

IN THE UNITED STATES DISTRICT COURT
FOR NORTHERN DISTRICT OF ILLINOIS
EASTERN DIVISION

WILLIAM ERIC GRAHAM and RONALD P. GRAHAM, on behalf of themselves and all others similarly situated,

Plaintiffs,

vs.

TAYLOR CAPITAL GROUP, INC., f/k/a COLE TAYLOR FINANCIAL GROUP, INC., COLE TAYLOR BANK, RELIANCE ACCEPTANCE GROUP, INC., JEFFREY W. TAYLOR, BRUCE W. TAYLOR, SIDNEY J. TAYLOR, HOWARD B. SILVERMAN, IRWIN H. COLE, LORI COLE, DEAN L. GRIFFITH, MELVIN E. PEARL, SOLWAY F. FIRESTONE, ADELYN DOUGHERTY, WILLIAM S. RACE, ROSS J. MANGANO and RICHARD W. TINBERG,

Defendants.

98C 0779

JUDGE ALESIA

MAGISTRATE JUDGE PSHMAN
No.

DOCKETED
FEB 10 1997

CLASS ACTION COMPLAINT

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Plaintiffs, individually and on behalf of all others similarly situated, by their undersigned attorneys, allege the following upon information and belief, except as to paragraphs 10 and 11, which are alleged upon their personal knowledge as to themselves. Plaintiffs' information and beliefs are based upon an investigation conducted by counsel which included, *inter alia*, a review and analysis of the public filings with the Securities and Exchange Commission ("SEC") made by Cole Taylor Financial Group, Inc. ("Cole Taylor"), Taylor Capital Group, Inc. ("Taylor Capital") and Reliance Acceptance Group, Inc. ("Reliance"), securities

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analyst reports and advisories about these companies, and newspaper articles and press releases concerning them and the "split-off" of Reliance from Cole Taylor. Based upon such investigation, plaintiffs believe that substantial evidentiary support exists for the allegations set forth herein.

NATURE OF THE ACTION

1. This is a class action brought on behalf of all shareholders of Cole Taylor Financial Group, Inc. ("Cole Taylor") who were solicited by a Proxy Statement dated October 15, 1996 ("Proxy") to vote at the Annual Meeting of Stockholders of Cole Taylor (the "Stockholders' Meeting"), held on November 15, 1996 in Chicago, Illinois (the "Class"). Through the Proxy, the Cole Taylor shareholders were asked to approve a "split-off" of the company's subprime automobile finance business, which provides financing for purchases of automobiles by individuals who generally have poor credit histories, from Cole Taylor's traditional banking operations (the "Split-Off Transaction").

2. Cole Taylor was jointly owned and controlled by members of the Cole and Taylor families, with each family owning at least 25 percent of the outstanding common stock of Cole Taylor. The two families agreed to a transaction whereby the Cole Taylor's wholly owned subsidiary, Reliance Acceptance Corporation ("RAC"), Cole Taylor's finance subsidiary, along with Cole Taylor's used automobile receivables business, would be split-off into a new publicly held corporation, Reliance, to be managed by the Cole family, while Cole Taylor's banking business, Cole Taylor Bank, would become privately held by the Taylor family in Taylor Capital. Pursuant to this agreement, the Taylor family would, among other things, exchange all of its stock

in Cole Taylor (totalling approximately 4.25 million shares) for complete ownership of its banking interests. This stock was valued in the transaction as being worth \$33 per share.

3. Based on the information contained in the Proxy, in which the Board of Directors of Cole Taylor, including members of both the Cole and the Taylor families, recommended approval of the Split-Off Transaction, the Cole Taylor shareholders approved the Split-Off Transaction at the Shareholders' Meeting. The Split-Off Transaction was ultimately consummated on February 12, 1997, with Cole Taylor Bank becoming the Chicago area's largest privately owned bank, with assets totalling \$1.8 billion, while Reliance began operation as a public company.

4. On February 14, 1997, only *two days* after the Split-Off Transaction became final, Reliance shocked its new shareholders by issuing a press release which reported that it would "make significant provisions for credit losses for the fourth quarter of 1996," which would require it to report a substantial loss for the quarter. Two weeks later, on March 3, 1997, Reliance issued its formal 1996 year-end results, in which it disclosed that it was taking a loan loss provision of \$18 million during the quarter.

5. Over the rest of the year, Reliance continued to report further increases in its loan loss provisions, along with other financial difficulties, leading to a precipitous decline in the price of the Reliance common stock. On November 15, 1996, when the Cole Taylor stockholders voted to approve the Split-Off Transaction, its stock price was \$28 per share. Today, the price is less than \$1 per share, representing a collapse in value of more than 99 percent.

6. The Cole Taylor shareholders approved the Split-Off Transaction, and agreed to allow the profitable Cole Taylor Bank to split off from Reliance, based on the representations contained in the Proxy concerning the financial condition and prospects of the new company. The Proxy, however, was materially false and misleading because of the omission of critical facts concerning Reliance and its business practices. Among other things, the Proxy misrepresented that Reliance was appropriately protecting itself from credit losses by purchasing automobile sales contracts at a discount, when Reliance had already changed its policies *prior to the date of the Proxy* because of its recognition of the fact that such discounts would be insufficient to offset anticipated credit losses. Moreover, the Proxy misrepresented that it only purchased sales contracts which complied with Reliance's proper underwriting standards, when, in fact, at least *30 percent* of the contracts violated Reliance's own underwriting standards and such standards were, in any event, inadequate to protect the company from losses.

7. As a result of its false and misleading Proxy, the defendants have violated Sections 14(a) and (e) of the Securities Exchange Act of 1934 ("Exchange Act"), and Rule 14(a)-9 promulgated thereunder. Moreover, the defendants, who jointly held majority control over Cole Taylor, owed the highest fiduciary duty of loyalty, honesty and fairness to the company's minority shareholders, including the duty to be scrupulously fair in their dealings with them. In addition, Cole Taylor, directly and through its wholly-owned subsidiary, Cole Taylor Bank, owed a fiduciary duty under the Employee Retirement Income Security Act of 1974 ("ERISA") to certain members of the Class who owned stock under Cole Taylor's Employee Stock Ownership Plan (the "ESOP") and the Cole Taylor 401(k)/Profit Sharing Plan (the "Profit Sharing Plan"), including

the duty not to engage in self-dealing. By engaging in the Split-Off Transaction and permitting the Taylor family to take ownership over the banking assets for egregiously inadequate consideration, and by misrepresenting the financial condition and prospects of Reliance, the defendants breached their fiduciary duty to the Class under common law and ERISA. Plaintiffs and the Class have been damaged by the defendants' misconduct as alleged herein and are entitled to appropriate relief.

JURISDICTION AND VENUE

8. This action arises under Sections 14(a) and (e) and 20(a) of the Securities Exchange Act of 1934 ("Exchange Act"), 15 U.S.C. §§ 78j(b), n(a) and (e), and 78(t), and the rules and regulations promulgated thereunder, including SEC Rule 14a-9, promulgated thereunder, and under ERISA, 29 U.S.C. § 1001, *et seq.* Jurisdiction is based upon Section 27 of the Exchange Act, 15 U.S.C. §78a, under Section 502 of ERISA, 29 U.S.C. § 1132, and under 28 U.S.C. §1331 (federal question jurisdiction).

9. Venue is proper in this District pursuant to § 27 of the Exchange Act, and 28 U.S.C. § 1391(b). Cole Taylor, the predecessor company of defendants Taylor Capital and Reliance, maintained its principal executive offices here, Taylor Capital continues to maintain its principal executive offices here, and Reliance has offices located and conducts substantial business in this District. Moreover, many of the acts complained of herein, including the preparation and distribution of the allegedly misleading Proxy occurred in this District, and the individual defendants, many of whom reside here, served as members of the Board of Directors of the Illinois-based Cole Taylor. In connection with such acts,

transactions and conduct, defendants used the means and instrumentalities of interstate commerce, including the United States mails, interstate telephone communications and the facilities of national securities exchanges and markets.

THE PARTIES

10. Plaintiff William Eric Graham owned 1,200 shares of common stock of Cole Taylor as of September 20, 1996 and was thereby solicited with the Proxy by the defendants to approve the Split-Off Transaction. Following the approval of the merger by the Cole Taylor shareholders, and the consummation of the Split-Off transaction, the plaintiff became a Reliance stockholder.

11. Plaintiff Ronald P. Graham owned 2,504 shares of common stock as a participant in the ESOP and the Profit Sharing Plan and was thereby solicited with the Proxy by Cole Taylor, through its wholly-owned subsidiary, Cole Taylor Bank, to approve the Split-Off Transaction. Following the approval of the merger by the Cole Taylor shareholders, and the consummation of the Split-Off transaction, the plaintiff became a Reliance stockholder.

12. Defendant Taylor Capital is a corporation organized under the laws of the State of Delaware whose principal executive offices are located at 350 East Dundee Rd., Wheeling, Illinois. Taylor Capital is a bank holding company which was formed by the Taylor family defendants prior to February 12, 1997, to accomplish the transaction which is the subject of this action. The Taylor family owns a majority of the common stock of Taylor Capital.

13. Defendant Cole Taylor Bank is a \$1.8 billion bank with its headquarters located in Illinois. It is wholly-owned by Taylor Capital and, prior to the Split-Up Transaction, was wholly-owned by Cole Taylor. At the time of the Shareholder Meeting, Cole Taylor Bank was the trustee of Cole Taylor's ESOP and the Profit Sharing Plan under ERISA.

14. Defendant Reliance is a corporation organized under the laws of the State of Delaware, whose principal executive offices are located at 400 North Loop 1604 East, San Antonio, Texas. The common stock of Reliance is listed on NASDAQ. Until February 12, 1997, Reliance was known as Cole Taylor Financial Group, Inc. Reliance currently manages approximately \$31 million of automobile finance receivables through its offices in Illinois, which were transferred to it by the Taylor family pursuant to the Split-Off Transaction.

15. Defendant Jeffrey W. Taylor was at all times material hereto, and until February 12, 1997, the Chairman of the Board of Directors and Chief Executive Officer of Cole Taylor and chairman of its banking subsidiary. Defendant Jeffrey Taylor has been the chairman of the Board of Directors and Chief Executive Officer of Taylor Capital since its formation.

16. Defendant Bruce W. Taylor was until February 12, 1997, a director and President of Reliance and a director and the Chief Executive Officer of Reliance's finance subsidiary. Bruce Taylor has been the President and a director of Taylor Capital since its formation.

17. Defendant Sidney J. Taylor was a co-founder, and until February 12, 1997, served as Chairman of the Executive Committee, of Cole Taylor. Since 1984 and at all material times hereto, he also was a director of the Cole Taylor and its operating subsidiaries. Sidney Taylor is the father of Jeffrey and Bruce Taylor.

18. Defendant Thomas Barlow has been the Chief Executive Officer and Chairman of the Board of Directors of RAC since January 1993. Barlow has also been a director of Cole Taylor since 1993. On February 12, 1997, Barlow became the Chief Executive Officer of Reliance. In May 1997, Barlow was forced to resign from that position.

19. Defendant Howard B. Silverman has been a director of Cole Taylor and Chairman of the Board of Directors of RAC since 1992. Silverman, who is a resident in the State of Illinois, became Chairman of the Board of Reliance on February 14, 1997. Following the resignation of Barlow, Silverman also became of the Chief Executive Officer of Reliance.

20. Defendant Irwin H. Cole was a co-founder and, at all times material hereto, a director of Cole Taylor. He also served as Vice Chairman of Cole Taylor's Executive Committee and was Vice Chairman and a director of RAC. Irwin Cole and his family currently own approximately 35% of the stock of the Reliance.

21. Defendant Lori Cole is the daughter of Irwin Cole, and, since 1995 and at all material times hereto, was a director of Cole Taylor and RAC. Following the Split-Off Transaction, Lori Cole became a director Reliance and Chairman of its Executive Committee.

22. Defendant Dean L. Griffith is, and was at all times material hereto, a director of the Cole Taylor, and was a member of the Audit Committee. Following the Split-Off Transaction, Griffith became a director, and member of the Audit Committee, of Reliance.

23. Defendant Melvin E. Pearl was a director of the Cole Taylor from 1984 to February 12, 1997. At all relevant times, Pearl was also a member of Cole Taylor's Executive Committee and Chairman of the Audit Committee, and served as a director of RAC. Pearl, who is a partner at the law firm of Katten, Muchin & Zavis, which was counsel to the Cole Taylor and its finance subsidiaries and received substantial fees as a result, has been a director of Taylor Capital since its formation before February 12, 1997.

24. Defendant Solway F. Firestone has been a director of the Cole Taylor since 1994, and served as a member of its Audit Committee. From 1983 to 1997, Firestone was also a director of Cole Taylor's banking subsidiary. Following the Split-Off Transaction, Firestone became a director of Reliance and Chairman of its Audit Committee.

25. Defendant Adelyn Dougherty was a director of the Cole Taylor until February 12, 1997. Dougherty has also been a director of Taylor Capital since its formation.

26. Defendant William S. Race was a director of Cole Taylor and RAC until February 12, 1997. Race served as the Chief Financial Officer of the Cole Taylor from 1990 until August 1995, was its Executive Vice President until the end of 1995, and was Treasurer of RAC until the Split-Off Transaction.

27. Defendant Ross J. Mangano is, and was at all times material hereto, a director of the Cole Taylor and RAC, and a member of Cole Taylor's audit committee.

28. Defendant Richard W. Tinberg was a director of Cole Taylor until February 12, 1997.

29. The Individual Defendants constituted senior management and/or directors of Cole Taylor and its operating subsidiaries, and at all times material to this Complaint, had the power to control, and did in fact control, the day to day operations of Cole Taylor and its subsidiaries. Moreover, because of their position with Cole Taylor at the time of the dissemination of the Proxy and the Shareholders' Meeting, they had access to the material, adverse, non-public information about Cole Taylor's and Reliance's internal control structure, as well as its financial condition, and had access to internal corporate documents, including Cole Taylor's and Reliance's operating plans, budgets and forecasts, and reports of actual operations. Based on their role as directors and/or senior executive officers of Cole Taylor, each of the Individual Defendants were controlling persons of Cole Taylor under the applicable federal securities laws.

30. The Taylor and Cole families, and the members of the Board of Directors affiliated with each family, jointly controlled a majority interest in Cole Taylor. As such, the defendants owed the Cole Taylor minority public shareholders the highest fiduciary duty of loyalty, honesty and fairness. Similarly, as trustees to the ESOP and the Profit Sharing Plan, Cole Taylor, through its wholly-owned subsidiary, Cole Taylor Bank, owed a fiduciary duty to the participants in those employee benefit plans under ERISA.

CLASS ACTION ALLEGATIONS

31. Plaintiffs bring this action as a class action pursuant to Fed. R. Civ. P. 23(a) and (b)(3), on behalf of themselves and the Class of all Cole Taylor common stockholders who were solicited to vote at the November 15, 1996 Shareholder Meeting and who were damaged by the consummation of the Split-Off Transaction. Plaintiff Ronald P. Graham also brings this action on behalf of himself and a subclass of all members of the ESOP or the Profit Sharing Plan at the time of the Shareholder Meeting (the "ERISA Subclass"). Unless otherwise indicated, all references to the "Class" also includes members of the ERISA Subclass. Excluded from the Class are the defendants herein, including members of the immediate family of each defendant and individuals identified herein, their affiliates, partners, successors and assigns.

32. Members of the Class are geographically diverse and so numerous that their joinder is impracticable. According to the Proxy, as of September 20, 1996, there were in excess of 6,500 beneficial owners of 14,758,569 shares of Cole Taylor common stock. Each of these shares entitled the holder to one vote at the shareholder meeting. The exact names and addresses of each Class member can be ascertained through appropriate discovery.

33. Plaintiffs' claims on behalf of each Class are typical of claims of other Class members as plaintiffs and all members of the Class sustained damages arising from defendants' misconduct as alleged herein.

34. Plaintiffs will fairly and adequately represent the interests of the Class and have retained counsel who are experienced and competent in class action and securities and

ERISA litigation. Plaintiffs have no interests which are contrary to or in conflict with those of the Class members they seeks to represent.

35. A class action is superior to any other available means for the fair and efficient adjudication of this controversy. There will be no difficulty in the management of this action as a class action.

36. Common questions of law and fact exist as to all members of the Class and predominate over any questions affecting only individual class members. The predominant questions of law and fact include, *inter alia*:

- a. Whether the federal securities laws were violated by defendants as alleged herein;
- b. Whether ERISA was violated by defendants as alleged herein;
- c. Whether the statements defendants made to the public in the Proxy were misleading and failed to disclose material facts;
- d. Whether defendants acted with the requisite degree of scienter;
- e. Whether defendants negligently drafted each of the Proxy statements identified herein;
- f. Whether the consideration provided by the Taylor family in the Split-Off Transaction was grossly unfair and inadequate in exchange for the banking assets of Cole Taylor;
- g. Whether the defendants owed a fiduciary duty to the members of the Class, as minority shareholders of Cole Taylor;

h. Whether the defendants breached their fiduciary duty to the members of the Class; and

I. Whether Class members have sustained damages and, if so, the proper measure thereof.

SUBSTANTIVE ALLEGATIONS

The Proxy and The Split-Off Transaction

37. On October 10, 1996, Cole Taylor issued a Proxy Statement pursuant to Section 14(a) of the Exchange Act, which solicited the approval of the shareholders of the Split-Off Transaction. Pursuant to the terms of this Transaction, as agreed to in a Share Exchange Agreement dated as of June 12, 1996 between Cole Taylor and certain members of the Taylor family, the Split-Off Transaction would include Cole Taylor's exchange of (A) all of the stock of a newly formed subsidiary of Cole Taylor Bank holding all of the capital stock of the Bank for (B) between 4,000,000 and 4,500,000 shares of Cole Taylor common stock owned by the Taylor family. As part of the Transaction, Cole Taylor Bank would form a new wholly owned subsidiary ("New Reliance") to which the Bank would contribute (i) its used automobile receivables business, (ii) an amount in cash, depending on the number of shares contributed by the Taylor family and the fair market value of the automobile receivables (the "First Cash Component"), and (iii) an amount of cash based on Cole Taylor's investments in Alpha Capital Fund II, L.P., a small business investment company, and CT Mortgage Company, Inc., a wholly owned subsidiary of Cole Taylor (the "Second Cash Component").

38. The Taylor family agreed that it would contribute automobile receivables with a fair market value of between \$30,000,000 and \$31,000,000. If the automobile receivables had a fair market value of \$30,000,000 and the Taylor family contributed 4,250,000 shares of Cole Taylor common stock, the First Cash Component would be \$60,000,000. If the stock component was more or less than 4,250,000 shares, the First Cash Component would be increased or decreased, respectively, by \$33 per share, and the First Cash Component would also be decreased to the extent the fair market value of the automobile receivables exceeded \$30,000,000.

39. New Reliance, which would consist of all of the assets contributed by the Taylor family, would then be merged with RAC, a pre-existing wholly owned subsidiary of Cole Taylor, into Reliance Acceptance Group, Inc. This would then be the remaining publicly traded company managed by then-present management of Cole Taylor (except for the Taylor family). All of the capital stock of the Bank would be privately held by the Taylor family. Thus, the Split-Off Transaction, as proposed to the Cole Taylor shareholders, would result in the Cole Taylor Bank going private while the shareholders would now be investing in a company engaged solely in the sub-prime automobile finance business. As explained in the Proxy:

The Split-Off Transactions, if approved and consummated, will effect a fundamental change in the nature of the Company's business. The Company will cease its traditional commercial and consumer banking business, which has historically provided the substantial majority of the Company's revenues and income. The Company will retain the consumer finance business of RAC, which commenced operations in January 1993, and the Bank's used automobile receivables business, which commenced operations in 1982. After the Split-Off, the

Company's business will focus almost entirely on the automobile finance market. In connection with the Split-Off Transactions, the Company will change its name to Reliance Acceptance Group, Inc. . . .

Proxy at 52.

40. In explaining the background of the negotiations between the Taylor and Cole families leading up to the proposed Split-Up Agreement, the Proxy reported that the Cole Taylor Board had received several proposals from parties interested in the possibility of acquiring the company. One such proposal called for an exchange of stock at a price equal to approximately \$28.55 per share of common stock, for a total value of approximately \$416 million. In addition, one party proposed a cash price for just the banking subsidiary of \$240 million, although the financial advisers to Cole Taylor believed the price could be increased to \$250 million. In response to these proposals, the Taylor family increased their offer for the Split-Off Transaction, leading to the eventual proposal presented in the Proxy. Given that the Cole Taylor Board recommended the Split-Off Transaction, these representations in the Proxy suggested to the shareholders that it would have a value at least equivalent to \$240 million, the value of the banking subsidiary which was given to the Taylor family as its consideration in the transaction. Since the Taylor family had agreed to give \$30 million in automobile receivables and \$60 million in cash, the stock portion of their contribution therefore could be assumed to equal approximately \$150 million. At 4,250,000 shares, shareholders therefore were being told that the stock had a fair market value of over \$30 per share.

41. Because the Cole Taylor subscribers were being asked to agree to become shareholders of a newly formed automobile finance company, rather than a company

in which most of its profits came from commercial and consumer banking, it was critical that they understand the nature of the new company and type of business it conducted. Therefore, the defendants provided substantial details concerning these issues in the Proxy. Among other things, the Proxy stated:

[RAC] commenced operations as a separate subsidiary of [Cole Taylor] in January 1993 and, at September 30, 1996, operated 47 Reliance Acceptance Corp. offices . . . To date, [RAC's] operations have focused on purchasing closed-end retail sales finance contracts, primarily in connection with sales of used automobiles.

[RAC] operates through a network of decentralized branch offices under the name of Reliance Acceptance Corp., each staffed with a branch manager who reports to an experienced regional director. A typical Reliance Acceptance Corp. branch is located in an office building that is reasonably close to the new and used car automobile dealers that send sales finance contracts to [RAC's] branch offices for the purchase approval. Having no direct loans, but only sales finance contracts in their portfolio, permits branch offices to operate efficiently with a small staff and control their overhead expenses.

Dealer Loan Organization. Each branch office of [RAC] purchases sales finance contracts from dealers located in its local market area. Relationships are established with automobile dealers by each branch after performing credit reviews on the dealer. Approved dealers enter into contractual relationships with [RAC]. This contract specifies, among other things, the percentage of dealer discount for possible credit loss that will be deducted from the purchase proceeds of sales finance contracts and the processing fees to be paid by the dealer for each contract purchased by [RAC]. [RAC] competes for business on the basis of service, namely in short response time for approval or disapproval of credit applications, consistent application of [RAC's] underwriting standards, and immediate funding of sales finance contract purchases upon delivery of all required documents. Pursuant to this business strategy, [RAC] has significantly increased the number of dealers with which it contracts to over 1,200 as of December 31, 1995 from approximately 1,000 as of December 31, 1994 and from approximately 300 as of December 31, 1993.

Id.

42. With respect to RAC's underwriting procedures, the Proxy states:

[RAC] purchases each sales finance contract in accordance with its underwriting standards and procedures, which are intended to assess the applicant's ability to repay the amounts due on the loan and the adequacy of the financed vehicle as collateral. The majority of automobiles financed by [RAC] range in age from used current year models to those that are five years old with less than 100,000 miles. Most of [RAC's] customers have some derogatory credit history, but have performed satisfactorily in previous automobile financing transactions.

Id.

43. With respect to the procedures used by RAC to account for, and protect itself from, credit losses, the Proxy states:

Nonrefundable Dealer Discounts. As protection to [RAC] for possible credit losses, [RAC] purchases sales finance contracts at an average discount of 8% and credits a nonrefundable dealer discount in the amount of such discount for the purpose of absorbing credit losses. Amounts in this account are not refundable to dealers, nor are dealers required to fund losses in excess of the reserves. The applicable discount is negotiated with each dealer. These dealer discounts, net of charges to dealer discounts for loan losses, are accreted to income over the terms of the loans using the level yield method. Under [RAC's] revolving credit agreement, the ratio of the allowance for loan losses and nonrefundable dealer discounts to the net finance receivables must equal the greater of four percent or the preceding twelve-month net charge-off percentage . . . In addition to the loss protection provided by the unamortized, nonrefundable dealer discounts, in the event of a significant rise in interest rates, [RAC] would likely attempt to negotiate a larger discount with its dealers.

Id. at 53. In sum, Reliance did not establish credit loss reserves to account for the anticipated default on a number of its subprime customers, but instead accounted for such losses through

the discounts it paid to its dealers for the sales finance contracts. The amount of these dealer discounts, after accounting for losses, were then included as income for the company.

44. The Proxy also incorporated by reference Cole Taylor's Form 8-K dated October 10, 1996, which provided the company's restated historical financial statements for discontinued operations to reflect the Share Exchange Agreement, calling for the Split-Off Transaction. Cole Taylor's independent auditors, KPMG Peat Marwick LLP ("Peat Marwick") issued an opinion letter to the Board of Directors which represented that the restated 1995 and 1994 consolidated financial statements stated "fairly, in all material respects, the financial position of Cole Taylor . . . and subsidiaries as of December 31, 1995 and 1994 and the results of their operations and their cash flows for the years then ended in conformity with generally accepted accounting principles." Form 8-K at 3. In notes to Cole Taylor's financial statements, Peat Marwick reiterated RAC's policies for accounting for credit losses:

Allowance for Credit Losses and Nonrefundable Dealer Discounts: In conjunction with the financing of installment contracts, agreements are entered into with dealers whereby nonrefundable dealer discounts are established to protect [RAC] from potential losses associated with such contracts. These dealer discounts, net of charges to dealer discounts for loan losses, are accreted to income over the terms of the loans using the level yield method. All nonrefundable dealer discounts are available to charge accounts against. Any dealer discounts not used to absorb losses are available for accretion into income.

In 1994 [RAC] maintained both an allowance for credit losses and a nonrefundable dealer discount. Subsequent experience had indicated to management that the nonrefundable dealer discount is adequate to absorb possible losses on credits that may become uncollectible. Accordingly, the allowance for credit losses was taken into income in 1994. Management's opinion in determining the adequacy of the nonrefundable dealer discounts to absorb losses is based on historical experience of the portfolio, estimates of the collectibility of

the accounts, the value of the underlying collateral, and current economic conditions.

Id. at 11.

45. Similarly, the Proxy also incorporated by reference Cole Taylor's Form 10-Q for the second quarter ending June 30, 1996, which was filed with the SEC on August 14, 1996. This, too, summarized RAC's loan loss policies:

In conjunction with the purchase of sales finance contracts by [RAC], agreements are entered into with dealers whereby amounts are withheld as a discount to provide protection from potential losses associated with such contracts. These nonrefundable dealer discounts are available to cover losses on sales finance contracts.

Effective January 1, 1996, [RAC] adopted the practice of accumulating loss data on individual pools of loans based on month of origination (pools). The nonrefundable dealer discount within each pool is available to cover losses incurred on the pool or to be accreted into income over the estimated life of the related loans, based upon management's estimate of loan losses. To the extent management's estimate of losses by pool exceeds the related available dealer discount, income accretion, if any, would cease and a loan loss reserve would be established through charges to operating expense. Prior to January 1, 1996, the discount was accreted into income over the contractual life of the loan, subject to aggregate loan charge-offs.

Form 10-Q at 8.

46. The policy of accumulating loss data for individual pools of loans provided a means by which the defendants could monitor on a frequent basis the amount of non-refundable dealer discounts available within each pool to cover losses. The same information would also permit the defendants to know when losses threatened to exceed the discounts or otherwise increase over prior levels.

47. In addition to summarizing its loan loss reserve policies, the Proxy also summarized RAC's procedures for ensuring that its branch offices were following appropriate procedures:

Internal Reviews. [RAC] policy provides that each branch office be formally examined at least every three months by a regional director. This examination includes a review of the quality of the sales finance contracts that were purchased by the branch, business development activities and internal operating procedures to ensure compliance with established policies.

Id. Through such reviews, RAC was purportedly in a position to ensure that its branch offices were complying with company underwriting and other operating policies, so as to avoid unnecessary credit risks and losses.

48. According to the Proxy, the Split-Off Transaction was "intended to maximize shareholder value and to resolve substantial disagreements that have arisen among members of the Taylor Family and the Cole Family and certain other directors regarding the strategic direction of the Company." *Id.* at 27. In particular, while members of the Cole family wished to "explore a possible strategic transaction involving the Bank," such as a possible sale, the Taylor family opposed such proposals. *Id.* As a means to account for this disagreement, the two families therefore concluded that the Taylor family should assume private ownership of the banking operations while the Cole family would continue to manage a public company focused on the automobile finance industry. Among other things, by being freed from the banking umbrella, Reliance would avoid "current regulations [which] limit the ability of bank holding company-owned finance companies to maximize the funding for non-bank holding company-owned and independent finance companies." *Id.* Reliance would

thereby be able to maximize its use of commercial paper and other financing strategies to fund its operations which were not possible as part of a bank holding company. *Id.*

49. The Proxy outlined the risks of the shareholders agreeing to the new public company focusing exclusively on the subprime automobile finance industry. Such risks included:

[RAC's] business has focused primarily on the subprime automobile finance market. The subprime automobile finance market is comprised of customers who are deemed to be relatively high credit risks due to various factors, including, among other things, the manner in which they have handled previous credit, the absence or limited extent of their prior credit history or their limited financial resources. Consequently, the automobile loans acquired by [RAC], relative to prime consumer credit contracts, bear finance charges at a higher rate but also involve a higher probability of default and greater servicing costs. There can be no assurance that [RAC's] systems and controls will continue to be adequate or that the rate of future defaults and/or losses will be consistent with prior experience or at levels that will maintain the Company's profitability. In light of these risks, [RAC] currently maintains a reserve that is established by purchasing sales finance contracts from the dealers at a discount and setting aside a portion of such discounts against which losses are charged. Because [RAC] has limited operating results on which to base any expectations regarding future credit losses, there can be no assurance that the dealer reserves will prove sufficient to cover the actual losses experienced by [RAC].

Id. at 20-21.

50. Notwithstanding these risks, however, the Proxy emphasized that "[t]he Board of Directors considered these risks but determined that they were substantially outweighed by the benefits of the Split-Off Transactions." *Id.* at 28. Thus, the Board unanimously approved the Split-Off and recommended that the shareholders vote in favor.

51. As further support for the Split-Off Transaction, the Proxy also highlighted the opinions of The Chicago Corporation ("Chicago Corp.") and Sandler O'Neil Corporate Strategies, a division of Sandler O'Neil & Partners, L.P. ("Sandler O'Neil"), both of which had been retained by Cole Taylor as financial advisers. Both Chicago Corp. and Sandler O'Neil opined in letters dated June 12, 1996 that the Split-Off Transaction was "fair, from a financial point of view, to the non-Taylor Family stockholders of the Company." *Id.* at 13.

52. In the Chicago Corp. opinion, it stated that it had reviewed the Cole Taylor audited financial statements for the three years ended December 31, 1995 and unaudited financial statements for the quarter ended March 31, 1996, as well as "other internally generated Company reports relating to asset/liability management, asset quality and so forth," and had "reviewed and analyzed," among other things, "other information bearing upon the financial and operating condition of the Company and material prepared in connection with the proposed transaction," and had "performed such other analyses and examinations and considered such other factors as we have, in our sole judgment, deemed appropriate." Proxy at C-2 (June 12, 1996 Chicago Corp. Fairness Opinion). Based on its detailed analysis, Chicago Corp. then concluded that "the Consideration to be received by the Company pursuant to the Agreement is fair from a financial point of view, to the non-Taylor Family shareholders of the Company." *Id.* at C-3.

53. Similarly, Sandler O'Neil stated in its opinion that it had "reviewed," *inter alia*, Cole Taylor's financial statements, "financial analyses and forecasts of the

Company, the Bank and [RAC], respectively," "the views of senior management of the Company, the Bank and [RAC] concerning the current business operations, results thereof, financial condition and future prospects of the Company, the Bank and [RAC], respectively," and "such other information, financial studies, analyses and investigations and financial, economic and market material as we considered relevant." *Id.* at D-2 (June 12, 1996 Sandler O'Neil Fairness Opinion). It then reiterated the opinion of Chicago Corp. that "the consideration to be received by the Company pursuant to the Agreement is fair from a financial point of view, to the non-Taylor Family shareholders of the Company." *Id.* at D-3.

54. On October 14, 1996, Cole Taylor Bank, as the Trustee of the ESOP and the Profit Sharing Plan under ERISA, disseminated a copy of the Proxy to all ESOP and Profit Sharing Plan members and solicited their vote on the Split-Off Transaction at the Shareholder Meeting. In the cover letter to the members of the ERISA Subclass, Cole Taylor Bank summarized the proposed Split-Off Transaction and stated:

Recommendation of the Board of Directors and Fairness Opinions.

The Board of Directors of the Company unanimously recommends that the stockholders vote for the approval of the Share Exchange Agreement and the Split-Off Transaction. The Board has received opinions from The Chicago Corporation ("Chicago Corp.") and Sandler O'Neill Corporate Strategies, dated June 12, 1996, each stating that, as of that date and on the basis of and subject to the certain assumptions, the consideration to be received by the Company pursuant to the Share Exchange Agreement is fair from a financial point of view to the non-Taylor Family Stockholders of the Company.

55. Through the numerous and detailed disclosures in the Proxy, the defendants represented to the Cole Taylor stockholders that any potential risks arising from the

nature of the subprime automobile market were offset by Reliance's careful underwriting policies and its credit loss procedures, including the discounts it received for the sales contracts, which ensured that the Company was properly protected from unanticipated credit losses. As such, the stockholders had every reason to believe that the proposed Split-Off Transaction was in their best interest and that the Company was receiving fair compensation from the Taylor family.

56. The information contained in the Proxy in support of the Split-Off Transaction was confirmed on October 31, 1996, after the Proxy had been disseminated but before the Shareholder Meeting, when Cole Taylor issued a press release to report its financial results for the third quarter ending September 30, 1996. Highlighting the results for its "continuing operations," which consisted solely of Reliance, Cole Taylor reported "an 87 percent jump in net income from continuing operations . . . to \$3.9 million, or \$0.26 per share, compared with \$2.1 million, or \$0.14 per share, for the third quarter of 1995." It also reported that continuing operations had earned net income of \$10.7 million for the first three quarters of the year, or \$0.69 per share, compared to only \$4.5 million, or \$0.30 per share, for the comparable period in 1995.

57. In the press release, Cole Taylor went on to emphasize improvements in its accounting system, stating:

Reliance successfully upgraded its loan accounting system to a more sophisticated system during the second quarter of 1996, and in doing so, management intentionally refrained from opening new offices until the conversion was complete. Following the conversion, 10 new offices were opened in the third quarter, bringing the number of offices to 47 at September 30, 1996.

This upgrade of the accounting system facilitated the defendants' ability to monitor the performance of its outstanding contracts, including default and repossession rates, such that they would be aware when credit losses began to overtake the discounts designed to cover such losses.

58. Cole Taylor also reported that its non-refundable dealer discounts, used to protect Reliance from credit losses, was \$14.0 million as of September 3, 1996, or 4.0 percent of finance receivables. This amount compared to \$12.7 million, or 5.4 percent of finance receivables at the end of 1995. Explaining this decline, Cole Taylor stated:

The lower percentage is the result of Reliance's policy, adopted at the beginning of 1996, of writing down repossessed vehicles to estimated realizable values immediately upon repossession, rather than waiting until the cars are sold. Further, Reliance was an industry leader when, as of the beginning of this year, it adopted the static pool methodology of monitoring and maintaining the adequacy of these discounts that are set aside to absorb possible credit losses.

59. The day before the Shareholder Meeting, on November 15, 1996, Cole Taylor filed its Form 10-Q with the SEC, formally announcing its financial results for the third quarter of 1996. In its 10-Q, Cole Taylor reiterated its policy with respect to potential credit losses, stating:

The non-refundable dealer discount within each pool is available to cover losses incurred on the pool or to be accreted into income over the estimated life of the related loans, based upon management's estimate of loan losses. To the extent management's estimate of losses by pool exceeds the related available dealer discount, income accretion, if any, would cease and a loan loss reserve would be established through charges to operating expense. Prior to January, 1996, the discount was accreted into income over the contractual life of the loan, subject to aggregate loan charge offs.

60. The Shareholder Meeting was held as scheduled on November 15, 1996.

Cole Taylor issued a press release that same day announcing the shareholders had approved the Split-Off Transaction, "as expected." It also reported that the transaction was expected to be completed by the end of the year.

61. The representations made by the defendants in the Proxy, and related public releases and SEC filings, convinced the market that, upon the consummation of the Split-Off Transaction, Reliance would be in a strong financial position. On December 3, 1996, Duff & Phelps Credit Rating Co. ("Duff & Phelps") announced that it had assigned a "BB+" rating to the subordinated debt which Reliance would be assuming following consummation of the Split-Off Transaction, raising the rating from "BBB-." In explaining the improved rating on the debt, Duff & Phelps emphasized the procedures purportedly utilized by Reliance to protect itself from credit losses:

The ratings reflect Reliance's size and nearly four-year track record, its conservative financial profile and its consistent asset quality performance. Although Reliance is a relatively new entrant in sub-prime auto, the management team, led by Thomas L. Barlow, its president and chief executive officer, has substantial industry experience.

Reliance employs a de-centralized, branch-based approach to underwriting and collections that relies heavily on the branch manager's judgment and experience. The branch-based platform allows Reliance to deliver high-quality, localized service to the dealers and to achieve a better collections experience with customers. A very low ratio of accounts to employees (90:1) enables Reliance to aggressively service the portfolio and achieve a better cumulative net loss experience than competitors targeting the same credit quality customer. Notwithstanding its obvious benefits, the branch-based platform does result in higher operating expense levels, compared with its centralized competitors.

Despite the high-risk nature of its customers, Reliance maintains a moderate business risk profile due to its conservative underwriting criteria, pricing structure and reserving policy. Advance rates cannot exceed 100 percent of vehicle wholesale book value. The approximately 8 percent acquisition discount more than covers expected credit losses. Moreover, Reliance was one of the first companies in the industry to adapt the static pool methodology of accounting for the dealer discount.

62. Shortly thereafter, on December 6, 1996, Cole Taylor announced that the consummation of the Split-Off Transaction, at which point the name of the public company would be changed to Reliance Acceptance Group, Inc., was anticipated to occur in January 1997, rather than year end 1996.

63. On December 10, 1996, another rating agency, Fitch Investors Service ("Fitch") also improved Reliance's rating. Fitch reported that it had affirmed a rating of "F-2" on the commercial paper which Reliance would assume following consummation of the Split-Off Transaction, and had removed the paper from FitchAlert, where it had been placed on June 14, 1996. Explaining its decision, Fitch stated:

The affirmation reflects the company's pro forma capital structure, following the proposed split off from Cole Taylor Bank, good asset quality coupled with adequate reserve coverage and strong management team led by Thomas L. Barlow, its President and Chief Executive Officer. . . .

. . . .
Thus far, Reliance's asset quality has been good, based on its consistent underwriting discipline, but its limited operating history makes the portfolio susceptible to economic downturns. The company normally purchases used car contracts at an 8% discount and allots most of the discount into non-refundable dealer reserves. Losses charged off against the reserve were 5.48% of managed receivables for the nine months ended Sept. 30, 1996, providing for a reasonable cushion against charge-offs.

64. Cole Taylor announced on February 7, 1997 that the Split-Off Transaction would be consummated on February 12, 1997. The reported consideration for the transaction would be "the surrender and reduction of 4,500,000 outstanding shares of the Company's common stock, \$50,750,000 in cash and the transfer of \$31,000,000 in fair market value of bank-qualified automobile finance receivables from the Bank to the parent Company." Cole Taylor also reported that, as a result of the transaction, Reliance would have equity capital that exceeds \$100 million, permitting it "to continue to exceed its debt to equity ratios necessary to maintain its investment grade credit rating." In addition, the press release stated that "[p]reparation for the split-off transaction has caused the Company to take additional time, beyond the time historically taken, to prepare and issue its 1996 financial statements," with such statements to be reported "upon completion of the Company's annual audit which is expected to be in about two weeks."

65. On February 12, 1997, Reliance announced the consummation of the Split-Off Transaction. Beginning on February 13, 1997, its shares would trade on NASDAQ under the new symbol of RACC. According to the press release, "[n]o action is required by Cole Taylor shareholders, as 'old' Cole Taylor Financial Group, Inc. stock certificates represent the same number of shares of the renamed company, Reliance Acceptance Group, Inc."

The Post-Transaction Revelations

66. Remarkably, only two days after the Split-Off Transaction was consummated, on February 14, 1997, Reliance issued its first press release which disclosed,

for the first time, that the Company's previously touted underwriting standards and loan loss reserve policies were not adequate. In particular, Reliance announced that "it would make significant provisions for credit losses for the fourth quarter of 1996," requiring it to report a loss for the quarter, compared to the net income of \$3.9 million in the prior quarter.

67. In a March 3, 1997 press release, Reliance issued its formal results for year-end 1996, announcing that it had lost \$8.6 million from continuing operations in the fourth quarter as a result of an *\$18 million* provision for loan losses. In explaining this result, Reliance stated:

The loan loss provision of \$18 million during the fourth quarter arose as a result of two primary factors. First, the company had changed the manner in which it handled the disposition of repossessed automobiles, engaging a third party to sell the majority of repossessed vehicles through regional auctions. While the company had expected to realize close to the "trade in" value of the vehicles from these auctions, actual results proved to be significantly less than that which had been previously realized when the repossessed vehicles were placed on consignment and sold at retail dealer lots. The company has since returned to selling the majority of these vehicles on retail dealer lots, a process that typically takes longer than the auction process, but which historically has generated results within acceptable margins for the company. Management expects that future losses from repossessions will more closely align with historical levels as a result of returning to this practice.

Secondly, in a high-growth environment, especially for a relatively young company such as Reliance, continual reassessment and readjustment of estimates is required. Based on the company's most recent analysis, management determined that the repossession rate and loss per repossessed vehicle had increased, necessitating an upward adjustment to loss projections and reserves. "We have taken the necessary steps to ensure that the reserves in our existing portfolio are adequate and that we control the amount of credit losses," said Tom Barlow, president and chief executive officer.

Management believes that the existing policy of purchasing sales finance contracts from dealers at a discount of approximately 8 percent is sufficient to cover losses on new loans. Beginning in the fourth quarter of 1996, the company ceased accreting any of this discount into earnings. Moreover, the company has implemented tighter standards on the credit quality of loans that can be approved at a local branch office and have trained and instructed its branch managers that repossession of vehicles is the last resort to working with borrowers that are unable to keep their payments current.

68. Reliance reported in this announcement that, while its *total* interest and fee income for the fourth quarter of 1996 was \$19,747,000 (with net income, after expenses, totalling \$13,317,000), it was taking a charge of \$18,000,000 for credit losses. Thus, whereas Reliance previously had *no* reserves, touting the fact that its discounted purchases from dealers were more than sufficient to offset any losses, now it was taking a charge for such losses that nearly equalled the total income for the entire quarter. Clearly, Reliance's explanation was not sufficient to explain the magnitude of the write-off.

69. Although Reliance reported that the first reason for the losses was the fact that it received less by using a third party to auction repossessed vehicles, instead of dealers, a change which was *not* disclosed in the Proxy, the company failed to identify how significant an effect this had on the total credit losses of \$18 million. As for the second reason, a "reassessment" of estimates, it was clear from the Company's report that it had known of the problem from at least the beginning of the fourth quarter. In particular, it conceded that in the beginning of the fourth quarter it had "ceased accreting any of [its dealer] into earnings." It had done so for an obvious reason -- it *knew* that losses were exceeding the discounts, thereby not permitting it to claim earnings from them.

70. This conclusion is reinforced by Reliance's Form 10-K, filed with the SEC on March 31, 1997 to report the year-end financial results. With respect to its use of dealer discounts, the 10-K stated:

Nonrefundable Dealer Discounts. As protection to [Reliance] for possible credit losses, [Reliance] purchases sales finance contracts at a discount from its stated amount for the purpose of absorbing credit losses. Discounts are not refundable to dealers; nor are dealers required to fund losses in excess of the discount. The applicable discount is negotiated with each dealer. These dealer discounts, net of charges to dealer discounts for loan losses, *have previously been accredited to income over the terms of the contracts using the level-yield method.* [Reliance] discontinued accretion of the dealer discount on October 1, 1996 to provide greater protection for possible credit losses. In addition to the loss protection provided by the unamortized, nonrefundable dealer discounts [Reliance] has established an allowance to absorb potential credit losses not covered by the remaining discount. (Emphasis added.)

71. Significantly, the defendants had disclosed in both their 1996 second and third quarter 10-Qs that "[t]o the extent management's estimate of losses by pool exceeds the related available dealer discount, income accretion, if any, would cease and a loan loss reserve would be established through charges to operating expense." Thus, when they changed their policy as of October 1, 1996 to discontinue any accretion of the dealer discount it was clearly because management had recognized that losses would "exceed" such discounts, requiring the creation of a loan loss reserve. Yet, this material fact was *not* disclosed in the Proxy, dated October 15, 1996. Instead, the defendants waited until March 31, 1997, well *after* the Split-Off had been consummated.

72. Reliance's disclosure in its March 3, 1997 press release that it had to implement "tighter standards on the credit quality of loans that can be approved at a local

branch office" also underscored the fact that Reliance's underwriting standards were insufficient, notwithstanding the disclosures to the contrary in the Proxy.

73. Indeed, according to an August 25, 1997 report on Reliance and the Split-Off Transaction in *Crain's Chicago Business*, analysts did not believe Reliance's explanation that its poor financial results were caused by industry conditions. Instead, analysts blamed Reliance's "own fundamentals for its dim performance and prospects." According to Robert Ollech, an analyst for Milwaukee-based Principal Financial Securities, Inc., Reliance management made the startling admission during a March 1997 conference call that "as many as 30% of the loans it bought contained exceptions to the company's credit standards." This is directly at odds with the representations in the Proxy that Reliance "purchases each sales finance contract in accordance with its underwriting standards and procedures." Proxy at 52.

74. Notwithstanding the devastating news reported by Reliance so soon after the close of the Split-Off Transaction, it was only the tip of the iceberg. On May 7, 1997, Reliance issued a press release to report on its results for the first quarter of 1997. Disclosing a net loss from continuing operations of \$9.9 million for the quarter, Reliance announced that it had to make a provision of another \$22.2 million to increase its total loan loss reserves. This increased Reliance's total reserves for possible credit losses from 4.1% of finance receivables as of year-end 1996 to 7.5% at the end of the first quarter of 1997.

75. Reliance also announced that Barlow, its President and Chief Executive Officer, was resigning, with Chairman Silverman to assume the CEO duties. Attempting to explain the poor financial results, Silverman stated:

Our highest priority is credit quality. Credit underwriting practices have resulted in unacceptable default rates, and these practices are being changed immediately, even if it means a reduction in volume growth. The recent quarter's results have caused us to breach certain covenants in our loan agreements, and I have initiated discussions with our lenders in order to assure their confidence and continued support. Our policies and procedures regarding repossessions and the disposition of repossessed vehicles will also be thoroughly reviewed in order to determine whether they produce the maximum economic results for our Company. Finally, we will reform branch systems and procedures with a view toward better and more cost efficient ways of processing our activities.

76. Although Reliance announced that Barlow, whose purported expertise had contributed to the strengthened financial ratings of Reliance prior to the consummation of the Split-Off Transaction, had resigned, in fact he had been fired due to the poor financial results. Barlow subsequently sued Reliance in Texas state court for wrongful termination.

77. On July 17, 1997, Reliance issued another press release, this time reporting that it had received an extension of its secured credit agreement from its lenders. At the same time, Reliance announced that it expected to report another significant loss for the second quarter of 1997 due to the need to take additional actions "to strengthen loan loss reserves during the quarter." It quoted Silverman, however, as stating that "[w]e believe that Reliance will return to profitability in the third quarter."

78. This report was followed up by Reliance in an August 14, 1997 press release which issued its formal second quarter results. This time, Reliance's net loss had skyrocketed to \$40.2 million, "attributed to a \$60.9 million provision for potential credit losses on its existing \$430.2 million portfolio of net finance receivables contracts." This

increase in credit loss reserves raised total reserves to 16% of finance receivables. With respect to the poor results, Silverman stated:

Since installing new executive management during this past quarter, we have taken actions to strengthen our underwriting, collections and disposition activities. We believe that, with the additional loan loss provision taken in the second quarter, our total reserves will be sufficient to cover potential credit losses in our existing portfolio. With the changes we have implemented in the way we do business, we do not expect to experience the same type of loss provision going forward.

79. Again, however, news only got worse, as Reliance announced on November 14, 1997 that it would report a net loss of \$12.8 million for the third quarter of 1997. The loss included another \$10 million provision for future credit losses.

80. On November 15, 1996, when the stockholders were asked to approve the Split-Off Transaction, the price of the Cole Taylor common stock was \$28 per share. As the true, undisclosed facts concerning Reliance's financial condition have slowly emerged into the market, however, the price has plummeted. Today, it is literally a penny stock, trading at below \$1 per share. The Cole Taylor stockholders who placed their trust and confidence in the new company have lost virtually their entire investment.

The Misleading Nature Of The Proxy

81. The Proxy was materially false and misleading due to its omission of numerous facts concerning Reliance and its financial and operating conditions. First, the Proxy misrepresented that it applied appropriate underwriting standards in determining whether to purchase automobile sales contracts in order to ensure an appropriate level of risk. In fact, at least 30 percent of the contracts purchased by Reliance were in violation of its own

underwriting standards and had to be purchased through undisclosed exceptions. Second, the Proxy misrepresented that Reliance had adequately protected itself from credit losses through the use of discounts to purchase sales contracts from dealers, with the remainder of such discounts, after adjusting for losses, being accreted to income. What shareholders were not told was that by at least October 1, 1996, prior to the date of the Proxy, Cole Taylor already knew that its discounts were insufficient to cover anticipated losses, requiring a material change in its policies whereby it no longer permitted the discounts to be accreted to income. Third, the Proxy failed to disclose that Reliance had changed its prior practice of selling repossessed vehicles through dealers, but instead were auctioning them off through third parties, a change in policy that led directly to a substantial reduction in the ultimate recovery obtained by Reliance. Fourth, the proxy misrepresented that Reliance used appropriate underwriting procedures, and maintained adequate checks and controls over its branch offices, when, in contrast, its underwriting procedures were inadequate and insufficient to ensure against excessive losses and there were improper procedures in place to control the branch offices.

82. The misrepresented or undisclosed information described herein would have been highly material to the decision of the Cole Taylor shareholders concerning how to vote on the proposed Split-Off Transaction, which was based on the value being provided by the Taylor family in exchange for their Reliance common stock. Had the shareholders known of the extent of the problems, and how dramatic it might effect Reliance's earnings and its common stock price, they may well have taken appropriate steps to stop the transaction from

being consummated or, alternatively, demanded far better consideration for the Cole Taylor banking operations.

83. Because of the material misrepresentations and omissions contained in the Proxy as alleged herein, the defendants have violated the federal securities laws.

Breach of Fiduciary Duty

84. Given the undisclosed facts concerning the excessive losses in Cole Taylor's subprime automotive finance business, and the defendants' failure to comply with their own underwriting standards, the value of the assets contributed by the Taylor family in the Split-Off Transaction was grossly unfair, inadequate and substantially below the fair or inherent value of the banking assets which they received in return. In sum, the value of the equity of the banking assets was materially greater than the consideration being offered.

85. The Split-Off Transaction therefore denied plaintiffs and other Class members their rights to share proportionately in the true value of Cole Taylor's assets and future growth in profits and earnings. The Taylor family appropriated the profitable banking assets and the on-going banking business for themselves at a price which was substantially less than their fair market value. In so doing, the Taylor family engaged in self-dealing to the detriment of the Class members.

86. The Taylor family, and their associates who assumed management positions with Taylor Capital following the consummation of the Split-Off Transaction, had a clear and direct incentive to engage in the deceptions and breach of fiduciary duty alleged herein, as they obtained the valued banking assets of Cole Taylor for unfair and inadequate

consideration. The Cole family, and their associates who assumed management positions with Reliance following the consummation of the Split-Off Transaction, had a similar clear and direct incentive to engage in the deceptions and breach of fiduciary duty alleged herein, as they obtained control over the Reliance assets, through which they hoped to maximize the value of their own investments by continuing to mislead the investment public concerning Reliance's financial condition and prospects.

87. The defendants, who controlled a majority interest in Cole Taylor, were not acting in good faith toward plaintiffs and the Class; have breached their fiduciary duty to plaintiffs and the Class; and have willfully participated in unfair dealing toward plaintiffs and the Class.

COUNT I

FOR VIOLATIONS OF §14(a) AND (e) OF THE EXCHANGE ACT AND RULE 14(a)-9

88. Plaintiffs repeat and reallege each of the foregoing paragraphs as if fully set forth herein.

89. The defendants made materially misleading statements and failed to disclose material facts concerning Reliance's financial condition and prospects, the nature and extent of the problems it was experiencing with its loans, and the value of its common stock.

90. The defendants made the misleading statements identified herein and omissions of material facts in connection with a solicitation of stockholders to vote for the Split-Off Transaction. Absent these false and misleading statements, the defendants would not

have persuaded plaintiffs and the Class to approve the Transaction, at least under the specified conditions.

91. Taylor and Reliance are liable as the former component parts of Cole Taylor, the issuer of the Proxy. The Individual Defendants, as directors and/or senior executive officers of Cole Taylor, were controlling persons of the corporate defendants and authorized and approved the Proxy. Moreover, the Individual Defendants recommended to the Class members through the Proxy that they approve the Split-Off Transaction based on false and misleading information.

92. The defendants named herein were responsible for the contents of the Proxy and none of them made a reasonable investigation nor possessed reasonable grounds for the belief that the statements contained in the Proxy were true and without omissions of any material fact and were not misleading. In approving, authorizing or permitting the dissemination of the Proxy with the material misrepresentations and omissions alleged herein, the defendants acted negligently, recklessly or knowingly. They knew or were negligent or reckless in not knowing of the undisclosed or misrepresented facts.

93. At the time of their receipt of the Reliance stock, plaintiffs and other members of the Class were without knowledge of the facts concerning the wrongful conduct alleged herein and could not have reasonably discovered those facts prior to the end of the Class Period. Less than one year elapsed from the time that plaintiffs discovered or reasonably could have discovered the facts upon which this claim is based to the time that plaintiffs filed their Complaint herein.

94. As a direct result of defendants' misleading statements and omissions of material facts, plaintiffs and the Class have been damaged in an amount to be determined at trial.

COUNT II

FOR BREACH OF FIDUCIARY DUTY

95. Plaintiffs repeat and reallege each of the foregoing paragraphs as if fully set forth herein.

96. As majority shareholders and directors and/or executive offices of Cole Taylor, the defendants owed the highest fiduciary duty of loyalty, honesty and fairness to the plaintiffs and the Class, as Cole Taylor's minority shareholders, including the duty to be scrupulously fair in their dealings with them.

97. By entering into the Split-Off Transaction, which provided the minority shareholders unfair and inadequate compensation for Cole Taylor's banking assets, and by misrepresenting the financial condition and prospects of the remaining public company, the defendants breached their fiduciary duty owed to plaintiffs and the Class.

98. As a direct result of the actions of the defendants, plaintiffs and other members of the Class have been damaged in that they were the victims of unfair dealing and did not receiving the fair value of their interests in Cole Taylor.

COUNT III

ON BEHALF OF THE ERISA SUBCLASS FOR VIOLATION OF ERISA

99. Plaintiff Ronald P. Graham repeats and realleges the foregoing paragraphs.

100. The defendants, through Cole Taylor Bank, Cole Taylor's wholly-owned subsidiary, were fiduciaries to plaintiff and the members of the ERISA Subclass, as participants and beneficiaries of employee benefit plans, the ESOP and the Profit Sharing Plan.

101. The defendants breached their fiduciary obligations owed to the plaintiff and the members of the ERISA Subclass under ERISA by intentionally or recklessly misrepresenting the terms and conditions of its the Split-Off Transaction and by engaging in self-dealing at the expense of ESOP and the Profit Sharing Plan by removing Cole Taylor's most valuable asset, the Cole Taylor Bank, for inadequate and unfair consideration.

102. As a result of the violations of ERISA alleged herein, plaintiff and the members of the ERISA Subclass have suffered injury, for which they are entitled to appropriate relief, including, but not limited to, the equitable relief of disgorgement by Taylor Capital and the members of the Taylor Family of the profits they earned by unfairly assuming ownership of Cole Taylor Bank.

PRAYER FOR RELIEF


WHEREFORE, plaintiffs on behalf of themselves and the Class pray for judgment as follows:

1. Declaring this action to be a proper class action maintainable pursuant to Fed. R. Civ. P. 23(a) and (b)(3) on behalf of the Class as defined herein;
3. Awarding plaintiffs and the Class compensatory money damages;
4. Awarding plaintiff Ronald P. Graham and the ERISA Subclass appropriate relief under ERISA;
5. Awarding plaintiffs and the Class pre-judgment and post-judgment interest along with reasonable attorneys' fees and expenses, including experts' fees;
6. Awarding plaintiffs the costs and disbursements of this action; and
7. Awarding such other relief as this Court may deem just and proper.

JURY DEMAND

Plaintiffs demand a trial by jury of all issues so triable.

DATED: February 6, 1998



MARVIN A. MILLER
KENNETH A. WEXLER
ADAM J. LEVITT
MILLER FAUCHER CAFFERTY
and WEXLER LLP
30 N. LaSalle St.
Suite 3200
Chicago, IL 60602
(312) 782-4880

**POMERANTZ HAUDEK BLOCK &
GROSSMAN**
STANLEY M. GROSSMAN
D. BRIAN HUFFORD
100 Park Avenue
New York, NY 10017
Telephone: 212/661-1100

BERMAN DeVALERIO & PEASE, LLP
GLEN DeVALERIO
One Liberty Square
Boston, MA 02109
(617) 542-8300

Attorneys for Plaintiffs

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PLAINTIFF'S SWORN CERTIFICATION

I, William E. Huber, hereby certify that the following is true and correct to the best of my knowledge, information and belief:

1. I have reviewed the complaint filed herewith in the captioned action (the "Complaint"), and have authorized the filing thereof.
2. I am willing to serve as a representative party on behalf of the class (the "Class") as defined in the Complaint, including providing testimony at deposition and trial, if necessary.
3. As of September 20, 1996, I held 1200 shares of common stock of Cole Taylor Financial Group, Inc. and, as such, received a Proxy Statement dated October 15, 1996 soliciting my vote at the November 15, 1996 Shareholder Meeting.
4. I did not purchase these securities at the direction of my counsel, or in order to participate in any private action arising under the Securities Exchange Act of 1934.
5. During the three year period preceding the date of my signing this Certification, I have not sought to serve, nor have I served, as a representative party on behalf of a class in a private action arising under the Securities Exchange Act of 1934.
6. I will not accept any payment for serving as a representative party on behalf of the Class beyond my pro rata share of any possible recovery, except for an award, as ordered or approved by the court, for reasonable costs and expenses (including lost wages) directly relating to my representation of the Class.

Signed under penalties of perjury this 3 day of FEBRUARY, 1998.

William Eric Graham

PLAINTIFF'S SWORN CERTIFICATION

I, Ronald P. Graham, hereby certify that the following is true and correct to the best of my knowledge, information and belief:

1. I have reviewed the complaint filed herewith in the captioned action (the "Complaint"), and have authorized the filing thereof.
2. I am willing to serve as a representative party on behalf of the class (the "Class") as defined in the Complaint, including providing testimony at deposition and trial, if necessary.
3. As of September 20, 1996, I held 2,504 shares of common stock of Cole Taylor Financial Group, Inc. and, as such, received a Proxy Statement dated October 15, 1996 soliciting my vote at the November 15, 1996 Shareholder Meeting.
4. I did not purchase these securities at the direction of my counsel, or in order to participate in any private action arising under the Securities Exchange Act of 1934.
5. During the three year period preceding the date of my signing this Certification, I have not sought to serve, nor have I served, as a representative party on behalf of a class in a private action arising under the Securities Exchange Act of 1934.
6. I will not accept any payment for serving as a representative party on behalf of the Class beyond my pro rata share of any possible recovery, except for an award, as ordered or approved by the court, for reasonable costs and expenses (including lost wages) directly relating to my representation of the Class.

Signed under penalties of perjury this 3rd day of February 1978

[Handwritten Signature]

Sworn to before me this
3rd day of February, 1978

Calvin L. Insala
Notary Public

