[ORAL ARGUMENT NOT YET SCHEDULED]

No. 14-5243
(Consolidated with Nos. 14-5254, 14-5260, and 14-5262)

IN UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

PERRY CAPITAL LLC, for and on behalf of
investment funds for which it acts as investment manager,

Plaintiff-Appellant,

v.

JACOB J. LEW, in his official capacity as the
Secretary of the Department of the Treasury, et al.,

Defendants-Appellees.

On Appeal from the United States District Court for the
District of Columbia (Nos. 1:13-cv-01025-RCL, etc.)

BRIEF OF JONATHAN R. MACEY AS AMICUS CURIAE IN SUPPORT OF APPELLANT AND REVERSAL

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CERTIFICATE AS TO PARTIES, RULINGS, AND RELATED CASES

Pursuant to Circuit Rule 28(a)(1), I hereby certify as follows:

(A) Parties and Amici. All parties, intervenors, and amici appearing before the district court and in this Court are listed in the Initial Opening Brief for Institutional Plaintiffs (filed June 29, 2015) or in the Initial Opening Brief for Class Plaintiffs (filed June 30, 2015).

(B) Rulings Under Review. Accurate references to the rulings at issue appear in the two aforementioned briefs.

(C) Related Cases. Accurate references to related cases appear in the two aforementioned briefs.

Dated: July 6, 2014.

s/ Eric Grant
Eric Grant

Counsel for Amicus Curiae
Jonathan R. Macey

CERTIFICATE REGARDING SEPARATE AMICUS BRIEF

Pursuant to Circuit Rule 29(d), I hereby certify that a separate brief for Amicus Curiae Jonathan R. Macey is necessary. As elaborated in the Interest of Amicus Curiae section below (p. 1), Amicus teaches corporate law, corporate finance, and securities regulation at one of the nation's leading law schools. His extensive research and recognized expertise in these fields is especially valuable in discussing how the challenged governmental action has deprived Plaintiff shareholders of all economically beneficial uses of their property and otherwise interfered with their reasonable investment-backed expectations.

Dated: July 6, 2014.

s/ Eric Grant
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GLOSSARY

FHFA	Federal Housing Finance Agency
GSEs	Government-sponsored enterprises and the district court's shorthand for the Federal National Mortgage Association and the Federal Home Loan Mortgage Corporation
Op.	Memorandum Opinion, Doc. 51 in 1:13-cv-01025-RCL (filed Sept. 30, 2014)
Third Amendment	Third Amendment to the Senior Preferred Stock Purchase Agreements between the United States Department of the Treasury and the Federal Housing Finance Agency, as conservator to the Federal National Mortgage Association and the Federal Home Loan Mortgage Corporation, dated August 17, 2012, and the declaration of dividends pursuant to the Third Amendment beginning on January 1, 2013

INTEREST OF AMICUS CURIAE[1]

Amicus is a law professor who teaches corporate law, corporate finance, securities regulation, and bankruptcy at Yale Law School. His interest is in preventing regulatory takings jurisprudence from being misinterpreted to condone the Third Amendment to the Senior Preferred Stock Purchase Agreements between FHFA and Plaintiff shareholders, or to condone the Amendment's corresponding net worth sweeps. To those ends, Amicus urges this Court to assess the Third Amendment's net worth sweeps in light of their complete destruction of the value of Plaintiff shareholders' shares, as well as their complete disregard for the statutory limits on FHFA's regulatory powers. This brief draws on Amicus Curiae's research and expertise in these areas to analyze this issue for the benefit of the Court.

ARGUMENT

I. Owning shares in a regulated entity does not deprive Plaintiff shareholders of a cognizable property interest in the dividends or liquidation preferences that shareholders expect to receive when they purchase their shares.

Property rights, in the takings context, "includes the entire 'group of rights inhering in the citizen's [ownership].'" *Penn Central Transportation Co. v. City of New York*, 438 U.S. 104, 142 (1978) (quoting *United States v. General Motors*

[1] Counsel for Amicus Curiae certifies that no counsel for any party authored this brief in whole or in part, and that no person or entity other than Amicus Curiae or his counsel made a monetary contribution intended to fund the brief's preparation or submission. All parties have consented to the filing of this brief.

Corp., 323 U.S. 373, 378 (1945)). Thus, while FHFA's conservatorship may trim the "bundle of property rights" held by the Plaintiff shareholders in relation to their stock ownership, it cannot eliminate Plaintiff shareholders' cognizable property interest in future dividends and liquidation preferences. FHFA as a conservator has the right to constrain Plaintiff shareholders' property only via its statutorily granted regulatory powers.

A. Plaintiff shareholders had no reason to expect the entirety of the GSEs' net profits to be seized.

As the District Court noted, "plaintiffs 'voluntarily entered into [investment contracts with] the highly regulated' GSEs." Op. at 49 (quoting *Golden Pacific Bancorp v. United States*, 15 F.3d 1066, 1073 (Fed. Cir.), *cert. denied*, 513 U.S. 961 (1994)). Nevertheless, as discussed below, the Third Amendment steps outside the bounds of FHFA's statutorily-prescribed tools for regulation. Because FHFA exceeded its statutory authority in carrying out the Third Amendment's net worth sweeps, Plaintiff shareholders could not have "reasonably expected" the entirety of the GSEs' net profits to be seized in a self-awarded FHFA dividend like that effected by the Third Amendment. *See District Intown Properties Limited Partnership v. District of Columbia*, 198 F.3d 874, 883 (D.C. Cir. 1999) (holding that District Intown could "reasonably expect" the Shipstead-Luce Act to affect its rights of development), *cert. denied*, 531 U.S. 812 (2000).

The magnitude of the change in FHFA's self-entitlement to payment between the Second and Third Amendment speaks to the unpredictable and shocking nature of the Third Amendment's effects on the Plaintiff shareholders' shares. "Under the Third Amendment net worth sweep[s], the GSEs paid Treasury nearly $130 billion in 2013. . . . [U]nder the former dividend arrangement requiring payment equivalent to 10% of Treasury's existing liquidation preference, the GSEs would have owed [*only*] $19 billion." Op. at 9. While the Plaintiff shareholders could *not* reasonably expect "regulation [would] not be strengthened to achieve established legislative ends," *District Intown*, 198 F.3d at 884, Plaintiff shareholders *could* reasonably expect their shares to maintain a value greater than zero.

The Government recently raised the issue that some Plaintiff shareholders purchased their shares *after* the enactment of the Third Amendment. This fact, however, does not extinguish Plaintiff shareholders' ability to bring a takings claim. The Supreme Court has rejected "the argument that postenactment purchasers cannot challenge a regulation under the Takings Clause, reasoning that some "enactments are *unreasonable* and do not become less so through passage of time or title." *Palazzolo v. Rhode Island*, 533 U.S. 606, 626-27 (2001) (emphasis added). Plaintiff shareholders who purchased shares after the enactment of the Third Amendment should not be barred from claiming that the Third Amendment's net worth sweeps constitute regulatory takings.

B. 12 U.S.C. § 4617(b)(2)(A)(i) does not grant the FHFA the right to seize dividends, intended for shareholders, for itself.

The governing statute grants FHFA the power to assume "all rights, titles, powers, and privileges of the regulated entity, and of any *stockholder, officer, or director* of such regulated entity." 12 U.S.C. § 4617(b)(2)(A)(i) (emphasis added). Assuming the rights of a stockholder, for example, FHFA has the right to elect directors. Additionally, assuming the rights of a director, FHFA has the right to execute decisions related to dividend allocation.

This statute, however, does not give FHFA the right to declare discretionary dividends for itself alone. No stockholder, officer, or director has the right to declare all prospective dividends for itself alone. Therefore, the right to seize all dividends for oneself cannot have devolved to FHFA by means of the conservatorship. With this statutory constraint in mind, the Third Amendment's net worth sweeps overstep FHFA's legislated authority by seizing all of the GSEs' net profits in a self-awarded and exclusive dividend.

The district court relied on *California Housing Securities, Inc. v. United States*, 959 F.2d 955 (Fed. Cir.), *cert. denied*, 506 U.S. 916 (1992), and on *Golden Pacific Bancorp* in holding that shareholders of statutorily regulated financial institutions "lacked the requisite property interests to support a takings claim." Op. at 44. These cases, however, dealt with significantly different exercises of regulatory power. In *California Housing Securities*, for example, the RTC as a conservator

liquidated assets and liabilities. 959 F.2d at 956. Likewise, in *Golden Pacific Bancorp*, the court assessed a regulation that merely declared Golden Pacific insolvent and appointed the FDIC as its conservator. 15 F.3d at 1068. Neither of these cases contemplated regulatory action that surpassed the conservator's statutory calling, as the Third Amendment's net worth sweeps did here.

II. The Third Amendment's net worth sweeps constitute regulatory takings.

For at least a century, the "general rule" has been that "while property may be regulated to a certain extent, if regulation goes too far it will be recognized as a taking." *Pennsylvania Coal Co. v. Mahon*, 260 U.S. 393, 415 (1922). The Third Amendment — which, put simply, "requires Fannie Mae and Freddie Mac to pay a quarterly dividend to Treasury equal to the entire net worth of each Enterprise, minus a small reserve that shrinks to zero over time," Op. at 8 — is one such regulation that has gone so far as to effect a regulatory taking via its net worth sweeps.

A. The Third Amendment's net worth sweeps constitute *per se* regulatory takings, as they deprive Plaintiff shareholders of "all economically beneficial uses" of their property.

As the Third Amendment's net worth sweeps deprive Plaintiff shareholders of all economically beneficial uses of their property, they constitute *per se* regulatory takings. "Our precedents stake out . . . categories of regulatory action that generally will be deemed *per se* takings for Fifth Amendment purposes. . . . [A] categorical rule applies to regulations that completely deprive an owner of '*all*

economically beneficial us[e]' of her property." *Lingle v. Chevron U.S.A. Inc.*, 544 U.S. 528, 538 (2005) (quoting *Lucas v. South Carolina Coastal Council*, 505 U.S. 1003, 1019 (1992) (emphasis in *Lucas*)). Likewise, as the district court itself acknowledged, *see* Mem. Op at 47: "When the owner of real property has been called upon to sacrifice *all* economically beneficial uses in the name of the common good, that is, to leave his property economically idle, he has suffered a taking." *Lucas*, 505 U.S. at 1019. Moreover, "[w]here the State seeks to sustain regulation that deprives land of *all economically beneficial use*, we think it may resist compensation only if the logically antecedent inquiry into the nature of the owner's estate shows that the proscribed use interests were not part of his title to begin with." *Id.* at 1027 (emphasis added).

For example, the Supreme Court reasoned in *Pennsylvania Coal*: "To make it commercially impracticable to mine certain coal has very nearly the same effect for constitutional purposes as appropriating or destroying it." 260 U.S. at 414 (finding restriction against coal mining to be a taking of preexisting mining rights). In *Penn Central*, on the other hand, the Supreme Court upheld a New York regulation against a takings challenge because the regulation permitted Penn Central to continue the "present uses" of its property and "not only to profit from the [property] but also to obtain a 'reasonable return' on its investment" 438 U.S. at 136.

The Third Amendment's net worth sweeps render it impossible for Plaintiff shareholders to profit via dividends or sale, and thus bar Plaintiff shareholders' collection of any profits or "reasonable return[s] on [their] investment." *Id.* By denying Plaintiff shareholders these faculties, the Third Amendment's net worth sweeps deprive Plaintiff shareholders of "all economically beneficial uses" of their property. *Lucas*, 505 U.S. at 1027. Moreover, unlike in *Penn Central*, the Third Amendment's net worth sweeps necessarily interfere with the "present uses" of the Plaintiff shareholders' shares, as those shares can be used *only* for the purposes of dividend collection in the present and capital gains in the future.

The district court held to the contrary, concluding that "the Third Amendment has had no economic impact on the plaintiffs' alleged dividend or liquidation preference rights." Op. at 48. In so concluding, the district court erred by mistakenly relying on current analyses of tradability to determine the Third Amendment's impact on the value of Plaintiff shareholders' shares.

If there is no hope of a shareholder ever receiving returns from a company in either dividends or capital gains, the economic value of that stock is zero, and the shares are devoid of any economically beneficial use. The sole reason that Plaintiff shareholders' shares currently trade at values above zero is that market anticipates the Third Amendment will be struck down in this very litigation. As such, the marketability of the Plaintiff shareholders' shares — i.e., the fact that the shares

trade at a price above zero — is dependent on the non-zero probability that the Third Amendment's net worth sweeps will be adjudicated to be regulatory takings (or other remediable violations of law). Thus, Plaintiff shareholders' shares' current trading value is irrelevant to a discussion of the true economic impact of the Third Amendment.

B. Alternatively, the *Penn Central* factors weighed in balance and in an ad hoc fashion establish the Third Amendment's net worth sweeps as regulatory takings.

Even if the Court disagrees that the Third Amendment's net worth sweeps are *per se* regulatory takings, a *Penn Central* analysis clearly demonstrates that the sweeps' qualify as regulatory takings. Outside the *per se* category, "regulatory takings challenges are governed by the standards set forth in *Penn Central*." *Lingle*, 544 U.S. at 531.

As the District Court acknowledged, *see* Op. at 48, "[t]here are three main factors to be considered in *Penn Central*'s ad hoc inquiry [to determine the existence vel non of a regulatory taking]: the character of the government action, the regulation's economic effect on the claimant, and the effect on investment-backed expectations." *District Intown*, 198 F.3d at 883. Moreover, a "plaintiff is not required to demonstrate favorable results under all three *Penn Central* factors in order for the Court to find a taking — it is a balancing test." Op. at 48.

1. Regardless of the "character of the government's action" in relation to the Third Amendment, the other two factors are sufficient to evidence a regulatory taking.

Admittedly, the Third Amendment does not accomplish a "permanent physical occupation" of property sufficient to semi-automatically trigger the character prong of the *Penn Central* analysis. *Loretto v. Teleprompter Manhattan CATV Corp.*, 458 U.S. 419, 435 (1982). Nevertheless, the weight of the two remaining components of the *Penn Central* balancing test cause character analysis in this particular case to be unnecessary for finding a regulatory taking.

2. The economic effects of the Third Amendment's net worth sweeps are severe.

As discussed in Section II.A above (pp. 5-8), the Third Amendment's net worth sweeps have severe economic effects. The severity of these economic effects signals a regulatory taking under the *Penn Central* analysis. "Primary among the [*Penn Central*] factors are 'the economic impact of the regulation on the claimant . . . .'" *Lingle*, 544 U.S. at 538-39 (quoting *Penn Central*, 438 U.S. at 124).

a. The Third Amendment's net worth sweeps deprive Plaintiff shareholders of any and all hope for dividends in the future.

By requiring that the GSEs "pay, as a dividend, the amount by which their net worth for the quarter exceeds a capital buffer of 3 billion," and declaring that "the capital buffer gradually declines over time by $600 million per year, and is

entirely eliminated in 2018," FHFA effectively eliminated any and all possibility of dividends for Plaintiff shareholders in the future. Op. at 8.

b. The Third Amendment's net worth sweeps drastically decrease the probability of capital gains upon the sale of Plaintiff shareholders' shares.

Given the strong relationship between market price and probability for dividends and capital gains, the looming decrease in the GSEs' per share price is *not* "contingent upon future events that may not occur as anticipated, or indeed may not occur at all." Op. at 34 (quoting *Texas v. United States*, 523 U.S. 296, 300 (1998)). By seizing all net profits of the GSEs for the foreseeable future, the Third Amendment's net worth sweeps *will* negatively impact the value of Plaintiff shareholders' shares. The price of a share of stock reflects the present value of the future income and capital gains that the capital markets estimate will be paid on a per share basis. This future income stream comes in the form of dividends and capital gains expected in the future. These future capital gains are derived from shareholders' ability to sell his or her shares on the market, in the context of a tender offer or a merger, or in some other fundamental corporate restructuring.

The Third Amendment's net worth sweeps have decreased the probability of future dividends and capital gains for the GSEs' shares to zero due to their seizure of all net profits. As a result of these seizures, the future income stream determining the GSEs' price per share is effectively zero, and that fact will likewise cause

Plaintiff shareholders' shares to be valued at zero.[2] Shares with zero value are largely untradeable and illiquid, thus leaving Plaintiff shareholders with no means for extracting a return on their investment.

3. The Third Amendment's net worth sweeps interfered with Plaintiff shareholders' reasonable "investment-backed expectations."

The Third Amendment's net worth sweeps interfere with Plaintiff shareholders' ability to "use the property precisely as it has been used." *Penn Central*, 438 U.S. at 136. Shares like those purchased by Plaintiff shareholders in the GSEs are used "precisely" as tools for investment. Shareholders possess "investment-backed expectations" in their ability to capture dividends and capital gains from their shares. The Third Amendment's net worth sweeps directly counter Plaintiff shareholders' ability to use their property "precisely as it has been used," namely, in the pursuit of profits and returns.

In *District Intown*, this Court emphasized that the "primary expectations" for the property were not disturbed, as District Intown was prevented only from the non-traditional use of developing the property's lawns into apartment buildings. 198 F.3d at 883. In contrast, the Third Amendment's net worth sweeps disable the

[2] See the immediately following Section II.B.3 for a discussion of why Plaintiff shareholders' shares have not yet decreased in value to zero.

Plaintiff shareholders from exercising their *primary* and *traditional* expectations for their shares: collecting, or aspiring to collect, dividends and capital gains.

Some may argue that those Plaintiff shareholders who purchased shares after the Third Amendment went into effect have no reasonable investment-backed expectations contrary to the net worth sweeps. This argument ignores the simple fact that the shares purchased after the Third Amendment went into effect retained a positive value based on investors' reasonable expectation that the confiscatory net worth sweeps would be ruled illegal. Thus, at the time of purchase, not only Plaintiff shareholders, but the capital markets themselves, reasonably believed (and still believe) that the Third Amendment's net worth sweeps would be overturned in court. This is what gave the shares a positive value after the Third Amendment went into effect. Consequently, regardless of whether or not their shares were purchased prior to the Third Amendment's enactment, each Plaintiff shareholder had and continues to have reasonable investment-backed expectations of holding a stock regulated by FHFA only to the extent legally permissible. Because it was — and is — reasonable to believe that the net worth sweeps are not legally permissible, investors who purchased their shares after the Third Amendment went into effect had legitimate investment-backed expectations at the time of their purchases.

a. It is a violation of Plaintiff shareholders' fundamental rights for a firm to deprive them of any and all hope for dividends in the future.

Admittedly, "shareholders only have the right to receive such dividends as are declared by the corporation's board of directors. Directors have no obligation to declare dividends and may reinvest the corporation's profits rather than distribute them to shareholders." Julian Velasco, *The Fundamental Rights of the Shareholder*, 40 U.C. Davis L. Rev. 407, 414 (2006).

The district court, however, misread the discretionary declaration of a dividend to FHFA alone, to the exclusion of Plaintiff shareholders, as a legitimate corporate action. On the contrary, the government has no more right to declare that all dividends belong to it than do corporate directors have the right to declare that they, rather than shareholders, should receive all dividend payments. Under the Third Amendment, Plaintiff shareholders have *no* hope of dividends in the future, as all future net profits will be seized by FHFA. Through this mechanism, Plaintiff shareholders have been deprived of their ability to pursue their preexisting investment-backed expectations of receiving any dividends granted in the future.

As the District Court pointed out and as recognized above, whether or not a dividend will be issued is not up to the shareholder. Nevertheless, the Court in *Pennsylvania Coal* was not preoccupied with the guarantee that the plaintiffs would indeed find coal, but instead their ability to mine for it. Neither are we here con-

cerned with the guarantee that Plaintiff shareholders *will* be granted a dividend. Plaintiff shareholders' investment-backed expectations inhere in the *possibility* of future dividends, a possibility that is completely thwarted by FHFA's seizure of *all* net profits and its self-awarded right to *all* future dividends. It is this decreased *probability* in dividends (decreased to zero) that should concern the Court.

b. Purchasers of shares reasonably expect those shares to retain their tradability and liquidity.

"[S]hareholders have a strong right to sell shares and to any resulting profit. This right of alienation is of the utmost importance to shareholders both because it is a means of obtaining economic benefit from their investment in the corporation and because it is their means of exit should they become dissatisfied with management." Velasco, *supra*, at 425 (footnote omitted). The Third Amendment's net worth sweeps and their effects on the value of the GSEs' shares described above interfere with Plaintiff shareholders' reasonable "investment-backed expectation" that the shares in which they purchased a property interest will remain liquid. By effectively decreasing the GSEs' per share value to zero, the Third Amendment's net worth sweeps deprive Plaintiff shareholders of liquidity should they choose to sell their ownership stake in the GSEs. No investor will purchase valueless shares, and thus Plaintiff shareholders will be unable to collect capital gains from exiting their ownership in the GSEs.

III. Under the District Court's conception of a regulatory taking, no share of stock could ever be subject to a regulatory taking.

The district court erred in its overemphasis of Treasury's discretion to refrain from declaring a dividend as an indicator that no regulatory taking occurred. *Any* conservator and or government entity in control of *any* company will *always* have discretion about whether or not to pay a dividend. It is not the discretion of the FHFA as a conservator that is relevant here, but instead the impact of that discretion on the probability of future dividends and/or capital gains that renders the Third Amendment's net worth sweeps regulatory takings.

CONCLUSION

The Third Amendment's dividends of all net profits changed the probability that Plaintiff shareholders will receive periodic payments of dividends to zero, decreased the future value of their shares to zero, and concomitantly extinguished their ability to collect capital gains through sale. The only way that Plaintiff shareholders will receive a return on their investment is if Plaintiffs prevail in this litigation. Because the Third Amendment's net worth sweeps accordingly deprive Plaintiff shareholders of all economically beneficial uses of their property, the net worth sweeps are *per se* regulatory takings.

Alternatively, the Third Amendment's net worth sweeps qualify as regulatory takings under the *Penn Central* test by interfering with Plaintiff shareholders' investment-backed expectations in the *possibility* of future dividends and capital

gains and by concomitantly effecting a decrease in the economic value of the GSEs' shares to *zero*.

The district court mistakenly read 12 U.S.C. § 4617(b)(2)(A)(i) to justify these destructive economic effects by authorizing FHFA's seizure of the GSEs' future net profits. The district court stated: "Any sense of unease over the defendants' conduct is not enough to overcome the plain meaning of HERA's text. Here, the plaintiffs' true gripe is with the language of a statute that enabled FHFA and, consequently, Treasury, to take unprecedented steps to salvage the largest players in the mortgage finance industry before their looming collapse triggered a systemic panic." Op. at 52. The statute, however, does *not* provide FHFA with the regulatory power to commit the seizures provided for by the Third Amendment. FHFA's self-awarded and exclusive dividend was an unauthorized expansion of its regulatory authority and further evidences the Third Amendment's net worth sweeps' character as regulatory takings.

Dated: July 6, 2014.

Respectfully submitted,

s/ Eric Grant
Eric Grant
Jonathan R. Macey

Counsel for Amicus Curiae
Jonathan R. Macey

CERTIFICATE OF COMPLIANCE

I hereby certify that this brief complies with the type-volume limitation of Fed. R. App. P. 29(d) because this brief contains 3,692 words, excluding the parts of the brief exempted by Fed. R. App. P. 32(a)(7)(B)(iii).

Dated: July 6, 2014.

s/ Eric Grant
Eric Grant

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CERTIFICATE OF SERVICE

I hereby certify that I electronically filed the foregoing with the Clerk of the Court by using the appellate CM/ECF system on July 6, 2014.

I hereby certify that all participants in the case are registered CM/ECF users and that service will be accomplished by the appellate CM/ECF system.

Dated: July 6, 2014.

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