**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.	No. 14-5254

FAIRHOLME'S PUBLIC REPLY IN SUPPORT OF ITS MOTION FOR JUDICIAL NOTICE AND SUPPLEMENTATION OF THE RECORD

Fairholme's motion for judicial notice and supplementation of the record identified evidence that calls into question the integrity of the proceedings before the district court. But rather than attempting to defend the materials they presented below, Defendants argue that those materials are irrelevant because, in their view, HERA permitted FHFA and Treasury to conspire to nationalize Fannie and Freddie by expropriating the value of the Companies' private equity securities for the Federal Government and ensuring that the Companies remain under perpetual Government control at a time when the Companies were entering a period of record-breaking profitability. The unbridled scope of Defendants' understanding of their own power is startling, but more troubling still is their attempt to defend their actions with misleading—and in key respects false—submissions to the district court. De-

fendants would no doubt prefer that this Court affirm the district court while blinding itself to the false and misleading record presented below, but this Court cannot properly do so.

I. THE PURPOSES AND EFFECTS OF THE NET WORTH SWEEP ARE RELEVANT TO THIS APPEAL

Defendants contend that the materials identified in Fairholme's motion are irrelevant to the issues on appeal because this Court can affirm even if it accepts Fairholme's account—borne out by the evidence submitted with Fairholme's motion—of the purposes and effects of the Net Worth Sweep. Treasury's Opp'n to Fairholme's Sealed Motion for Judicial Notice 10–13 (Aug. 20, 2015) ("Treas. Br."); Opp'n of Appellees Federal Housing Finance Agency et al. to Fairholme's Motion for Judicial Notice 7–13 (Aug. 20, 2015) ("FHFA Br."). But there is no proper path to affirmance by which this Court could simply ignore Fairholme's motion. Fairholme's evidence corroborates the allegation that the Net Worth Sweep was not adopted to arrest any purported "death spiral" of dividend payments, but rather was designed to prevent Fannie and Freddie from ever rebuilding capital or returning to a sound and solvent condition that would allow the Companies to exit conservatorship in their existing form, while at the same time enriching the Federal Government by expropriating the economic interests of the Companies' private shareholders and granting Treasury alone the right to reap the record-breaking profits the Companies were projected to generate. Only if the Court is

prepared to rule in Defendants' favor even accepting these factual premises need it not concern itself with the materials identified in Fairholme's motion. But that is not the basis on which the district court ruled below, and Defendants are simply wrong when they argue that their preferred disposition of this appeal makes Fairholme's evidence irrelevant to all of the issues before the Court.

While Defendants strenuously argue that the district court ruled in their favor without consideration of their proffered—and now demonstrably misleading and inadequate—record submissions, a close reading of the district court's opinion shows otherwise. The district court held that Fairholme "fail[ed] to demonstrate by a preponderance of the evidence . . . that FHFA's execution of the Third Amendment violated HERA." Op. 20. In reaching that conclusion, the district court asked "whether the Third Amendment *actually* resulted in a *de facto* receivership," *id.* at 21; found that, contrary to the allegations of Fairholme's complaint, the agreement "was executed by two sophisticated parties" without coercion, *id.* at 23; and credited FHFA's assertion that it "executed the Third Amendment to ameliorate the existential challenge of paying the dividends [the Companies] *already* owed," *id.* at 19; *see also id.* at 6 n.7 (rejecting Fairholme's contention that the Companies were not required to pay dividends in cash under their original agreements with Treasury). Those passages of the district court's opinion make clear that it refused to credit the allegations in Fairholme's complaint, despite declaring

Treasury's administrative record and FHFA's document compilation to be "irrelevant" to its decision. *Id.* at 21; *see* Institutional Pls.' Opening Br. 73–77 (June 29, 2015).

To be sure, there are passages in the district court's opinion implying that FHFA and Treasury are free to do *anything* with Fannie and Freddie—including extinguishing the rights of their private shareholders and operating them for the exclusive benefit of the Federal Government—so long as the Companies "maintain an operational mortgage finance business and are . . . profitable." Op. 25. But it is evident that Defendants themselves do not believe that HERA so thoroughly immunizes governmental misconduct, for they dispute facts that they claim the Court can assume for purposes of this appeal. Thus, both Defendants elide the fact that before the Net Worth Sweep the Companies were free to pay Treasury its dividends with additional stock rather than in cash, *see* Treas. Br. 3; FHFA Br. 7; Treasury asserts that the Companies' debt to Treasury was "increasing" when the Net Worth Sweep was announced, Treas. Br. 7; and it also makes much of its claims that the Companies needed government assistance when FHFA took them over in 2008, Treas. Br. 2–4; *but see* Brief Amici Curiae of Timothy Howard and the Coalition for Mortgage Security in Support of Appellants 13–15 (July 6, 2015). Each of these factual assertions is made in an effort to rebut Plaintiffs' factual allegations that the purported "death spiral" justification for the Net Worth Sweep was

pretextual and that the Net Worth Sweep was designed to award Treasury a massive windfall at the expense of the Companies' private shareholders and to guarantee that the Companies will remain under perpetual Government control by preventing them from retaining profits and rebuilding capital.

In any case, the views of the district court and the Defendants make no difference to the proper disposition of Fairholme's motion, which ultimately depends on whether *this Court* concludes that the materials at issue would assist it in deciding Fairholme's appeal. The materials are highly relevant in two respects. First, Defendants' improper purposes for adopting the Net Worth Sweep and their efforts to conceal those purposes via misleading, and in some respects false, submissions to the district court are a striking illustration of the dangers inherent in adopting Defendants' unbounded understanding of the scope of HERA's jurisdictional bar, 12 U.S.C. § 4617(f). To be sure, this Court has said that an equivalent provision governing bank conservatorships "effect[s] a sweeping ouster of courts' power to grant equitable remedies," *Freeman v. FDIC*, 56 F.3d 1394, 1399 (D.C. Cir. 1995), but it has also made clear that the courts may intervene whenever a federal conservator "act[s] beyond, or contrary to, its statutorily prescribed, constitutionally permitted, powers or functions," *id.* at 1398 (internal quotation marks omitted). Any such possibility of judicial review is meaningless if a conservator is free to donate to its sister agency the assets of the companies under its control and then dissemble

about what it did with impunity. Perhaps no case in the history of federal conservatorships more clearly demonstrates why Congress could not have intended to remove the judicial check in even the most extreme cases of misconduct by an agency appointed to act as conservator for a privately owned financial institution.

Second, once this Court rejects the implausible legal theory that Defendants advocate, it will then have to decide how to dispose of the remainder of this appeal. Even if Defendants were correct that the district court's decision rested entirely on threshold legal determinations, that would not prevent this Court from considering Plaintiffs' cross-motion for summary judgment that was pressed below. *See, e.g.*, *Mendoza v. Perez*, 754 F.3d 1002, 1020 (D.C. Cir. 2014) (reaching merits of APA summary judgment motion where district court had erroneously dismissed case on threshold jurisdictional grounds); *WildEarth Guardians v. Jewell*, 738 F.3d 298, 308 n.4 (D.C. Cir. 2013) (same); *Friends of Blackwater v. Salazar*, 691 F.3d 428, 434 n.* (D.C. Cir. 2012) (reaching alternative arbitrary and capricious argument where district court had erroneously ruled for plaintiffs on other grounds). The district court should have entered summary judgment in Fairholme's favor even based on the misleading and incomplete materials that were before it, and this Court should say as much on appeal, because on its face the Net Worth Sweep is directly at odds with FHFA's and Treasury's statutory authorities. But at an absolute minimum, the materials identified in Fairholme's motion show that a remand

for compilation of true administrative records is necessary, because without a proper administrative record the Court cannot *deny* Fairholme's summary judgment motion, or affirm the judgment below, on the basis of anything but the most extreme reading of Section 4617(f).[1]

II. THE EXISTENCE OF THE MATERIALS IDENTIFIED IN FAIRHOLME'S MOTION IS A PROPER SUBJECT FOR JUDICIAL NOTICE

Defendants do not contest the authenticity of the materials identified in Fairholme's motion, and it follows that *the existence* of those materials is not subject to reasonable dispute and can be readily determined from the materials themselves. *See* FED. R. EVID. 201(b)(2). Irrespective of the truth of the matters asserted in those materials, an important legal conclusion ineluctably follows from their undisputed existence: the evidence Defendants submitted to the district court represents an incomplete and highly misleading picture of what was actually before the agencies when they imposed the Net Worth Sweep. Judicial review of administrative action only works if agencies are forthcoming about the reasons and factual bases for their decisions, and Defendants' failure to offer any explanation for submissions that now appear to have been calculated to lead the courts astray is deeply

[1] The importance of the materials identified in Fairholme's motion to the proper disposition of this appeal makes them appropriate subjects for supplementation of the record. *See* Fairholme's Sealed Motion for Judicial Notice 18–19 (July 29, 2015); *In re AOV Indus., Inc.*, 797 F.2d 1004, 1012 (D.C. Cir. 1986).

troubling.

Despite never contesting the authenticity of the materials identified in Fairholme's motion, Defendants nevertheless argue that the Court should not take judicial notice of them. Treas. Br. 13–15; FHFA Br. 13–15. But Defendants' discussion of the applicable legal principles is widely off the mark. As an initial matter, Defendants do not even mention the two cases most like this one. In *Walter O. Boswell Memorial Hospital v. Heckler*, 749 F.2d 788, 792 (D.C. Cir. 1984), and *NRDC v. Train*, 519 F.2d 287, 291–92 (D.C. Cir. 1975), this Court examined materials that agencies failed to submit to the district court, determined on the strength of those materials that the administrative records were incomplete, and remanded for consideration in light of what was actually before the defendant agencies when they made their decisions. Defendants' demonstrably misleading submissions to the district court call for a similar approach here.

Defendants are wrong when they suggest that judicial notice of court records is limited to noticing that a suit was filed or that proceedings were held. *See* FHFA Br. 13–14; Treas. Br. 14. This Court in *Walter O. Boswell*, for example, determined that an administrative record was incomplete by examining materials that the agency had submitted in another case. 749 F.2d at 792–93. And while FHFA says that the Court in *United States v. Dancy* "merely took judicial notice that 'District Court proceedings . . . ha[d] been held,' " FHFA Br. 14 (quoting 510 F.2d

779, 786 (D.C. Cir. 1975)), review of this Court's opinion shows otherwise: "[i]nformation generated" in other litigation "raise[d] the possibility" that materials before the *Dancy* Court "suffer[ed] from highly serious procedural and substantive defects," 510 F.2d at 786. Numerous other cases are to similar effect. *See, e.g.*, *Gomez v. Wilson*, 477 F.2d 411, 416 n.28 (D.C. Cir. 1973) (taking notice of contents of affidavits filed in other litigation); *Xydas v. United States*, 445 F.2d 660, 667 n.22 (D.C. Cir. 1971) (taking notice of hearing transcript to establish what attorney knew at the time of hearing).

Finally, Treasury's complaint that it has "had no opportunity to respond" to materials that it pointedly declines to discuss does not deserve to be taken seriously. *See* Treas. Br. 14–15. If the Court takes judicial notice of the materials, the significance of which is addressed at length in Fairholme's motion, Treasury will be able to respond to them in its principal brief. Alternatively, the Court could order supplemental briefing on the materials' significance.

III. DISCOVERY OF INFORMATION IMPROPERLY WITHHELD IN THE PROCEEDINGS BELOW MAKES REMAND APPROPRIATE

FHFA resists Fairholme's alternative request for a remand for amendment of the complaint on futility grounds. FHFA Br. 15–16. But the materials in Fairholme's motion reveal at least two facts that deserve consideration by the district court following appropriate amendment of the complaint. First, Redacted

Redacted

See Motion for Judicial Notice 8. Second,

Redacted

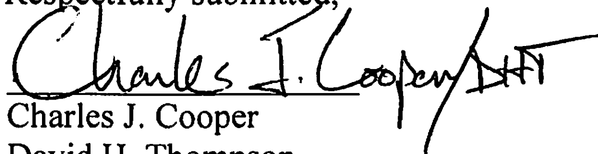
. *See id.* at 12–13. Fairholme was unaware of those facts when it filed suit, and they do not appear in its complaint. If the Court concludes that the district court should consider in the first instance the significance of those and the other facts that can reasonably be inferred from the materials at issue, a remand would be appropriate.

CONCLUSION

For the foregoing reasons, the Court should grant Fairholme's motion for judicial notice and supplementation of the record.

Date: August 31, 2015

Respectfully submitted,



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CERTIFICATE OF SERVICE

I hereby certify that a true and correct copy of the foregoing was filed with the Clerk's office this 31st day of August, 2015, and was served upon counsel for Defendants listed below via First Class U.S. Mail:

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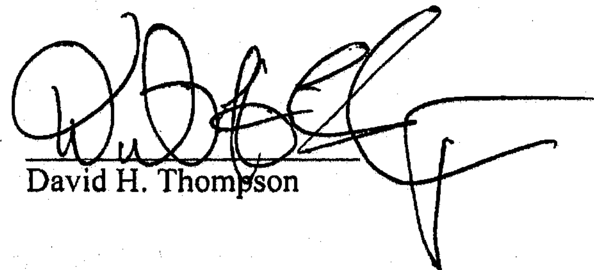
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