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

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

FAIRHOLME FUNDS, INC., *et al.*,
Plaintiffs-Appellants,

v.

FEDERAL HOUSING FINANCE AGENCY, *et al.*,
Defendants-Appellees.

On Appeal from the United States District Court for the District of Columbia

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OPPOSITION OF APPELLEES FEDERAL HOUSING FINANCE AGENCY, MELVIN L. WATT, FANNIE MAE, AND FREDDIE MAC TO APPELLANT FAIRHOLME FUND, INC.'S MOTION FOR JUDICIAL NOTICE AND TO SUPPLEMENT THE RECORD

Howard N. Cayne
Asim Varma
David B. Bergman
Michael A.F. Johnson
Dirk C. Phillips
Ian S. Hoffman
ARNOLD & PORTER LLP
555 Twelfth Street, NW
Washington, DC 20004
(202) 942-5000
Howard.Cayne@aporter.com

Counsel for Appellees Federal Housing Finance Agency and Melvin L. Watt

Paul D. Clement
D. Zachary Hudson
BANCROFT PLLC
500 New Jersey Ave. NW, 7th Floor
Washington, D.C. 20001
(202) 234-0090
pclement@bancroftpllc.com

Counsel for Appellee Federal National Mortgage Association

Michael J. Ciatti
Graciela Maria Rodriguez
KING & SPALDING LLP
1700 Pennsylvania Ave. NW
Washington, DC 20006
(202) 626-5508
mciatti@kslaw.com

Counsel for Appellee Federal Home Loan Mortgage Corporation

INTRODUCTION

This is an appeal from a grant of motions to dismiss. By definition, there are no facts in dispute. The plaintiffs in the above-captioned case were free to—and did—allege a one-sided version of events favoring their theory of the case. The district court was required to—and did—accept those allegations as true for purposes of resolving the motions to dismiss. Plaintiff-Appellant Fairholme nevertheless seeks to inject into this appeal hundreds of pages of discovery materials obtained in connection with a different case filed in a different court, all in an effort to substantiate factual allegations that the court below already assumed to be true in dismissing this action. Fairholme offers no explanation as to how this material could be relevant to resolving the purely legal issues governing the resolution and disposition of this appeal. Nor could it: the court below dismissed all of the claims based on purely legal grounds, declaring FHFA's Document Compilation and Treasury's Administrative Record "irrelevant" to its decision.

In the alternative, Fairholme also seeks immediate remand of this case to the district court prior to consideration of the merits of its pending appeal. As with its initial request for judicial notice, Fairholme leaves to the Court's speculation what new allegations it would add to its dismissed complaint on remand and how such additional allegations conceivably could lead to a different legal result. No basis exists for granting either request.

BACKGROUND

At issue in this appeal are suits brought by multiple holders of the shares of Federal National Mortgage Association ("Fannie Mae") and Federal Home Loan Mortgage Corporation ("Freddie Mac," and, together with Fannie Mae, the "Enterprises"), all of which were issued prior to the placement of the Enterprises into statutory conservatorships on September 6, 2008. The Enterprises are corporations chartered by Congress to provide liquidity to the national housing finance market. The Federal Housing Finance Agency ("FHFA")[1] is an independent agency created by the Housing and Economic Recovery Act of 2008 ("HERA") (Pub. L. No. 110-289, § 1101, 122 Stat. 2654, 2661 (codified at 12 U.S.C. § 4511 *et seq.*)). Under HERA, FHFA serves as the regulator of the Enterprises. *See* 12 U.S.C. § 4513(a). HERA also grants the Director of FHFA authority to appoint the agency conservator or receiver of the Enterprises. *Id.* § 4617(a)(1).

On September 6, 2008, having concluded that the Enterprises could not continue to operate safely and soundly and fulfill their critical public mission without intervention, FHFA's Director placed the Enterprises in conservatorships. As Conservator and on behalf of the Enterprises, FHFA entered into agreements

[1] FHFA files this opposition together with the Enterprises and Melvin L. Watt, in his official capacity as Director of FHFA.

with the Department of Treasury—commonly known as the Senior Preferred Stock Purchase Agreements ("PSPAs")—by which billions of taxpayer dollars were used to keep the Enterprises afloat and prevent them from falling into mandatory receivership and liquidation. In exchange for providing this lifeline to the Enterprises, the PSPAs granted Treasury a comprehensive package of rights, including: (1) an initial senior liquidation preference of $1 billion for each Enterprise; (2) warrants to acquire 79.9% of the Enterprises' common stock for a nominal payment; (3) payment from each Enterprise of a mandatory and cumulative annual dividend in the amount of 10% of the funds drawn from Treasury under the agreement; and (4) entitlement to a periodic commitment fee ("PCF"), over and above the 10% dividend, "intended to fully compensate" taxpayers for the continuing Treasury commitment of funds.

In order to avoid statutory receivership and liquidation mandated by Congress in HERA, the Enterprises must maintain a positive net worth. Under the PSPAs, Treasury committed to provide funding as necessary to return the Enterprises to a positive net worth position. If in any calendar quarter an Enterprise's net worth is negative—meaning that its liabilities exceed its assets in accordance with U.S. Generally Accepted Accounting Principles ("GAAP")—the Conservator draws funds from Treasury on behalf of the Enterprise in the amount necessary to eliminate the then-existing net worth deficit. Both Enterprises

required their first Treasury draws to eliminate their then existing negative net worth positions—signifying that all shareholder equity had been exhausted—soon after their placement into conservatorships. To date, the Enterprises have drawn more than $187 billion in taxpayer funds from Treasury and have also paid dividends to Treasury pursuant to the PSPAs. Appellants challenge none of the actions taken by Treasury and the FHFA from September 6, 2008 up to August 16, 2012, actions that included the investment and commitment of hundreds of billions of dollars of taxpayer funds to maintain the operations of the Enterprises.

As Conservator, FHFA "immediately succeed[ed] to ... all rights, titles, powers, and privileges of the [Enterprises], and of any stockholder, officer or director of [the Enterprises]." *Id.* § 4617(b)(2)(A). As will be set forth more fully in the merits briefing, Congress vested the Conservator with broad powers to "[o]perate" the Enterprises, "carry on the business" of the Enterprises, enter into contracts on behalf of the Enterprises, "transfer or sell any [Enterprise] asset . . . without any approval," and take actions to put the Enterprises in a "sound and solvent condition" and "preserve and conserve" their assets. *Id.* § 4617(b)(2). And the Conservator is authorized to exercise these powers in the manner it "determines is in the best interests of the [Enterprises] or the Agency." *Id.* § 4617(b)(2)(D), § 4617(b)(2)(J)(ii). HERA's anti-injunction provision, 12 U.S.C. § 4617(f),

insulates from judicial review the manner in which FHFA carries out its powers and functions as Conservator.

Despite this jurisdictional bar, Fairholme and the other shareholder plaintiffs sued to challenge the Conservator's August 17, 2012 agreement to modify the compensation for Treasury for its massive financial support of the Enterprises. Pursuant to this modification, known as the "Third Amendment" to the PSPAs, Treasury agreed not to exercise its contractual right to assure full taxpayer compensation by imposing the PCF, for so long as profits, if any, achieved by the Enterprises were used to compensate taxpayers. To achieve this modification, the Third Amendment replaced both the fixed 10% dividend and the PCF with a variable quarterly dividend in the amount of the Enterprises' positive net worth. Plaintiffs challenge the necessity for and the terms of the Third Amendment. They claim that it was intended to wind down and "effectively nationalize[]" the Enterprises, and that it subsequently resulted in "windfall" payments to Treasury when, in 2013, the Enterprises released valuation allowances initially booked on certain deferred tax assets during the housing crisis. Mot. 2, 7.

FHFA and the Enterprises moved to dismiss the complaints. The district court granted the motion, dismissing the cases under Rule 12(b)(1) and 12(b)(6). Op. 52. Although FHFA moved, in the alternative, for summary judgment on one of Fairholme's seven claims, the district court never reached the merits of that

motion in light of its Rule 12(b) dismissal of the entire complaint. *See id.* The district court likewise denied the cross motion for summary judgment filed by Fairholme and other plaintiffs without reaching the merits of that motion. *See id.*

Separately, Fairholme and other shareholders filed suits against the United States in the Court of Federal Claims ("CFC") alleging that the Third Amendment effected a constitutional taking of their property.[2] The CFC cases, to which FHFA and the Enterprises are not parties, are in the midst of jurisdictional discovery. Fairholme, having already had its claims or the claims of its subsidiary dismissed by two federal courts, now seeks to inject into this appeal hundreds of pages of documents and deposition testimony from jurisdictional discovery in the CFC that was not submitted to or considered by the district court, asking that judicial notice be taken of these materials.

[2] Additionally, three cases raising similar issues have been filed in other federal courts. The first case was dismissed in February and the plaintiff—a subsidiary of one of the Fairholme Plaintiffs here who was also represented by Fairholme's lead counsel—elected not to appeal. *See Continental Western Ins. Co. v. FHFA*, No. 14:-cv-00042, 2015 WL 428342 (S.D. Iowa Feb. 3, 2015). The second and third cases, *Saxton v. Federal Housing Finance Agency*, No. 1:15-cv-00047 (N.D. Iowa) and *Jacobs v. Federal Housing Finance Agency*, No. 1:15-cv-00708 (D. Del.), were only recently filed.

ARGUMENT

I. The Documents That Are The Subject Of Fairholme's Motion Are Not Relevant To The Court's Resolution Of The Purely Legal Issues Presented By This Appeal.

In its motion, Fairholme argues that judicial notice and supplementation of the record are warranted in order to "assure that this case is not decided on the basis of a false factual premise." Mot. 4. But the district court did not resolve this case based on any "factual premise" other than the facts alleged by plaintiffs' own complaints. The district court accepted all of the allegations in Fairholme's complaint and all of the other complaints as true, and nevertheless granted defendants' motions to dismiss based on threshold legal issues, concluding that "HERA's unambiguous statutory provisions … compel[led] the dismissal of all of the plaintiffs' claims." Op. 52; *see also* Op. 10, 11 ("the complaint is construed liberally in plaintiffs' favor" and the court "assume[s] the truth of all material factual allegations"). Accordingly, the documents Fairholme seeks to place before this Court are irrelevant to the issues on appeal.

Fairholme's motion focuses much of its attention on the Document Compilation, including the declaration of Mario Ugoletti, which FHFA filed below. FHFA submitted its Document Compilation only in connection with its alternative motion for summary judgment with respect to the plaintiffs' APA

claims,[3] an alternative motion that the district court never addressed. Fairholme argues that discovery from the CFC action undercuts the information reflected in the Document Compilation, but the district court expressly found the Document Compilation, submitted by FHFA only in support of its alternative motion for summary judgment, "irrelevant" to its decision to grant the motions to dismiss. Op. 21. And the court did not once reference the Ugoletti declaration (or the issue of deferred tax assets), let alone use it as a basis for decision. Thus, the Document Compilation itself and whether the CFC discovery materials contradict anything in it are irrelevant to this appeal.

Moreover, to the extent that Fairholme seeks to use the CFC discovery materials to support the allegations of its dismissed complaint in the district court, the materials are redundant and unnecessary. The district court expressly accepted the plaintiffs' allegation as true in dismissing each of their complaints. This Court too is required to accept plaintiffs' allegations. *Nattah v. Bush*, 605 F.3d 1052, 1057 (D.C. Cir. 2010). Fairholme thus does not need and it would controvert long-established basic legal procedure to supplement the record with materials that

[3] FHFA's motion in the district court expressly stated that the Document Compilation was "rel[ied] upon … exclusively for the purposes of [the FHFA Defendants'] alternative request for summary judgment on Plaintiffs' arbitrary and capricious claims under the APA, should the Court decide it has jurisdiction over such claims." FHFA, Melvin L. Watt, Fannie Mae, and Freddie Mac Combined Motion to Dismiss, and in the Alternative, for Summary Judgment, *Fairholme Funds, Inc. v. FHFA*, No. 13-cv-1053 (D.D.C. Jan. 17, 2014), Dkt. 28 at 17 n. 11.

purport to prove up the allegations already accepted by the district in dismissing its complaint.

For example, Fairholme claims that "[d]ocuments produced in the CFC indicate that the Net Worth Sweep was meant to facilitate a wind down" of the Enterprises; that FHFA knew there was a potential that the Enterprises' deferred tax asset valuation allowances "might be reversed in the not-so-distant future," leading to a substantial increase in the Enterprises' net worth and the dividends payable to Treasury; and that FHFA knew at the time the Third Amendment was executed that it "was not necessary to prevent the [Enterprises] from running through the available Treasury funding commitment." Mot. 9-11, 13, 15-16. But the dismissed complaints already contain allegations to that effect—that the Third Amendment was intended to "expedite the wind down of Fannie Mae and Freddie Mac;"[4] that release of the valuation allowances could—and did—result in

[4] Complaint, *Fairholme Funds, Inc. v. FHFA*, No. 13-1053 (D.D.C. July 10, 2013), Dkt. 1 (hereinafter "Fairholme Compl.") ¶¶ 71-72 ("Statements by both FHFA and Treasury provide further confirmation that the Net Worth Sweep ….would 'expedite the wind down of Fannie Mae and Freddie Mac,'" "contract[] [the Companies'] operations," and "reinforce the notion that the [Companies] will not be building capital as a potential step to regaining their former corporate status."); Complaint, *Perry Capital LLC v. Lew*, No. 13-1025 (D.D.C. July 7, 2013), Dkt. 1 (hereinafter "Perry Compl.") ¶ 47 (Third Amendment "ensured that Treasury would be the only beneficiary of the Companies' profitability and that the Companies would be wound down."); *Id.* ¶ 55 (the Third Amendment, "which necessarily involves dissipating [the Enterprises'] assets and property, is incompatible on its face with FHFA's charge to put the Companies back into 'a sound and solvent condition'…").

"extraordinary payments to Treasury;"[5] and that the Enterprises "had returned to profitability," "were demonstrably solvent," and were capable of "pay[ing] the 10% dividend" when FHFA and Treasury executed the Third Amendment.[6] Indeed, the district court expressly referenced these very allegations—and explained in its opinion why they were insufficient as a matter of law to save the complaints from dismissal:

> [T]o determine whether it has jurisdiction to adjudicate claims for equitable relief against FHFA as a conservator, the Court must look at

[5] Fairholme Compl. ¶ 73 ("FHFA's Office of Inspector General recognized that, as a result of the Net Worth Sweep, reversal of the Companies' deferred tax assets valuation allowances could result in 'an extraordinary payments to Treasury.'"); *id.* ¶ 75 ("over $50 billion of Fannie's profitability resulted from the release of the Company's deferred tax assets valuation allowance—the same non-cash asset that previously created massive paper losses for the Company."); Perry Compl. ¶¶ 5-6 (the deferred tax asset valuation allowances "reflected exceedingly pessimistic views about the Companies' future financial prospects" when imposed in 2008 and by 2012 "it had become clear that the Companies' financial condition had recovered to the point that … the Companies have been able to reverse the write-downs of their deferred tax assets"); *Id.* ¶ 45 ("in the first two quarters of 2012, the Companies posted sizeable profits totaling more than $10 billion. The Companies' 10-Qs disclosed that they expected to be consistently profitable for the foreseeable future. These projected future profits meant that the Companies would be able to remove the valuation allowance against their deferred tax assets, worth approximately $ 100 billion, in future years.").

[6] Fairholme Compl. ¶¶ 8-9 (at the time of the Third Amendment, "the housing market was already recovering," "both Fannie and Freddie had returned to profitability" and "were demonstrably solvent and able to pay the 10% dividend"); *Id.* ¶ 59 ("Together, the Companies' return to profitability and the stable recovery of the housing market showed that the Companies could in time redeem Treasury's Government Stock and provide a return on investment to owners of their Preferred Stock"); *Id.* ¶ 64 (the Third Amendment was executed when "it was becoming clear that [the Enterprises] had the earnings power to redeem Treasury's Government Stock and exit conservatorship"); Perry Compl. ¶ 47 ("By 2012, the fact that the Companies were returning to financial health and would soon be able to position themselves to redeem the Government Preferred Stock was—or at least should have been—obvious to Treasury and the FHFA. But instead of taking steps to aid that process, Treasury and FHFA entered into the Third Amendment, which ensured that Treasury would be the only beneficiary of the Companies' profitability…").

> *what* happened, not *why* it happened. For instance, the Court will examine whether the Third Amendment *actually* resulted in a *de facto* receivership … not what FHFA has publicly stated regarding any power it may or may not have, as conservator to prepare the GSEs for liquidation … ***FHFA's underlying motives or opinions -- i.e., whether the net worth sweep would arrest a downward spiral of dividend payments … increase payments to Treasury, or keep the GSEs in a holding pattern … do not matter for purposes of § 4617(f)***.

Op. 21-22 (final emphasis added).[7]

Given that the district court accepted as true the facts as plaintiffs have alleged them, the documents Fairholme seeks to add to the record have no possible relevance to the issues on appeal. *See Whiting v. AARP*, 637 F.3d 355, 364-65 (D.C. Cir. 2011) (judicial notice of materials that "merely contain[] facts alleged in the Complaint" is improper on review of a motion to dismiss, "which turns on the adequacy of the well-pleaded factual allegations [that are] assumed to be true"); *Jergens v. Ohio Dep't of Rehab. & Corrections Adult Parole Auth.*, 492 F. App'x 567, 569 (6th Cir. 2012) (declining judicial notice request where court records were "introduced merely to bolster factual allegations").

[7] The district court also did not leave Plaintiffs' discovery motion below "unaddressed." Mot. 20. Instead, contrary to Fairholme's assertion, it correctly denied that motion as moot based on its dismissal of the Plaintiffs' cases on jurisdictional grounds. Order, *Fairholme Funds, Inc. v. FHFA*, No. 13-cv-1053(D.D.C. Sept. 30, 2014), Dkt. 58 at 2 ("For the reasons explained in the Memorandum Opinion dismissing the plaintiffs' cases issued this date, the plaintiffs' motion for supplementation of the administrative record, limited discovery, suspension of briefing on the defendants' dispositive motions, and a status conference is hereby denied as moot.").

The record on appeal "consists solely of the original papers and exhibits filed in the district court, [any] transcript of the proceedings, and the certified copy of the docket," and appellate review ordinarily is unaffected by extra-record matters. *Beyene v. Hilton Hotels, Corp.*, 573 F. App'x 1, 1-2 (D.C. Cir. 2014); *see also Carter v. George Washington Univ.*, 387 F.3d 872, 877 (D.C. Cir. 2004). Although appellate courts may, under circumstances not present here, judicially notice extra-record facts, they generally decline to do so where, as here, the proffered extra-record facts are not relevant to resolution of the appeal. *See, e.g.*, *Weisberg v. U.S. Dep't of Justice*, 705 F.2d 1344, 1362 (D.C. Cir. 1983) (declining to exercise judicial notice powers where "new evidence" would not "cast[] doubt" on issues on appeal); *Bichindaritz v. Univ. of Wash.*, 550 F. App'x 412, 413 (9th Cir. 2013) (denying motion for judicial notice of materials from related proceedings that were "unnecessary to the resolution of the issues presented on appeal").

In this case, there is no need for the Court to look beyond the district court record. The district court granted FHFA's and the Enterprises' motion to dismiss based solely on its analysis of whether the Third Amendment fell within the Conservator's "statutorily prescribed, constitutionally permitted, powers or functions.'" Op. 12-13. Concluding—based on the complaints, statute, and case law—that the Third Amendment passed that test, the court ruled that Section

4617(f) bars all APA claims alleging that FHFA acted arbitrarily and capriciously in exercising its statutory powers. Op. 13-15. The district court, because it did not need to, did not address FHFA's alternative motion for summary judgment; it did not reach, because it lacked jurisdiction to do so, the merits of Fairholme's or the other plaintiffs' claims; and it did not rely on FHFA's Document Compilation in rendering its decision. In sum, the proffered documents are not necessary to address the purely legal arguments that the district court resolved below in dismissing Plaintiffs' claims under Rule 12(b).[8]

II. In Any Event, The CFC Discovery Materials Are Not Proper Subjects Of Judicial Notice.

Although Fairholme argues that its "request for judicial notice fits comfortably within this Court's precedents" because "[t]his Court has long been

[8] Fairholme does not point to a single instance in which the district court actually relied upon the Document Compilation or Administrative Record in resolving the motions to dismiss. This omission is dispositive and sufficient to deny Fairholme's motion. However, in their merits briefs, Plaintiffs assert that the court below "repeatedly relied on facts outside the complaints to resolve disputes over facts at the core of Appellants' claims." Perry Capital LLC, Arrowood Indemnity Co., and Fairholme Funds, Inc. Initial Opening Brief, *Perry Capital LLC v. Lew*, Nos. 14-5243, 14-5254, 14-5260, 14-5262 (D.C. Cir. June 29, 2015), Doc. 1560037 at 74. There is no serious support for this assertion, which ignores the district court's multiple statements that it was assuming the truth of all facts alleged in the complaints. Plaintiffs claim that the court below "credited FHFA's assertion" that it executed the Third Amendment to end the problem of circular draws "rather than to enrich Treasury." *Id.* But the district court unequivocally stated that it need not and would not resolve this dispute over whether FHFA had improper motives in executing the Third Amendment—including whether it was executed to "arrest a downward spiral" or "increase payments to Treasury"— instead holding that "FHFA's underlying motives or opinions … *do not matter* for purposes of § 4617(f)," which bars "claims [that] ask the Court, directly or indirectly, to evaluate FHFA's rationale." Op. 21-22 (emphasis added).

willing to take judicial notice of facts based on the records in other cases," Mot. 4, none of the cases Fairholme relies upon are remotely similar to its requests for judicial notice here. *Dupree v. Jefferson*, 666 F. 2d 606, 608 & n. 1 (D.C. Cir. 1981), for example, involved judicial notice of the fact that the appellant had previously sued the D.C. police department, not the truth of any filings made in connection with those suits. Similarly, *United States v. Dancy*, 510 F.2d 779, 786 (D.C. Cir. 1975), merely took judicial notice that "District Court proceedings … ha[d] been held."

Unlike these cases, the documents produced in discovery in the CFC case are not the types of "official court records" of which courts routinely take notice to determine, for example, whether an issue was "actually litigated" in another forum. *E.g.*, *Lopez v. Howard*, No. 06-2361, 2007 WL 708989, at *1 (3d Cir. Mar. 9, 2007) (taking judicial notice of docket sheets and opinion from other court). Fairholme simply attached these documents as exhibits to motions it made in the CFC litigation in seeking relief from that court's protective order. Fairholme cannot use judicial notice "to rely on … substantive facts within those exhibits, many of which are disputed, to support [its] appeal." *Davis v. City of Clarksville*, 492 F. App'x 572, 578 (6th Cir. 2012) (denying judicial notice request). Courts cannot notice the content of deposition transcriptions or other discovery materials as indisputable facts and "[can]not consider the statements contained in [such]

document[s] for the truth of the matter asserted, even at the motion-to-dismiss stage." *In re Omnicare, Inc. Sec. Litig.*, 769 F.3d 455, 467 (6th Cir. 2014); *see also In re Oracle Corp. Sec. Litig.*, 627 F.3d 376, 386 n. 1 (9th Cir. 2010) (denying request for judicial notice of deposition transcript in appeal of summary judgment decision because "the content of a deposition is not a clearly established 'fact' of which this panel can take notice").

III. Fairholme's Alternative Request For Remand Should Be Denied.

At the close of its motion Fairholme suggests that the case be remanded so that it can amend its complaint. Mot. 19-20. Fairholme does not contest that the purportedly new facts are already subsumed within its current allegations, or explain what specific new allegations it would make. Nor does Fairholme show that any new allegations would lead to a different outcome in light of the rulings already made by the district court. Fairholme's remand suggestion fails on this basis alone.

Moreover, if the district court believed that it needed to resolve questions of fact, or that it was necessary to convert the motions before it into ones for summary judgment, it easily could have done so. It did not. Instead, the district court accepted the allegations as true, decided the matter on the pleadings, and dismissed the claims as a matter of law. That ruling is what is on appeal before this Court. Sending this matter back to the district court for unspecified

amendments to bolster factual allegations already made and assumed true makes no sense and would impose on the district court and the parties obligations that directly conflict with the purpose of Federal Rules of Civil Procedure; viz., that they "secure the just, speedy, and inexpensive determination of every action and proceeding." Fed. R. Civ. P. 1.

CONCLUSION

For the foregoing reasons, the Court should deny Fairholme's Motion for Judicial Notice and Supplementation of the Record.

Dated: August 20, 2015

Respectfully submitted,

/s/ Howard N. Cayne
Howard N. Cayne
Asim Varma
David B. Bergman
Michael A.F. Johnson
Dirk C. Phillips
Ian S. Hoffman
ARNOLD & PORTER LLP
555 Twelfth Street, NW
Washington, DC 20004
(202) 942-5000
(202) 942-5999 (fax)
Howard.Cayne@aporter.com

Counsel for Appellees Federal Housing Finance Agency and Melvin L. Watt

/s/ Michael J. Ciatti
Michael J. Ciatti
Graciela Maria Rodriguez
KING & SPALDING LLP
1700 Pennsylvania Ave. N.W.
Washington, DC 20006
(202) 626-5508
mciatti@kslaw.com

Counsel for Appellee Federal Home Loan Mortgage Corporation

/s/ Paul D. Clement
Paul D. Clement
D. Zachary Hudson
BANCROFT PLLC
500 New Jersey Ave. N.W., 7th Floor
Washington, D.C. 20001
(202) 234-0090
pclement@bancroftpllc.com

Counsel for Appellee Federal National Mortgage Association

CERTIFICATE OF SERVICE

I hereby certify that on August 20, 2015, I electronically filed the foregoing document with the United States Court of Appeals for the District of Columbia Circuit by using the appellate CM/ECF system.

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

/s/ Howard N. Cayne
Howard N. Cayne

Counsel for Appellees Federal Housing Finance Agency and Melvin L. Watt