

materially underreported Commonwealth's non-performing loans, and materially understated and underreported its other real estate owned ("OREO") in its filings with the Commission. In addition, throughout this period, Commonwealth and its executives misleadingly touted Commonwealth's asset quality, underwriting practices, credit monitoring and adequacy of its ALLL based on current collateral values in Commonwealth's filings and earnings releases. Both the ALLL and OREO were materially important metrics for evaluating a bank like Commonwealth.

2. The consistent message in Commonwealth's filings and public statements was that Commonwealth's portfolio of loans was conservatively managed according to strict underwriting standards aimed at keeping Commonwealth's loan losses low during a time of unprecedented economic turmoil. In reality, internal practice deviated so much from what the investing public was told that, beginning in 2008, Commonwealth understated its ALLL by approximately 17% to 25% with a corresponding understatement to its reported loss before income taxes for fiscal year 2008 of approximately 64%, understated its OREO in two quarters by approximately 19% to 20% with a corresponding understatement of Commonwealth's reported loss before income taxes in the first quarter of 2010 of approximately 35%, and underreported its total non-performing loans throughout the entire period by at least 30%.

3. Woodard, Commonwealth's then Chairman of the Board, President and Chief Executive Officer, knew of the true state of the Bank's loan portfolio and was involved in the activity to hide the deterioration of many of the loans at issue. He was also responsible for the misleading public statements and in particular those in earnings releases. Fields, then a Commonwealth Executive Vice President and Senior Commercial Loan Officer with the largest portfolio of loans, knowingly engaged in the activity that masked the Bank's rapidly

deteriorating loan portfolio. Sabol, then Commonwealth's Chief Financial Officer, knew of the masking practices, and knew, or was reckless in not knowing, of the effect of these practices on Commonwealth's financial statements and disclosures.

4. By the time Woodard and Fields left Commonwealth at the end of 2010, the Bank had become so critically undercapitalized that state banking regulators closed the Bank, sold substantially all of its assets to another bank, and appointed the Federal Deposit Insurance Corporation (the "FDIC") as receiver.

5. By engaging in the misconduct described herein, Woodard, Sabol and Fields violated, or aided and abetted others in the violation of, the antifraud, reporting, internal controls, and record-keeping provisions of the federal securities laws. For these violations, the Commission seeks a judgment against all three defendants ordering injunctive relief, civil penalties, permanent officer and director bars, and other appropriate and necessary equitable relief.

JURISDICTION AND VENUE

6. This Court has jurisdiction over this action pursuant to Securities Act of 1933 (the "Securities Act") Section 22(a) [15 U.S.C. § 77v(a)] and Securities Exchange Act of 1934 (the "Exchange Act") Sections 21(d), 21(e), and 27 [15 U.S.C. §§ 78u(d), 78u(e), and 78aa] and 28 U.S.C. § 1331.

7. Venue is proper in this Court pursuant to Securities Act Section 22(a) [15 U.S.C. §77v(a)] and Exchange Act Section 27 [15 U.S.C. § 78aa] because certain of the acts, practices, transactions and courses of business constituting the violations alleged herein occurred within this judicial district.

8. In connection with the transactions, acts, practices and courses of business alleged in this Complaint, Woodard, Sabol and Fields have directly or indirectly made use of the means or instrumentalities of interstate commerce, of the mails, or of the facilities of a national securities exchange in connection with the transactions, acts, practices, and courses of business alleged in this Complaint.

DEFENDANTS

9. **Edward J. Woodard, Jr.**, age 69, is a resident of Norfolk, Virginia. From in or about 1987 through December 31, 2010, he was a director, Chairman of the Board of Directors (the "Board"), President and Chief Executive Officer (the "CEO") of Commonwealth. On April 20, 2010, Commonwealth's Board replaced Woodard as Chairman of the Board. Woodard continued to serve as a director on Commonwealth's Board until December 31, 2010, when he retired from his positions as director, President and CEO of Commonwealth. In 2008, Commonwealth paid Woodard a salary in the amount of \$575,250, contributed to his pension and deferred compensation in the amount of \$117,594, and paid him other compensation in the amount of \$6,339, bringing his total compensation to \$699,183. In 2009, Commonwealth paid Woodard a salary in the amount of \$571,250 and other compensation in the amount of \$4,839, bringing his total compensation to \$576,089. In 2010, Commonwealth paid Woodard a salary in the amount of \$530,000 and other compensation in the amount of \$923,991, bringing his total compensation to \$1,453,991. Woodard invoked his Fifth Amendment right against self-incrimination during testimony in the Commission's investigation.

10. **Cynthia A. Sabol**, age 49, is a resident of Virginia Beach, Virginia. From in or about February 2004 through September 23, 2011, Sabol was Commonwealth's Executive Vice President (an "EVP"), Chief Financial Officer (the "CFO"), Secretary and principal accounting

officer. Sabol ceased to be employed by Commonwealth after the bank's closure. In 2008, Commonwealth paid Sabol a salary in the amount of \$212,000, contributed to her pension and deferred compensation in the amount of \$45,152, and paid her other compensation in the amount of \$5,425, bringing her total compensation to \$262,577. In 2009, Sabol received the same salary and pension and deferred compensation benefit from Commonwealth but received other compensation in the amount of \$703, bringing her total compensation to \$257,855. In 2010, Commonwealth paid Sabol a salary in the amount of \$212,000 and other compensation in the amount of \$126,189, bringing her total compensation to \$338,189. Sabol is a certified public accountant licensed to practice in Virginia, and her license still is active. Sabol invoked her Fifth Amendment right against self-incrimination during testimony in the Commission's investigation.

11. **Stephen G. Fields**, age 49, is a resident of Chesapeake, Virginia. From in or about December 2003 through December 2004, Fields was Senior Vice President and Commercial Loan Officer of Commonwealth. In or about December 2004, Woodard promoted Fields to EVP and Commercial Loan Officer. Fields held that position until December 9, 2010, when Commonwealth terminated Fields' employment. Prior to being employed by Commonwealth, Fields was employed as a bank examiner with the Federal Reserve Bank of Richmond. Fields invoked his Fifth Amendment right against self-incrimination during testimony in the Commission's investigation.

ISSUER

12. **Commonwealth Bankshares, Inc.**, a bank holding company, is a Virginia corporation with its principal place of business in Norfolk, Virginia. Commonwealth's common stock was registered with the Commission under Exchange Act Section 12(b) at all relevant times and was listed on the NASDAQ Stock Market LLC ("NASDAQ"). Commonwealth

primarily conducted its business through the Bank, a Virginia state-chartered commercial bank and a wholly-owned banking subsidiary of Commonwealth, whose financial statements were consolidated into Commonwealth's financial statements.

13. On June 18, 2007, Commonwealth filed a Form S-3 with the Commission to register approximately one million shares of Commonwealth's common stock that certain shareholders previously had acquired pursuant to a private placement so that those shareholders could sell their stock on the open market. On June 27 and 28, 2007, respectively, Commonwealth filed Forms S-8 with the Commission to register approximately 800,000 shares of Commonwealth's common stock as part of its 401(k) Profit Sharing Plan. Each of these documents specifically incorporated Commonwealth's annual, periodic and current filings with the Commission, including all filings Commonwealth made during the relevant period. Additionally, at all times relevant to this complaint, the offerings described in the Form S-3 and the Forms S-8 continued to be in effect.

14. On April 15, 2011, Commonwealth filed with the Commission its Form 10-K for the year ended December 31, 2010, which was its last annual report. In that Form 10-K, Commonwealth reported that, as of June 30, 2010, the aggregate market value of the voting and non-voting common equity held by its non-affiliates was approximately \$18 million and, as of March 25, 2011, there were approximately 7 million shares of common stock outstanding.

15. On August 15, 2011, Commonwealth filed with the Commission its Form 10-Q for the quarter ended June 30, 2011, which was its last periodic filing.

16. On September 23, 2011, the Virginia State Corporation Commission's Bureau of Financial Institutions (the "SCC") and the Federal Deposit Insurance Corporation (the "FDIC"), which insured the deposits held by the Bank, closed the Bank and entered into a purchase and

assumption agreement with a subsidiary of a privately held bank holding company to assume the deposits of the Bank. Commonwealth's common stock closed trading that day at \$0.11.

17. On September 26, 2011, the next trading day following the SCC's and FDIC's closure of the Bank, Commonwealth's common stock closed at \$0.05, or 55% lower than the previous close.

18. On November 11, 2011, NASDAQ filed a Form 25 with the Commission, in which it stated that it had delisted Commonwealth's common stock from the NASDAQ exchange for failing to satisfy the exchange's requirements.

FACTUAL ALLEGATIONS

Background

19. In 1987, Woodard created Commonwealth and took it public. Under Woodard's leadership, Commonwealth grew from an institution with minimal profits to a major regional bank that reported record profits nearly every year. By 2006, Commonwealth's assets had grown to approximately \$715 million, of which the Bank's loan portfolio accounted for \$670 million.

20. In July 2006, Woodard adopted a strategic plan for Commonwealth, a principal goal of which was to reach one billion in assets by December 31, 2009. As part of this goal, Commonwealth began to make substantially more construction and development loans than it previously had made. By December 31, 2006, Commonwealth's exposure to such loans climbed to approximately \$179 million, or 27%, of gross loans. Commonwealth's exposure to construction and development loans continued to climb in 2007 and 2008, when its exposure to such loans amounted to approximately \$223 million, or 28%, and \$295 million, or 29%, of gross loans, respectively. Virtually all of Commonwealth's construction and development loans related to properties located in Norfolk and Virginia Beach, Virginia.

21. On September 3, 2008, Woodard announced that Commonwealth had exceeded assets of approximately one billion more than a year before the date contemplated in the July 2006 strategic plan.

22. Beginning in or about 2006, the Norfolk commercial real estate market began to show signs of distress. As time progressed, the market trends continued to worsen. Condominiums and office space were particularly hit. At the end of 2008, office space and condominium prices were both down approximately 10% from 2007 nationally. At the end of 2009, the trend had worsened for these two categories of real estate, with office space prices down approximately 23% and condominium prices down approximately 22% nationally.

The Financial Fraud at Commonwealth

23. The financial fraud at Commonwealth arose primarily from the understatement of Commonwealth's ALLL and OREO with respect to two loans. Both loans were real estate development loans; one loan was originated to renovate and convert a hundred-year defunct hotel located in downtown Norfolk, Virginia into condominiums and then office space, while the other loan was originated to develop condominiums. The effect of these understatements was to materially understate Commonwealth's ALLL for the years ended December 31, 2008 and 2009, its OREO for the quarters ended March 31 and June 30, 2010, and its reported loss before income taxes for the year ended December 31, 2008 (relating to the understatement of the ALLL) and for the quarter ended March 31, 2010 (relating to the understatement of OREO).

24. Both the ALLL and OREO were financial disclosures that were important to investors. For Commonwealth, these two metrics took on even greater importance, as total loans comprised approximately 94% and 81% of its total assets in 2008 and 2009, respectively.

***Commonwealth Understated its ALLL for the Years Ended December 31, 2008
and 2009 and its Loss Before Income Taxes for the Year Ended December 31, 2008***

Legal and Accounting Requirements for ALLL

25. The ALLL is an estimate of probable losses that reduces the book value of loans and leases to the amount that is expected to be collected. The ALLL is a materially important financial metric for banks whose principal assets are loans. Inasmuch as the ALLL represents the bank's assessment of probable losses on its loans, increases to the ALLL reflect an assessed deterioration of its loan portfolio. In addition, any increase in the ALLL (a balance sheet item) is accompanied by the recording of a provision for loan losses (an income statement item), thereby impacting a company's reported income or losses.

26. Both banking regulators and the Commission have emphasized the importance of the ALLL to bank financial disclosure. For example, on December 13, 2006, the Board of Governors of the Federal Reserve System, the FDIC, the Office of the Comptroller of the Currency, the Office of Thrift Supervision, and the National Credit Union Administration issued the *Interagency Policy Statement on the Allowance for Loan and Lease Losses*, in which they stated that the ALLL "represents one of the most significant estimates in an institution's financial statements and regulatory reports." In the wake of the financial crisis, in August 2009, the Commission's Division of Corporation Finance sent an illustrative letter to the CFOs of certain public companies, a sample of which it posted on the Commission's website, stating that "[c]lear and transparent disclosure about how you account for your provision and allowance for loan losses has always been critically important to an investor's understanding of your financial statements."

27. Under generally accepted accounting principles ("GAAP"), Commonwealth was required to assess probable losses associated with its impaired loans. GAAP states that a loan is

impaired when “it is probable that the creditor will be unable to collect all amounts due according to the contractual terms of the loan agreement.” Accounting Standards Codification (“ASC”) 310-10-35-16. If a loan is impaired, the bank must measure the amount of impairment and record a loan loss expense with a corresponding increase to the ALLL. GAAP further provides that “a creditor shall measure impairment based on the present value of expected future cash flows discounted at the loan’s effective interest rate, except that as a practical expedient, a creditor may measure impairment based on a loan’s observable market price, or the fair value of the collateral if the loan is a collateral-dependent loan.” ASC 310-10-35-22. GAAP permits the impairment on collateral dependent-loans to be measured using the fair value of the collateral, less cost to sell. ASC 310-10-35-23.

28. Thus, a key consideration for whether additional loss provisions are required under GAAP for impaired loans is the “fair value” of the collateral. GAAP defines fair value as “[t]he price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.” ASC 820-10-35-2. Although GAAP does not specify the precise manner in which fair value is to be determined, fair value is measured from the perspective of factors considered by market participants. In commercial real estate, it is widely recognized that the most persuasive evidence (absent an actual sale) is a recent appraisal performed by an independent and certified real estate appraiser. Commission Staff Accounting Bulletin No. 102, 66 Fed. Reg. 36,457, 36,462 n.44 (July 6, 2001). In the absence of a current appraisal, other forms of evidence have to be used, but all information known at the time must be considered. ASC 450-20-25-6. Commonwealth’s written lending policy provided that a written appraisal was the only way to determine the fair value of collateral securing collateral-dependent loans.

29. Commonwealth was required, by Item 7 of Rule 9-03 of Commission Regulation S-X, to record its ALLL as a line item on its consolidated balance sheet. Any increase in ALLL must be accompanied by the recording of a provision for loan losses (an income statement item), thereby increasing reported losses before income taxes.

Woodard, Sabol and Fields Were Responsible for Commonwealth's ALLL

30. During the relevant period, Woodard and Sabol were responsible for Commonwealth's ALLL. As Chairman of Commonwealth's Board, Woodard attended Board meetings where the ALLL was presented and approved the ALLL for inclusion in Commonwealth's financial statements. Woodard, along with Sabol, signed each of Commonwealth's annual and quarterly reports on Commonwealth's behalf and signed a certification attached as an exhibit to each report certifying, among other things, that he had read the report and, based on his knowledge, "the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant [Commonwealth] as of, and for, the periods presented in this report." Thus, Woodard, along with Sabol, was ultimately responsible for the proper and accurate reporting of Commonwealth's financial condition to the investing public.

31. As CFO, Sabol oversaw and was responsible for the calculation and accuracy of the ALLL. Like Woodard, Sabol signed each of Commonwealth's annual and quarterly reports on Commonwealth's behalf and signed a certification attached as an exhibit to each report certifying, among other things, that she had read the report and, based on her knowledge, "the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant [Commonwealth] as of, and for, the periods presented in this report." Thus, Sabol, along with

Woodard, was ultimately responsible for the proper and accurate reporting of Commonwealth's financial condition to the investing public.

32. During the relevant period, Fields also had responsibility for Commonwealth's ALLL. For the year ended December 31, 2008, Fields prepared the initial calculation of the ALLL and presented it to the Board for its approval. Beginning with the reporting period ended March 31, 2009, Fields did not perform the initial ALLL calculation, but he was responsible for obtaining the documentation supporting the loans and any impairment to be recorded, including the appraisals valuing the collateral.

Commonwealth's Understated ALLL and Loss Before Income Taxes – 345 Granby Street

33. George P. Hranowskyj ("Hranowskyj") and Eric H. Menden ("Menden") were business partners who owned and operated numerous real estate investment and development entities. Throughout the relevant period, Hranowskyj and Menden were so-called "friends of the bank," an internal designation given to certain troubled borrowers who performed favors to personally benefit Commonwealth officers. Together, Hranowskyj and Menden purchased, or attempted to purchase, foreclosed property or property owned by Woodard's son on at least 12 occasions between in or about 2008 and 2010 with financing provided by Commonwealth. In exchange, Woodard and Fields caused Commonwealth to provide Hranowskyj and Menden with lower interest rates and additional loans that Hranowskyj and Menden used to keep their businesses afloat and for personal purposes.

34. In 2006, Hranowskyj and Menden obtained a \$16 million construction loan from Commonwealth for the purchase and renovation of a defunct hotel, located at 345 Granby Street, Norfolk, Virginia ("345 Granby Street") into condominiums (the "345 Granby loan"). Loan proceeds were to be disbursed as work progressed on the renovation of 345 Granby Street. Total

loans to Hranowskyj and Menden fluctuated between approximately \$37 million and \$41 million, and represented Commonwealth's largest loan relationship and the 345 Granby Street loan was the Bank's single largest loan.

35. The 345 Granby loan was a collateral-dependent loan under GAAP because it was "[a] loan for which the repayment is expected to be provided solely by the underlying collateral." ASC Master Glossary.

36. Shortly after Commonwealth originated the 345 Granby loan, the Norfolk condominium market began to soften and, as a result, Hranowskyj and Menden changed the renovation plans from condominiums to office space. By changing the renovation plans, Hranowskyj and Menden incurred unanticipated additional costs, and the project was stalled as of mid-2008.

37. In 2008, Hranowskyj and Menden sought – and received – full funding of the \$16 million loan facility. In order to obtain the full \$16 million, Commonwealth required a re-appraisal of the historic building that served as the primary collateral for the loan. Fields ordered a re-appraisal of 345 Granby Street and instructed the appraiser to provide a value for the property "as stabilized." "As stabilized" appraisals project the value of the completed project with stabilized occupancy. The resulting appraisal, dated May 31, 2008, valued the building upon completion and stabilized occupancy at approximately \$20 million (the "345 Granby Street appraisal").

38. The 345 Granby Street appraisal overvalued 345 Granby Street based on the following incorrect assumptions:

a. The 345 Granby Street appraisal provided an “as stabilized” value but did not deduct the cost to complete from the as completed value. By mid-2009, the renovation of the building was only between 60% and 65% complete.

b. The 345 Granby Street appraisal included, as gross building area and net rentable space, approximately 5,000 square feet of basement crawl space that had low ceilings, no windows, and for which the rental rate that could be achieved in the market if finished to standard build out was not high enough to warrant the expenditure.

c. The 345 Granby Street appraisal treated undeveloped space on five floors as developed.

d. The 345 Granby Street appraisal based the calculation of the dollar value of the net rentable area on comparable sales that included newer Class A office buildings when the building was more properly compared to Class B or C office buildings.

39. Menden knew the 345 Granby Street appraisal overvalued the property because of each of the issues alleged above in Paragraph 38. He had multiple contemporaneous conversations with Fields and also with Woodard in which he conveyed his concern that the property was significantly overvalued and the basis for his concern.

40. As alleged below in Paragraphs 41 through 51, Sabol knew, or was reckless in not knowing, that there were issues with the valuation of 345 Granby Street.

41. In 2009, Commonwealth’s internal auditor raised concerns to Sabol and Woodard about the 345 Granby loan. Specifically, on March 9, 2009, the internal auditor noted that loan files, including the 345 Granby loan file, lacked sufficient documentation to assess impairment on the loan. Separately, on July 3, 2009, the internal auditor conducted a review of the loan files for the 345 Granby loan and alerted Woodard and Sabol to a number of significant issues relating

to the loan and the reliability of its valuation. Specifically, he noted the lack of documentation supporting the basis for the disbursements on the loan, what the project would cost to complete and what income might be expected when it was complete. He also raised several potential problems with the 2008 appraisal. He noted that the sales comparables used in the 2008 appraisal, which were from 2007, were too old to be reliable given the negative impact of the financial recession on the local commercial rental market. He further noted that the appraisal's cost approach "seriously limits the Bank's ability to determine if the Bank of the Commonwealth is over funding a construction project." He recommended that more accurate and current data be obtained before any more funds were released.

42. On July 6, 2009, in an email on which Sabol was copied, the internal auditor again raised concerns to Commonwealth's Vice President of Credit Administration that the total Hranowskyj and Menden loan exposure was in excess of approximately \$30 million, which exceeded the maximum amount of credit that Commonwealth legally could extend to a single borrower or loan relationship by over approximately \$10 million. Again, the internal auditor warned that no further funds should be advanced to Hranowskyj or Menden until the issue of the lending limit was resolved.

43. Despite the internal auditor's concern on July 8, 2009, Commonwealth made available up to \$1.9 million to Hranowskyj and Menden for the renovations of 345 Granby Street. The loan was approved at an executive loan committee chaired by Woodard on that date, the minutes of which were reviewed and approved of at a Board meeting on August 18, 2009, which Woodard chaired and Sabol attended.

44. Also in 2009, two separate independent credit consultants raised concerns to Woodard and Sabol about the credit quality of the entire Hranowskyj and Menden loan

relationship, including the 345 Granby loan. Specifically, in August 2009, one consultant prepared a report summarizing its review of 260 borrowers representing approximately 60% of the Bank's total loan portfolio. Hranowskyj's and Menden's loans, including the 345 Granby loan, were among the loans the consultant individually reviewed. Regarding the 345 Granby loan, the consultant highlighted the fact that the appraisal that valued the collateral securing the loan reflected only the "as stabilized" value, which was "not the appropriate value to obtain for a project that will be vacant upon completion of renovation." The credit consultant also told Woodard and Sabol that the Hranowskyj and Menden loan relationship had experienced delinquency, that the collateral pledged might not fully protect the bank in the event of default, and that the relationship was not being monitored effectively. Then, in October 2009, a second credit consultant reviewing Commonwealth's loans also raised concerns regarding Hranowskyj's and Menden's loans, including the 345 Granby loan, to Sabol, citing, among other things, the low quality of the financial information on file, insufficient cash flow coverage, Hranowskyj's and Menden's demonstrated inability to repay the principal on their loans, and consistent late payments by the guarantors on their loans. The credit consultant concluded that the collateral value of 345 Granby Street "as is" was insufficient to cover outstanding debt and that "collateral shortfall currently exists for 'as is' value."

45. Sabol also knew, or was reckless in not knowing, that Hranowskyj and Menden were experiencing financial difficulties. She knew, or was reckless in not knowing, they were having difficulty meeting their payment obligations and that Fields was taking steps to mask this fact. In November 2009 and January 2010, the internal auditor alerted Sabol multiple times by e-mail to the fact that demand deposit accounts for Hranowskyj and Menden were overdrawn in

excess of approximately \$620,000 and that the overdrawn amounts were being used to fund the renovations to 345 Granby Street. Sabol did not respond to the internal auditor's e-mails.

46. Commonwealth used the 345 Granby Street appraisal's \$20 million value to calculate impairment on the 345 Granby loan for 2008 through 2009. Because the 345 Granby Street appraisal did not account for the correct square footage, use appropriate comparables or take into account the cost to complete, it did not reflect the fair value of the property, and the resulting impairment calculation was not reasonable.

47. The impairment calculation for the 345 Granby loan caused false entries to be reflected in Commonwealth's books, records and accounts. Specifically, the impairment calculation was embodied in a list of adversely classified assets which was presented to Commonwealth's Board for approval at meetings attended by Woodard, Sabol and Fields. These lists, which served as the basis for Commonwealth's ALLL in its consolidated balance sheets, listed each criticized loan examined for impairment and the impairment associated with each criticized loan. The lists then totaled all of the impairments, and the total of the impairments comprised the individual loan component of the ALLL in Commonwealth's consolidated balance sheets included in the financial statements filed with the Commission. Prior to filing Commonwealth's annual and quarterly reports with the Commission, Sabol presented the final ALLL calculation to Woodard and the rest of the Board at Board meetings for approval.

48. As a consequence of Commonwealth's failure to reasonably calculate impairment with respect to the 345 Granby loan, for the year ended December 31, 2008, Commonwealth understated its ALLL by approximately 25% and its loss before income taxes by approximately 64%. For the year ended December 31, 2009, Commonwealth understated its ALLL by approximately 17%.

49. On January 29, 2010, Commonwealth announced that it intended to restate its ALLL for the period ended September 30, 2009 to increase its ALLL from approximately \$41 million to \$64 million, or a \$23 million increase. Of the \$23 million increase, approximately \$10 million was attributable to downgrades of individual loans and loan relationships. The \$23 million increase did not include any material additional allowance attributable to the 345 Granby loan. Had appropriate allowance been included for the 345 Granby loan, the restatement would have been significantly larger as described in the preceding Paragraph 48.

50. On February 1, 2010, the next trading day following Commonwealth's announcement of its restatement, Commonwealth's stock closed at \$1.73, a \$0.12, or 6%, decline from the prior close.

51. In 2011, new Commonwealth management ordered two new appraisals. The new appraisals, using more appropriate square footage, comparable sales and "as is" values, resulted in dramatically lower values. Those appraisals valued the 345 Granby property "as is" at approximately \$2 million and \$4 million, respectively, and valued it "as if stabilized" at approximately \$4 million and \$6 million, respectively. By in or about April 2011, Commonwealth had written off approximately \$13 million of the \$16 million loan.

52. Based on the facts alleged in Paragraphs 33 through 51, Woodard knew, or was reckless in not knowing, that Commonwealth's ALLL was understated for the years ended December 31, 2008 and 2009, and that Commonwealth's books, records and accounts reflected false entries related to the ALLL. Woodard knew, or was reckless in not knowing, that the 345 Granby loan was significantly impaired and that this impairment was not reflected in the ALLL.

53. Based on the facts alleged in Paragraphs 33 through 51, Sabol knew, or was reckless in not knowing, that Commonwealth's ALLL was understated for the years ended

December 31, 2008 and 2009, and that Commonwealth's books, records and accounts reflected false entries related to the ALLL. Sabol knew, or was reckless in not knowing, that the 345 Granby loan was significantly impaired and that this impairment was not reflected in the ALLL.

54. Based on the facts alleged in Paragraphs 33 through 51, Fields knew that Commonwealth's ALLL was understated for the years ended December 31, 2008 and 2009, and that Commonwealth's books, records and accounts reflected false entries related to the ALLL, because Menden told him that the 2008 appraisal falsely overvalued 345 Granby Street.

Commonwealth Understated its OREO for the Quarters Ended March 31 and June 30, 2010 and its Loss Before Income Taxes for the Quarter Ended March 31, 2010

55. On March 10, 2010, Commonwealth in effect foreclosed on its loan to Pretty Lake Village LLC ("PLV"), a limited liability company set up to develop a condominium project in Norfolk Virginia, when it took possession of the collateral securing the loan pursuant to the terms of a Forbearance and Loan Modification Agreement (the "Forbearance Agreement"). As described below, as a result of this action, Commonwealth understated its "other real estate owned" or "OREO" and its loss before income taxes for the first and second quarters of 2010.

Legal and Accounting Requirements for OREO

56. Generally, the largest component of OREO consists of assets taken in settlement of troubled loans through surrender or foreclosure. Foreclosed assets include all assets received in full or partial satisfaction of a receivable and include real property. Foreclosed assets also include loans that are treated as if the underlying collateral had been foreclosed because the institution has taken possession of the collateral, even though legal foreclosure or repossession proceedings have not taken place. GAAP requires that foreclosed and repossessed assets should be classified as a separate balance sheet amount or included in other assets on the balance sheet with separate disclosures in the notes to the financial statements. ASC 310-10-45-3. OREO was

a materially important financial metric to investors evaluating Commonwealth. For issuers like Commonwealth, increasing OREO levels reflected an increase in loans being foreclosed on and thus reflected deterioration of the Bank's loan portfolio.

57. Since the Forbearance Agreement resulted in Commonwealth, in satisfaction of the loan to PLV, taking physical possession of portions of the PLV property, under the facts alleged here, GAAP required the property received (*i.e.*, OREO) to be recognized at fair value less cost to sell. ASC 310-40-40-2. GAAP required Commonwealth to record any excess of the recorded investment in the loan above the fair value of the property less cost to sell as a loss.

58. Rule 9-03 Item 10(4) of Regulation S-X required Commonwealth to record OREO as a line item on its consolidated balance sheet if OREO exceeded 30% of stockholders' equity, which OREO did for Commonwealth during the relevant period. Rule 9-04 Item 14(d) of Regulation S-X required Commonwealth to record on its income statement any loss on OREO. If the fair value of the OREO, less cost to sell, was less than the unpaid principal balance of the loan, an increase in OREO must be accompanied by the recording of a loss on OREO (an income statement item), thereby increasing losses before income taxes.

Woodard and Sabol Were Responsible for Commonwealth's OREO

59. As Commonwealth's CEO and CFO, Woodard and Sabol, were ultimately responsible for the proper and accurate reporting of Commonwealth's financial condition to the investing public. Both signed each of Commonwealth's annual and quarterly reports on Commonwealth's behalf and signed a certification attached as an exhibit to each report certifying, among other things, that each had read the report and, based on each of their knowledge, Commonwealth's financial statements, which included line items for OREO on its balance sheet and loss on OREO in its income statement, fairly presented in all material respects

the financial condition, results of operations and cash flows of Commonwealth for the period covered by the report.

Commonwealth's Understated OREO and Loss Before Income Taxes – PLV

60. On November 23, 2005, Commonwealth approved a loan in the amount of \$11 million to PLV to develop condominiums in Norfolk, Virginia (the "PLV loan"). The PLV loan was a collateral-dependent loan under GAAP because it was "[a] loan for which the repayment is expected to be provided solely by the underlying collateral." ASC Master Glossary. By in or about December 2007, PLV had drawn down virtually the entire \$11 million loan.

61. During the course of the project, the condominium market in Norfolk declined dramatically. As of late 2007, only four of the 29 units had been sold, and many others remained under construction.

62. As of early 2008, Woodard and Sabol knew, or were reckless in not knowing, that the PLV loan was experiencing severe distress and was at risk for failure. On February 15, 2008, Commonwealth modified the PLV loan and lent an additional approximately \$2 million in exchange for the pledge of additional collateral. A month-and-a-half later, on March 26, 2008, Woodard approved the modification to the PLV loan at a loan executive committee meeting that he chaired. On April 15, 2008, Woodard and the Board reviewed the modification to the PLV loan during a meeting Sabol attended.

63. On October 25, 2008, Commonwealth purportedly obtained an updated appraisal for PLV which valued the collateral at approximately \$9 million.

64. On November 5, 2008, at a meeting Sabol attended, Woodard and the Board approved the classification of the PLV loan as non-accrual, which signified that the prospect for payment in full of principal and interest was in doubt. At the same meeting, Woodard and the

Board also approved classifying the PLV loan as a "Substandard Non-Accrual" loan on the adversely classified assets list. The PLV loan continued to be reported as a substandard non-accrual loan on lists reviewed and approved by Woodard and the Board meetings that followed that Sabol also attended.

65. On June 17, 2009, Woodard approved Commonwealth's write-down of approximately \$2 million of the PLV loan's unpaid principal balance at a loan executive committee meeting that he chaired. The \$2 million write-down lowered the unpaid principal balance on the PLV loan to approximately \$8 million. On July 28, 2009, Woodard and the Board reviewed the \$2 million write-down during a meeting Sabol attended.

66. By the end of 2009, the challenging condominium market continued and Commonwealth evaluated the PLV loan for impairment. In doing so, it valued the collateral using the amount purportedly reflected in an October 2008 collateral valuation, found there to be no impairment, and did not record any allowance for the PLV loan.

67. By early 2010, the PLV loan continued to experience severe financial difficulties and Commonwealth and PLV's principals began to explore workout scenarios with Commonwealth. Prior to the execution of the Forbearance Agreement, Woodard met with PLV's principals on at least two occasions to discuss workout scenarios. During those meetings, Woodard was told about PLV's financial difficulties and of the negotiations surrounding the Forbearance Agreement.

68. On March 8, 2010, two days prior to the execution of the Forbearance Agreement, Woodard signed a memorandum addressed to Commonwealth's closing department authorizing the department to release for closing the loan package relating to the PLV guarantors' and principals' purchase of the 11 completed units.

69. On March 10, 2010, Commonwealth entered into the Forbearance Agreement with PLV's principals. The Forbearance Agreement released PLV's principals and guarantors from the loan in exchange for PLV's principals and guarantors purchasing 11 completed units, thereby reducing the collateral securing the PLV loan from 29 units to 14 units. Commonwealth financed the principals' and guarantors' purchase of the completed units. The Forbearance Agreement was effectively a foreclosure and essentially converted the remaining units into OREO because, after execution of the Forbearance Agreement, Commonwealth had actual possession of the collateral.

70. Following the execution of the Forbearance Agreement, Commonwealth reduced the unpaid principal balance on the PLV loan as of March 31, 2010, from approximately \$8 million to approximately \$4 million. Commonwealth did not record any impairment on PLV for the quarters ended March 31 or June 30, 2010.

71. Following the execution of the Forbearance Agreement, Woodard and Sabol knew, or were reckless in not knowing, that Commonwealth had taken possession of PLV and was treating the remaining PLV units as though they were owned by Commonwealth. Commonwealth had the keys to the remaining units. Commonwealth also hired a real estate agent to market the unfinished units in Commonwealth's possession and hired vendors to make cosmetic repairs and complete the unfinished units. From March 26, 2010 through August 27, 2010, Commonwealth disbursed at least \$150,000 to various vendors as payment for painting, repairing and completing the remaining units. Woodard selected the general contractor to coordinate the vendors and participated in meetings to select the vendors. Woodard signed off on virtually all of these payments. Additionally, Sabol reviewed and approved the booking of these disbursements in Commonwealth's general ledger.

72. On April 4, 2010, Commonwealth's internal auditor sent a memorandum to Commonwealth's audit committee, a copy of which Sabol received, in which he reported, among other things, that "[m]anagement disclosed to Audit that during 2010 the Bank will refinance the original credit by adding another borrower and then sell the remaining units to other parties by offering Bank-offered financing."

73. Commonwealth did not classify PLV as OREO until May 31, 2011. Commonwealth's failure to classify PLV as OREO during the quarters ended March 31 and June 30, 2010 caused it to understate its OREO in its financial statements by approximately 19% and 20%, respectively.

74. The understatement of OREO caused a corresponding understatement of Commonwealth's loss before income taxes for the quarter ended March 31, 2010 of approximately 35%.

75. Based on the facts alleged in Paragraphs 60 through 74, Woodard knew, or was reckless in not knowing, that Commonwealth's OREO was understated for the quarters ended March 31 and June 30, 2010, and that the books, records and accounts relating to Commonwealth's OREO were false because he knew that the PLV loan was experiencing severe distress and was at risk for failure; that Commonwealth was exploring workout scenarios that included the Forbearance Agreement; and that, following the execution of the Forbearance Agreement, that Commonwealth had taken possession of PLV and was treating the remaining PLV units as though they were owned by Commonwealth.

76. Based on the facts alleged in Paragraphs 60 through 74, Sabol knew, or was reckless in not knowing, that Commonwealth's OREO was understated for the quarters ended March 31 and June 30, 2010, and that the books, records and accounts relating to

Commonwealth's OREO were false because she knew that the PLV loan was experiencing severe distress and was at risk for failure and that, following the execution of the Forbearance Agreement, that Commonwealth had taken possession of PLV and was treating the remaining PLV units as though they were owned by Commonwealth.

The Disclosure Fraud at Commonwealth

77. In addition to the financial fraud, Commonwealth also (1) underreported its exposure to non-performing loans, (2) underreported its exposure to OREO, and (3) made false and misleading disclosures in its Management Discussion and Analysis section (the "MD&A") and elsewhere regarding asset quality, underwriting practices and overall financial health.

Rules Regarding Disclosures

78. Regulation S-K Item 303(a) required Commonwealth to discuss in its public filings any "information that the registrant believes to be necessary to an understanding of its financial condition [or] changes in its financial condition." 17 C.F.R. § 229.303(a). Instruction 13 to Item 303(a) provided that "[t]he attention of bank holding companies is directed to the information called for in Guide 3." *Id.* § 229.303(a) Instruction no. 13. Item III.C.1 of Industry Guide 3 requested bank holding companies, like Commonwealth, to disclose certain information about loan portfolios, either in tables within the description of the business or in the MD&A section of its filings with the Commission. Sec. & Exchange Comm'n, *Securities Act Industry Guides, Statistical Disclosure by Bank Holding Companies ("Guide 3")* at 7-8, available at <http://www.sec.gov/about/forms/industryguides.pdf>. This information included, among other things, non-accrual loans and accruing loans that are 90 days past due. *Id.* In addition, Item III.C.2 sought disclosure of loans "where known information about possible credit problems of borrowers . . . causes management to have serious doubts as to the ability of such borrowers to

comply with the present loan repayment terms and which may result in disclosure of such loans pursuant to Item III.C.1.” *Id.* at 8. Instruction 13 related to full fiscal years but also called for information for interim periods if the information was necessary to keep the information from being misleading. 17 C.F.R. § 229.303(a) Instruction no. 13.

79. Pursuant to the provisions described above in Paragraph 78, Commonwealth disclosed loans it deemed to be non-accrual in its disclosure of non-performing loans.

80. Commonwealth had no legal obligation to make additive disclosures concerning asset quality, underwriting practices and overall financial health but, having spoken on such subjects, it had a duty to speak accurately and completely.

Woodard and Sabol Were Responsible for Commonwealth’s Disclosures

81. During the relevant period, Woodard and Sabol were responsible for Commonwealth’s disclosures. As Commonwealth’s CEO and CFO, Woodard and Sabol, were ultimately responsible for the accurate reporting of Commonwealth’s financial condition in its public filings and statements and for ensuring that Commonwealth’s books, records and accounts were accurate. Both Woodard and Sabol signed each of Commonwealth’s annual and quarterly reports on Commonwealth’s behalf and each signed a separate certification attached as an exhibit to each report stating, among other things, that each of them had reviewed the report and, based on each of their knowledge, the report did not contain any untrue statement of a material fact or omit to state a material fact. Sabol also signed Commonwealth’s current reports on Commonwealth’s behalf which, among other things, furnished copies of earnings releases to the Commission.

Commonwealth Underreported its Nonperforming Loans

82. From November 6, 2008 through August 16, 2010, Commonwealth underreported its non-performing loans.

83. Commonwealth's reporting of its non-performing loans began with what was known as a past due report, which was one of Commonwealth's books, records and accounts. The past due report was an internal list of all loans that were in default of principal or interest for at least 30 days, as well as all loans classified as non-accrual.

84. Commonwealth's written lending policy directed loan officers to classify loans as non-accrual when, among other things, (a) "[t]he loan is in default of principal or interest for a period of 90 days or more, unless the loan is both well secured and in the process of collection" or (b) the "[p]rospect for payment in full of principal and interest is in doubt."

85. Commonwealth generated a draft of the past due report each month. After the draft was generated, the Commonwealth employee who prepared the report reviewed the report with loan officers to see if there was a reason why a loan that appeared to be past due or non-accrual should not be classified as such. If a loan officer asked for a loan classified as past due or non-accrual on the report to be removed from the report, the removal was called an administrative removal.

86. One of the main bases for removing loans from the past due report were change-in-terms agreements, or "CITAs," as they were known within Commonwealth. CITAs were short-form loan modification documents that loan officers generated to extend the maturity date of loans or to extend additional credit without having to submit the loan for the same review and approval process as newly originated loans. If a loan officer presented the Commonwealth

employee who prepared the draft past due report with a CITA, the loan would be administratively removed from the past due report.

87. After the loan officers had reviewed the past due report and loans with CITAs had been administratively removed from the report, the report was presented to Commonwealth's Board for the Board's review and approval.

88. On a quarterly and annual basis, once the report had been approved by the Board, Commonwealth's accounting department used the report to prepare the disclosures in Commonwealth's quarterly and annual filings of the dollar value of all loans past due for 90 days or more and all loans classified as non-accrual. The sum of these two numerical disclosures were, in turn, disclosed in Commonwealth's quarterly and annual filings as non-performing loans, which Commonwealth defined in its written disclosures as "loans accounted for on a non-accrual basis (as judgmentally determined by management based upon anticipated realization of interest income) [and] loans which are contractually past due 90 days."

89. During the relevant period, Commonwealth executed a large number of CITAs around the end of the quarter to improperly administratively remove loans from the past due report for at least two large loan relationships. Commonwealth executed at least 129 CITAs for loans made to Hranowskyj and Menden which, as alleged above in Paragraph 34, was one of Commonwealth's largest loan relationships. Commonwealth also executed at least 91 CITAs for loans made to individuals or entities associated with Thomas E. Arney ("Arney"), who owned several local businesses.

90. Like Hranowskyj and Menden, throughout the relevant period, Arney also was a "friend of the bank," an internal designation given to certain troubled borrowers who performed favors for Commonwealth officers, including favors to personally benefit Commonwealth

officers. Arney purchased, or attempted to purchase, OREO property or property owned by Woodard on at least four occasions during 2008 through 2010 with financing provided by Commonwealth. In exchange, Woodard and Fields caused Commonwealth to provide Arney with additional loans that Arney used to keep his businesses afloat and for personal purposes.

91. The improper use of CITAs with respect to Arney's, Hranowskyj's and Menden's loans masked the fact that they were non-accrual and prevented them from being included as non-performing loans reported in Commonwealth's public filings.

92. Fields executed the CITAs alleged in Paragraph 89 on Commonwealth's behalf and caused them to be removed from the past due report. At the time Fields executed these CITAs, he knew of the following:

- a. That Arney, Hranowskyj and Menden were experiencing severe financial difficulties and could not repay the principal owed at the original maturity date and were having difficulty making interest payments.
- b. That but for the CITAs, Arney, Hranowskyj and Menden would have been 90 or more days contractually past due on interest or principal payments.
- c. Pursuant to Commonwealth's lending policy, the Arney, Hranowskyj and Menden loans were non-accrual because all three were experiencing severe financial difficulties and the prospect for repayment of the loans was in doubt.
- d. That the Arney, Hranowskyj and Menden loans should have been on the past due report.
- e. That the dollar volume of loans listed in the past due report was provided to Commonwealth's Board and was the basis for the amounts reported in

Commonwealth's quarterly and annual filings with the Commission as non-performing loans.

93. As Commonwealth's CEO and Chairman of the Board, Woodard approved the list compiling Commonwealth's non-performing loans that were, in turn, reported in Commonwealth's public filings, which he signed. At the time he did so, he knew, or was reckless in not knowing, of the following:

a. Arney, Hranowskyj and Menden were experiencing extreme financial difficulties and that the prospect for repayment of the loans was in doubt.

b. Arney's, Hranowskyj's and Menden's loans were non-accrual and should have been on the past due report.

c. Fields executed CITAs for Arney's, Hranowskyj's and Menden's loans and was directing that loans be removed from the past due report based on the CITAs.

d. But for the CITAs, Arney's, Hranowskyj's and Menden's loans would have been 90 or more days contractually past due on interest or principal payments.

e. The dollar volume of loans listed in the past due report approved by Commonwealth's Board as 90 days past due and non-accrual was the amount reported in Commonwealth's quarterly and annual filings with the Commission as non-performing loans.

f. Given the size of the Arney, Hranowskyj and Menden loans, that the underreported amounts were material.

94. Sabol, as Commonwealth's CFO, signed its public filings. During the relevant times, she knew, or was reckless in not knowing, of the following:

a. That Fields was executing large amounts of CITAs for the Arney, Hranowskyj and Menden loans.

b. Throughout the relevant period, Sabol received memoranda each month that identified the loans that were being administratively removed from the past due report prior to its presentation to the Board.

c. As early as 2007, internal and external auditors and others raised concerns about the excessive use of CITAs and the possibility that they were being improperly used.

d. On November 5, 2008 and January 20, 2009, Commonwealth's internal auditor informed Sabol that he was concerned about the use of CITAs at Commonwealth and suggested that loan officers were keeping otherwise-impaired loans artificially current through these extensions.

e. Similarly, in early 2009 and early 2010, banking regulators raised concerns that Commonwealth's liberal use of CITAs made it difficult to track the true performance of the loans and could be used to mask problem loans.

f. On March 11, 2010, Commonwealth's external auditor provided Sabol with a summary of concerns with respect to Commonwealth's internal controls, which included the "excessive" use of CITAs.

g. Given the size of the Arney, Hranowskyj and Menden loans, that the underreported amounts were material.

95. Commonwealth's failure to report Arney's, Hranowskyj's and Menden's loans as non-performing caused Commonwealth to underreport its non-performing loans by at least 30%.

Commonwealth Underreported its OREO

96. Commonwealth also disclosed its exposure to OREO in its results of operations. As alleged in Paragraph 81, Woodard and Sabol were responsible for Commonwealth's disclosures, and their responsibility included Commonwealth's written disclosures in its results of operations. During the quarterly periods ended March 31 and June 30, 2010, for the reasons that Commonwealth understated its exposure to OREO in its consolidated balance sheets as alleged in Paragraphs 60 through 76, Commonwealth also underreported its OREO in its results of operations.

97. Based on Paragraphs 60 through 76, Woodard knew, or was reckless in not knowing, that Commonwealth's OREO was underreported for the quarters ended March 31 and June 30, 2010, and that the books, records and accounts were inaccurate for the reasons alleged in Paragraph 75.

98. Based on Paragraphs 60 through 76, Sabol knew, or was reckless in not knowing, that Commonwealth's OREO was underreported for the quarters ended March 31 and June 30, 2010, and that the books, records and accounts were inaccurate for the reasons alleged in Paragraph 76.

***Commonwealth's False and Misleading Disclosures
Regarding Asset Quality and Underwriting Practices***

99. From November 10, 2008 through August 16, 2010, Woodard and Sabol each made public statements that materially misrepresented Commonwealth's underwriting practices and financial health. These public statements were made in Commonwealth's third and fourth quarter 2008 earnings releases, which were furnished to the Commission as exhibits to Forms 8-K filed November 6, 2008, and February 11, 2009, respectively; 7 Forms 10-Q, including an

amended Form 10-Q filed March 31, 2010, and 2 Forms 10-K, all filed between November 6, 2008, and August 16, 2010.

100. For example, Woodard and Sabol each made, or authorized the issuance of by signing, the following statement: "Asset quality remains a top priority for our company and our underwriting standards have always been very stringent." This statement appeared in Commonwealth's third and fourth quarter of 2008 earnings releases, which were furnished to the Commission as exhibits to Forms 8-K filed November 6, 2008 and February 11, 2009, respectively, and in Commonwealth's Form 10-K for the year ended December 31, 2008 (the "2008 10-K").

101. Woodard and Sabol also each made, or authorized the issuance of by signing, the following statement, which appeared in the 2008 10-K: "In response to the downturn, the Company [Commonwealth] has strengthened our underwriting practices and has become selective in seeking new loans and relationships."

102. Woodard and Sabol also each made, or authorized the issuance of by signing, the following statements, which appeared in the 2008 10-K, in Commonwealth's Form 10-K for the year ended December 31, 2009 (the "2009 10-K"), in the Forms 10-Q for the periods ended September 30, 2008, March 31, 2009, June 30, 2009, September 30, 2009, March 31, 2010, and June 30, 2010, and in the Form 10-Q/A for the period ended September 30, 2009:

a. "Management has taken a proactive approach to monitoring these loans and will continue to actively manage these credits to minimize loss."

b. "Based on current collateral values, management believes the specific reserve is adequate to cover any shortfalls resulting from the sale of the underlying collateral."

103. Woodard and Sabol also each made, or authorized, the following statement, which appeared in the 2009 10-K: “In response to the downturn, the Company [Commonwealth] has strengthened our underwriting practices and has been proactively monitoring and managing our existing portfolio.”

104. The statements quotes in Paragraphs 100 through 103 were material to investors since, as alleged in Paragraphs 20 and 24, loans comprised a substantial part of Commonwealth’s business, a reasonable investor would have considered disclosures about Commonwealth’s asset quality, underwriting practices and loan monitoring in deciding whether to invest in Commonwealth.

105. The statements quoted in Paragraphs 100 and 101 were false and misleading because they misleadingly conveyed the impression that Commonwealth stringently vetted loans. In fact, as Woodard and Sabol both knew, or were reckless in not knowing, Commonwealth’s underwriting standards were extremely weak. For example, as alleged below in Paragraphs 108 through 125, Commonwealth funded loans without current financial statements from borrowers, without current or accurate appraisals for collateral securing loans, without completing global cash flow analyses, and without adequate collateral. Each of these underwriting deficiencies was elevated to Woodard and Sabol throughout the relevant period. Furthermore, during the relevant period, as alleged below in Paragraphs 108 through 125, Woodard knew, or was reckless in not knowing, that he was circumventing Commonwealth’s underwriting standards, and both Woodard and Sabol knew, or were reckless in not knowing, that Fields also was doing the same.

106. The statements quoted in Paragraphs 102.a and 103 were false and misleading because they misleadingly promoted the impression that management was actively involved in the evaluation of the loans when, in fact, they were not. In particular, Sabol did little, if

anything, to review the credit analysis that formed the basis for the ALLL. Even criticism from two separate credit consultants retained to evaluate Commonwealth's loans does not appear to have caused Woodard or Sabol to undertake any additional scrutiny. Further, the lack of documentation, a problem both Woodard and Sabol were well aware of, particularly relating to site inspections, the financial health of guarantors and the value of collateral are inconsistent with statements assuring "proactive management." Finally, as alleged in Paragraph 124, Woodard knowingly circumvented Commonwealth's internal controls that prevented the proactive management of the Bank's loan portfolio.

107. The statement quoted in Paragraph 102.b was false and misleading because it misleadingly conveyed the impression that Commonwealth had current collateral values for the majority of its loans when, in fact, it did not. As alleged in more detail in Paragraphs 108 through 125, Commonwealth's external and internal auditors repeatedly flagged the issue of stale appraisals for Woodard and Sabol, particularly highlighting the need for current collateral values in the aftermath of the financial crisis. The specific assurance that Commonwealth had such crucial current information on which to base its reserve assessment, is difficult to characterize as anything but a lie.

Commonwealth's Internal Controls Violations

108. The financial and disclosure fraud alleged above in Paragraphs 23 through 107 occurred alongside fundamental control problems with respect to obtaining and maintaining critical documentation, all of which were in violation of Commonwealth's written lending policy. In particular, Commonwealth lacked appraisals supporting the fair value of collateral securing construction and development loans, guarantor financial information and reports

reflecting site inspections, all required by Commonwealth's written lending policy and crucial for Commonwealth's accurate financial reporting.

109. Commonwealth's written lending policy required loan officers to obtain appraisals at loan origination and reappraisals as dictated by market factors and the condition and quality of the loan. Commonwealth's written lending policy also required loan officers to obtain and update financial information from loan guarantors and to inspect projects to determine their current status.

110. As CEO and CFO of Commonwealth, respectively, Woodard and Sabol were ultimately responsible for designing, implementing and monitoring Commonwealth's internal accounting controls. Furthermore, as an employee of Commonwealth, Fields was required to conduct business within the limits established by Commonwealth's internal controls.

111. During the reporting periods relevant to this Complaint, as Commonwealth acquired more construction and development loans to meet Woodard's goal of becoming a "billion-dollar bank," Fields and other senior loan officers routinely failed to obtain appraisals, guarantor financial information or site inspections at closing or to update them throughout loan administration. As a result, Commonwealth's loan files lacked, or contained outdated, appraisals, guarantor financial information and proof of inspection. Many of the documentation and problematic practices noted regarding the 345 Granby loan, the Arney, Hranowskyj, Menden and PLV loan relationships described generally above in Paragraphs 33 through 98, were more systemic and were noted as such to Woodard, Sabol and Fields by internal and external auditors, bank regulators and third party consultants.

112. Beginning at least as early as 2006, Fields routinely violated Commonwealth's written lending policies by failing to obtain and update appraisals, guarantor financial

information and proof of inspections. In particular, in March 2006, the internal auditor wrote in a report sent to Woodard that, for Arney, “many of the loan inspection sheets were not signed off on by Mr. Fields.”

113. Also beginning in 2006, Commonwealth’s internal and external auditors began to highlight the issue of missing and stale appraisals and guarantor financial statements to Woodard and Sabol in separate reports they received and reviewed.

114. By at least mid-2008, Woodard and Sabol regularly received detailed tracking reports listing all of the credit data and collateral documentation that was missing from the files of loans that Commonwealth’s loan officers, including Fields, had originated (the “exception reports”). These exception reports, which were often several hundred pages in length, reflected that hundreds of Commonwealth loans had been funded without appraisals and other key documentation.

115. In November 2008, the internal auditor sent Woodard and Sabol a report which highlighted that the “key controls” exceptions had increased more than sevenfold and “[m]any of these exceptions include[d] missing appraisals”

116. Fields’ loan files that were missing, or contained stale, documents were tracked internally in widely disseminated exception reports that reported on missing or stale documents in Commonwealth’s loan officers’ loan files. These reports were quite voluminous and reflected around 1,000 exceptions during 2008. Fields’ portfolio of loans regularly reflected the largest number of exceptions, averaging around approximately 25% of the total reported exceptions.

117. During in or about 2008 and 2009, Fields was advised on multiple occasions by Commonwealth’s credit review and administration department that his loan files were missing, or contained stale, appraisals, guarantor financial information and proof of inspections.

118. Fields ignored the repeated notifications that his loan files were missing, or contained stale, appraisals, guarantor financial information and proof of inspections and failed to obtain or update the documents. For example, Fields inspected 345 Granby Street only once and allowed Hranowskyj and Menden to draw down the 345 Granby loan without submitting certifications that work had been performed on the property. Furthermore, Fields received draw requests from Hranowskyj and Menden that consisted of inflated figures, which Fields accepted without question.

119. Commonwealth's external auditor wrote in its report to the Board and management dated March 11, 2009, which Woodard and Sabol received, that the large volume of missing and outdated appraisals in loan files constituted a significant deficiency over the controls for the ALLL, arising in large part from documentation deficiencies. In fact, the external auditor found that the credit files, particularly those for the critical watch list loans, lacked guarantor financial statements and "current information to adequately determine whether a loan is impaired or the amount of impairment."

120. On April 29, 2009, the internal auditor sent an e-mail to Woodard and Sabol attaching a draft credit review report which reported that, based on a review of 143 loans on Commonwealth's watch list loans (*i.e.*, loans classified as special mention), (1) 127 lacked or contained stale guarantor tax returns, (2) 93 lacked or contained stale guarantor personal financial statements; (3) 59 lacked or contained stale borrower corporate tax returns, and (4) 23 lacked evidence of inspection.

121. In May 2009, Commonwealth retained an outside credit consulting firm to perform a comprehensive loan review. On July 10, 2009, during the outside credit consulting

firm's review, Woodard and Sabol were notified by a representative of the credit consultant of the following concerns regarding Commonwealth's adherence to its internal controls:

a. "In many cases, the loan process has lacked adequate controls and adequate documentation to allow for an informed opinion as to the quality of the credit and in the case of development and construction loans, the stage of completion or even what remains unsold."

b. "A simple statement that a project is x% complete is not adequate. We need an independent inspection report. A statement that the builder states that x dollars are needed to complete the project is just that 'a statement.' It indicates no knowledgeable assessment of the project."

122. In August 2009, after reviewing approximately 60% of the construction and development loans, the credit consultant provided a report to Woodard and Sabol which found a myriad of problems and again raised concerns about the lack of financial statements or proof of inspections and the age of appraisals in loan files deemed to be impaired:

a. "Site inspection reports have not been prepared to document that a site visit occurred and that work in place supported the draw request. . . . [t]he lack of this information hampers the ability to assess the stage of completion of a project or the adequacy of collateral value to protect the loan from loss."

b. Commonwealth's loan "files do not document an attempt to determine the volume of liquid assets and recurring cash flow of borrower/guarantor and thus the ability to service the debt."

c. "[N]ew appraisals are needed to document the present value of collateral, especially for those loans that BOC [Bank of the Commonwealth] deem to be impaired."

d. "The volume of files lacking current financial data was high. Greater diligence is needed in maintaining up-to-date financial data."

123. In March 2010, Commonwealth's external auditor concluded that the deficiencies over the ALLL observed during its prior year's audit continued to exist and constituted a material weakness over internal controls for the ALLL. In a report seen by Woodard and Sabol, the external auditor noted that "credit files [were] . . . inadequately maintained" and warned that, "without proper maintenance of credit files there is no way to be certain that all the necessary information needed to adequately assess the relationship is present." Prior to the issuance of that report, Sabol received an e-mail from Commonwealth's external auditor describing Commonwealth's lack of current appraisals as one of several "concerns with respect to internal controls and the audit."

124. In addition to Commonwealth's persistent failure to obtain and update appraisals, guarantor financial information or proof of inspection, Woodard also waived loan officers' compliance with the closing department, a control instituted in 2009 to prevent loan officers from funding loans before they obtained current and comprehensive financial information from borrowing entities and guarantors. Although Commonwealth's internal auditor urged Woodard and Sabol to install a closing department as early as November 2006, the internal auditor's suggestion was ignored until 2009. Once the closing department was in place, Woodard routinely waived the closing department's requirements and allowed loans to be funded before loan officers obtained complete guarantor financial information, including loans to large relationships such as Hranowskyj and Menden.

125. Commonwealth's external auditor also concluded that there existed a significant deficiency over the controls for the closing department caused by Woodard's excessive use of

management override of the closing department, observing that “the CEO waived many of [the] necessary items to close the loans[,]” and warned that “[t]he use of management override should only be used in rare circumstances”

Woodard and Sabol Lied to Commonwealth’s External Auditor

126. As part of the external auditor’s audit of Commonwealth’s financial statements for the years ended December 31, 2008 and December 31, 2009, Woodard and Sabol signed management representation letters addressed to Commonwealth’s external auditor. These letters, dated March 11, 2009 and March 26, 2010, respectively, made the following representations to the external auditor:

- a. Commonwealth’s financial statements were prepared in accordance with GAAP.
- b. Management had disclosed to the external auditor all of its non-performing assets.
- c. Management had made provision for losses that may be incurred in the collection of loans.
- d. The methodology for determining Commonwealth’s fair value disclosures was based on reasonable assumptions.
- e. All documentation necessary to substantiate amounts and assertions in the financial statements had been and would be maintained according to Commonwealth’s policies.

127. These representations were false. As alleged in Paragraphs 23 through 125, above, at the times when Woodard and Sabol made these representations, Woodard and Sabol knew the following facts:

a. The collateral-dependent 345 Granby loan had substantial problems, particularly surrounding the valuation of the collateral, which resulted in the understatement of Commonwealth's ALLL and loss before income taxes.

b. The past due reports that were used to report the dollar volume of Commonwealth's non-performing loans falsely omitted loans to Arney, Hranowskyj and Menden, which should have been reported as non-performing given the known doubt of repayment.

c. Commonwealth's loan files were missing substantial documentation. Specifically, Commonwealth had failed to obtain and update appraisals, guarantor financial statements, and site inspection certifications, all of which were used to determine whether and to what extent a loan was impaired under GAAP.

FIRST CLAIM FOR RELIEF

Violations of Exchange Act Section 10(b) and Exchange Act Rule 10b-5 (Against Woodard and Sabol)

128. Paragraphs 1 through 127 are realleged and incorporated by reference as if set forth fully herein.

129. By engaging in the conduct described above, Woodard and Sabol, directly or indirectly, by use of the means or instrumentalities of interstate commerce, or by use of the mails, or of the facilities of a national securities exchange, in connection with the purchase or sale of Commonwealth securities, with scienter: (a) employed devices, schemes, or artifices to defraud; (b) made untrue statements of material facts or omitted to state material facts necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading; and (c) engaged in acts, practices, or courses of business which operated

or would operate as a fraud or deceit upon other persons, including purchasers and sellers of Commonwealth securities.

130. By engaging in the conduct described above, Woodard and Sabol violated, and unless enjoined again will violate, Exchange Act Section 10(b) [15 U.S.C. § 78j(b)] and Exchange Act Rule 10b-5 [17 C.F.R. § 240.10b-5].

SECOND CLAIM FOR RELIEF

Aiding and Abetting Violations of Exchange Act Section 10(b) and Rules 10b-5 (Against Fields)

131. Paragraphs 1 through 130 are realleged and incorporated by reference as if set forth fully herein.

132. By engaging in the conduct described above, Commonwealth and/or other persons, directly or indirectly, by use of the means or instrumentalities of interstate commerce, or by use of the mails, or of the facilities of a national securities exchange, in connection with the purchase or sale of Commonwealth securities, with scienter: (a) employed devices, schemes, or artifices to defraud; (b) made untrue statements of material facts or omitted to state material facts necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading; and (c) engaged in acts, practices, or courses of business which operated or would operate as a fraud or deceit upon other persons, including purchasers and sellers of Commonwealth securities.

133. By engaging in the conduct described above, Fields knowingly provided substantial assistance to and thereby aided and abetted Commonwealth and/or other persons in its violations of Exchange Act Section 10(b) and Exchange Act Rule 10b-5 thereunder [17 C.F.R. § 240.10b-5]; therefore, Fields is liable pursuant to Exchange Act Section 20(e) [15 U.S.C. § 78t(e)].

134. Unless restrained and enjoined, Fields will continue to aid and abet violations of Exchange Act Section 10(b) [15 U.S.C. § 78j(b)] and Exchange Act Rule 10b-5 [17 C.F.R. § 240.10b-5].

THIRD CLAIM FOR RELIEF

**Violations of Securities Act Sections 17(a)
(Against Woodard and Sabol)**

135. Paragraphs 1 through 134 are realleged and incorporated by reference as if set forth fully herein.

136. By engaging in the conduct described above, Woodard and Sabol, directly or indirectly, in the offer and sale of Commonwealth securities, by use of the means and instruments of transportation and communication in interstate commerce and by use of the mails: (1) with scienter, employed devices, schemes, or artifices to defraud; (2) obtained money or property by means of untrue statements of material fact or omitted to state material facts necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading; and (3) engaged in transactions, practices, or courses of business which operated or would operate as a fraud or deceit upon purchasers.

137. As alleged in Paragraphs 9 and 10, Woodard and Sabol received money from Commonwealth.

138. By engaging in the conduct described above, Woodard and Sabol violated, and unless enjoined again will violate, Securities Act Section 17(a) [15 U.S.C. § 77q(a)].

FOURTH CLAIM FOR RELIEF

Aiding and Abetting Violations of Exchange Act Section 13(a) and Exchange Act Rules 12b-20, 13a-1, 13a-11 and 13a-13 (Against all Defendants)

139. Paragraphs 1 through 138 are realleged and incorporated by reference as if set forth fully herein.

140. Exchange Act Section 13(a) [15 U.S.C. § 78m(a)] and Exchange Act Rules 13a-1, 13a-11 and 13a-13 [17 C.F.R. §§ 240.13a-1, 240.13a-11, 240.13a-13] require issuers of registered securities to file with the Commission factually accurate annual, quarterly and periodic reports. Exchange Act Rule 12b-20 [17 C.F.R. §§ 240.12b-20] provides that, in addition to the information expressly required to be included in a statement or report, there shall be added such further material information, if any, as may be necessary to make the required statements, in the light of the circumstances under which they are made, not misleading.

141. Based on the conduct alleged above, Commonwealth violated Exchange Act Section 13(a) [15 U.S.C. § 78m(a)] and Exchange Act Rules 12b-20, 13a-1, 13a-11 and 13a-13 [17 C.F.R. §§ 240.12b-20, 240.13a-1, 240.13a-11, 240.13a-13].

142. By engaging in the conduct described above, Woodard knowingly provided substantial assistance to and thereby aided and abetted Commonwealth and/or other persons in its violations of Exchange Act Section 13(a) [15 U.S.C. § 78m(a)] and Exchange Act Rules 12b-20, 13a-1, 13a-11 and 13a-13 [17 C.F.R. §§ 240.12b-20, 240.13a-1, 240.13a-11, 240.13a-13]; therefore, Woodard is liable pursuant to Exchange Act Section 20(e) [15 U.S.C. § 78t(e)].

143. By engaging in the conduct described above, Sabol knowingly provided substantial assistance to and thereby aided and abetted Commonwealth and/or other persons in its violations of Exchange Act Section 13(a) [15 U.S.C. § 78m(a)] and Exchange Act Rules 12b-

20, 13a-1, 13a-11 and 13a-13 [17 C.F.R. §§ 240.12b-20, 240.13a-1, 240.13a-11, 240.13a-13]; therefore, Sabol is liable pursuant to Exchange Act Section 20(e) [15 U.S.C. § 78t(e)].

144. By engaging in the conduct described above, Fields knowingly provided substantial assistance to and thereby aided and abetted Commonwealth and/or other persons in its violations of Exchange Act Section 13(a) [15 U.S.C. § 78m(a)] and Exchange Act Rules 12b-20, 13a-1, 13a-11 and 13a-13 [17 C.F.R. §§ 240.12b-20, 240.13a-1, 240.13a-11, 240.13a-13]; therefore, Fields is liable pursuant to Exchange Act Section 20(e) [15 U.S.C. § 78t(e)].

145. Unless restrained and enjoined, Woodard, Sabol and Fields will continue to aid and abet violations of Exchange Act Section 13(a) [15 U.S.C. § 78m(a)] and Exchange Act Rules 12b-20, 13a-1, 13a-11 and 13a-13 [17 C.F.R. §§ 240.12b-20, 240.13a-1, 240.13a-11, 240.13a-13].

FIFTH CLAIM FOR RELIEF

Violations of Exchange Act Section 13(b)(5) (Against all Defendants)

146. Paragraphs 1 through 145 are realleged and incorporated by reference as if set forth fully herein.

147. Exchange Act Section 13(b)(5) [15 U.S.C. § 78m(b)(5)] prohibits any person from knowingly circumventing a system of internal accounting controls, knowingly failing to implement a system of internal accounting controls, or knowingly falsifying required books, records, and accounts.

148. By engaging in the conduct described above, Woodard, Sabol and Fields violated, and unless enjoined again will violate, Exchange Act Section 13(b)(5) [15 U.S.C. § 78m(b)(5)].

SIXTH CLAIM FOR RELIEF

**Violations of Exchange Act Rule 13b2-1
(Against all Defendants)**

149. Paragraphs 1 through 148 are realleged and incorporated by reference as if set forth fully herein.

150. Exchange Act Rule 13b2-1 [17 C.F.R. § 240.13b2-1] prohibits any person from falsifying, or causing to be falsified, books, records, and accounts.

151. By engaging in the conduct described above, Woodard, Sabol and Fields violated, and unless enjoined again will violate, Exchange Act Rule 13b2-1 [17 C.F.R. § 240.13b2-1].

SEVENTH CLAIM FOR RELIEF

**Violations of Exchange Act Rule 13b2-2
(Against Woodard and Sabol)**

152. Paragraphs 1 through 151 are realleged and incorporated by reference as if set forth fully herein.

153. Exchange Act Rule 13b2-2 [17 C.F.R. § 240.13b2-1] prohibits making, or causing to be made, materially false or misleading statements to an accountant in connection with audits, reviews or examinations of an issuer's financial statements or in the preparation or filing of an issuer's documents or reports required to be filed with the Commission; or omitting to state, or causing another person to omit to state, material facts necessary in order to make statements made, in light of the circumstances under which such statements were made, not misleading, to an accountant in connection with audits, reviews or examinations of an issuer's financial statements or in the preparation or filing of an issuer's documents or reports required to be filed with the Commission.

154. By engaging in the conduct described above, Woodard and Sabol violated, and unless enjoined again will violate, Exchange Act Rule 13b2-2 [17 C.F.R. § 240.13b2-2].

EIGHTH CLAIM FOR RELIEF

Violations of Exchange Act Rule 13a-14 (Against Woodard and Sabol)

155. Paragraphs 1 through 154 are realleged and incorporated by reference as if set forth fully herein.

156. Exchange Act Rule 13a-14 [17 C.F.R. § 240.13a-14] requires an issuer's principal executive and principal financial officer, to sign a certification stating that, to the best of the principal executive's and principal financial officer's knowledge, there were no untrue statements of material fact or omissions of a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading.

157. By engaging in the conduct described above, Woodard and Sabol violated, and unless enjoined again will violate, Exchange Act Rule 13a-14 [17 C.F.R. § 240.13a-14].

PRAYER FOR RELIEF

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

(i) Permanently restrains and enjoins defendants Woodard and Sabol from violating Securities Act Section 17(a) [15 U.S.C. § 77q(a)], Exchange Act Sections 10(b) and 13(b)(5) [15 U.S.C. §§ 78j(b) and 78m(b)(5)], and Exchange Act Rules 10b-5, 13a-14, 13b2-1 and 13b2-2 [17 C.F.R. §§ 240.10b-5, 240.13a-14, 240.13b2-1 and 240.13b2-2];

(ii) Permanently restrains and enjoins defendants Woodard and Sabol from aiding and abetting violations of Exchange Act Section 13(a) [15 U.S.C. § 78m(a)], and Exchange Act Rules 12b-20, 13a-1, 13a-11 and 13a-13 [17 C.F.R. §§ 240.12b-20, 240.13a-1, 240.13a-11 and 240.13a-13];

(iii) Permanently restrains and enjoins defendant Fields from violating Exchange Act Section 13(b)(5) [15 U.S.C. § 78m(b)(5)], and Exchange Act Rule 13b2-1 [17 C.F.R. § 240.13b2-1];

(iv) Permanently restrains and enjoins defendant Fields from aiding and abetting violations of Exchange Act Sections 10(b) and 13(a) [15 U.S.C. §§ 78j(b) and 78m(a)], and Exchange Act Rules 10b-5, 12b-20, 13a-1, 13a-11 and 13a-13 [17 C.F.R. §§ 240.10b-5, 240.12b-20, 240.13a-1, 240.13a-11 and 240.13a-13];

(v) Orders Woodard and Sabol to pay penalties pursuant to Securities Act Section 20(d) [15 U.S.C. § 77t(d)] and Exchange Act Section 21(d)(3) [15 U.S.C. § 78u(d)(3)];

(vi) Orders Fields to pay penalties pursuant to Exchange Act Section 21(d)(3) [15 U.S.C. § 78u(d)(3)];

(vii) Permanently bars Woodard and Sabol pursuant to Securities Act Section 20(e) [15 U.S.C. § 77t(e)] and Exchange Act Section 21(d)(2) [15 U.S.C. § 78u(d)(2)], from acting as an officer or director of any issuer that has a class of securities registered under Exchange Act Section 12 [15 U.S.C. § 78l] or that is required to file reports pursuant to Exchange Act Section 15(d) [15 U.S.C. § 78o(d)];

(viii) Permanently bars Fields pursuant to Exchange Act Section 21(d)(2) [15 U.S.C. § 78u(d)(2)], from acting as an officer or director of any issuer that has a class of securities registered under Exchange Act Section 12 [15 U.S.C. § 78l] or that is required to file reports pursuant to Exchange Act Section 15(d) [15 U.S.C. § 78o(d)]; and

(ix) Grants such other relief as this Court may deem necessary and proper.

Dated: January 9, 2013
Washington, D.C.

Respectfully submitted,

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