. No. DEK015017).

<sup>753</sup> Undated handwritten note from Hillary Clinton to Rick Donovan, Rose attorney (Doc. No. 105-00003698); H. Clinton 4/25/98 Depo. at 89-90 (Mrs. Clinton's testimony about the note).

<sup>754</sup> Undated handwritten note from Hillary Clinton to Rick Donovan (Doc. No. 105-00003698); H. Clinton 4/25/98 Depo. at 89-90 (Mrs. Clinton's testimony about the note).

<sup>755</sup> Memo from Richard Donovan, Rose attorney, to Hillary Rodham Clinton (Jan. 23, 1986) (Doc. No. 105-00003675).

Seth got from his attorney."<sup>756</sup> Despite legal work and discussions between McDougal, Lyon, and Jack Castin, there is no evidence the proposal ever moved beyond the discussion stage.<sup>757</sup> Mrs. Clinton acknowledged in 1998 that Donovan did legal research for Madison Guaranty "to find out whether it is even possible under the law to do what apparently Mr. Ward and McDougal want to do, and we didn't give him the answer he wanted to hear, because we told him it was not possible."<sup>758</sup>

**v. Mrs. Clinton and Rose Worked on the Utilities Issues.**

As part of the IDC sale, Seth Ward had purchased the sewer and water utilities, which serviced the entire IDC property. The utilities were important because McDougal previously had difficulty securing utilities for another nearby Madison Guaranty development -- Maple Creek -- several miles south of the IDC property. McDougal intended to connect the utilities facilities at Castle Grande to Maple Creek and also to his proposed future development at Lorange Heights, located immediately south of Castle Grande,<sup>759</sup> between Castle Grande and Maple Creek. After the sale of the IDC utilities to Ward, McDougal explored the possibility of extending the utility service outside the former IDC property, and had Rose perform legal work on the issue.

Reinforcing the conclusion that Ward was not the true owner of the property, even though on

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<sup>756</sup> Memo from Jim McDougal, to Jim Guy Tucker, Mitchell, Williams, Selig, Jackson and Tucker attorney (Feb. 7, 1986) (Doc. No. 174-00230962).

<sup>757</sup> See J. McDougal 4/2/97 GJ at 128.

<sup>758</sup> H. Clinton 4/25/98 Depo. at 89.

<sup>759</sup> See Memorandum from Rick Donovan to Hillary Rodham Clinton (Feb. 17, 1986) (Doc. Nos. 105-00003642 through 3653) (focusing on whether services could be sold to Maple Creek).

paper Ward "owned" the utilities, Rose billed the legal work on this matter to the Madison Guaranty IDC file. In Donovan's memo to Mrs. Clinton of February 17, 1986, it is stated that Madison Guaranty purchased the stock of IDC's subsidiary, the Industrial Service Corporation, which had necessary permits regarding the utility.<sup>760</sup> In fact, Ward had purchased the stock to the company as part of his purchase of the sewer and water facilities. Mrs. Clinton later testified that she did not think she was aware the sewer and water utility was purchased by Seth Ward.<sup>761</sup>

In 1998, Mrs. Clinton testified that she did not "have any independent understanding" of the utility issue.<sup>762</sup> She also testified that she

believe[d] that when Madison bought the IDC property, there was a utility, a water and sewer system on the property. And that when Madison was looking at ways to develop the property, one of the questions they faced was whether that utility either could be expanded or the services sold to customers beyond the boundary of the Industrial Corporation land. So, they wanted some legal analysis of what their options were.<sup>763</sup>

The billing records show work on the utility issue was first done by Rose attorney R. Davis Thomas in mid-October 1985 -- two weeks after Ward's straw purchase of the utilities. On October 18, Thomas billed the IDC matter 3.5 hours for "Research on what approvals, permits, etc. are necessary to operate sewer and water facilities; multiple telephone conferences with state agencies; memo to W. Hubbell."<sup>764</sup> By 1995, Thomas could not remember anything about the

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<sup>760</sup> See Memorandum from Rick Donovan to Hillary Rodham Clinton (Feb. 17, 1986) (Doc. No. 105-00003642) ("facts" section of the memo on who purchased the utilities).

<sup>761</sup> H. Clinton 4/25/98 Depo. at 92.

<sup>762</sup> Id. at 91.

<sup>763</sup> Id. at 91-92.

<sup>764</sup> Rose Billing Records (Jan. 1986) (Doc. No. DEK015017). Neither The Independent

research or preparation of a memorandum.<sup>765</sup>

Mrs. Clinton had not yet billed to the IDC matter before October 18. Webb Hubbell was listed on the New Client Master Form as the attorney responsible. Thus, the first legal research on the matter resulted in a memorandum addressed to him, not Mrs. Clinton.<sup>766</sup>

After Thomas's October 18, 1985 work, specific billing entries on utility issues did not appear again until February 1986, shortly before the utilities were sold. On February 11, 1986, Donovan researched the need to register as a public utility and whether Madison Guaranty could sell water services outside Castle Grande to a business outside the IDC development and to another real estate development, Maple Creek.<sup>767</sup>

Donovan telephoned people at two state agencies: the Arkansas Department of Health and the Arkansas Public Service Commission ("PSC"). Donovan concluded, in his February 17,

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Counsel, nor any other investigative body, located a copy of this memo. Hubbell had no specific recollection of the memo beyond the information in the billing records. See Hubbell 8/22/96 GJ at 108.

<sup>765</sup> Thomas 12/19/95 RTC Int. at 13.

<sup>766</sup> Between October and February, there were no entries in the billing records showing work on utility issues. Mrs. Clinton participated in twelve unspecified conferences with Seth Ward between November 14, 1985 and January 7, 1986. In addition, Mrs. Clinton billed Madison Guaranty for two conferences with Hubbell on November 20 and November 26, 1985 -- one month after the memorandum from Thomas on his utility research. Mrs. Clinton also billed Madison Guaranty on the IDC matter for an additional 14.5 hours of unaccounted time.

<sup>767</sup> Rose Billing Records (Mar. 1986) (Doc. No. DEK015019); Memo from Rick Donovan to Hillary Rodham Clinton (Feb. 17, 1986) (Doc. Nos. 105-00003642 through 3653). McDougal had said the research was requested because Jim Guy Tucker was concerned about whether the utilities would be subject to regulation, especially because he was about to purchase the utility. McDougal said it would have been logical for him to call Mrs. Clinton on a matter involving state agencies, though he did not remember any specific conversations with her on any utility issues. J. McDougal 8/96-6/97 Int. at 22; J. McDougal 4/2/97 GJ at 129-30.

1986 memorandum addressed to Mrs. Clinton, that Madison Guaranty did not have to register as a public utility, but that it did need to get licenses and permits from the Arkansas State Board of Health and the Arkansas Pollution Control Commission.<sup>768</sup> He also concluded that Madison Guaranty could sell sewer and water services to customers outside the original parcel development as long as service to the original parcel area was not impaired.<sup>769</sup>

In 1998, Mrs. Clinton testified "we did some work for Madison Guaranty on legal issues relating to that [sewer and water] utility."<sup>770</sup> She said, "[t]he only information that I learned was the work that Rick Donovan did concerning the approvals and permits that were necessary."<sup>771</sup>

**c. Madison Financial Prepared to Sell the Utilities to Castle Sewer and Water.**

On Tuesday, February 18, 1986, the day after Donovan's memorandum, Jim McDougal wrote Andy Clark and Don Denton to prepare for the sale of the sewer and water utilities.<sup>772</sup> On Thursday, February 20, Madison Guaranty's Executive Committee approved the sale of the sewer and water facilities to Castle Sewer and Water Corporation -- a newly formed Arkansas corporation owned by Jim Guy Tucker and R. D. Randolph.<sup>773</sup> Tucker had Castle Sewer & Water

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<sup>768</sup> Memo from Rick Donovan, Rose attorney, to Hillary Rodham Clinton (Feb. 17, 1986) (Doc. Nos. 105-00003642 through 3653; RIC 000048 through 59).

<sup>769</sup> Id.

<sup>770</sup> H. Clinton 4/25/98 Depo. at 69.

<sup>771</sup> Id. at 70.

<sup>772</sup> Memo from Jim McDougal to Andy Clark, Rose attorney (Feb. 18, 1986) (Doc. No. 56-00125840); Memo from Jim McDougal, to Don Denton, Senior Vice-President, Madison Guaranty (Feb. 18, 1986) (Doc. No. 56-00125872).

<sup>773</sup> Articles of Incorporation of Castle Sewer and Water Corporation (Dec. 31, 1985)



incorporated with the help of his law firm in the few days after December 31, 1985.<sup>774</sup> Notes showed that Tucker continued his preparations for the purchase of the utilities throughout the month of January 1986.<sup>775</sup> Tucker completed an application for a loan from David Hale and CMS for financing on February 14, 1986.<sup>776</sup>

Madison Financial and Castle Sewer & Water signed a purchase agreement on February 20, 1986.<sup>777</sup> Castle Sewer & Water was to purchase 100 percent of the stock of the Industrial Service Corporation ("ISC") from Seth Ward.<sup>778</sup> Castle Sewer & Water did not want to register the ISC stock for the sale (from Ward to Castle Sewer & Water). To proceed without registering the stock, the parties needed approval from the ASD commissioner, Beverly Bassett. On Friday, February 21, 1986, Breck Speed, an attorney at Mitchell Williams, wrote Bassett requesting

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(Doc. Nos. 199-00206313 through 206320); Denton 8/19/94 FDIC-OIG Aff. at 4. On February 20, 1986, the Madison Guaranty Executive Committee also approved the Dean Paul \$825,000 loan. Loan Submission Worksheet (Feb. 20, 1986) (Doc. No. 174-00102631).

<sup>774</sup> Tucker 3/18/98 GJ at 137-139.

<sup>775</sup> Tucker's undated handwritten notes (Doc. Nos. 083-00001367 through 1370); Tucker's handwritten notes (Jan. 29, 1986) (Doc. Nos. 083-00001374 through 1379); Tucker's handwritten notes (Jan. 17, 1986) (Doc. Nos. 083-00001159 through 1160).

<sup>776</sup> Tucker's loan from CMS was made possible by the fraudulent loan of \$825,000 to Dean Paul and the resulting infusion of money into CMS.

<sup>777</sup> Offer and Acceptance for the purchase of Castle Sewer and Water Corp. (Feb. 14, 1986) (Doc. No. 56-00127552). Entries in John Latham's calendar also reflect possible discussions within Madison Guaranty at this time. On February 13, 1986, Latham notes "Seth" and "Don . . . complete sale from Seth" Latham's calendar (Feb. 13, 1986) (Doc. Nos. AAP-0016936 through 16937). Latham also had "Seth" on his calendar entry for February 20, 1986 the day the purchase agreement was signed. Latham's calendar (Feb. 20, 1986) (Doc. No. AAP-0016948).

<sup>778</sup> ISC was a holding company set up by IDC to operate the sewer and water facilities and hold the necessary operating permits and licenses. Ward had purchased all the stock in ISC

approval of the ISC stock sale to Castle Sewer & Water.<sup>779</sup>

**d. Madison Guaranty Received Formal Notice of the FHLBB Examination.**

In late 1985 and early 1986, Madison Guaranty officials knew -- and had for several months -- that the FHLBB would conduct an examination of Madison Guaranty<sup>780</sup> by at least mid-February 1986.<sup>781</sup> Madison received official notification from the FHLBB on February 24, 1986, that the examination would begin on Monday, March 4, 1986. The FHLBB sent various questionnaires for Madison Guaranty's management to complete, which had to be completed "as of" February 28, 1986.<sup>782</sup> The examination presented serious problems for Madison Guaranty and the Castle Grande project, due to Madison Guaranty's books and records being "poorly documented."<sup>783</sup>

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as part of the earlier IDC transaction.

<sup>779</sup> Letter from James B. Speed II, Mitchell Williams attorney, to Beverly Bassett, Arkansas Securities Department Commissioner (Feb. 21, 1986) (Doc. Nos. 143A-00002107 through 2109); see also Letter from John S. Selig, Mitchell, William, Selig and Tucker attorney to Beverly Bassett, Arkansas Securities Department Commissioner (Feb. 26, 1986 (Doc. Nos. 143A-00002103 through 2106) (amending request).

<sup>780</sup> Latham 3/28/95 GJ at 38-39.

<sup>781</sup> Memo from Sarah Hawkins, Madison Guaranty Senior Vice President, to John Latham, Madison Guaranty Executive Vice President (Feb. 13, 1986) (Doc. No. 105-00054850). The memo said Hawkins had learned of the examination "from a source close to the examiners" and had confirmed it with John Mack, the examiner-in-charge.

<sup>782</sup> Letter from James B. Jared, Supervisor, Federal Home Loan Bank of Dallas, to John Latham, President, Madison Guaranty (Feb. 24, 1986) (Doc. Nos. 99-00022828 through 22830).

<sup>783</sup> Denton 8/20/96 GJ at 42. Denton, a former federal bank examiner, later said:

Financial statements were absent, mortgages frequently were not recorded if, in fact, executed. Title searches were non-existent in many cases. Descriptions of the reason for the extension [of] credit and the support for the credit were often

**e. Friday, February 28, 1986.**

On Friday, February 28, 1986, a lot of activity occurred at Madison Guaranty on the Castle Grande development. Examiners were due at Madison Guaranty the next Monday. The parties to the Castle Grande transactions rushed to complete their business before the examiners came.<sup>784</sup> Don Denton responded to questions in the grand jury on this matter:

- Q. Were Madison Guaranty Savings & Loan loaning Seth Ward \$1.15 million on a non-recourse basis -- that is, so that he would have no risk, would that be a red flag -- would that have been a red flag to the examiners?
- A. Yes, particularly since Madison [Financial] was also purchasing part of that same property.
- Q. So would it send a signal to the examiners perhaps that there may be more here, that these two people are buying this property together or maybe one for the other, is that right?
- A. Obviously, a non-recourse note carries more risk than a note with recourse. So the non-recourse note would certainly draw more attention from a regulator, from the examiner.
- Q. Did you do prior to the examiners coming in to sort of take care of that situation? That is, put down the red flag so the examiners would not see that Mr. Ward was the holder of a non-recourse note for \$1.15 million?
- A. Yes, the note was paid off.

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not in the files. Credit applications were frequently not generated or not executed by the borrowers. . . . So the files were generally just not documented.

Denton 8/20/96 GJ at 42-43; see also id. at 44 (indicating that when Denton warned McDougal of the propriety of doing a deal at Madison Guaranty, McDougal "kind of grinned to me and said, well, Mr. Banker, you've got a lot to learn. He said, this is a savings and loan. This is not a bank. This is kind of like a candy store. You can do whatever you want to do. And the candy store term kind of stuck with me. And I think it pretty well described what McDougal's attitude about the savings and loan was").

<sup>784</sup> Denton 8/22/96 GJ at 48-50.

Q. At whose direction was it paid off?

A. McDougal.

Q. And the purpose was -- was the purpose solely to -- so that the examiners would not question what was going on?

A. I don't know if that was solely the purpose. I think it was the primary purpose. It was to get the non-recourse note off the books.

Q. Did anyone tell you at the institution prior to the examiners coming in to get ready for a flurry of activity or something to that effect?

A. I don't recall such a statement. I just don't recall having -- I know there was a flurry of activity, but I don't recall there being an announcement that one was coming. There easily could have been. I just don't recall.<sup>785</sup>

By the end of that Friday, several Madison Guaranty-related transactions closed, which later would gain the attention of examiners and criminal investigators:

- Loan from Madison Guaranty to finance sale of property north of 145th Street to Senator J. William Fulbright.
- \$1.05 million loan from Madison Guaranty to Castle Sewer and Water to finance sale of the utility.
- \$825,000 loan to Dean Paul, Ltd., to finance the purchase of property from David Hale.

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<sup>785</sup> Denton 8/22/96 GJ at 48-50. At his 1996 criminal trial, McDougal testified the arrival of the examiners did not influence the timing of the transactions. See generally Tr. at 7017-19, United States v. McDougal, et al., No. LR-CR-95-173 (E.D. Ark.) (testimony of J. McDougal).

**i. Sale of Property North of 145th Street to Senator Fulbright.**

On February 28, 1986, virtually all land north of 145th street -- except a portion called Holman Acres -- was sold to Senator J. William Fulbright.<sup>786</sup> Before the sale, the property was transferred from Ward to Madison Financial and then sold by Madison Financial to Senator Fulbright. Senator Fulbright purchased the land for \$770,000, which was then used to pay down Ward's \$1.15 million loan from Madison Guaranty.<sup>787</sup> After the Fulbright and Castle Sewer & Water sales closed, Ward's \$1.15 million loan (loan no. 2962) was marked "paid in full," with the balance of \$70,000 carried over to another Madison Guaranty loan to Ward.<sup>788</sup> That \$70,000 loan (loan no. 3359) was unsecured, had an interest rate of 12 percent per annum, and was due in a single payment scheduled for August 25, 1986.

The sale of Ward's Castle Grande property and use of the sale proceeds to pay off Ward's \$1.15 million loan implicated the terms of the original September 24, 1985 agreement between Ward and McDougal. The original September 24, 1985 agreement gave Madison Guaranty with an option to re-purchase Seth Ward's property from Ward at any time for the amount of his nonrecourse loan plus all accrued interest. Once the February 28, 1986 transactions occurred, the

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<sup>786</sup> Warranty Deed from Madison Financial to J. W. Fulbright (Feb. 28, 1996) (Doc. Nos. 56-00127325 through 127329); Denton 8/20/96 GJ at 47-48 (discussing the sale to Fulbright).

<sup>787</sup> See Denton 8/20/96 GJ at 47 (indicating that Denton "applied the proceeds" of the Castle Sewer and Water sale and the purchase by former Senator Fulbright to "Seth Ward's note, bringing the total down to something like \$70,000. The original, if you recall, was 1.15 million. And those other loan sales brought the total down to something around \$70,000"); J. McDougal 4/2/97 GJ at 89 (discussing the purchase by Senator Fulbright at a "purchase price" of \$770,000).

<sup>788</sup> Loan Documentation from Madison Guaranty to Seth Ward (Oct. 15, 1985) (Doc. Nos. 396-00000248 through 251); see also Hubbell 8/22/96 GJ at 102 (discussing the pay off of

terms of the original September 24, 1985 agreement gave Madison Guaranty an option to re-purchase Holman Acres -- Ward's remaining Castle Grande property -- for the remaining \$70,000 balance of Ward's \$1.15 million loan.

Madison Guaranty did not exercise its option to buy Holman Acres from Ward for \$70,000. Instead, Ward and Madison Guaranty later used Holman Acres as: 1) collateral for a March 31, 1986 \$400,000 loan from Madison Guaranty to Ward; 2) the subject property for a \$400,000 May 1, 1986 option agreement; and 3) collateral on a June 6, 1986 \$70,000 loan to Ward. As discussed below, in December 1986, Ward returned the Holman Acres property to Madison Guaranty instead of repaying his March 31 and June 6, 1986 loans.<sup>789</sup> Also as discussed below, the backdated September 24, 1985 agreement between Ward and Madison Guaranty exempted Holman Acres from the option to purchase contained in the original September 24 agreement. This change was necessary to disguise the fraud committed by Denton and Ward when Madison Financial agreed to pay \$400,000 for a parcel that Madison Financial already had a right to purchase for \$70,000.

**ii. The Sale of the Utility to Castle Sewer & Water.**

On Friday, February 28, 1986, the sale of utilities stock and facilities from Madison Financial to Castle Sewer and Water closed. Castle Sewer & Water paid \$1.2 million for the

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"the big note, the million dollar note" and the left over \$70,000).

<sup>789</sup> Ward did repay \$100,000 of the March 31, 1986 \$400,000 loan. Denton 8/20/96 GJ at 67; Ward 2/12/96 Senate Whitewater Comm. Depo at 39-40.

Castle Grande sewer and water system.<sup>790</sup> Madison Guaranty made two loans, one for \$950,000 and the other for \$100,000 for this purchase. As detailed below, Capital Management Services, a company owned by David Hale, loaned Castle Sewer & Water Corporation \$150,000 as a down payment for this purchase."<sup>791</sup>

Proceeds from the Castle Sewer & Water sale, along with proceeds of a sale of most of the property north of 145th Street to Senator Fulbright (discussed above), were used to pay off Ward's \$1.15 million loan from Madison Guaranty.<sup>792</sup> In addition, Arkansas Securities Commissioner Beverly Bassett issued an order approving the ISC stock sale.<sup>793</sup>

**iii. Madison Guaranty \$825,000 Loan to Dean Paul, Ltd.**

The purchase of the utility was facilitated by the fraudulent \$825,000 loan made on February 28, 1986 to Dean Paul, Ltd. On February 20, 1986, McDougal arranged for Madison Guaranty to loan Dean Paul \$825,000.<sup>794</sup> With that loan, Paul purchased three parcels of property from David Hale.<sup>795</sup> To justify a loan that large, Hale, with the assistance of Bill Watt, secured fraudulent appraisals that greatly overvalued the properties from Robert Palmer, a Little Rock

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<sup>790</sup> Denton 8/19/94 FDIC-OIG Aff. at 4.

<sup>791</sup> Id.

<sup>792</sup> Denton 8/20/96 GJ at 47-48.

<sup>793</sup> Findings of Fact, In the Matter of: Proposed Sale of Stock by Seth Ward to Castle Sewer and Water Corporation, Case No. 66-11-S (State of Ark. Securities Department) (Feb. 28, 1986) (Doc. Nos. 143A-00002110 through 2111).

<sup>794</sup> Tr. at 1960-61, United States v. McDougal, et al., No. LR-CR-95-173 (E.D. Ark.) (testimony of Paul); see also Tr. at 1109-11, United States v. McDougal, et al., No. LR-CR-95-173 (E.D. Ark.) (testimony of Denton).

<sup>795</sup> Tr. at 3099, United States v. McDougal, et al., No. LR-CR-95-173 (E.D. Ark.)

appraiser.<sup>796</sup> With the payment from Paul for the over-valued properties, the real estate transactions netted Hale approximately \$500,000 in "profits," which Hale put into CMS. This money allowed CMS to receive an additional \$1.5 million in funding from the SBA, and raised CMS's per-individual loan limit from \$150,000 to \$300,000.<sup>797</sup>

CMS then loaned funds to McDougal's designees. There were four such loans, all of which were fraudulent because the true nature of the transactions and the people benefited were purposefully concealed. The four such loans were: 1) \$149,000 to Larry E. Kuca, McDougal's business partner;<sup>798</sup> 2) \$65,000 to Stephen A. Smith, (Tucker and McDougal's business partner) d/b/a The Communications Company;<sup>799</sup> 3) \$300,000 to Susan McDougal, doing business as

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(testimony of Hale).

<sup>796</sup> Tr. at 2178-79, United States v. McDougal, et al., No. LR-CR-95-173 (E.D. Ark.) (testimony of Palmer).

<sup>797</sup> Tr. at 3959-60, United States v. McDougal, et al., No. LR-CR-95-173 (E.D. Ark.) (testimony of Hale); see also Tr. at 3293, 3714-15, 3847, United States v. McDougal, et al., No. LR-CR-95-173 (E.D. Ark.) (testimony of Hale).

<sup>798</sup> Letter from Larry E. Kuca to David Hale (undated) (Doc. No. 0000276); Tr. at 4658-59, 4661, United States v. McDougal, et al., No. LR-CR-95-173 (E.D. Ark.) (testimony of Kuca). Kuca used the proceeds of the loan to pay off an "advance" made to him by another McDougal-related entity, Campobello Properties. Tr. at 4661, United States v. McDougal, et al., No. LR-CR-95-173 (E.D. Ark.) (testimony of Kuca). The "advance" had been used by McDougal and Kuca to finance the purchase of certain real estate while evading regulatory limitations on Madison Guaranty. Tr. at 4652-54, United States v. McDougal, et al., No. LR-CR-95-173 (E.D. Ark.) (testimony of Kuca). Details relating to this loan are discussed in Vol. I, Appendix 5.

<sup>799</sup> Loan Proposal prepared by The Communication Company (Doc. No. G-00001247). The loan proposal was fraudulent. See Tr. at 4807, United States v. McDougal, et al., No. LR-CR-95-173 (E.D. Ark.) (testimony of S. Smith) (discussing guilty plea); Tr. at 4833-34, 4836, United States v. McDougal, et al., No. LR-CR-95-173 (E.D. Ark.) (testimony of S. Smith). Smith used the proceeds of the loan payoff a loan taken out at Worthen Bank. Doc. No. 144-00014630 (Handwritten note from Steve Smith); Tr. 4838, United States v. McDougal, et al., No. LR-CR-95-173 (E.D. Ark.) (testimony of S. Smith). The Worthen Bank loan had financed the



"Master Marketing," a fictitious advertising business;<sup>800</sup> and 4) \$150,000 to Castle Sewer and Water, an entity controlled by Tucker for the purchase of the Castle Grande sewer and water system.

CMS's \$150,000 loan to Castle Sewer & Water closed on February 28, 1986. When the loan was made, Tucker was listed as owning two-thirds of the Castle Sewer and Water stock, and R. D. Randolph owned the remaining one-third. CMS gave Tucker the check made out to Castle Sewer and Water for \$150,000.<sup>801</sup> Tucker endorsed the check,<sup>802</sup> and used the \$150,000 proceeds as a down payment on a \$1,200,000 purchase of the sewer and water system from Madison Financial.<sup>803</sup> Castle Sewer and Water gave a \$1,050,000 promissory note to Madison Financial to cover the remainder of the purchase;<sup>804</sup> Madison Financial assigned the note to Madison Guaranty the same day.

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purchase of real estate by a company jointly owned by McDougal, Smith and Jim Guy Tucker. Tr. at 4812, United States v. McDougal, et al., No. LR-CR-95-173 (E.D. Ark.) (testimony of S. Smith). Details relating to this loan are discussed in Vol. I, Appendix 5.

<sup>800</sup> Details relating to the loan to Mrs. McDougal and the use of the proceeds of the loan to benefit Whitewater Development are discussed in Vol. II, Part A of this Report. Part A also discusses the evidence relating to Hale's and Jim McDougal's allegation that President Clinton knew of the fraudulent Master Marketing loan and of the purposes to which it was put.

<sup>801</sup> Tr. at 3263-64, United States v. McDougal, et al., No. LR-CR-95-173 (E.D. Ark.) (testimony of Hale).

<sup>802</sup> Id. (testimony of Hale).

<sup>803</sup> Id. at 4002-03 (testimony of Hale).

<sup>804</sup> Id. at 1307 (testimony of Denton).

**iv. Mrs. Clinton's Activities.**

Mrs. Clinton's activities on February 28, 1986 remain somewhat unclear. She billed the IDC file for .8 hours, with the only description of the work written as "Seth Ward." Given her work on the utilities issue, this Office examined whether this billing related to the contemporaneous purchase of the utility from Seth Ward by Castle Sewer & Water. No documentary evidence relating to these actions were discovered. Mrs. Clinton testified that she did not recall the events of that day.

In 1998, Mrs. Clinton provided the following testimony about her February 28, 1986 activities:

Q. Now, I want to give you a couple of -- on February the 28th of '86, we know that this utility was sold to Castle Sewer and Water, which is a company which was incorporated by Mr. Tucker. The stock in ISC, which had been purchased by Ward, was transferred from Seth Ward to Castle Sewer and Water. That all occurred on February the 28th of '86.

You have an entry in your billing records on 2/28/86 for eight-tenths of an hour, and you just have the word Seth Ward. What did you do that day with Mr. Ward.

A. I have nothing to add to what the billing records say. I have no, no independent recall of anything, other than what the billing records say.  
. . . .

I thought I remembered something also going on, you know. Becky Arnold, who was our paralegal, was still doing research with Rick Donovan on 2/25, 2/28/86. So, if I were, again merely guessing, which is all I can do because I don't have any direct knowledge, I would guess that whatever she was researching at the County Planning Office, at the Historical Society with the Arkansas Historical Commission, is something she reported to me and/or to Rick Donovan and it fell to me to tell Mr. Ward the results of whatever that research was.<sup>805</sup>

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<sup>805</sup> H. Clinton 4/25/98 Depo. at 94-95.

Asked about the February 28, 1986 transactions, Mrs. Clinton said she "knew nothing about any such transactions. I did not learn anything about any such transactions until years later in the course of all these investigations."<sup>806</sup> Mrs. Clinton also said she learned "many years later" that "Mr. Tucker bought this sewer and water service."<sup>807</sup> Additionally, Mrs. Clinton testified that she did not speak with Ward about his selling his utility to Jim Guy Tucker, and that "we were not involved in the sale. There was no work we did on that sale. I didn't know about the sale."<sup>808</sup> Mrs. Clinton said she thought she did not know about the February 28, 1986 "as of" date of the FHLBB examination.<sup>809</sup>

Webb Hubbell knew about the transactions, however. He had talked to Ward about the payoff of Ward's \$1.15 million loan at about the time of the February 28, 1986 transactions.<sup>810</sup> In 1997, David Hale, for the first time, said that he remembered speaking to Mrs. Clinton on February 28, 1986, saying she called Hale's office trying to locate Jim McDougal. According to Hale, Mrs. Clinton said she needed to speak to McDougal prior to closing.<sup>811</sup>

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<sup>806</sup> Id. at 96.

<sup>807</sup> Id. at 98.

<sup>808</sup> Id. at 103.

<sup>809</sup> Id. at 104.

<sup>810</sup> Hubbell 8/22/96 GJ at 49-50. "He would -- as I said, we were over at his house, and occasionally he would call and ask me to meet him at the Little Rock Club or somewhere for drinks after work," Hubbell remembered later. "He would tell me about the sales that were going on of the IDC property, who was buying them, and how much commission he was making." Hubbell 8/22/96 GJ at 49; see also Hubbell 8/22/96 GJ at 102 (discussing the pay off of "the big note, the million dollar note" and the left over \$70,000).

<sup>811</sup> Hale 2/6/97-12/4/97 Int. at 2-3. The Independent Counsel's investigation developed

**D. March 1986 Federal Examination and Attempted Cover-Ups; The McDougals Were Removed by Federal Regulators.**

**1. Examiners Looked at Castle Grande and Other Land Deals.**

FHLBB examiners arrived at Madison Guaranty on March 4, 1986, and immediately focused on sales to insiders, including Castle Grande.<sup>812</sup> An internal FHLBB memorandum circulated before the examination began shows examiners were looking at "conflict of interest/prohibited transactions," and whether the institution had complied with the six percent direct investment limitation, net worth requirements, and the 1984 Supervisory Agreement.<sup>813</sup> Sources had already told the FHLBB there was illegal insider activity at Madison Guaranty.<sup>814</sup> After staying for several months, examiners uncovered massive fraud, leading federal regulators to require Madison Guaranty to remove the McDougals and John Latham from control.

**a. Ward Demanded His "Commissions"; Cross Loans Were Executed to Conceal them from Examiners.**

In March 1986, shortly after federal examiners arrived at Madison Guaranty, "Ward began to talk about being paid his sales commissions for his participation in the Castle Grande acquisition,"<sup>815</sup> telling Madison Guaranty President John Latham he wanted his "commissions"

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no evidence to corroborate Hale's statement in this regard.

<sup>812</sup> J. Clark 7/13/96 Int. at 1.

<sup>813</sup> Inter-Office Memo from Steve Paar, examiner, Federal Home Loan Bank Board, to Examiner-in-Charge (Feb. 24, 1986) (Doc. Nos. 99-00022808 through 22810).

<sup>814</sup> Undated notes from meeting between FHLBB and confidential source [redacted to protect identity of source] (Doc. Nos. 005619 through 5620).

<sup>815</sup> Denton 8/20/96 GJ at 52.

paid immediately.<sup>816</sup> Ward warned Denton he would "sue the bastards" if he was not paid.<sup>817</sup>

Denton later said Ward requested "[s]omething in approximately \$300,000, which I understood to be 10% sales commission."<sup>818</sup> "He wanted his commissions," Webb Hubbell agreed, "[t]hat was first and foremost on his mind."<sup>819</sup>

Under the original September 24, 1985 agreement, Madison Financial owed Ward commissions for the sales of that part of the Castle Grande property held in Ward's name.<sup>820</sup> But Madison Financial did not have enough money to pay Ward.<sup>821</sup> Madison Guaranty had money, but Madison Financial was the entity that owed Ward his "commissions."<sup>822</sup> Madison Guaranty could not lend Madison Financial the money because that would violate the six percent limitation on investment by Madison Guaranty in its service corporation.

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<sup>816</sup> Latham 6/8/88 Depo. at 9, Ward v. Madison Guaranty, No. 87-7580 (E.D. Ark) (Doc. No. 140-00019053); Ward 2/12/96 Senate Whitewater Comm. Depo at 36 ("I demanded that I get -- be paid my commission. And I was told that -- by John Latham, that Madison Financial Corporation was not in a financial position at that time to pay me").

<sup>817</sup> Denton 9/6/96 FDIC-OIG Statement at 2; see also Tr. at 234, Ward v. Madison Guaranty, No. 87-7580 (E.D. Ark.) (testimony of John Latham) (Doc. No. 341-00004145) ("Q. And, when Seth Ward was complaining about needing money from Financial for what they owed him, then you worked out a deal where Guaranty stepped in and made available some funds to him, didn't you? A. That's correct").

<sup>818</sup> Denton 8/20/96 GJ at 53.

<sup>819</sup> Hubbell 8/22/96 GJ at 50.

<sup>820</sup> That Madison Financial would pay commissions to Ward was unusual because Ward was not involved in sales of Castle Grande property. Jim McDougal had arranged both the Fulbright and the Castle Sewer and Water sales. Denton 8/20/96 GJ at 54-55.

<sup>821</sup> Id. at 54; see also Tr. at 222, Ward v. Madison Guaranty, No. 87-7580 (E.D. Ark.) (testimony of John Latham) (Doc. No. 341-00004133); Ward 2/12/96 Senate Whitewater Comm. Depo. at 36 (indicating that Latham told Ward that Madison Financial did not have the funds to pay Ward); Latham 8/20/96 GJ at 25.

Federal examiners began examining the relationship between Ward, Castle Grande, and Madison Guaranty. One of the first aspects of Castle Grande examiners questioned was the \$1.15 million loan that Madison Guaranty had given Seth Ward for his portion of the purchase price from IDC. On March 31, 1986, examiner Darlene Ford, requested the Seth Ward loan file.<sup>823</sup> She was told the file was checked out to a Madison Guaranty employee and could not be found.<sup>824</sup> The next day, April 1, 1986, lead examiner Jim Clark, began looking into the IDC transaction and the \$1.15 million non-recourse loan to Ward. Madison Guaranty did not have copies of disbursement checks, so Ford contacted Beach Abstract on April 1, 1986, and asked Dennis Nelson for copies.<sup>825</sup> Beach Abstract, which did substantial business with Madison Guaranty, resisted providing copies of the checks, telling Ford and Clark that copies could not be produced without Ward's prior consent and approval.<sup>826</sup> Clark had several conversations with Nelson in an attempt to obtain copies of checks.<sup>827</sup>

Madison Guaranty decided to advance Ward his "commissions" by having Madison

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<sup>822</sup> Denton 8/20/96 GJ at 62.

<sup>823</sup> FHLBB Examiner D. Ford's notes (Mar. 31, 1986) (Doc. No. 99-00042727).

<sup>824</sup> Id.

<sup>825</sup> FHLBB Examiner D. Ford's notes (Apr. 1, 1986) (Doc. No. 99-00042768); Clark 7/26/96 Int. at 2.

<sup>826</sup> Beginning on April 1, 1986, Ford and Clark's handwritten notes describe telephone conversations with Nelson of Beach Abstract and his refusal to provide the IDC checks without Ward's approval. FHLBB Examiner D. Ford's notes (Doc. No. 99-00042768); FHLBB Examiner FHLBB Examiner J. Clark's notes (Doc. Nos. 99-00042769 through 42771); Clark 7/26/96 Int. at 2.

<sup>827</sup> Clark 7/26/96 Int. at 2.

Guaranty "loan" him money until Madison Financial could pay him.<sup>828</sup> On March 31, 1986 (the same day Darlene Ford asked to see the Seth Ward loan file), Madison Guaranty officials created two loan notes that connected Seth Ward and Madison Financial. The intent was to get cash into Ward's hands and to document Madison Financial's obligation to Ward. The first note, dated March 31, 1986, documented a \$400,000 loan from Madison Guaranty to Ward.<sup>829</sup>

On March 31 and April 1, 1986, Madison Guaranty fulfilled the new Ward loan with two checks to Ward for \$300,000 and \$100,000.<sup>830</sup> The loan represented Ward's Castle Grande "commission."<sup>831</sup> The terms of the note said the "loan" carried a 12 percent interest rate and would become due May 30, 1986.<sup>832</sup> The note was secured by Holman Acres,<sup>833</sup> even though under the original September 24, 1985 agreement, Madison Guaranty already had the legal right to purchase that property for the unpaid balance of Seth Ward's earlier \$1.15 million loan -- which then was \$70,000.<sup>834</sup>

A second note, also dated March 31, 1986, documented a \$400,000 loan from Seth Ward

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<sup>828</sup> Denton 8/20/96 GJ at 59.

<sup>829</sup> Loan Documentation from Madison Guaranty S & L to Seth Ward (Mar. 31, 1986) (Doc. No. 56-00125991).

<sup>830</sup> Cashier's Check No. 4224 from Madison Guaranty payable to Seth Ward for \$300,000.00 on "loan #4027-50"; Cashier's Check No. 4228 from Madison Guaranty payable to Seth Ward for \$100,000.00 on "loan #4027-50" (Apr. 1, 1986) (Doc. No. 56-00125995).

<sup>831</sup> Latham 8/20/96 GJ at 25-27.

<sup>832</sup> Extension Agreement (May 30, 1986) (Doc. No. 56-00125994) (extending due date to Nov. 30, 1986).

<sup>833</sup> Loan from Madison Guaranty to Seth Ward (Mar. 31, 1986) (Doc. No. 56-00125991).

<sup>834</sup> Letter from Seth Ward to Jim McDougal (Sept. 24, 1985) (Doc. Nos. 99-00035000-01 341-00004332 through 4333).

to Madison Financial.<sup>835</sup> Madison Financial never actually received \$400,000 from Ward,<sup>836</sup> because, as John Latham later said, the whole purpose was merely to establish or "document" Madison Financial's obligation to pay Ward's commissions.<sup>837</sup> The loan was never listed as a liability or as accrued commissions on Madison Financial's books, which would have been a subject of the examiner's scrutiny. The loans are referred to as "cross loans" because Ward's \$400,000 obligation to Madison Guaranty was intended to offset exactly Madison Financial's corresponding \$400,000 obligation to Ward.<sup>838</sup> Ward testified that the purpose of the unfunded note from Madison Financial to him was to insulate him from being liable for principal and

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<sup>835</sup> Loan documentation from Seth Ward to Madison Financial (Mar. 31, 1986) (Doc. No. 56-00125991).

<sup>836</sup> Denton 8/20/96 GJ at 61.

<sup>837</sup> Latham 8/20/96 GJ at 26-27. Hillary Clinton had billed Madison Guaranty for a "telephone conference with John Latham" on March 21. In 1995, she testified that she had "no recollection of any conversation with him at all." H. Clinton 4/22/95 Depo. at 5. In addition to the March 21, 1986 conference between Mrs. Clinton and John Latham, the billing records reveal that Mrs. Clinton billed Madison Guaranty for other conferences with John Latham on April 23, 24, and 26; July 24, and September 20, 1985. Rose Billing Records (May, Aug., & Nov. 1985) (Doc. Nos. DEK014942, 014978, 014991). Latham said the note was intended to demonstrate Madison Financial's obligation to pay Ward his commissions "should something happen to the people that, you know, were cognizant of this . . . . We structured this note as evidence of that debt." Tr. at 222, Ward v. Madison Guaranty, No. 87-7580 (E.D. Ark.) (testimony of John Latham) (Doc. No. 341-00004133).

<sup>838</sup> Madison Financial Board of Directors Resolution (Apr. 4, 1986) (Doc. No. 396-00000527). The loan is reflected in John Latham's calendar for April 3, 1986: "Don -- . . . [illegible - sv corp?] loan to Seth . . . 70k + int note to Seth [illegible] 145 street property [illegible]." Latham's calendar (Apr. 3, 1986) (Doc. No. 038342); see also Denton 8/20/96 GJ at 60 (explaining the purpose of the unfunded note was to protect Seth Ward because, without the unfunded note, "if Madison did not pay Seth the money, then Seth could conceivably have to repay the other loan that Madison had made him").



interest on the \$400,000 loan he received from Madison Guaranty.<sup>839</sup>

Don Denton directed the preparation of the \$400,000 cross loans<sup>840</sup> and later said Madison Guaranty's \$400,000 loan to Ward was "a loan to pay Ward his commissions due from the sale of Castle Grande real estate. Ward had commissions of \$300,000 due. The balance of \$100,000 was to pay a \$70,000 note that . . . was the deficiency from the repayment of the original \$1,150,000."<sup>841</sup> Denton remembered "the other \$30,000 was to pay interest on those two obligations until they were paid by Madison."<sup>842</sup>

**b. On April 7, 1986, the Original Cross Notes Were Replaced; Denton's April 7, 1986 Telephone Conference with Mrs. Clinton.**

On April 7, 1986, the March 31, 1986 cross loans were replaced with new notes. The original note from Ward to Madison Guaranty for \$400,000 was replaced with another note for \$400,000.<sup>843</sup> The \$400,000 loan note from Ward to Madison Financial was replaced by two

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<sup>839</sup> Tr. at 150-51, Ward v. Madison Guaranty, No. 87-7580 (E.D. Ark.) (Doc. No. 341-00004060-62) (testimony of Seth Ward). Hubbell admitted in 1996 that he spoke contemporaneously with Ward about the cross loans. Hubbell 8/22/96 GJ at 52-55.

<sup>840</sup> Denton 8/20/96 GJ at 55-56.

<sup>841</sup> Id. at 58.

<sup>842</sup> Id. at 58-59. In his Ward v. Madison Guaranty deposition, Denton expressed some doubt about what he knew about the cross loans and when he knew it. Denton said he prepared the cross loans as ordered by Latham. He also said the information in a memorandum to Latham explaining the cross loans may have included some speculation ("I sure was giving a lot of opinions without a lot of information wasn't I? These damn memos -- would you strike that?") Denton 5/24/88 Depo. at 64, Ward v. Madison Guaranty, No. 87-7580 (E.D. Ark.); see Memo from Denton to Latham (July 14, 1986) (Doc. No. DD000000052).

<sup>843</sup> Loan from Madison Guaranty to Seth Ward (Mar. 31, 1986) (Doc. No. 56-00125991).

separate notes: one for \$300,000 and the other for \$70,943.47.<sup>844</sup> The amounts corresponded to Denton's understanding of how the \$400,000 loan from Madison Guaranty to Ward was structured. He understood that \$300,000 corresponded to Ward's commissions, and \$70,943.47 corresponded to the amount remaining outstanding from Ward's loan to purchase the IDC property plus interest up to April 7, 1986 (the amount carried over into a new note on February 28, 1986). After April 7, 1986, there were now three active promissory notes related to Ward's role as IDC/Castle Grande straw purchaser: 1) the \$400,000 note from Ward to Madison Guaranty reflecting the funds he had received; 2) the unfunded \$300,000 note from Madison Financial to Ward; and 3) the unfunded \$70,943.47 note from Madison Financial to Ward.

On April 7, 1986, Don Denton also received a telephone message from Sandra Moody, Hillary Clinton's secretary, asking Denton to call Mrs. Clinton.<sup>845</sup> Rose billing records for April 7, 1986, show a conference call between Mrs. Clinton and Denton about the IDC matter.<sup>846</sup> The computerized Rose billing memorandum reflects an entry for Mrs. Clinton on the IDC matter on April 7, 1986, for 0.2 hour for "Telephone conference with Don Denton,"<sup>847</sup> which was edited by hand to 0.5 hour.<sup>848</sup>

When FDIC Inspector General investigators questioned Denton on June 3, 1996, about

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<sup>844</sup> Ward \$300,000 "loan" to Madison Financial (Apr. 7, 1986) (Doc. No. 56-00126454); Ward \$70,943.47 "loan" to Madison Financial (Apr. 7, 1986) (Doc. No. 396-00000525).

<sup>845</sup> Telephone message slip to Don Denton (Apr. 7, 1986) (Doc. No. DD-00000241).

<sup>846</sup> Rose Billing Records (Mar. 1986) (Doc. No. DEK015030).

<sup>847</sup> Id.

<sup>848</sup> Id.

the April 7, 1986 billing entry, Denton could not remember the call:

DENTON was questioned concerning a ROSE billing entry that indicated that he spoke with CLINTON on April 7, 1986 relative to the IDC matter. DENTON said that he had no recollection of the call, and believed that the entry may have been in error. He said that there was an April 1, 1986 telephone message from CLINTON to him that he had maintained, but that he did not recall what the purpose of that call was.<sup>849</sup>

On June 11, 1996, Denton told investigators that reviewing a copy of Rose billing records had caused him to remember the April 7, 1986 conversation with Mrs. Clinton, which he said dealt with Seth Ward's cross notes. Denton "said that since the earlier [June 3, 1996] interview, he had recalled that he did have a conversation with CLINTON concerning WARD loans at MGSL."<sup>850</sup>

The memorandum of interview also said

DENTON was questioned concerning his recollection of this phone call at this time. He said that after the earlier interview, he reviewed a copy of the ROSE LAW FIRM billing records that he had obtained from the media. He said that after confirming to himself that there was a bill by CLINTON for a discussion with him concerning IDC on April 7, 1986, he gave the matter thought and also reviewed the documents that he had retained.

He said that when he reviewed the documents, he found a copy of the March 31, 1986 note from WARD to MFC that had handwriting on it, dated April 7, 1986, indicating that the note was replaced by a \$300,000 and \$70,943 note. He also reviewed two notes dated April 7, 1986 for those amounts that he had left handwritten messages on that said "Replacement notes - 5-5-86 (the \$300,000 note), and "Copies of new note -- Signed 5-5-86 (the \$70,943 note).

He said that he noted that the May 5, 1986 dates match the date of the option for WARD property at 27 and 28 Holman Acres, the property that secured loan #4027.

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<sup>849</sup> Denton 6/3/96 FDIC OIG Int. at 10 (uppercase in original).

<sup>850</sup> Denton 6/11/96 FDIC OIG Int. at 2.

DENTON said that, after reviewing these documents and giving the matter some thought, he recalled the telephone call with CLINTON. DENTON could not recall where he obtained the copies of the replacement notes or who or when they were prepared.<sup>851</sup>

Denton remembered telling Mrs. Clinton "there could be a problem with the notes as they constituted in effect a parent entity fulfilling the obligation of a subsidiary."<sup>852</sup> He said Mrs. Clinton "summarily dismissed" his concern in a way he understood meant she wanted him to manage thrift matters, and she would manage legal matters.<sup>853</sup>

In August 1996, Denton told the grand jury about his telephone call with Mrs. Clinton:

Q. Tell the ladies and gentlemen of the grand jury what happened when you called Sandra in Hillary Clinton's office back.

A. I returned the call and was immediately connected with Hillary Clinton. We exchanged a couple of hellos, how are you, the conversation was very short. I was told that she was working on a transaction involving Seth Ward and Madison Financial, and that she was [seeking] information so she could document the obligation that Madison owed Seth. In other words, the \$400,000 obligation. She understood that Seth had been loaned the 400 by Madison Guaranty Savings & Loan. And she was working on a transaction that would document Madison Financial's obligation to pay . . . Seth Ward his commissions.

Q. What type of document was she talking about?

A. She was talking about a promissory note.

Q. So what was your response to what she was saying?

A. I cautioned her that the Madison Financial obligation was not a direct set-off or direct tie to Madison Guaranty's loan. I pointed out that Madison

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<sup>851</sup> Denton 6/11/96 FDIC OIG Int. at 3-4 (uppercase in original).

<sup>852</sup> Id. at 3.

<sup>853</sup> Id.

Guaranty had loaned Seth the money, but Seth was owed money by Madison Financial Corporation. She rather summarily dismissed my concerns and indicated that she'd take care of the lawyering.

Q. What happened after that?

A. I informed her that the \$400,000 note from Madison Financial -- excuse me -- from Madison Financial to Seth had already been prepared. And she asked that we supply a copy of that note, which I did. I had an employee of Madison deliver that note.

Q. To whom?

A. To the Rose Law Firm.

Q. And then also the note that you had prepared, was it the first note on April -- pardon me -- on March 31st, or was it a note drafted on that day, April 7th?

A. I don't recall which it would have been. It was--as I recall, it was the \$400,000 note. I'll note now that the replacement notes were also dated April 7th, so I don't recall specifically which ones were delivered.

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So I think on April 7th, two notes were replaced, the 300 plus the 70, to take care of the remaining \$300,000 balance on the original note plus the \$70,000 note. And it more clearly identified them. Rather than a total note for 400, it broke it down into two notes, with those specific amounts, the 300 and the 70,000 note.

Q. Did you and Mrs. Clinton discuss that in your telephone call on April 7th?

A. I don't recall whether we did or not.

Q. Your memory is you just discussed the \$400,000 note?

A. That was the reason of her inquiry. I may or may not have informed her that the 300 plus the 70 had already been done. I just don't recall now.

Q. Had you ever dealt with Mrs. Clinton before that phone call?

A. I had not.

- Q. Were you surprised that she called?
- A. Yeah, I had never spoken with the governor's wife, so I think I was surprised from that standpoint. I did know that she was acquainted with Seth Ward through the Airport Commission. She served as attorney for the Airport Commission, and Seth Ward had been on that commission for a number of years and I believe was chairman at the time. And I knew that Hillary Clinton was a friend, as well as a business associate of Webb Hubbell, Mr. Ward's son-in-law. So I knew they worked together, but that was certainly my first conversation with Mrs. Clinton.
- Q. To your knowledge, had Mrs. Clinton represented Seth Ward before?
- A. I don't know whether she had or not.
- Q. To your knowledge, had Mrs. Clinton represented Madison before that phone call?
- A. I have since learned that she did. At the time, I do not believe that I was aware of that.
- Q. Who did you believe was Mr. Ward's attorney at that time?
- A. Webb Hubbell.
- Q. Who did you think that she represented at the time you received the phone call from her on April 7th?
- A. Seth Ward.<sup>854</sup>

In 1998, Mrs. Clinton testified that she did not know about the April 7, 1986 billing entry:

"From looking at the billing records, it merely states telephone conference with Don Denton. I

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<sup>854</sup> Denton 8/20/96 GJ at 63-67. In a 1996 interview, Denton said he subsequently had a conversation with Seth Ward about Mrs. Clinton's failure to understand the problem the cross notes presented. Denton 6/26/96 Int. at 5. Denton had known Ward since 1977, and could not remember him ever using an attorney other than Hubbell, though Denton did not question Ward about Mrs. Clinton's involvement. Id. at 5.

believe that it had to do with a matter referred to as Babcock in the billing records."<sup>855</sup> Mrs.

Clinton nevertheless acknowledged that the April 7, 1986 billing entry is listed under the "IDC matter," not Babcock:

A. I can only say that based on the billing records, and based on the information I have seen, if you look at the 4/7/86 entry, which is the 12-minute telephone conference, and yes it was billed to IDC, but I don't think that was correct, because it was followed two days later by an hour and a half conference with Mr. Denton concerning the loan participation that Savers Savings and Loan had that Madison was interested in resolving. And then all of the time on Babcock concerns those loans and Mr. Denton is one of the people that I spoke with and had conferences with.

So, I believe, based on the evidence that I see and the fact that Mr. Denton was involved in this Babcock matter, that that is what that first telephone conference also pertained to.

Q. Why wasn't it billed to number four, General, or some other matter?

A. That's a good question, Mr. Ewing, and as I've looked at these billing records carefully, over the last days, there are a lot of questions I have about that. There are a number of errors, and I attribute it to secretarial, clerical accounting errors. But I think that's where the telephone conference with Mr. Denton rightly belongs.<sup>856</sup>

Mrs. Clinton said she knew nothing about the April 7, 1986 cross loans.<sup>857</sup> She also testified she did not know that federal examiners were then reviewing Madison Guaranty.<sup>858</sup>

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<sup>855</sup> H. Clinton 4/25/98 Depo. at 127. The Babcock matter was a loan workout -- unrelated to IDC -- that Mrs. Clinton worked on for Madison Guaranty with Don Denton's help. Mrs. Clinton billed the Babcock file for 1.5 hours on April 9, 1986, for a conference with Don Denton.

<sup>856</sup> Id. at 126-27.

<sup>857</sup> Id. at 128-29.

<sup>858</sup> Id. at 104.

**c. Examiners Learned about Ward's Compensation for His Role in the IDC Transaction; an Option Agreement Was Used to Conceal the True Nature of the Transactions.**

Sometime in April 1986, FHLBB examiners found a copy of the original September 24, 1985 agreement between Seth Ward and Jim McDougal.<sup>859</sup> This agreement had not been produced to the examiners, who already knew about the cross loans to Ward and wanted to determine whether the loans were part of the commission payments to him. This was significant to the examiners because if the loans were commission payments that Madison Financial owed Ward, the \$400,000 loan from Madison Guaranty to Ward violated the six percent direct investment limitation by using Madison Guaranty money to fund a Madison Financial obligation. The peculiar documentation for this payment of commissions would violate the federal law requiring Madison Guaranty's records reflect the true nature of its transactions.<sup>860</sup>

**i. Clark Questioned Denton, and Denton's False Explanation Created the Need for the Option Agreement to be Quickly Created.**

Examiner Jim Clark asked Denton about the cross loans in late April 1986.<sup>861</sup> Clark's notes reflect that Denton falsely told Clark the two loans were unrelated.<sup>862</sup> Denton told Clark the

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<sup>859</sup> Clark and other examiners found the document after normal business hours at Madison Guaranty while searching through some desk drawers. Clark 7/13/96 Int. at 3.

<sup>860</sup> 18 U.S.C. § 1006; see also J. Clark 7/13/96 Int. at 3.

<sup>861</sup> FHLBB Examiner J. Clark's notes (Mar. 4, 1986) (Doc. No. 99-00043209). Even before this conversation, Clark had had concerns about how forthcoming Madison Guaranty was being. He thought that Madison Guaranty was playing games with the examiners; either not providing relevant documents or tampering with the files it gave to them. J. Clark 10/27/94 Int. at 23.

<sup>862</sup> FHLBB Examiner J. Clark's notes (Mar. 4, 1986) (Doc. No. 99-00043209).



loans to Ward from Madison Guaranty were for business debts and a tax payment.<sup>863</sup> He said the note purporting to be a loan to Madison Financial from Ward was documentation of a previous obligation of Madison Financial to purchase a piece of property (Holman Acres) from Ward.<sup>864</sup> Denton told the examiners the loan would never be funded because they were only using the loan note temporarily while they waited for Ward's attorney (Webb Hubbell) to draw up an option agreement.<sup>865</sup> Denton told Clark he would provide them with a copy of the option when it was done.<sup>866</sup>

This transaction described by Denton to the examiners was inconsistent with Madison Financials' existing contractual rights. Under the original September 24, 1985 agreement, as of February 28, 1986, Madison Financial already had the right to re-purchase Holman Acres from

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<sup>863</sup> Id.

<sup>864</sup> Id.

<sup>865</sup> Id. Denton recorded a similar explanation in a memo to Latham. Memo from Denton to Latham (July 14, 1986) (Doc. No. DD000000052). After the FHLBB meeting in Dallas on July 11 where the FHLBB insisted on the resignations of McDougal and Latham, Latham asked Denton to write several memoranda outlining his understanding of various transactions, including the payment of Ward's commissions. Denton responded in a memo to Latham which recited the commissions owed to Ward and said after Ward was advanced \$300,000 by Madison Guaranty:

In the interim, pending preparation of an option agreement whereby Madison Financial would purchase the northeast corner from Seth, a note was drawn in the amount of \$300,000 dated April 7, 1986, payable to Seth Ward, executed by Madison Financial Corporation. This note was later destroyed and replaced by a similar note. An option agreement was drawn dated May 1, 1986, obligating Seth to sell the property to Madison if it so opted. This option was in the amount of \$400,000 and I am assuming this would cover the \$300,000 note, the \$70,000 note, and interest on those two obligations.

Memo from Denton to Latham (July 14, 1986) (Doc. No. DD000000052).

Ward for the unpaid balance, \$70,000, left on Ward's \$1.15 million loan. There was no need to enter into another agreement to pay Ward \$400,000 for this property.

**ii. Hubbell Drafted the April 30, 1986 Employment Agreement for Ward.**

In a document ostensibly dated April 30, 1986, Madison Financial and Seth Ward entered into an agreement articulating Ward's purported employment terms at Madison Financial.<sup>867</sup> The agreement said Madison Financial was "engaged in the development and sale of property" and that Ward would "assist in coordinating activities relating to planning, developing, engineering and implementation of roads, buildings, and recreational facilities to be constructed on properties owned by Madison."<sup>868</sup> Ward's "compensation" was described as "a \$25,000 year retainer, payable in bi-weekly installments of \$961.54 beginning Thursday, May 15, 1986 and such other compensation as agreed to by both parties."<sup>869</sup> The terms required Ward to "make available his services to Madison [Financial] at least six hours a day, five days a week."<sup>870</sup> Jim McDougal, John Latham, and Seth Ward signed the agreement.<sup>871</sup>

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<sup>866</sup> FHLBB Examiner J. Clark's notes (Mar. 4, 1986) (Doc. No. 99-00043209).

<sup>867</sup> Agreement between Seth Ward and James B. McDougal (Apr. 30, 1986) (Doc. No. 027161).

<sup>868</sup> Id.

<sup>869</sup> Id.

<sup>870</sup> Id. By its terms, the agreement was entered into "by and between Madison Financial [C]orporation (hereinafter 'Madison') and Seth Ward (hereinafter 'Ward')." Id.

<sup>871</sup> Id. The date on the employment agreement corresponded to the federal examiners second "as of" date. When the federal examination of Madison Guaranty began on March 3, 1986, the "as of" date of the examination was February 28, 1986. The federal examiners changed the "as of" date to April 30, 1986, "[b]ecause of the length of the examination." FHLBB Office

**iii. May 1, 1986: Mrs. Clinton Billed Madison Guaranty for Preparing the Option Agreement.**

Jim Clark told Darlene Ford to follow up on the option agreement referred to by Denton. Ford returned to Denton about the option on Tuesday, April 29, 1986. Her notes reflect that Denton told her they were still waiting for the option.<sup>872</sup> Two days later, on Thursday, May 1, 1986, Mrs. Clinton billed the Madison Guaranty IDC file for two hours for: "conference with Seth Ward; telephone conference with Seth Ward regarding option; telephone conference with Mike Schaffler [sic]; prepare option."<sup>873</sup>

Hubbell said he spoke with Mike Schaufele about the option and Ward's related efforts to collect "commissions" from Madison for Ward's role in the IDC/Castle Grande transactions: "At one time Mr. Ward was trying to have his commissions that were owed, when he got paid, not be ordinary income, but be capital gains, and he talked to Mike about it," Hubbell later said.<sup>874</sup> "I'm

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of Examinations and Supervision, Report of Examination, Madison Guaranty Savings & Loan Assoc., Docket No. 7601 at 7a n.1. Ward and Hubbell discussed the employment agreement. Hubbell 8/22/96 GJ at 104. Hubbell said he "could have" had a role in drafting the employment agreement, although remembering that he told Ward that he "ought to get whatever his deal was in writing." Hubbell 8/22/96 GJ at 104. According to Hubbell, when Ward asked, "Why do you think that?" Hubbell said, "that I felt that it was wise, especially if he was going to be dealing with Mr. McDougal, that he ought to get his agreement in writing." Hubbell 8/22/96 GJ at 104-05.

<sup>872</sup> Ford's notes said: "I [Darlene] talked to Don Denton and he said that the option had not been drawn yet but he would give it to us. He said the notes will never be funded." FHLBB Examiner D. Ford's notes (Apr. 29, 1986) (Doc. No. 99-00043209). Ford documented an April 29, 1986 conversation with Denton in which Denton said "the option had not been drawn." Ford 7/29/96 Int. at 2.

<sup>873</sup> Rose Billing Records (May, 1986) (Doc. No. DEK015031). The reference to "Mike Schaffler" apparently refers to Seth Ward's accountant, Mike Schaufele.

<sup>874</sup> Hubbell 8/22/96 GJ at 90.

not a tax lawyer. And Mike told me that, actually, there was a way to do it, using an option. I remember that part of it. Again, I couldn't set it up. I didn't have any idea how to do it, but Mike said it was possible."<sup>875</sup> When shown the May 1, 1986 option agreement, Hubbell said he was not sure whether it was the option agreement he discussed with Schaufele, but said, "I suspect it is."<sup>876</sup> The option was signed for Madison Financial by Latham and notarized on May 12, 1986.<sup>877</sup> Latham later testified that the March 31, 1986 \$400,000 loan to Ward "was done really at that time in lieu of the option."<sup>878</sup> The May 1, 1986 option, he said,

more concretely or more accurately reflects the nature of the transaction, that being that the service corporation owed Seth \$300,000 in commissions. In the initial purchase of all of that property, Seth retained tracts 27 and 28 of Holman Acres as his commission, which was later to be bought by the service corporation. The option allows the service corporation to buy the property from Seth, thus Seth receives the \$300,000, and the service corporation would have the property."<sup>879</sup>

Latham also testified, explaining why the note was for \$400,000:

Q. Now, you've testified that the note was to evidence -- the note given by

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<sup>875</sup> Id.

<sup>876</sup> Id. at 91; see also id. at 94 ("I don't know. I mean, Seth usually told me about his business, and that's why I'm hesitant, but I don't remember the option"); id. at 93 ("Q. Did you ever talk to your father-in-law about that option around that period of time, or in 1986? A. I'm sure I did, but the specifics I'm not sure because, like I said, later on, my understanding of the option and the notes all related to the commissions, and I was told I was wrong on that, okay?"); and id. ("I mean, I had conversations with Mike, okay, about the option, and I've had conversations with Seth, but on that day that she billed for, I don't believe so").

<sup>877</sup> Option to Purchase Real Estate (May 1, 1986) (Doc. Nos. 99-00043196 through 43208).

<sup>878</sup> Tr. at 223, Ward v. Madison Guaranty, No. 87-7580 (E.D. Ark.) (testimony of John Latham) (Doc. No. 341-00004134).

<sup>879</sup> Id.

MFC to Ward was evidence of \$300,000; the option was to effectuate the intent, which was to purchase tracts 27 and 28 [Holman Acres] from Mr. Ward for \$300,000. Then Mr. Ward would have the money, and Madison Financial Corporation would have the land; is that correct?

A. Yes, that's correct.

Q. Now, the option is in the amount of \$400,000. Do you know why it's taken for \$400,000?

A. No, other than when it was drawn up it may have been to offset the note, which was also for \$400,000. I believe at the time the balance on the note was 300,000, that 100,000 had been paid off, the 300,000 remaining being -- what I remember as being the amount of the commissions. That would be the only thing I could think of on the option.<sup>880</sup>

Don Denton's testimony corroborated Latham:

Q. Did you discuss the option agreement with Seth Ward?

A. Yes.

Q. Do you remember what you talked about with him?

A. Yes. The intent of the option was to document the fact that Seth Ward was going to sell that property to Madison Financial in the future. And it was my understanding from talking with Ward that when he sold that property, he would take the money that he received from that sale and pay back Madison [Guaranty] on the earlier March 31st loan.

Q. So the option agreement was very closely related to the payment to Mr.

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<sup>880</sup> Id. at 224 (testimony of John Latham) (Doc. No. 341-00004135); see also id. at 229 (Doc. No. 341-00004140) ("Q. And shortly after [the March 31, 1986 \$400,000 loan from Madison to Ward] was executed Mr. Ward paid back \$100,000 of that loan, did he not? A. I believe that's correct. Q. Within a matter of perhaps a week? A. I think that's correct"). According to a July 14, 1986 memo from Don Denton to John Latham, Ward returned \$100,000 on April 23, 1986. Memo from Denton to Latham (July 14, 1986) (Doc. No. DD000000052). McDougal did not remember anything about the drafting of the option agreement. McDougal said he was in a manic state and let Latham handle all of the mechanics of the transaction. J. McDougal 8/96-6/97 Int. at 19.

Ward of his commissions?

A. Yes. It was to -- the option was to document how Ward was to receive the money to repay his loan to Madison Guaranty Savings & Loan.

Q. Did you discuss the option agreement with Mr. Latham?

A. Yes.

Q. Tell us about that discussion.

A. Generally, the same understanding that the original March 31st loan and the renewals were done on April 7th in the amount of \$300,000 plus 70. That those loans would be repaid when Madison bought the property from Seth, which was covered under the option. The money then would go to repaying Madison [Guaranty's] loans that Seth owed.<sup>881</sup>

Denton gave a copy of the option to examiner Darlene Ford on May 7, 1986.<sup>882</sup> Ford reviewed the legal description of the property and noticed that it was wrong.<sup>883</sup> The option did not refer to Holman Acres, but rather to the property that Davis Fitzhugh purchased on February 28, 1986.<sup>884</sup> Ford pointed out the erroneous description to Denton, who had the first two pages of

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<sup>881</sup> Denton 8/20/96 GJ at 68-69. The parties never exercised the option. Ward eventually simply returned Holman Acres to Madison Guaranty, with Hubbell's help, by means of a December 1986 quitclaim deed, as a means of avoiding repayment of the outstanding non-recourse loans that this parcel secured.

<sup>882</sup> Copy of option with Ford's handwritten notes (May 1, 1986) (Doc. No. 99-00043196 through 43201).

<sup>883</sup> Ford 7/29/96 Int. at 2-3.

<sup>884</sup> This same property description appears on an attachment to a release deed given to Seth Ward by Madison Guaranty dated December 30, 1985. Martha Patton, Webb Hubbell's secretary at Rose, said she believes that she typed the attachment. Patton 9/25/96 Int. at 2. The incorrect legal description used in the option pertained to the property purchased by Davis Fitzhugh, which was prepared by Edward G. Smith & Associates on or before March 31, 1986. See Little Rock South Industrial Park NE Corner Legal Description (Mar. 31, 1986) (MGSL-FR-00000028). This identical legal description appeared in a release deed given by Madison

the option re-typed to accurately describe Holman Acres as the subject property.<sup>885</sup>

**iv. Mrs. Clinton Drafted the Option Agreement.**

Mrs. Clinton testified that she did not think she drafted the May 1, 1986 option agreement "from scratch":

Q. Mrs. Clinton, we -- the bank examiners were in the bank during this time. There is evidence that there were these cross loans where Mr. Ward was advanced monies by Madison, but to cover the obligation, he then on paper loans money back to Madison, but it was not funded. That later, on May 1st, '86 there was an option agreement put in place of this document.

Now, we know now that you apparently drafted the option agreement that took the place of this document here.

A. I don't believe I drafted the option agreement [.]

Q. But you billed for it?

A. It, it was billed for. That is correct, along with several other activities in a two-hour period on May the 1st.

Q. Did you actually bill the client and list on the records of your law firm, draft option agreement?

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Financial to Seth Ward. The parties had failed to release the Fitzhugh property from Ward's mortgage on the \$1.15 million loan. A partial release deed, with a legal description as a separate page, was prepared on December 30, 1985. Partial Release Deed granted to Ward by Madison Guaranty (executed Dec. 12, 1985) (Doc. Nos. 105-00046413 through 46414).

<sup>885</sup> Ford's notes on the option she received from Denton state: "Talked to Don Denton. He said that this land description goes with the Fitzhugh mortgage property and that this description is in error. He said it should be the property known as Tract 27 and 28 of Holman Acres on which Ward (unintelligible)." FHLBB Examiner D. Ford's notes (May 1, 1986) (Doc. No. 99-00043196); see also Ford 7/29/96 Int. at 2-3; Clark 7/26/96 Int. at 2-3. Denton had the first two pages of the incorrect option re-typed. Denton 6/26/96 Int. at 5. The corrected version of the option retyped at Denton's direction is referenced with Doc. No. 99-00043202; see also Denton 8/20/96 GJ at 70 (discussing the retyping of the first two pages of the May 1, 1986 option agreement).

- A. Draft option agreement is what that says [on the billing records], that's right. But I do not believe I drafted that option agreement from scratch. That would not be something I would do.<sup>886</sup>

Documentary evidence established that Mrs. Clinton did participate in the drafting of the option agreement. First, Mrs. Clinton billed Madison Guaranty for doing so.<sup>887</sup> Second, the document bore her unique Rose computer code.<sup>888</sup> Third, Mrs. Clinton once had a file labeled "Ward Option," which she ordered to be destroyed in July 1988, along with her other Madison Guaranty files.<sup>889</sup>

Hillary Clinton said it was not unusual for Ward to stop by Rose and demand that a piece of legal work be taken care of immediately.<sup>890</sup> This supported the inference that after Ford's follow-up request for the option on April 29, 1986 (Tuesday), Ward went to Rose in person on May 1, 1986 (Thursday). "Ward's attorney [Hubbell]" was out of town or unavailable -- Hubbell

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<sup>886</sup> H. Clinton 4/25/98 Depo. at 129. Seth Ward testified that he did not remember discussing the option (either the May 1 version or the corrected May 7 version) with Mrs. Clinton, though he may have. Ward 2/12/96 Senate Whitewater Comm. Depo at 49; see also Ward 2/12/96 Senate Whitewater Comm. Depo at 53 ("I do not remember Mrs. Clinton being involved"). Ward 1/17/96 GJ at 82. Because Ward always spoke of Hubbell when discussing IDC matters, it was McDougal's opinion that Hubbell probably prepared the option agreement and that Mrs. Clinton had no involvement in it. J. McDougal 8/96-6/97 Int. at 16.

<sup>887</sup> Rose Billing Records (May, 1986) (Doc. No. DEK015032) (among items for two hour block was "prepare option").

<sup>888</sup> See Option to Purchase Real Estate at 3 (May 5, 1986) (Doc. Nos. 010996 through 11001). In the bottom-right corner is the code "0190g" which was Mrs. Clinton's word processing code. FDIC-OIG Supplemental Report on Rose Law Firm Conflicts of Interest at 43-44, WA-94-0016 (Sept. 20, 1996).

<sup>889</sup> Memo from Mary Russell, Rose File Clerk, to Mrs. Clinton at 2 (July 21, 1988) (Doc. No. FDICHRC 0163).

<sup>890</sup> H. Clinton 2/14/96 FDIC Int. at 13.



was then in trial against Jim Guy Tucker.<sup>891</sup> Ward appears to have asked Mrs. Clinton to prepare the option in Hubbell's absence. Mrs. Clinton either drafted or participated in the drafting, after making phone calls to both Ward and his accountant, Mike Schaufele (as noted, Ward was concerned about the tax treatment of his arrangement with Madison).<sup>892</sup>

**v. The Option Concealed the True Nature of the Transactions from Examiners.**

Federal examiners Jim Clark and Darlene Ford said the existence of the option hindered their investigation.<sup>893</sup> A memorandum of an interview with Clark read:

WARD's status as a straw purchaser allowed MGS&L to evade the 6% investment limitation in MFC; management made a valiant effort to hide this and used the option agreement to hide WARD's commission payment. CLARK only learned that WARD's \$400,000 loan was really commission after reading LATHAM's trial testimony in WARD's lawsuit against MGS&L [in 1988]. CLARK now concludes that WARD's commission payment was a "sham" to disguise WARD's straw man involvement in the IDC transaction. In the end, the option agreement seemed to support the idea that WARD's \$400,000 loan was unconnected to the cross loans, when, in fact, the commission payment disguised as a loan was really a direct investment in MFC. The option successfully threw the examiners off the trail of the cross loans and they never did connect payment of WARD's commission to WARD's \$400,000 loan.<sup>894</sup>

Although Clark and Ford were suspicious of the cross loans and the option, the existence

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<sup>891</sup> See Tucker 3/18/98 GJ at 187 ("He [Hubbell] couldn't have done it -- he couldn't have spent much time that day because he was in trial with me. And I mean, this was a very complex trial. And maybe he could have broken to do something totally different, but I would be surprised -- very surprised if he could have"). Jim Guy Tucker and Hubbell had also been out of town in depositions many times prior to the start of the trial.

<sup>892</sup> Schaufele had no memory of his discussion with Mrs. Clinton on May 1, 1986. Schaufele 1/30/96 GJ at 28-29.

<sup>893</sup> Ford 7/29/96 Int. at 2-3; Clark 7/13/96 Int. at 3-4; and Clark 7/26/96 Int. at 3-4.

<sup>894</sup> Clark 7/26/97 Int. at 3-4.

of an option was concrete documentary evidence supporting Madison Guaranty's claim that the cross loans were unrelated to the original September 24, 1985 agreement. The option supported the story Madison Guaranty officials told the examiners -- the unfunded April 7, 1986 note was intended to document Madison Financial's intention to purchase Holman Acres from Ward.

The FDIC-OIG later concluded that:

[E]ntries in the billing materials and other evidence suggest that former Rose Law Firm Partners Hillary Rodham Clinton and Webster L. Hubbell performed work that appears to have facilitated the payment of substantial commissions to Ward, who acted as a straw buyer for Madison Financial in the IDC transaction. . . . The method of payment of commissions evaded regulations designed to protect the safety and soundness of the institution, and violated the integrity of its books and records. Further, Madison Guaranty used a document drafted by Clinton to deceive Federal bank examiners as to the true nature of the payments to Ward.<sup>895</sup>

Whether the option was exercised or not, its existence was intended to deceive the examiners, and it did so. Ward was paid over \$380,000 for his role in the IDC transaction at a time when the institution was in financial distress. The option concealed these payments from examiners who were then looking at whether Madison Guaranty had violated the direct investment limitation by having Madison Guaranty pay obligations owed by its service corporation, Madison Financial. The option played a key role in deceiving the examiners into accepting Madison Guaranty's explanations the loans to Ward were unrelated to his commissions.<sup>896</sup> Mrs. Clinton's statements about the option agreement are discussed in Chapter 3

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<sup>895</sup> FDIC-OIG Supplemental Report on Rose Law Firm Conflicts of Interest, WA-94-0016 at ii-iii (Sept. 20, 1996).

<sup>896</sup> That Madison Guaranty management had misrepresented the purpose of the cross loans to examiners was made clear by subsequent statements and testimony of Madison Guaranty personnel. In a July 22, 1986 memorandum to Don Jack, Latham's attorney, Latham said 1)

of this Part.

**2. The Evidence of Wrongdoing Uncovered by the Examiners Ultimately Led to an Order Requiring McDougal and Others to Resign; Mrs. Clinton Returned the Madison Guaranty Retainer.**

**a. Examiners Submitted Interim Reports That Criticized Madison Guaranty.**

Federal examiners continued their examination, but cooperation from Madison Guaranty management became strained. Jim Clark submitted his sixty-day interim report to Rolf Coburn on May 8, 1986.<sup>897</sup> Clark and the examiners thought that Madison Guaranty's management was obstructing their investigation, providing evasive answers to questions, and manipulating the institution's files in response to specific inquiries. The report said its conclusions had not been discussed with Madison Guaranty management, in part, because Clark was "concerned that management will use the information gained on the specific direction of the investigation to hide, destroy, or otherwise limit our access to crucial records."<sup>898</sup> The report was critical of Madison Guaranty and said the investigation of just three of Madison Guaranty's real estate projects -- Maple Creek Farms, Castle Grande, and Twelfth and Main -- had resulted in losses exceeding Madison Guaranty's entire net worth.<sup>899</sup> The report stressed that Madison Guaranty's problems

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Ward's loans and the May 1, 1986 option were related; and 2) Madison Guaranty's records were manipulated to deceive the examiners. Latham wrote the memorandum just one week after the FHLLB forced him to resign from Madison Guaranty. See Memo from John Latham, Madison Guaranty Executive Vice President to Don Jack, Latham's attorney (July 22, 1986).

<sup>897</sup> Sixty-Day Interim Report (May 8, 1986) (Doc. Nos. 99-00038802 through 38817).

<sup>898</sup> Id. at 1 (Doc. No. 99-00038802).

<sup>899</sup> The report said as of March 31, 1986, the total investment in the three projects was \$10,602,000. Of this, the examiners considered \$2,728,000 a loss and the remainder

stemmed from "straw" transactions and land "flips" to insiders, and accused Madison Guaranty management of using the Castle Grande development to generate fictitious profits for Madison Financial by using arbitrarily low cost allocations to generate high profits on initial sales "leaving high costs and large losses for future sales as in Maple Creek."<sup>900</sup>

**b. Non-Recourse Agreements Were Executed as "A Way of Protecting Seth's Interest"; Madison Guaranty Lent Seth Ward an Additional \$93,000.**

In documents bearing the date June 6 and June 9, 1986, but which were backdated, John Latham and Seth Ward executed three non-recourse agreements.<sup>901</sup> The first two non-recourse agreements, dated June 6, 1986, modified Seth Ward's Castle Grande loans (the \$70,000 February 25, 1986, and \$400,000 March 31, 1986 loans) and relieved him of personal liability for

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substandard. Madison Guaranty's entire net worth as of March 31, 1986 was only \$2,371,000. Id. at 2 (May 8, 1986) (Doc. No. 99-00038803).

<sup>900</sup> Id. at 10 (Doc. No. 99-00038811).

<sup>901</sup> June 6, 1986 was the maturity date on the \$70,000 February 25, 1986 loan. The loan note was originally dated June 9, 1986, but it was altered by hand to read June 6, 1986. Don Denton said loan numbers at Madison were computer generated such that higher loan numbers came later in time than lower loan numbers. Accordingly, the renewal loan, loan 4221, issued after 4215. Because loan 4215 issued on June 10, 1986, loan 4221 must have issued on or after June 10, 1986. See FDIC-OIG 9/20/96 Supp. Rep. at 4 n.4; Loan no. 4215-76 (June 10, 1986) (Doc. No. SEN33180); Denton 9/6/96 FDIC-OIG Statement at 6-7. Don Denton said: "since #4221 was a renewal of loan #3359 [the \$70,000 February 25, 1986 loan], it is likely that it was backdated to the date of maturity of the note being replaced. When advised that #3359 had not reached maturity, DENTON said that he believed that since #3359 was unsecured, the renewal was done to secure the loan with the Holman Acres property which could then be returned to the institution in lieu of repayment." Id. at 7. Additionally, "DENTON said that MGSL's loan numbers were computer generated and 'not manipulable.' DENTON said that loan #4221, dated June 6, 1986, 'could not have occurred before a note' with an earlier number." Id. at 6.

them.<sup>902</sup> The effect of the release agreements was to benefit Seth Ward (to the detriment of Madison Guaranty) by converting his outstanding loans from recourse to non-recourse loans. If Seth Ward did not repay the two loans (which he did not), Madison Guaranty could recover only Holman Acres to satisfy what he owed, and could not seek recovery from him individually.

On approximately June 9, 1986, Madison Guaranty lent Seth Ward another \$70,000 to pay off his February 25, 1986 \$70,000 loan.<sup>903</sup> Holman Acres served as collateral for this second \$70,000 loan, and another release agreement made the second loan non-recourse, secured only by Holman Acres.

Additionally, Madison Guaranty lent Seth Ward \$93,000 on June 10, 1986,<sup>904</sup> which he did not repay. This was apparently unrelated to the Castle Grande property. Ward deeded Holman Acres to Madison Guaranty rather than repay his \$300,000 and \$70,000, and the \$93,000 was involved in Ward's subsequent lawsuit against Madison Guaranty. The June 1986 release agreements enabled Seth Ward to avoid any personal liability for the losses Madison Guaranty

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<sup>902</sup> Latham 8/20/96 GJ at 46. The amendments to the loans are somewhat inaccurate in that some of them refer to the original \$400,000 loan dated March 31, 1986, which was replaced with the new notes on April 7, 1986. Nevertheless, in a document dated June 6, 1986, Latham and Ward executed two amendments relieving Ward of personal liability on loan no. 4027-50 in the original amount of \$400,000 (Doc. No. 56-00125991), and loan #3359-76 in the original amount of \$70,000 (Doc. No. 396-00000534). In a document dated June 9, 1986, Latham and Ward executed an amendment relieving Ward of personal liability on loan no. 4221-50 in the original amount of \$70,000 (Doc. No. 396-00000533).

<sup>903</sup> The loan note (loan no. 4221) said the interest rate on this loan was 10.5 percent. Loan Documentation from Madison Guaranty to Seth Ward (June 9, 1986) (Doc. No. 396-00000532).

<sup>904</sup> Loan documentation from Madison Guaranty to Seth Ward (June 10, 1986) (Doc. No. 341-00004355).

incurred as a direct result of his failure to repay the loans.

Latham later said of the non-recourse agreements: "It was -- it was just a way of protecting Seth's interest."<sup>905</sup> Similarly, Don Denton later said of the June 1986 releases, Ward now had the "same kind of obligation that he had on the original \$1.15 million, where he was not personally liable to repay it. In the event he elected to do so, he could simply give the land back and all would be forgiven."<sup>906</sup> The releases, Denton also said, were tied to the presence of the federal examiners.<sup>907</sup>

In a July 22, 1986 memorandum to his attorney Latham wrote:

Because it was not the intent of Seth or Jim for Seth to be at risk for the \$300,000 and his property I later executed a non-recourse agreement in June [1986] to

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<sup>905</sup> Latham 8/20/96 GJ at 47; see also id. at 48 ("This was just a means of protecting Seth should the Service Corporation not be able to pay its liabilities to Seth"). In the 1988 trial, John Latham discussed the purpose of the June 1986 releases:

Seth at this point in time was concerned because the service corporation at that time was not able to exercise that option and thereby buy the property from them and pay them the \$300,000 in cash. Yet he had a loan to the savings and loan in which he owed money to the savings and loan, secured by that property. He did not want to be in a position where the service corporation could not buy the property and thereby pay him the \$300,000 and yet he would have to pay the savings and loan back the \$300,000 that was owed on its note.

For that reason we released him from liability, not liability, but we released him from personal liability and set up the savings and loan's only recourse as going against the land itself so that if that case happened, if the service corporation could not pay Seth the \$300,000, then he would -- the savings and loan could take the property, and Seth would not have to pay the \$300,000 back to the savings and loan.

Tr. at 225, Ward v. Madison Guaranty, No. 87-7580 (E.D. Ark.) (testimony of Latham) (Doc. No. 341-00004136).

<sup>906</sup> Denton 8/20/96 GJ at 71.

<sup>907</sup> Id. at 71-72.

protect Seth. The non-recourse agreement was not placed in the file until mid-July with the intent that it not be seen by the examiners immediately.<sup>908</sup>

This was done at the direction of John Latham or Don Denton.<sup>909</sup> Latham was unsure if the non-recourse agreements would have any binding effect on Madison Guaranty, but he executed them to appease Ward.<sup>910</sup> Ward also received \$10,000 from Madison Financial by check, dated June 6, 1986, as partial payment of "commissions" owed him.<sup>911</sup>

On June 10, 1986, Mrs. Clinton billed the Madison Guaranty "general" matters file for a telephone conference with Rick Massey and an in-person conference with Ward.<sup>912</sup> This was Mrs. Clinton's only billing to Madison Guaranty that month.<sup>913</sup> In 1996, Mrs. Clinton was asked

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<sup>908</sup> Memo from John Latham, Madison Guaranty Executive Vice President, to Don Jack, attorney for John Latham at 3 (July 22, 1986).

<sup>909</sup> Latham 8/20/96 GJ at 48. "It was something that I didn't want -- and I don't remember why, but I didn't want the examiners asking questions about it at that point in time," John Latham later said. "And I can't remember if it was because -- well, I don't remember. I mean, it was -- I don't know. I think by that point I was just -- I didn't want to answer any more questions, but, yeah." *Id.* at 49.

<sup>910</sup> *Id.* at 49-50.

<sup>911</sup> Check No. 5364 from the account of Madison Financial Corporation payable to Seth Ward for \$10,000 (June 6, 1986) (Doc. No. SEN33172). Ward testified at his 1988 trial that the \$10,000 payment was to pay interest on the unfunded \$300,000 April 7, 1986 cross loan from Madison Financial to Seth Ward. Tr. at 186-87, Ward v. Madison Guaranty, No. 87-7580 (E.D. Ark.) (testimony of Ward) (Doc. Nos. NE-00000198 through 199). The April 7 note was unfunded. Additionally, a document entitled "Commission Account - due Seth Ward, July 1, 1986" and dated July 10, 1986 shows Ward's commissions as \$349,920 "[l]ess payments" of \$300,000 and \$10,000 for a total "[d]ue" of \$39,920 (Doc. No. SEN33166). The written version of this document is in Ward's handwriting, as Ward acknowledged at his 1988 trial (Doc. No. 341-00004351) (handwritten version); Tr. at 194-96, Ward v. Madison Guaranty, No. 87-7580, (E.D. Ark.) (Doc. Nos. NE-00000206 through 208) (testimony of Ward).

<sup>912</sup> Rose Billing Records (June 1986) (Doc. No. DEK015038).

<sup>913</sup> Rose Billing Records (June 1986) (Doc. No. DEK015037).

about this conference, shown some of the Ward loan documents dated in June, and asked if these were discussed when Ward saw her on June 10, 1986. Mrs. Clinton said she did not remember ever seeing the documents before or discussing them with Ward.<sup>914</sup>

By a document dated June 11, 1986, Ward returned the unfunded April 7, 1986 \$70,943.47 note with the explanation that "By reason of Madison Guaranty's modification, dated June 6, 1986, subject note [#3359-76] is, in effect, paid in full. Therefore Seth Ward is returning Madison Financial Corporation's note . . . in the amount of \$70,943.47 . . . by reason of being offset by subject listed note."<sup>915</sup> Although Ward returned the unfunded April 7, 1986 \$70,943.47 note, he kept the unfunded April 7, 1986 note for \$300,000. John Latham later stated that the unfunded \$300,000 note "should have been demanded."<sup>916</sup> As explained in Chapter 2 of this Part, Ward filed a lawsuit in which he asserted the unfunded April 7, 1986 \$300,000 note evidenced a debt owed to him by Madison Financial.

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<sup>914</sup> H. Clinton 2/14/96 FDIC Int. at 90-91.

<sup>915</sup> Document from Seth Ward (June 11, 1986) (Doc. No. 341-00004372); see also Tr. at 237, Ward v. Madison Guaranty, No. 87-7580 (E.D. Ark.) (Doc. No. 341-00004148) ("Q. Was the note for \$70,943.47 given back when Mr. Ward was released from his personal liability on a \$70,000 note? A. I believe it was") (testimony of Latham).

<sup>916</sup> Tr. at 235, Ward v. Madison Guaranty, No. 87-7580 (E.D. Ark.) (Doc. No. 341-00004146) (testimony of Latham); see also id. at 237-38 (Doc. Nos. 341-00004148 through 4149) ("Q. But, when they claimed they released him from the \$300,000 note, they didn't make any effort so far as you know to get back or get a release on any \$300,000 note they had given him? A. Not that I know of. It could have been asked for and never returned") (testimony of Latham).



**c. Parties Executed a June 24, 1986 Addendum to the September Agreement, which Materially Changed Ward's Compensation.**

An addendum to Ward and McDougal's earlier compensation agreement was drafted and executed in June 1986.<sup>917</sup> Madison Guaranty employee Patricia Heritage's notes reflected that John Latham asked her to acquire a copy of the agreement between Ward and McDougal about commissions on Castle Grande (the original September 24, 1985 agreement).<sup>918</sup> She was told to look for the agreement in a desk drawer, but neither Heritage nor anyone else in the office could find it.<sup>919</sup> As discussed above, the examiners had already found the letter.<sup>920</sup> Heritage then obtained from Ward a copy of the original September 24, 1985 agreement to use as a basis for the addendum.<sup>921</sup> Heritage drafted the addendum, which Ward signed, and Sue Strayhorn notarized on June 24, 1986.<sup>922</sup>

The addendum said Ward was to receive ten percent sales commission on all the IDC property he sold. In addition, he was to receive a ten percent commission on all IDC property sold for commercial development regardless of whether he made the sale or not and he was to

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<sup>917</sup> Letter from Seth Ward to Jim McDougal (June 24, 1986) (Doc. No. 396-00000700).

<sup>918</sup> Pat Heritage Daily Notes (June 1986) (Doc. No. AAP-0002505).

<sup>919</sup> Id.

<sup>920</sup> Clark 7/13/96 Int. at 3.

<sup>921</sup> Letter from Seth Ward to Jim McDougal containing handwritten note to Pat Heritage, assistant to John Latham, Madison Guaranty, from Seth Ward (Sept. 25, 1985) (Doc. Nos. 042154 through 42155).

<sup>922</sup> Addendum from Seth Ward to James B. McDougal, President, Madison Guaranty (June 24, 1986) (Doc. No. 027112).

receive a four percent commission on any sales of residential property.<sup>923</sup> When later asked about the June 24, 1986 addendum, McDougal said he did not remember it, but said he never would have agreed to a ten percent commission on sales not made personally by Ward.<sup>924</sup> McDougal said the other sales people would have been extremely upset at such an arrangement. Moreover, McDougal never would have agreed to pay ten percent commission to Ward for sales because McDougal himself -- and not Ward -- had arranged these sales.<sup>925</sup>

By the end of June 1986, Seth Ward had been paid a total of \$380,000 for his role as straw man in the IDC/Castle Grande matter.<sup>926</sup> That was not enough for Ward, though, because by a document dated July 1, 1986, he tried to obtain additional payments; according to Ward's summary, the \$300,000 and \$10,000 payments were simply to be subtracted from the amount of "commissions" still owed him.<sup>927</sup>

**3. The FHLLB Examination Culminated with a July 11, 1986 Meeting where Federal Regulators Demanded That the McDougals and Others Be Removed from Control of Madison Guaranty.**

By the end of June 1986, the examiners remained convinced that there were serious problems with both Madison Guaranty in general and the Castle Grande development in particular. The examiners assigned to the case wrote several memoranda outlining why Madison

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<sup>923</sup> Id.

<sup>924</sup> J. McDougal 8/96-6/97 Int. at 23.

<sup>925</sup> Id.

<sup>926</sup> \$300,000 of the \$400,000 March 31, 1986 loan; \$70,000 from the June 1986 loan; and another \$10,000 from the June 1986 payment.

<sup>927</sup> Commission Account Due Seth Ward (July 1, 1986) (Doc. No. 56-00126495).

Guaranty's real estate appraisals did not conform to the FHLBB rules.<sup>928</sup>

**a. Madison Guaranty Was Notified of the July Meeting with FHLBB.**

The FHLBB notified the Madison Guaranty board of directors by letter, dated June 19, 1986, that it had scheduled a meeting with them for July 24, 1986, in Dallas, Texas.<sup>929</sup> The letter reported that the examination of Madison Guaranty had found "matters of serious supervisory concern including unsafe and unsound practices." The letter criticized Madison Guaranty's failure to meet its net worth requirements in violation of the July 19, 1984 Supervisory Agreement, and transactions with affiliates and insiders. The letter required Madison Guaranty to immediately take six "corrective actions" before the scheduled meeting, the most relevant of which were that:

5) Madison Guaranty, or any of its subsidiaries, shall not finance any additional sales of real estate owned by the association or any of its subsidiaries, save for sales closed pursuant to legally binding commitments to provide such financing in existence at the date of this letter; [and]

6) [Madison Guaranty] shall not, and shall not allow any of its subsidiaries to transact business with any of the following named companies . . . and this office must be notified in writing prior to any payment of \$1,000 or more by [Madison Guaranty] to any of the following companies . . .

1. Castle Sewer and Water Company
2. Castle Industries, Inc.
3. The Wilson Co., Inc
4. Hot Stuff, Inc.

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<sup>928</sup> Memo from Jim Clark to the file (June 25, 1986) (Doc. No. 99-00037728); Memo from Jim Clark to the file at 2-3 (June 26, 1986) (Doc. Nos. 99-00037711 through 37712).

<sup>929</sup> Letter from Walter H. Faulk, FHLBB, to Board of Directors, Madison Guaranty Savings & Loan (June 19, 1986) (Doc. Nos. DEK218778 through 218780). The meeting was later moved up to July 11, 1986.

5. Abernathy Development
6. Sorenson Enterprise
7. Madison Marketing
8. Madison Real Estate
9. Designer Construction
10. Industrial Development Company of Little Rock (IDC)
11. Industrial Services Co. (ISC)
12. Madison Properties, Inc.
13. Dixie Continental Leasing, Inc.
14. Aunspaugh Designs
15. Master Developers, Inc.
16. Island Construction<sup>930</sup>

**b. Bassett Gave the Governor's Office a "Heads Up" about Madison Guaranty's Problems and the July 11 Meeting with the FHLBB.**

Beverly Bassett, who served as the Arkansas Securities Commissioner and Arkansas Savings and Loan Supervisor,<sup>931</sup> was notified about the FHLBB's upcoming meeting with Madison Guaranty's board of directors. And after receiving a copy of the June 19, 1986 letter from the FHLBB to Madison, Bassett sent a handwritten memorandum to Sam Bratton on July 2, 1986.<sup>932</sup> Bratton was a lawyer and a member of Governor Clinton's staff who acted as the liaison between the Governor's office and the Securities Department.<sup>933</sup> Bassett's memorandum, attaching a copy of the FHLBB's June 19, 1986 letter to Madison Guaranty's board of directors, said in full:

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<sup>930</sup> Letter from Walter H. Faulk, FHLBB, to Board of Directors, Madison Guaranty Savings & Loan at 2-3 (June 19, 1986) (Doc. Nos. DEK218779 through 218780).

<sup>931</sup> Bassett 11/8/95 GJ at 51-52.

<sup>932</sup> Memo from Beverly Bassett, Arkansas Securities Department Commissioner, to Sam Bratton, Liaison of the Education Department, Arkansas Governor's Office (July 2, 1986) (Doc. No. DEK218777).

<sup>933</sup> Senate Whitewater Comm. Hearing, supra note 147, at 14 (Jan. 25, 1996) (testimony

Madison Guaranty is in pretty serious trouble. Because of Bill's relationship w/ McDougal, we probably ought to talk about it. The meeting referred to in the attached letter has been moved up to July 11, 1986 and the FHLBB has asked me to be at the meeting.

Please note that while all of the FHLBB restrictions in the letter are serious, #5 & 6 effectively put Madison out of business.

"Thank you for your support."

BB<sup>934</sup>

Bassett said she notified Bratton because she wanted to keep the Governor's office informed so that it would be prepared for press inquiries in the event the institution was to be shut down.<sup>935</sup> Bassett said from her experience with Guaranty Savings & Loan Association of Harrison, Arkansas, a financial institution closed in December 1985 by the FHLBB, the closing of Madison Guaranty could create problems for the Governor.<sup>936</sup>

Asked to elaborate on one line from her memorandum -- "Because of Bill's relationship w[ith] McDougal, we probably ought to talk about it" -- Bassett said:

Well, it was my impression that Jim McDougal -- well, repeatedly told people, people in our office, people whoever, anywhere he went, that he was Bill Clinton's friend and no one -- I never heard that from Bill Clinton, but I had the distinct impression that Jim McDougal would make some effort -- might make some effort, if he found out, you know, or if he was concerned that something was fixing to happen, that he would try to intervene and that he would call the

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of B. Schaffer).

<sup>934</sup> Memo from Beverly Bassett, Arkansas Securities Department Commissioner, to Sam Bratton, Liaison of the Education Department, Arkansas Governor's Office (July 2, 1986) (Doc. No. DEK218777).

<sup>935</sup> Bassett 11/8/95 GJ at 99-100.

<sup>936</sup> Id. Vince Foster and Rose acted as counsel for the FHLBB and the FSLIC on the Guaranty matter.

governor's office, that he would make some effort to interfere. And we had had that same experience the year before with Guaranty Savings & Loan in Harrison, and I didn't want that to occur. My suggestion was that they shouldn't have anything to do with him at all.<sup>937</sup>

Bratton and Bassett discussed the memo and Madison Guaranty's situation.<sup>938</sup> Although Bassett was sure she sent the July 2 memorandum to Bratton,<sup>939</sup> she did not think she called Bratton immediately after the July 11 meeting.<sup>940</sup> Bassett said she did not discuss Madison Guaranty's situation with Governor or Mrs. Clinton.<sup>941</sup>

Bratton later testified that the July 2, 1986 memorandum was not the first time Bassett had told him that Madison Guaranty was in trouble.<sup>942</sup> Bratton also said he definitely remembered having spoken with Bassett about Madison Guaranty's situation both before and after the July 11 FHLBB meeting.<sup>943</sup> Bratton testified that he would have told Governor Clinton (or someone on his staff) about the information from Bassett, and these discussions with the Governor began some six to twelve months before the FHLBB meeting in Dallas.<sup>944</sup> Bratton said

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<sup>937</sup> Id. at 102. Bassett said she did not know in 1986 that McDougal had formerly served on Governor Clinton's staff and that McDougal was a business partner with the Clintons. Id. at 102-03.

<sup>938</sup> Id. at 99-100; Bratton 12/5/95 GJ at 11-12.

<sup>939</sup> Bassett 11/8/95 GJ at 107.

<sup>940</sup> Id. at 111-12.

<sup>941</sup> Id. at 107-08; 116-18.

<sup>942</sup> Bratton 12/5/95 GJ at 13.

<sup>943</sup> Id. at 10-12, 17-18.

<sup>944</sup> Bratton 1/5/96 Senate Whitewater Comm. Depo. at 178.

that the Governor asked Bratton to keep him advised on the matter, which he did.<sup>945</sup>

President Clinton testified that he did not ask to be kept apprised of Madison Guaranty's situation.<sup>946</sup> President Clinton later remembered that at some point he learned that Madison Guaranty was in dire straits, but he did not specifically remember a conversation with Bratton or Bassett on the subject, though he said that the conversation was possible.<sup>947</sup>

Bratton and Wright testified that they did not think they had any conversation with Mrs. Clinton about Madison Guaranty's situation.<sup>948</sup> President Clinton likewise did not remember any such discussions with Mrs. Clinton.<sup>949</sup>

**c. On July 10, a Memorandum Was Circulated at Rose Discouraging New or Expanded Representation of Thrifts.**

On Thursday July 10, 1986, Rose attorney Herb Rule circulated a memorandum to all attorneys at Rose about the firm's representation of thrifts and the FSLIC:

When we began our representation of FSLIC in the Guaranty Savings and Loan Receivership, one of our primary qualifications was that we did not represent any savings and loan associations generally or in regulatory matters.

We expect the Firm's fees from FSLIC this year on the Guaranty Receivership alone will exceed \$600,000. The Office of General Counsel has requested the Firm not take on any savings and loan representation, particularly with respect to associations in financial difficulty.

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<sup>945</sup> Id. at 176-77; see also Bratton 12/5/95 GJ at 15-16.

<sup>946</sup> W. Clinton 7/22/95 Depo. at 52.

<sup>947</sup> Id. at 57-58. President Clinton also testified he did not remember conversations with Hale about Madison Guaranty's troubles. Id. at 80-82.

<sup>948</sup> Bratton 12/5/95 GJ at 19; Wright 2/29/96 GJ at 44.

<sup>949</sup> W. Clinton 4/22/95 Depo. at 82.

Since it is likely that we may be called on to represent FSLIC in connection with other receiverships, both in and out of Arkansas, we want to avoid taking on any new or expanded representation of savings and loan associations or their affiliates without prior notice to and approval by the Executive Committee.

If you now represent any savings and loan associations or affiliates, please note the clients' names at the bottom of this sheet and return it to me. If you have any other questions, give me or Vince Foster a call.<sup>950</sup>

Rick Massey responded to Rule by sending him a handwritten note at the bottom of the memorandum:

For about the past year, Hillary and I have represented Madison Guaranty S&L. ~~in connection with~~ Madison has continually had regulatory net worth problems.

Massey<sup>951</sup>

In 1995, Mrs. Clinton said:

I believe that around that time the commercial section of our firm was doing work or about to do work that was for FSLIC maybe, if FSLIC was still in existence then. I don't remember.

But, in any event, there was an inquiry about doing work and the inquiry was circulated to the members of the firm about whether we did any work for savings and loans at that time, or were on retainer. And I believe at that point a decision was made that we weren't doing very much work for Madison and there was no point to continue the retainer, and to terminate that kind of relationship.<sup>952</sup>

In 1995, Mrs. Clinton could not remember receiving the July 10, 1986 memorandum from Herb Rule.<sup>953</sup> In 1998, Mrs. Clinton said the Rule memorandum was the impetus for her

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<sup>950</sup> Memo from Herb Rule, Rose attorney, to All [Rose] Attorneys, (July 10, 1986) (Doc. No. RIC120859).

<sup>951</sup> Id. (strikeout in original).

<sup>952</sup> H. Clinton 4/22/95 Depo. at 31.

<sup>953</sup> Id. at 32-33.



return of the Madison Guaranty retainer.<sup>954</sup>

**d. Madison Guaranty's July 11, 1986 Meeting with the FHLBB.**

On Friday, July 11, 1986, John Selig and Breck Speed, attorneys from Mitchell Williams, accompanied the Madison Guaranty board to Dallas.<sup>955</sup> The FHLBB regulators gave the Madison Guaranty board a cease and desist order requiring Madison Guaranty to agree to remove the McDougals (who did not attend), Latham, and the Henleys (Susan McDougal's brothers) from all responsibilities connected with the institution.<sup>956</sup> Latham would be allowed to remain as a consultant for a short time to aid in the transition. The Castle Grande development was one of the projects discussed as being improper.<sup>957</sup> Also discussed at the meeting was the appointment of Madison Guaranty board member Stephen Cuffman as temporary CEO to run the institution on an interim basis until a replacement could be found.<sup>958</sup> Selig, for the Board, requested some time to review and consider the order.<sup>959</sup>

After the board returned to Arkansas, Latham attended several meetings in response to the

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<sup>954</sup> Id. at 130-35.

<sup>955</sup> FHLBB Dawn Pulcer's handwritten notes at 1 (July 11, 1986) (Doc. No. 99-00022968). The board members were John Latham (Chairman), Steve Cuffman, C. Dennis Edwards, Jack Owen, Sarah Hawkins, and Charles Peacock.

<sup>956</sup> FHLBB Dawn Pulcer's handwritten notes at 8-12 (July 11, 1986) (Doc. Nos. 99-00022975 through 22979); Latham 3/28/95 GJ at 48-49.

<sup>957</sup> FHLBB Dawn Pulcer's handwritten notes at 12-13 (July 11, 1986) (Doc. Nos. 99-00022979 through 22980).

<sup>958</sup> Id. at 11 (Doc. No. 99-00022978).

<sup>959</sup> Id. at 12 (Doc. No. 99-00022979).

impending order.<sup>960</sup> McDougal resigned immediately,<sup>961</sup> and Latham resigned the next Thursday, July 17, 1986.<sup>962</sup>

#### **4. The Events of Monday, July 14, 1986.**

On Monday, July 14, 1986 the next business day after the FHLBB's actions, four significant events happened: 1) Betsey Wright, Governor Clinton's chief of staff, sent the Governor a memorandum discussing the McDougals' problems and asking whether Governor Clinton still had the Whitewater stock; 2) Seth Ward went to Madison Guaranty and presented a backdated, changed version of the September 24, 1985 compensation agreement; 3) Don Denton drafted a memo for John Latham describing Seth Ward's relationship with Madison Guaranty; and 4) Mrs. Clinton returned the Rose retainer to Madison Guaranty with a letter that minimized Rose's prior representation.

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<sup>960</sup> Latham's calendar for Saturday, July 12, 1986, reads:

John Selig - [illegible] pick up notes / S&L review C&D / Jim [illegible] discuss [illegible] / Bob Wilson's home - discuss him as CEO

His calendar for Sunday, July 13, reads:

S&L for review of C&D / Don [illegible] office / Jim Guy Tucker's office / Jim McDougal - [illegible] discuss options

Latham's calendar (July 12, 1986) (Doc. No. 038526). Latham was questioned about a number of his calendar entries by both the Independent Counsel and the FDIC, but not the specific entries for July 12 and 13, 1986. Latham remembered little, if anything, about his calendar entries and was of little help in deciphering his handwriting. Latham 8/20/96 GJ at 54-70; Latham 7/15/96 Int. at 3.

<sup>961</sup> Latham 3/28/95 GJ at 49.

<sup>962</sup> Handwritten letter from John Latham to the Madison Guaranty Board of Directors (July 17, 1986) (Doc. No. 212-00002944).

**a. Betsey Wright Sent Governor Clinton a Memo about the McDougals' Troubles.**

Betsey Wright sent a memorandum to Governor Clinton about McDougal and Whitewater stock indicating that she knew about Madison Guaranty's problems with the FHLBB.

The memorandum said:

White Water stock  
(McDougal's Company)

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Do you still have? (pursuant  
to Jim's current problems

If so, I'm worried about it.<sup>963</sup>

Governor Clinton sent Wright a handwritten reply at the bottom of the memorandum:

No -- Don't have any more  
B<sup>964</sup>

Wright said she had sent the memorandum because, although not publicly announced, "it was all over the streets" that McDougal was being ousted from Madison Guaranty.<sup>965</sup> Wright was worried that if the Clintons were still business partners with the McDougals, McDougal's removal, by association, could create a negative public perception of the Governor, who was running for reelection.<sup>966</sup>

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<sup>963</sup> Memo from Betsey Wright, Clinton campaign manager, to Governor Clinton (July 14, 1986) (Doc. No. 1221-00000901).

<sup>964</sup> Id.

<sup>965</sup> Wright 2/29/96 GJ at 33-34.

<sup>966</sup> Id. at 41-42.

**b. The Backdated September 24, 1985 Agreement.**

Seth Ward and Jim McDougal signed a second agreement, backdated to September 24, 1985, sometime after signing the original September 24, 1985.<sup>967</sup> The backdated agreement appeared to have been signed on or near July 14, 1986, when Ward went to Madison Guaranty and presented the agreement. "Backdating" is a crucial issue, because the cease and desist order presented by the FHLBB on July 11, 1986 would have prohibited Ward and McDougal from doing what they did using a current date.

The terms of the agreement represented a substantial improvement in Ward's position over the original agreement: Ward was to receive a ten percent commission on commercial property regardless of who sold the property, and a \$35,000 fee in return for the 270 day option. In addition, the backdated September 24, 1985 agreement: 1) increased the commissions owed to Seth Ward; and 2) excluded Holman Acres from Madison Guaranty's 270-day option to repurchase the IDC property held by Seth Ward.<sup>968</sup> The backdated September 24, 1985 agreement in the form of a letter from Seth Ward to Jim McDougal, stated:

Dear Mr. McDougal:

This is to set forth our agreement concerning the property commonly referred to as all the land owned by the Industrial Development Company of Little Rock and certain improvements thereon.

On or about the 13th day of September, 1985, Madison Guaranty Savings & Loan Association agreed to acquire all of the Industrial Development Company of Little

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<sup>967</sup> Letter from Seth Ward to Jim McDougal, with addendum (Sept. 24, 1985) (Doc. Nos. NE-00000017 through 19).

<sup>968</sup> Id.

Rock's property except the grounds and building commonly referred to as the Timex Building. In this agreement Madison has the right to assign its rights to any entity or individual. As part of our agreement, I have agreed to take title to all of the assets of the aforementioned property that is located immediately north of 145th Street, the water and sewer improvements, and the sewer treatment ponds, including the one located south of 145<sup>th</sup> Street. Madison Guaranty Savings & Loan Association will agree to lend me the purchase price for this property secured by a mortgage of those parcels and the sewer and water works. Madison Guaranty will pay \$35,000.00 to me to have an option for at least 270 days from the date of acquisition to purchase the property from me at any time, in whole or in part, for at least the pro rata amount of the note plus all accrued interest; except one parcel described:

Approximately 22-acres located and referred to as the Northeast Quadrant of the Interchange of Highway 65 and 145th Street. More specifically described in the attached legal description which is a part of this agreement.

It is the intention of both Madison and myself to attempt to develop all the property acquired from I.D.C. and sell it as quickly as possible. If the property or any portion thereof is sold during the 270-day period, the sale price will be mutually approved by me and Madison Financial Corporation. The proceeds of the sale will be applied toward the promissory note, less a 10% sales commission to be paid to me. At Madison's discretion, any particular piece of property may be deeded back to Madison prior to the execution of a sales transaction.

It is also agreed, in addition to the salary I am receiving from Madison Financial Corporation, I will receive 10% sales commission on all property sold, regardless who sells it, except residential property that will be located south of 145th Street, in which case I will receive 4% commission if sold by any other person. During the term of the option period, all of the net revenues of the water works and sewer department shall be forwarded directly to Madison Guaranty for application toward the note, unless such facilities are sold sooner. Madison Financial Corporation will also be responsible for all taxes, special assessments, dues, insurance premiums, etc. during the period of this option.

I would appreciate your acknowledging and agreeing to the terms of the letter of agreement.

Sincerely,

/s/ Seth Ward

Seth Ward

Acknowledged and accepted:

/s/ James B. McDougal  
James B. McDougal, President  
Madison Financial Corporation<sup>969</sup>

The property description of Holman Acres was attached as an "addendum" to the backdated September 24, 1985 agreement.<sup>970</sup>

When he was later asked about the backdated agreement, Jim McDougal acknowledged his signature on the document, but said that he did not remember when he signed it.<sup>971</sup> McDougal thought that if Ward had given him a backdated document he would have signed it, though if he had read the document carefully he would not have signed it.<sup>972</sup> McDougal said he had only agreed to give Ward a ten percent commission on the sales that he made and a four percent commission on sales by others. McDougal said had he agreed to a ten percent commission on all sales, it would have caused tremendous problems with the other employees.<sup>973</sup>

Ward later conceded that the document had been backdated, but he testified the letter was backdated by a matter of weeks though he could not remember precisely how many weeks.<sup>974</sup>

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<sup>969</sup> Id. (Doc. Nos. NE-00000017 through 18).

<sup>970</sup> Addendum to the property description of Holman Acres (Sept. 24, 1985) (Doc. No. NE-00000019).

<sup>971</sup> J. McDougal 8/96-6/97 Int. at 20.

<sup>972</sup> Id.

<sup>973</sup> Id.

<sup>974</sup> Ward 2/12/96 Senate Whitewater Comm. Depo at 20-22.

Ward said he realized shortly after executing the first letter that it did not accurately describe the terms of his deal with McDougal. Ward said that he asked Hubbell if it was legal to execute a corrected version of a contract to reflect the actual terms of an agreement while keeping the original date of the previously executed contract.<sup>975</sup> Ward said Hubbell answered that if the backdated agreement accurately reflected the terms of the agreement at that date, then it would be legally acceptable.<sup>976</sup>

The information in the letter and testimony of other witnesses established that the letter was backdated by substantially more than a matter of weeks:

- (1) The letter contained a legal description for the Holman Acres property that could not have been prepared until sometime after the middle of November 1985, when the property was surveyed.<sup>977</sup>
- (2) The Holman Acres property description that accompanied the backdated September 24, 1985 agreement was not prepared until March 31, 1986.<sup>978</sup>
- (3) John Latham testified that he remembered first seeing the document "around May or June of '86."<sup>979</sup>
- (4) As discussed above, McDougal and Ward executed an addendum to their compensation agreement dated June 24, 1986, drawn from the original September 24, 1985 agreement.<sup>980</sup> Thus, as Latham later testified, the June

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<sup>975</sup> Id. at 23.

<sup>976</sup> Id. Hubbell said that he might have told Ward that two parties could consent to modify their agreement. Hubbell 8/22/96 GJ at 105-06, 163.

<sup>977</sup> White 10/15/96 Int. at 5-6.

<sup>978</sup> See Little Rock South Industrial Park NE Corner Legal Description (Mar. 31, 1986) (Doc. No. MGSL-FR-00000028).

<sup>979</sup> Tr. at 227, Ward v. Madison Guaranty, No. 87-7580 (E.D. Ark.) (testimony of Latham) (Doc. No. 341-00004138).

<sup>980</sup> Addendum agreement (June 24, 1986) (Doc. No. 396-00000700). One copy of the

24, 1986 addendum "would almost go with -- with the one that doesn't speak about Holman Acres" -- the original September 24, 1985 agreement.<sup>981</sup> In other words, the backdated agreement was created after the June 24 addendum.

- (5) Don Denton testified that Ward presented him an unsigned copy of the backdated September 24, 1985 agreement on July 14, 1986. Denton said Ward returned later that day with an executed copy of the letter.<sup>982</sup>

This evidence was consistent with the sequence of events about the regulators' actions and with the changes made to the agreements. The compensation that Ward received from the June 24 addendum was close to that which he had obtained under the backdated September 24 agreement. The most important change between the two was the treatment of Holman Acres. The backdated September 24 agreement exempted Holman Acres from the original option that Madison Financial had for all property. If the agreement was accepted as genuine, it would have concealed the fraud Ward and the Madison Guaranty insiders had perpetrated when they used Holman Acres as a device to funnel more than \$300,000 in payments to Ward at a time when the examiners were keenly interested in Ward's compensation. The May 1 option agreement is the clearest example of this fraud: Madison Financial agreed to purchase for \$400,000 from Ward a piece of property that it already had an option to purchase for \$70,000. Madison Financial entering into such an option served no legitimate purpose.

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original September 24, 1985 agreement that was produced to the Independent Counsel had a handwritten note to Pat Heritage from Seth Ward that said this was the agreement used to draft the June 24, 1986 addendum. Agreement letter from Seth Ward to Jim McDougal (Sept. 24, 1985) (Doc. Nos. 042154 through 42155).

<sup>981</sup> Latham 8/20/96 GJ at 54.

<sup>982</sup> Denton 8/20/96 GJ at 75-76.



By replacing the original agreement, as well as the subsequent June 24 addendum, the backdated agreement benefited Ward at Madison Guaranty's expense. It increased the "commissions" owed Ward and it purported to provide him with a payment for the option, which Ward later would claim had been paid.<sup>983</sup> It excluded Holman Acres from Madison's option to repurchase from Ward the property he held for Madison Financial, paying Ward an additional amount (\$35,000) for a less extensive option.

The exclusion of Holman Acres was significant in determining Ward's motive in acquiring the agreement. After February 28, 1986, the terms of the original September 24, 1985 agreement provided Madison Guaranty with an option to repurchase Seth Ward's remaining IDC property (Holman Acres) for the unpaid balance (\$70,000) of his \$1.15 million loan. From February 28, 1986 to July 14, 1986, Ward and Madison used Holman Acres as:

- (1) collateral for the \$400,000 March 31, 1986 loan from Madison Guaranty to Ward (\$300,000 of which Ward never repaid);
- (2) the property supposedly sought by Madison Financial as represented by the \$400,000 March 31, 1986 and the \$300,000 and \$70,943.47 April 7, 1986 unfunded cross notes from Seth Ward (as "lender") to Madison Financial (as "borrower");
- (3) the property Madison sought an "option" to buy from Ward for \$400,000 in the form of the May 1, 1986 option; and
- (4) collateral for the \$70,000 June 1986 loan from Madison Guaranty to Seth Ward (that Ward did not repay).<sup>984</sup>

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<sup>983</sup> Ward 2/12/96 Senate Whitewater Comm. Depo at 112-13.

<sup>984</sup> In 1988, at the trial of Ward v. Madison Guaranty, an appraiser testified that Lots 27 and 28 of Holman Acres were worth \$170,000. Tr. at 177, Ward v. Madison Guaranty, No. 87-7580 (E.D. Ark.) (Doc. Nos. NE-00000308 through 311) (testimony of Pyron).

**c. Don Denton's July 14, 1986 Memorandum "RE: Ward, Seth."**

Don Denton wrote a memorandum dated July 14, 1986 to John Latham "RE: Ward, Seth."<sup>985</sup> Denton's memorandum expressed Denton's understanding of Ward's Castle Grande dealings:

It is my understanding that Seth had an arrangement with Madison Financial Corporation that he would receive a \$300,000 commission for his participation in the acquisition of part of the real estate acquired in September of 1985 from Industrial Development Corporation. It is also my understanding that Madison Financial Corporation was not in a position, from a liquidity standpoint, to make payment to Seth in early April 1986.

Seth had originally borrowed \$1,150,000 from Madison Guaranty for his part of the purchase. Subsequent sales reduced the balance of his loan to \$70,000 by early April of 1986. A new note was drawn in the amount of \$70,000, payable to Madison, which now matures November 30, 1986.

On March 31, 1986, Seth executed a note in the amount of \$400,000 secured by the northeast intersection of the Pine Bluff Freeway and 145<sup>th</sup> Street [Holman Acres]. We originally advanced the full \$400,000 with Seth subsequently repaying on April 23 \$100,000 of this loan. The current balance is \$300,600 which has been extended to November 30, 1986. In the interim, pending preparation of an option agreement whereby Madison Financial would purchase the northeast corner from Seth, a note was drawn in the amount of \$300,000 dated April 7, 1986, payable to Seth Ward, executed by Madison Financial Corporation. This note was later destroyed and replaced by a similar note. An option agreement was drawn, dated May 1, 1986, obligating Seth to sell the property to Madison if it so opted. This option was in the amount of \$400,000 and I am assuming this would cover the \$300,000 note, the \$70,000 note, and interest on those two obligations.

It is my understanding that title to some 50 acres on the northeast boundary of 145th Street remains in Seth's name and is not included in this option arrangement. This is the property that Peacock is currently developing for an

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<sup>985</sup> Memo from Don Denton, Senior Vice-President, Madison Guaranty, to John Latham (July 14, 1986) (Doc. No. DD000000052).

FHA project.

Seth has a third note with Madison Guaranty S&L which to my knowledge has no connection with the 145th Street project. This note is #4215 in the amount of \$93,000, dated June 10, 1986. This loan matures January 30, 1987 and is unsecured.

HDD/ly<sup>986</sup>

**d. Mrs. Clinton Returned the Madison Guaranty Retainer.**

On July 14, 1986, the first business day following the July 11, 1986 meeting between Madison Guaranty's board and the FHLBB, Mrs. Clinton had a letter delivered to Jim McDougal and John Latham, terminating Madison Guaranty's retainer relationship with Rose. The letter stated:

Dear Jim and John:

When you requested the Rose Law Firm represent Madison on a specific matter in April, 1985, I advised you that the firm would credit fees against a monthly retainer and then bill for whatever fees might be in excess of the retainer at the end of each month. Since that time, Madison has run a credit in its account at the end of every month.

We are also aware that since that time Madison has been relying and continues to rely on a number of other law firms to provide ongoing representation, and that our representation has been for isolated matters and has not been continuous or significant.

You currently have a credit with the Rose Law Firm of \$4,622.53. I am, therefore, returning the enclosed check our firm received for \$2,000 as an advance against legal fees for the month of July, 1986, and a check for the retainer credit in the amount of \$4,622.53.

We do not believe it appropriate for us to take a pre-payment of legal fees when

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<sup>986</sup> Memo from Don Denton to John Latham, Madison Guaranty Executive Vice President (July 14, 1986) (Doc. No. DD000000052).

there is only one matter we are representing Madison on, namely the negotiations with Savers over the Babcock and Econolodge loan participations. If you would like us to work on another specific matter, we would be glad to discuss it on a case-by-case basis.

Sincerely yours,

For the Rose Law Firm  
HILLARY RODHAM CLINTON<sup>987</sup>

Mrs. Clinton sent blind copies of the letter to Vince Foster and Herb Rule.<sup>988</sup>

In 1995, Mrs. Clinton was asked about the return of the retainer. She did not remember any conversations about Madison Guaranty's condition:

Q. Are you familiar with this letter?

.....

A. Yes, I am.

Q. Can you tell us by this letter what you all were doing?

A. We were terminating the retainer relationship with Madison and returning the accrued retainers that had already been deposited.

Q. And according to this, how much did you send back to them in July of '86?

A. Well, we returned a check for \$2000, and we sent a check for \$4,622.53.

Q. Other than this memo coming out from Mr. Rule, which basically is saying we are not supposed to take on or expand any representation of institutions, especially any with financial difficulty, can you tell us who you would have discussed this with, this whole matter of terminating this and sending the money back?

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<sup>987</sup> Letter from Hillary Rodham Clinton to Jim McDougal and John Latham (July 14, 1986) (Doc. Nos. RLF2 02989 through 2990).

<sup>988</sup> Id.

A. Well, I don't know specifically, but I would assume that Mr. Rule would have inquired further in response to Rick Massey's note, and there would have been some discussion amongst people, and then I would have been asked to write this letter if I was the billing attorney, and return the money.

Q. Do you recall today any discussions about if Madison was in serious financial difficulties at this point?

A. I do not recall any.<sup>989</sup>

In her February 1996 FDIC interview, Mrs. Clinton was again asked about this:

Q. Let's turn to tab 37 for a moment. Would this be an unsigned copy of a letter you sent to Mr. McDougal and Mr. Latham on July 14, 1986?

A. It appears to be, yes.

Q. And you had hand-delivered?

A. That's what it says on the first page of the letter.

Q. Why did you send this letter?

A. I believe, based on the documents which I have reviewed that the letter was in response to a decision by the firm that at the request of FSLIC, the general counsel's office, that the firm not take on any savings and loan representation, particularly with respect to associations in financial difficulty, and I'm reading from the memorandum from Herb Rule to all attorneys dated July 10, 1986.

And again, I have no specific recollection, but I believe that in response to this memorandum, Mr. Massey advised Mr. Rule that we had done work for Madison and that work was considered by the firm to be such that, in response to the Office of General Counsel, we should no longer continue it.

And I don't recall this, but again, just putting together the pieces of the

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<sup>989</sup> H. Clinton 4/22/95 Depo. at 34-35; see also id. at 37 (Mrs. Clinton stated that she does not remember any discussions about Madison's problems before July 14, 1986, when she returned the retainer to Madison).

documentation, I believe that I was asked to advise Mr. McDougal and Mr. Latham, which I did in this letter. We returned their accumulated retainer and on July 17, in a memo to Herb Rule, I advised him that we had sent the letter to Mr. McDougal and Mr. Latham.

Q. Now, the July 10 memo to which you made reference is the memo behind tab 36; is that right?

A. Yes, that's correct.

Q. And the July 17 memo is the memo behind tab 38?

A. That's right.

Q. Now, when you wrote your letter, the letter behind tab 37, it's correct, is it not, that you knew nothing about a meeting that had occurred a few days before between representatives of the Federal Home Loan Bank Board and the board of directors of Madison Guaranty?

A. That's correct.

Q. And when you wrote your letter, had you seen or heard about the letter dated June 19, 1986 that's behind tab 35?

A. I do not recall knowing about this letter, Mr. Ericson.

Q. Beverly Bassett Schaffer has testified recently that she told her liaison to the governor's office about the Federal Home Loan Bank Board meeting on July 11 a few days in advance of that meeting. And I'm afraid this is not a book because I got the copy yesterday.

I have here and I'd like to show you some documents that have been marked CCBW 884 through 888, which I received yesterday from counsel for Betsey Wright. The first page I understand to be a handwritten memo from Beverly Bassett.

The second, third and fourth pages are the June 19 letter we just looked at, and then the last page is, what I understand to be from testimony, a note from Betsey Wright to your husband dated July 14.

My first question is whether you've ever seen any of this before?

- A. No, I do not recall seeing any of this before, unless I saw it from my lawyers during the last year or two.
- Q. I meant at the time. As of July 14, 1986, had you learned from any source, including your husband, that the federal regulators were about to take action or contemplating action with respect to Madison Guaranty or McDougal?
- A. I do not recall learning that from any source.
- Q. Were you aware that an examination of Madison Financial was underway and had been underway for some months?
- A. I do not recall knowing that.
- Q. Going back to tab 36 for a moment, just a couple of questions -- just one really. At the bottom here, Rick Massey has written a note, the last part of which says "Madison has continually had regulatory net worth problems." Was that something you knew at this time?
- A. Well, I knew the idea behind the preferred stock offering was to try to raise money for Madison to be able to meet its capital requirements. I knew that back when the representation was undertaken by Mr. Massey.
- Q. And you knew also, didn't you, that unless and until Madison met its capital requirements, the securities department was not going to let Madison go ahead with the broker-dealer action?
- A. That's right. The securities commissioner had conditioned Madison's being able to go forward on its meeting its regulatory requirements.
- Q. Looking at tab 38 just for a second, is there any particular reason you would have cc'd Vince Foster on this July 17 memorandum?
- A. I believe that Mr. Rule mentions Mr. Foster in his memorandum that we were just looking at in the last sentence. "If you have any other questions, give me or Vince Foster a call." Mr. Foster was the attorney I worked for on the FSLIC representation and I assume that because he was mentioned in Mr. Rule's memo, I cc'd him.<sup>990</sup>

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<sup>990</sup> H. Clinton 2/14/96 FDIC Int. at 91-96. The July 17 memorandum mentioned in this

In her 1998 deposition, Mrs. Clinton testified:

Q. . . . Let me ask you about the July '86 -- we have asked you before, Mrs. Clinton, about the circumstances surrounding the return of the retainer of advance against fees on July the 14th of '86.

A. Uh-huh.

Q. We have previously shown you the memo from Beverly Bassett to Sam Bratton. Do you recall that? This was prior to the Home Loan Bank Board meeting with the Madison board.

A. I, I recall your showing that to me, but I had never seen it before.

Q. Okay. But I'll just give you dates. That's July 2nd of '86, and attached was a letter from the Home Loan Bank Board saying they wanted to meet with the Madison board, as a result of the exam that's been going on in March, April, May, June of '86.

Now, on the Monday following the meeting in Dallas, and I think we probably told you this last time, McDougal and Latham basically are told, you're out. McDougal is not at the meeting, but they told the board that Mr. McDougal and Mr. Latham had to be out. The next working day, you return the retainer back to Madison Guaranty. Do you recall that?

A. Yes.

Q. Now, I want to show you what's been marked as Exhibit 91. This is a memo that was produced to us by Bets[e]y Wright. I don't know if you know her handwriting or not?

A. I recognize that.

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testimony is discussed below. Although Mrs. Clinton did not remember any discussions about McDougal and Madison's problems before she returned the retainer, she has acknowledged that some discussions may have taken place. H. Clinton 4/22/95 Depo. at 37; see also H. Clinton 4/25/98 Depo. at 133 ("[T]he clear message was that if you weren't doing anything and there was, you know, no reason to continue the representation, then we should take another look at it. And in the case of Madison there hadn't been very much going on in that file").



Q. And then it's to apparently, Gov, or Governor, and then there is -- I was reminded of this. That's really not a backwards check if you are left-handed. But do you recognize that as the way your husband checks things off?

A. I do, and I recognize his writing on the bottom of the page, too.

Q. Okay. Now, this memo is on the first working day after McDougal has been shown the door at Madison. And the way it looks like to me, it says, "Whitewater stock, McDougal's company, do you still have pursuant to Jim's current problems? If so, I'm worried about it." And then it appears your husband has written, "No. Don't have any more."

Now, Ms. Wright was the chief of staff, was she not?

A. Yes, she was.

Q. And she was also a pretty good political advisor, was she not?

A. She was, indeed.

Q. Kind of one of the main ones that advised with your husband. Now, when she says she is worried about the Governor and McDougals, do you think that's what she's worried about there? Did you talk to her about this?

A. I don't recall talking to Bets[e]y about this at all. Bets[e]y was always worried. And she worried, I think, appropriately about everything.

Q. Well, why would you worry about McDougal?

A. I don't know. I'm just not surprised to see in her handwriting, "I'm worried." That was usually something she did on a regular basis.

Q. In political races, did you try to avoid negative associations?

A. Certainly. But that's not what was happening here.

Q. What's happening here?

A. Well, there was no linkage between anything that was going on inside Madison with Mr. McDougal and our firm's decision not to represent Madison any longer. It just so happened that about the time these actions

were occurring, Mr. Rule, who was one of our major commercial lawyers, sent around a memo asking that we no longer represent savings and loan associations.

Q. No, ma'am, it didn't say that. It says, the memo that Mr. Rule sent around, said you will not take on any new representations or expand any present representations without permission of the executive committee. It says nothing about stopping that. That's not so. Do you want to see a copy of that?

A. No, but the clear message was that if you weren't doing anything and there was, you know, no reason to continue the representation, then we should take another look at it. And in the case of Madison there hadn't been very much going on in that file.

Q. All right. On that same Monday that Ms. Wright wrote that memo, we also know that Mr. Ward walked into Madison that day and he had an unsigned backdated document basically saying, here was my arrangement with Madison for sales agreements. He comes back later again that day with a signed copy. All right.

Now, did you talk to Seth Ward on July the 14th, 1986?

A. I do not believe I talked to Seth Ward on July -- July, which, 14th? No.

Q. Yes, ma'am, that --

A. No.

Q. -- same day, that same Monday.

A. Not that I recall.

Q. All right. Let me hand you what we marked as Exhibit 92. The top document, I will represent to you, Mrs. Clinton, is some typewritten minutes of the Little Rock Airport Commission, which indicates it met on July the 14th, 1986 at 1:30. And present included Mr. Robert Wilson and Mr. Seth Ward. And also present was you. And then there is a Commission meeting.

Then I have actually attached there, we had gotten the minutes of the Airport Commission, and this is just -- somebody has compared the dates

of certain meetings between '84 and '89, and then indicated the days the minutes reflect that both you -- your attendance and Mr. Ward's attendance.

But, according to the minutes, on the same day that you sent this back to Madison, and the same day that Mr. Ward went into Madison, you are in Airport Commission meetings with Mr. Ward. Does it appear that's what this reflect[s]?

A. Yes. It appears we were both at the Airport Commission meeting.

Q. All right. We also know that the next day Mr. Wilson, who was there at the Airport Commission meeting, is at the Rose Law Firm meeting with Mr. Hubbell and Mr. Latham, and they are talking to Mr. Wilson about him perhaps buying the stock of Madison and taking over the institution. Mr. Wilson is being considered for that at the Madison board meeting on July 15th.

Now, my question to you is, did you talk to Bob Wilson or Seth Ward about Madison and its troubles?

A. I don't believe I did so at all, Mr. Ewing. I have no memory of that.<sup>991</sup>

On Thursday July 17, 1986, three days after Mrs. Clinton returned the Madison Guaranty retainer, she sent a memorandum to Herb Rule explaining it:

While you were on vacation, I sent the attached letter to Latham and McDougal concerning our representation of Madison. In the letter, I acknowledged that we were continuing to do work on only one matter, namely the Babcock and Econolodge loans. I received the other attachment from Savers to Denton concerning a request for the payment of expenses on the loans and drafted the attached response for Denton to send to Savers. Let's discuss this upon your return.<sup>992</sup>

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<sup>991</sup> H. Clinton 4/25/98 Depo. at 130-35 (emphasis supplied).

<sup>992</sup> Memo from Hillary Rodham Clinton to Herb Rule, Rose attorney (July 17, 1986) (Doc. No. 105-00003759). Mrs. Clinton also sent a copy of the memorandum to Vince Foster. Id.

In November 1986, Rose associate David Williams was asked to summarize the current and prospective clients Rose had withdrawn from or declined due to its representation of FSLIC.

On November 20, 1986, Williams wrote a memorandum summarizing the results of his survey:

Based upon a quick, informal survey with selected members of the firm, we have had either to withdraw from representation of present clients or decline representation of the following prospective clients due to our representation of FSLIC:

.....

9. Madison Guaranty Savings & Loan. Due to our representation of FSLIC, we have withdrawn from representation of Madison, which had been a previous client of ours generating estimated annual fees to the firm of approximately \$40,000.<sup>993</sup>

The memorandum was marked with handwritten edits, possibly by Foster or Mrs.

Clinton. The revised paragraph read:

9. Madison Guaranty Savings & Loan. Due to our representation of FSLIC, we have discontinued further representation of Madison. Hillary Clinton and others had represented [them?] from time to time on special assignments.<sup>994</sup>

#### IV. SUMMARY CONCLUSION

Mrs. Clinton began working for Madison Guaranty in April 1985. When later asked how it came to be that she represented Madison, Mrs. Clinton alluded to a long-unpaid bill for work done for McDougal's Madison Bank in Kingston and testified that her role was in securing payment of the bill before the Rose Firm began representation of McDougal's thrift, Madison Guaranty. Mrs. Clinton's testimony was factually inaccurate -- the "unpaid" bill had, in fact, been

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<sup>993</sup> Memo from David L. Williams, Rose Law Firm attorney to Vincent Foster Jr., Rose Law Firm attorney at 1, 3 (Nov. 20, 1986) (Doc. Nos. GS01967-69).

<sup>994</sup> Id. at 3.

paid more than 6 months prior to McDougal's hiring of Rose and Mrs. Clinton to represent Madison Guaranty.

Once hired, Mrs. Clinton performed a wide variety of work on behalf of Madison Guaranty. She, and the Rose Firm, initially worked on matters relating to efforts to raise capital through the sale of preferred stock. Later, the firm did a substantial amount of work relating to the acquisition and development of property from the IDC, which became known as Castle Grande. Mrs. Clinton personally worked on two regulatory issues relating to that development -- the possible construction of a brewery and the possible sale of water by the on-site utility to a business outside Castle Grande and to Maple Creek Farms.

The evidence conclusively established that Jim McDougal, Susan McDougal, Jim Guy Tucker, and David Hale engaged in a pattern and practice of fraud involving real estate transactions and fraud against financial institutions, using Madison Guaranty, Madison Financial, and CMS as the means by which their frauds were perpetrated. These frauds included the straw purchase of property at Castle Grande by Seth Ward, and other fraudulent transactions. As detailed in Volume II, Part A and Volume I, Appendix 5, these frauds also included the \$825,000 nominee loan to Dean Paul, the related CMS \$300,000 Master Marketing loan to Susan McDougal, and the related CMS \$150,000 loan to Jim Guy Tucker's corporation to buy the Castle Grande utility.

The Castle Grande transactions (and Ward's role in those transactions) were, ultimately, a focus of the federal bank examiners who suspected their fraudulent character. Initially, McDougal and Ward concealed Ward's role in the transaction through the creation of two "cross

notes." When that concealment proved ineffective, they caused the creation of an "option agreement" that succeeded (albeit only for a few months) in concealing the fraud. Some of the legal services Mrs. Clinton performed for Madison Guaranty were used (and misused) by McDougal and Madison Guaranty in their efforts to fend off and deceive federal and state bank regulators.