IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF KENTUCKY
SOUTHERN DIVISION AT PIKEVILLE

ARNETIA JOYCE ROBINSON,	)	
	)	
Plaintiff,	)	
v.	)	Case No. 7:15-cv-109-ART-EBA
	)	
THE FEDERAL HOUSING FINANCE	)	
AGENCY, *et al.*,	)	
Defendants.	)	

DEPARTMENT OF THE TREASURY'S REPLY IN SUPPORT OF ITS MOTION TO DISMISS THE AMENDED COMPLAINT

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INTRODUCTION

As was the case with the numerous lawsuits that preceded it, the claims in this suit fail for lack of jurisdiction and, further, fail to state a claim. First, the Housing and Economic Recovery Act of 2008 ("HERA"), 12 U.S.C. § 4617(f), precludes courts from ordering equitable relief that would interfere with the Federal Housing Finance Agency ("FHFA") in the exercise of its powers as conservator of Fannie Mae and Freddie Mac ("the GSEs"). Plaintiff's effort to set aside a contractual agreement of the conservator is the precise type of interference this section prohibits. And plaintiff cannot evade section 4617(f) by suing FHFA's counter-party, Treasury. Further, plaintiff's claims that Treasury exceeded its statutory authority misconstrue HERA, and are belied by recent legislation ratifying the Third Amendment.

Second, this suit runs afoul of HERA's prohibition against shareholder suits during conservatorship, 12 U.S.C. § 4617(b)(2)(A)(i). Plaintiff asserts that she can nevertheless bring a "direct" shareholder claim. This argument is doubly misconceived. Regardless of how she attempts to characterize them, plaintiff's claims are derivative because her alleged injury depends on an injury that the GSEs (allegedly) suffered, and because the "relief" that she seeks would flow to the GSEs. Even if her claims could be construed as "direct," it would not matter; plaintiff's claims, whether direct or derivative, fail under both section 4617(f) and section 4617(b) of HERA, and the Administrative Procedure Act ("APA") provides no cause of action for direct claims against Treasury or FHFA under these circumstances.

Finally, the district court's judgment in *Perry Capital*, an earlier-filed shareholder derivative lawsuit involving materially identical claims, has issue preclusive effect on this suit. Thus, for several independent reasons, the complaint should be dismissed.

I. HERA BARS PLAINTIFF'S CLAIMS AGAINST TREASURY.

A. Section 4617(f) Deprives the Court of Jurisdiction Over Plaintiff's Claims for Injunctive Relief Against Treasury.

Plaintiff's suit is barred by 12 U.S.C. § 4617(f), which provides that "no court may take any action to restrain or affect the exercise of powers or functions of [FHFA] as a conservator" of the GSEs. Like its analogue under the Financial Institutions Reform, Recovery and Enforcement Act ("FIRREA"), *see* 12 U.S.C. § 1821(j), HERA's jurisdiction-withdrawal provision "effect[s] a sweeping ouster of courts' power to grant equitable remedies" to parties challenging actions taken by FHFA as conservator. *Freeman v. FDIC*, 56 F.3d 1394, 1399 (D.C. Cir. 1995) (interpreting § 1821(j)); *Town of Babylon v. Fed. Hous. Fin. Agency*, 699 F.3d 221, 228 (2d Cir. 2012) (interpreting § 4617(f)); *see also* FHFA Reply at 3-18. This provision "by its terms, can preclude relief even against a third party . . . where the result is such that the relief 'restrain[s] or affect[s] the exercise of powers or functions of the . . . conservator . . .'" *Hindes v. FDIC*, 137 F.3d 148, 160 (3d Cir. 1998) (quoting 12 U.S.C. § 1821(j)). Plaintiff argues, implausibly, that these precedents do not apply because their claim against Treasury is "unrelated to the conduct of the conservatorship." Pl.'s Resp. in Opp'n to Defs.' Mot. to Dismiss 51, ECF No. 30 ("Opp."). This effort to distinguish the cases makes no sense on its own terms, as plaintiff is suing *the conservator* over the same transaction, seeking identical relief under the APA.

In any event, the cases and the text of the statute do not support plaintiff's approach. The anti-injunction language of section 1821(j) and section 4617(f) precludes any claim that would *affect* the conservator's operations: "section 1821(j) precludes a court order against a third party which would affect the FDIC as receiver, where the relief would have the same practical result as

an order directed against the FDIC in that capacity." *Hindes*, 137 F.3d at 161.[1] This approach is applied consistently across the federal courts. *See Telematics Int'l, Inc. v. NEMLC Leasing Corp.*, 967 F.2d 703, 707 (1st Cir. 1992) ("Permitting Telematics to attach the certificate of deposit, if that attachment were effective against the FDIC, would have the same effect, from the FDIC's perspective, as directly enjoining the FDIC from attaching the asset. In either event, the district court would restrain or affect the FDIC in the exercise of its powers as receiver."); *see also Dittmer Prop., L.P. v. F.D.I.C.*, 708 F.3d 1011, 1017 (8th Cir. 2013) ("[I]f plaintiffs such as Dittmer are allowed to attack the validity of a failed institution's assets by suing the remote purchaser, such actions would certainly restrain or affect the FDIC's powers[.]"); *St. George Maronite Catholic Church v. Green*, No. CIV.A. SA-94-CA-0334, 1994 WL 763743, at *4–*6 (W.D. Tex. July 25, 1994) (holding, despite allegations that "the contract with [a third party] arose as a result of fraud, a breach of good faith and fair dealing, and deceptive trade practices" that "§ 1821(j) bars any relief that would affect the contract between RTC–Receiver and [the third party], whether that relief is termed recession, declaratory, or anything else.").

Plaintiff seeks to restrain agreements that the conservator entered into to maintain the solvency of the GSEs after the financial crisis, and she pursues relief that would apply to both FHFA and Treasury: rewriting the Preferred Stock Purchase Agreements ("PSPAs") to retain features that plaintiff likes (the unprecedented and continuing commitment of hundreds of billions in taxpayer funds to the GSEs) but invalidating features that she dislikes (the variable dividend payments of the Third Amendment). *See* Am. Compl. ¶ 165, Prayer for Relief, ECF

[1] *Coit Independence Joint Venture v. Federal Savings and Loan Insurance Corp.*, 489 U.S. 561, 575 (1989), which predates FIRREA and HERA, does not support plaintiff's interpretation. Opp. 43. Plaintiff seeks to enjoin both sides of a contract agreed to by the conservator, which is exactly the type of "collateral attack[] attempting to restrain the receiver from carrying out its basic functions" that the Supreme Court recognized would be barred. *Coit*, 489 U.S. at 575.

No. 17. Any relief against either party to the PSPAs would "restrain or affect" the exercise of the conservator's powers in direct contravention of section 4617(f), and indeed two courts have already reached this exact conclusion with respect to the Third Amendment. *See Cont'l W. Ins. Co. v. Fed. Hous. Fin. Agency*, 83 F. Supp. 3d 828, 831, 840 & n.6 (S.D. Iowa 2015); *Perry Capital LLC v. Lew*, 70 F. Supp. 3d 208, 222–23 (D.D.C. 2014).[2] Contrary to plaintiff's assertion, the presumption of judicial review under the APA, Opp. 50–51, does not save her claims here. "The presumption favoring judicial review of administrative action is just that—a presumption . . . [L]ike all presumptions used in interpreting statutes, [it] may be overcome by specific language . . ." *Block v. Cmty. Nutrition Inst.*, 467 U.S. 340, 349 (1984). Section 4617(f)'s prohibition "qualifies as a reliable indicator of congressional intent to preclude review of non-monetary APA claims brought against both FHFA and Treasury." *Perry Capital LLC v. Lew*, 70 F. Supp. 3d at 221 (D.D.C. 2014).

B. Recent Legislation Confirms That the Third Amendment Constituted a Proper Exercise of Treasury's Authority Under HERA.

Plaintiff predicates her claims for relief on a single action: the agreement between the conservator and Treasury to amend the PSPAs for a third time. The newly enacted Consolidated Appropriations Act of 2016 ("the Act"), H.R. 2029 §702(b), 114th Cong. (2015) (enacted Dec. 18, 2015)), however, confirms that plaintiff's claims are foreclosed by HERA. As Treasury explained in its opening brief, the plain text of the new legislation establishes that Congress

[2] Plaintiff's claim that she must be able to obtain injunctive relief against the conservator's counter-party in order to enforce the purchase authority's sunset provision, Opp. 50, falls flat. Congress expressly authorized FHFA to turn to Treasury for essential capital, and expressly authorized Treasury to make the necessary capital investments in the GSEs. If Congress intended for the conservator's dealings with Treasury to be subject to challenge by shareholders, it would have expressly limited the "sweeping ouster" of judicial review it enacted in section 4617(f) of HERA. *Freeman*, 56 F.3d at 1399.

ratified Treasury's exercise of its authority to enter into the Third Amendment, as well as Treasury's right to receive the variable dividend right that plaintiff challenges in this case. *See* Treasury Mem. in Support of Mot. to Dismiss at 23–27, ECF No. 22-1 ("Treasury Mem."). First, Congress expressly recognized Treasury's ongoing authority under HERA to amend the original PSPA. *See id.* § 702(a)(2)(A) (referring to Treasury's authority to "amend[] and restate[]" the PSPAs). Second, Congress confirmed that the Third Amendment constituted a valid exercise of Treasury's ongoing authority to amend the original PSPAs. *See id.* (referring to Agreement as amended on "August 17, 2012"). And third, Congress expressly acknowledged Treasury's rights under the stock certificates issued in connection with the Third Amendment, including the variable dividend provision that plaintiff challenges here. *See id.* § 702(a)(2)(B).

Plaintiff nonetheless contends that no presumption of ratification can apply here because the new legislation does not expressly "mention the propriety of the Net Worth Sweep." Opp. 59. But the doctrine of ratification does not require Congress to explicitly express its approval of an agency's action: the whole point of the doctrine is that Congress is *presumed* to ratify the agency's interpretation of a statute if Congress amends the statute fully aware of that interpretation but takes no steps to halt the agency action. *See N. Haven Bd. of Ed. v. Bell*, 456 U.S. 512, 535 (1982); *see* Treasury Mem. 24–26 (citing authorities). This presumption applies here because Congress made other changes to Treasury's authority under HERA, but it did not indicate any disapproval of Treasury's actions in entering into the Third Amendment. *Id*. To the contrary, Congress *expressly* incorporated the variable dividend provision in the Third Amendment into the scope of the new legislation by referencing it in section 702(a)(2)(B). Thus, plaintiff's reliance on isolated remarks of legislators, Opp. 59–60, is unavailing; by predicating aspects of the new legislation on the Third Amendment, including the variable dividend,

Congress approved of the Third Amendment as consistent with Treasury's authority and the duties of the conservator under HERA.

II. PLAINTIFF IS BARRED FROM BRINGING CLAIMS BASED ON HER STATUS AS A SHAREHOLDER IN THE GSES DURING THE CONSERVATORSHIP.

Plaintiff's suit fails under a second, independent bar in HERA, which prohibits suits by shareholders of the GSEs during conservatorship. "[T]he plain meaning of [section 4617(b)(2)(A) of HERA] is that *all* rights previously held by [the GSEs'] stockholders, including the right to sue derivatively, now belong exclusively to the FHFA." *In re Fed. Home Loan Mortg. Corp. Derivative Litig*. (*In re Freddie Mac*), 643 F. Supp. 2d 790, 795 (E.D. Va. 2009).

Plaintiff attempts to evade section 4617(b)(2)(A) by arguing that the statute transferred only some shareholder rights to FHFA, while preserving a shareholder's right to bring a direct claim, Opp. 60–64, and that her claims are direct, not derivative, Opp. 66–73. In addition, she argues that, notwithstanding HERA, the APA provides her a cause of action to bring direct claims. Opp. 65–66. However, as explained below, the claims that plaintiff seeks to assert here are derivative, not direct, and are plainly barred under HERA no matter how they are characterized. In all events, regardless of whether the claims are construed as direct or derivative, they are barred under both HERA and the APA.

A. Plaintiff's Claims Are Derivative.

Plaintiff's claims are derivative, not direct, because they are based on allegations that Treasury's and FHFA's actions have injured the GSEs, and the requested relief would flow to the GSEs. Treasury Mem. 27–30, FHFA Mem. 27-31. To distinguish between a derivative and direct claim, "a court should ask: "[1] Who suffered the alleged harm—the corporation or the suing stockholder individually—and [2] who would receive the benefit of the recovery or other

remedy?" *Tooley v. Donaldson, Lufkin & Jenrette, Inc.*, 845 A.2d 1031, 1035 (Del. 2004); *see also id*. at 1039.

Here, the Court can most easily conclude Plaintiff's claims are derivative by considering the second prong first: because Plaintiff seeks *only* declaratory and injunctive relief that "would flow first and foremost to the [Enterprises]"—namely, an order vacating the Third Amendment and ordering Treasury to return to the Enterprises the dividends paid thereunder, Am. Compl. ¶ 165—her claims are derivative. *See Perry Capital*, 70 F. Supp. at 229 n.24 (finding claims derivative on this basis, irrespective of whether shareholders suffered direct harm). Indeed, Plaintiff seeks no relief that would flow to her directly.[3]

With respect to the first prong, Plaintiff admits her claims are based on alleged harm to the Enterprises. *See* Opp. 69 ("Plaintiff believes that the Net Worth Sweep also injured Fannie and Freddie"); *see also* Am. Compl. ¶¶ 25, 99, 109, 124, 163. This too is dispositive. Plaintiff nevertheless asserts her claims are direct because she is alleging that harm to herself *and* the Enterprises, by arguing "the Net Worth Sweep destroyed the value of her investments through the transfer of Fannie's and Freddie's entire net worth to Treasury." Opp. 69. This argument is flawed for two reasons. First, it ignores the fundamental principle that allegations based on the depletion of corporate assets assert a "classically derivative" injury. *In re J.P. Morgan Chase & Co. S'holder Litig.*, 906 A.2d 766, 771 (Del. 2006). Further, the relief that she seeks—a change

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[3] The authorities Plaintiff cites concerning the second prong are plainly off point. Opp. 72. In *Grimes v. Donald*, 673 A.2d 1207, 1213-14 (Del. 1996), the plaintiff sought only declaratory relief and "[m]onetary recovery [would] not accrue to the corporation as a result." Here, Plaintiff seeks declaratory relief *plus* the return of dividend payments to the Enterprises. And in *Gatz v. Ponsoldt*, No. CIV.A. 174-N, 2004 WL 3029868, at *8 and n.54 (Del. Ch. Nov. 5, 2004), the court addressed a transaction for which "the corporation ha[d] suffered no harm," and concluded that an "unwinding of th[at] transaction would not benefit the corporation." Here, Plaintiff specifically alleges harm to the Enterprises and seeks to return dividends to them.

in dividend terms and the return of dividends paid to Treasury pursuant to the Third Amendment—would flow to the GSEs, not to plaintiff directly.

Plaintiff cites no authority supporting her theory that her claim is based on an individual injury independent of an injury to the GSEs. Opp. 69. Plaintiff relies on *Gentile v. Rossette*, 906 A.2d 91 (Del. 2006), for the proposition that her challenge to an alleged "improper extraction or expropriation" of corporate profits to one class of shareholders qualifies as a direct claim. Opp. 69–71. But *Gentile* is inapposite. *See* Treasury Mem. 31–32. There, the corporation had issued excess shares to a majority shareholder, and "the shares representing the 'overpayment' embod[ied] both economic value and voting power." *Gentile*, 906 A.2d at 95–96. Treasury is not a majority shareholder of the GSEs, and the alleged "overpayment" of dividends on Treasury's senior preferred stock is in the form of cash, not additional voting stock. Thus, plaintiff's allegations do not bring this case within the *Gentile* exception.

Further, the Third Amendment did not affect the voting power or dividend rights of any other stockholder. Treasury does not hold voting rights, and other shareholders' voting rights and dividend payments were suspended when the conservatorships began, before the PSPAs (let alone the Third Amendment) were entered into. Plaintiff's inability to show that the Third Amendment changed the status of her voting rights or dividend rights distinguishes her suit from the direct claims described in *Gatz v. Ponsoldt*, 925 A.2d 1265, 1280–81 (Del. 2007) and other cases cited by plaintiff.[4] Plaintiff's claims instead depend upon an assertion of alleged

[4] For example, in citing *Starr Int'l Co. v. United States*, 106 Fed. Cl. 50 (2012), *appeal docketed*, Case Nos. 15-5103, 15-5133 (Fed. Cir. Aug. 14, 2015), plaintiff overlooks the key distinction that that case did not concern an entity in conservatorship. Further, because the Third Amendment did not result in the issuance of any new shares to any party, it did not dilute shares, as the plaintiff in *Starr International* was able to allege. *Id.* at 64; *see also Innovative Therapies, Inc. v. Meents*, No. 12–3309, 2013 WL 2919983, at *5 (D. Md. June 12, 2013) (declining to

wrongdoing that "deplete[d] corporate assets that might otherwise be used to benefit the stockholders, such as through a dividend," and her claims are therefore derivative. *Protas v. Cavanaugh*, No CIV.A 6555-VCG, 2012 WL 1580969, at *6 (Del. Ch. May 4, 2012).[5]

Plaintiff incorrectly asserts that her claims are direct under federal law because she qualifies as "adversely affected or aggrieved" person under section 702 of the APA. Opp. 65–66 (citing 5 U.S.C. § 702). The first problem with this argument is that the APA, by its own terms, provides no cause of action where, as here, another statute limits judicial review of the agency action in question. *Id.* § 701(a)(1); *see Heckler v. Chaney*, 470 U.S. 821, 828 (1985) ("[B]efore any [APA] review at all may be had, a party must first clear the hurdle of § 701(a)."). As explained above, section 4617(f) of HERA expressly bars judicial review of claims for equitable relief that would restrain or affect the exercise of the conservator's powers. In addition, section

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apply *Gentile* exception where, as here, the "allegations rest solely on a purported loss in the economic value of [plaintiff's] ownership stake rather than any loss of voting power"); *Nikoonahad v. Greenspun Corp.*, No. C09-02242, 2010 WL 1268124, at *5 (N.D. Cal. Mar. 31, 2010) (same)

[5] That plaintiff's claims are derivative under *Tooley* is consistent with the recent holding of *NAF Holdings, LLC v. Li & Fung (Trading) Ltd.*, 118 A.3d 175 (Del. 2015). Although the Delaware Supreme Court held that NAF could bring its contractual claim directly, it specifically distinguished NAF's claim, based on its individual rights under the contract, from the plaintiff-stockholders in *Tooley*, because in *Tooley*, the plaintiffs had no separate contractual right to bring a claim and had no contractual rights under the merger agreement. 118 A.3d at 182, n.10. So too here, plaintiff has no right to payment for her stock, nor does plaintiff assert breach of contract. Nor is the unpublished trial court decision in *In re: El Paso Pipeline Partners, L.P. Deriv. Litig.*, 2015 WL 7758609 (Del. Ch. Dec. 2, 2015) to the contrary. There, the court made clear that a claim for damages to a corporation must be brought as a derivative action: "Treating a dual-natured claim as *derivative* for purposes of *claim initiation* achieves the important goals of screening out weak claims and providing an efficient and centralized mechanism for conducting the litigation." 2015 WL 7758609 at *2 (emphasis added). *El Paso* treated the claim as direct only for purposes of "claim continuation," where a subsequent merger would deprive plaintiffs of standing to pursue an already-initiated action. The court also indicated that if the plaintiff sought the return funds to the corporation—as Plaintiff seeks here—the claim would be derivative under second prong of *Tooley*. *Id.* at *31-32.

4617(b) of HERA expressly bars claims by the GSEs' shareholders during conservatorship. *See Kellmer v. Raines*, 674 F.3d 848, 850 (D.C. Cir. 2012) (section 4617(b) of HERA "plainly transfers shareholders' ability to bring derivative suits . . . to FHFA."); *La. Mun. Police Emps. Ret. Sys. v. FHFA*, 434 Fed. Appx. 188, 191 (4th Cir.2011) (per curiam) (same).

Second, the direct/derivative inquiry does not turn on the statute under which the plaintiff sues, but on the nature of the harm alleged and the relief sought. *Tooley*, 845 A.2d at 1049. If the harm alleged and the relief sought are derivative, then a lawsuit to enforce the claim is barred by the HERA succession of rights provision. That is the case here: the injury of which plaintiff complains is the alleged overpayment of dividends by the GSEs to Treasury, and the injunctive relief that plaintiff seeks is directed to the GSEs. *See* Am. Compl. ¶ 165, Prayer for Relief.

In all events, federal law, like state law, recognizes the distinction between injuries to a corporation and injuries to its shareholders. *See Franchise Tax Bd. v. Alcan Aluminum Ltd.*, 493 U.S. 331, 336 (1990); *Canderm Pharmacal, Ltd. v. Elder Pharm., Inc.*, 862 F.2d 597, 603 (6th Cir. 1988) (discussing prudential shareholder standing rule under federal law); *Am. Airways Charters Inc. v. Regan*, 746 F.2d 865, 873 n.14 (D.C. Cir. 1984) ("no shareholder—not even a sole shareholder—has standing in the usual case to bring suit in an individual capacity on a claim that belongs to the corporation."). And the distinction between derivative (injury to the corporation) and direct (injury to the shareholder) claims applies fully to claims under the APA. *See Sec. Indus. & Fin. Markets Ass'n v. Commodity Futures Trading Comm'n*, 67 F. Supp. 3d 373, 408 (D.D.C. 2014) (dismissing APA claim based on shareholder standing rule). Plaintiff's efforts to cast herself as an aggrieved party under section 702 of the APA, Opp. 65–66, thus amount to nothing. Her APA claims are derivative and are barred by section 4617(b)(2)(A).

B. HERA's Explicit Transfer of All Shareholder Rights to the Conservator for the Duration of the Conservatorship Contains No Exception That Would

Permit Plaintiffs' Claims

No matter how plaintiff characterizes her claims, her standing to bring *any* action with respect to the assets of the GSEs is one of the "rights, titles, powers, or privileges" of shareholders that was transferred to FHFA upon its appointment as conservator. 12 U.S.C. § 4617(b)(2)(A)(i). Thus, regardless of whether plaintiff's claims are "direct" or "derivative," she may not proceed with any action premised on an alleged right she lacks standing to assert while the conservatorships remain in effect. Her claims thus fail under the plain language of 12 U.S.C. § 4617(b)(2)(A), which bars any shareholder claims over the assets of the GSEs. [6]

In apparent recognition of this fact, plaintiff asks this Court to depart from the statute's text to create a judicial exception that would permit derivative suits alleging a "manifest conflict of interest" on the part of the conservator. Opp. 73–77; *see also Delta Sav. Bank v. United States*, 265 F.3d 1017 (9th Cir. 2001); *First Hartford Corp. Pension Plan & Trust v. United States*, 194 F.3d 1279 (Fed. Cir. 1999). Both of those cases concerned derivative suits over *pre-*

[6] The cases cited by plaintiff in support of her right to assert a "direct" claim under the APA, Opp. 61, in fact demonstrate that artful pleading should not draw "a veneer over a derivative claim." *Levin v. Miller*, 763 F.3d 667, 670 (7th Cir. 2014). In *Levin*, the Seventh Circuit held that under FIRREA, any claim "with respect to . . . the assets of the institution" constitutes a derivative action. *Id.* at 672 (citing 12 U.S.C. § 1821(d)(2)(A)(i)). Claims upon the assets of the bank – including a claim alleging a breach of a fiduciary duty allegedly owed to the holding company investors – were derivative and thus transferred to the conservator. *Id.* at 670–71. In *Vieira v. Anderson (In re Beach First National Bancshares, Inc.)*, 702 F.3d 772 (4th Cir. 2012), the Fourth Circuit held that all but one of plaintiffs' claims were derivative, and barred by FIRREA. *Id.* at 777. Only one claim, involving an injury to a holding company's interest in an LLC rather than the failed bank itself, asserted "direct harm to [the holding company] unrelated to any defalcation at the [b]ank level," and was thus allowed to proceed. *Id.* at 780; *see also Barnes v. Harris*, 783 F.3d 1185, 1193 (10th Cir. 2015) (bank holding company had failed to establish "any harm to the Holding Company that is distinct and separate from the harm to the Bank"). Similarly, in *Plaintiffs in All Winstar-Related Cases at Court v. United States*, 44 Fed. Cl. 3, 10 (1999), the court stated that, "[t]he critical factor here is that the corporation, the thrift, has been or will be liquidated." The court's "holding … is limited to the liquidation context in which any surplus, as a matter of law, must be distributed to the shareholders." *Id*. at 11–12.

receivership claims against federal agencies, and neither case supports the proposition that shareholders can sue the conservator itself, or the counter-party to an action taken by the conservator. Such a holding would be particularly illogical in the conservatorship context. *See Perry Capital*, 70 F. Supp. 3d at 230–31; *see also* Treasury Mem. 33–34.

If a "conflict of interest" exception could be grafted on to the language of HERA, and then extended to apply to suits that challenge the actions of the conservator itself, the exception would swallow the rule that forbids shareholder suits in the first place. Under plaintiff's theory, the statute could be evaded as a simple matter of pleading, so long as the complaint includes an allegation that the conservator is improperly exercising its authority by refusing to pursue the claim. Such a result is inconsistent with the limitations on review that Congress created in HERA. *See Kellmer*, 674 F.3d at 850. Plaintiff's proposed "manifest conflict of interest" exception would thus go well beyond the bounds even of the cases that have adopted such an exception. *See* Treasury Mem. 34.

In a last-ditch effort to bypass the statutory text, plaintiff argues that HERA must not be read literally, because the statute's express prohibition of shareholder claims would otherwise "raise grave constitutional concerns." Opp. 63. No constitutional claims have been raised here, and thus there is no need to consider the extent to which § 4617(b)(2)(A) might bar review of a constitutional challenge. Moreover, the doctrine of constitutional avoidance "has no application in the absence of statutory ambiguity," *United States v. Oakland Cannabis Buyers' Coop.*, 532 U.S. 483, 494 (2001), and plaintiff has failed to show any ambiguity in the text of § 4617(b)(2)(A)(i). In any event, the statute's simple deferral of review of plaintiff's claim during the pendency of the conservatorship would raise no constitutional concerns, even if those claims had been raised here. *See Elgin v. Dep't of Treasury*, 132 S. Ct. 2126, 2132 (2012).

III. Plaintiffs' APA Claims Against Treasury Fail as a Matter of Law.

A. The Third Amendment Was Not a Purchase of New Securities.

In her opposition brief, plaintiff does not dispute that the "sunset provision" in 12 U.S.C. § 1719(g)(4) applies only to Treasury's authority to "purchase" securities.[7] Treasury's authority to "exercise any rights received in connection" with earlier purchases, as well as its authority to hold or sell securities, did not expire. *See id*. § 1719(g)(2)(D). Nor does she dispute that HERA applies the emergency determination requirement and statutory considerations to the authority to "purchase" securities only, not to Treasury's separate authority to hold or sell securities, or exercise rights received in connection with earlier purchases. *See id.* § 1719(g)(1); § 1719(g)(2). Her APA thus claims hinge on the premise that an amendment to the existing PSPAs should be treated as a "purchase" of "obligations and other securities." 12 U.S.C. § 1719(g)(1)(A).

Plaintiff argues that any "exchange of value" suffices to make an agreement restructuring payment obligations a "purchase." Opp. 54. But an "exchange of value" is also the touchstone of any valid contract amendment. *See, e.g., Robinson v. Ada S. McKinley Cmty. Servs.*, 19 F.3d 359, 364 (7th Cir. 1994) ("A valid modification requires an offer, acceptance, and consideration."); E. Allan Farnsworth, Farnsworth on Contracts § 4.21 (3d ed. 2004). And, as the *Perry Capital* court recognized, HERA's sunset provision serves to bar Treasury's purchase of "obligations or securities issued by the GSEs." *See* 70 F. Supp. 3d at 224. The Third Amendment created "a new formula of dividend compensation for a $200 billion-plus investment Treasury had *already* made," and did not result in the issuance of any stock or the pledging of any additional taxpayer funds by Treasury. *Id.* (emphasis added). Without an

[7] While this brief cites the relevant portions of Fannie Mae's charter, the cited language is identical in Freddie Mac's charter. *Compare* 12 U.S.C. § 1719(g), *with* 12 U.S.C. § 1455(*l*).

exchange of securities for money, there is no "purchase" of "obligations and other securities" under any meaning of those terms.

Plaintiff's argument is particularly anomalous in light of other provisions of HERA which explicitly recognize the distinction between a purchase and a modification to an existing agreement, and expressly provided funding for such modifications. *See* 12 U.S.C. § 1719(g)(3) ("[a]ny funds expended for the purchase of, or modifications to, obligations and securities, or the exercise of any rights received in connection with such purchases under this subsection shall be deemed appropriated at the time of such purchase, modification, or exercise."). Indeed, Congress has continued to recognize Treasury's ongoing authority to amend the PSPAs. *See* Consolidated Appropriations Act of 2016, § 702(a)(2)(A) (enacted Dec. 18, 2015).[8]

Even assuming that it were necessary that Treasury modify the PSPAs through the "exercise" of a reserved contractual "right," that requirement was satisfied here. When it entered into the Third Amendment, Treasury "exercise[d] [the] right[]," 12 U.S.C. § 1719(g)(2)(A)—explicitly conferred by the original PSPAs in 2008—to amend those contracts. *See* Ex. A. at 13, 27, ECF No. 22-2 ("This Agreement may be waived or amended solely by a writing executed by both of the parties hereto."). That Treasury exercised its right to amend jointly with FHFA makes it no less the exercise of a right. A contract confers a "right" to be "exercised" even when the right is to be exercised jointly. *See, e.g.*, *Public Serv. Co. of New Hampshire v. Hudson Light*

[8] Plaintiff also cites, Opp. 55, an Internal Revenue Service tax regulation, 26 C.F.R. § 1.1001-3, which address the circumstances in which "modification of the terms of a debt instrument" qualifies as an "exchange" of property, such that any financial gain resulting from the modification must be declared as income. Plaintiff provides no reason to believe that Congress intended the word "purchase" to be read synonymously with the word "exchange," as used by the IRS in a tax regulation addressing *debt* instruments, not *equity* instruments such as Treasury's preferred stock. *See Perry Capital*, 70 F. Supp. 3d at 224 (rejecting identical argument).

& Power Dep't, 938 F.2d 338, 345, 347 (1st Cir. 1991) (rejecting "attempt by appellants . . . to impede [one party's] exercise of its exclusive contract right to enter into an agreement with [the counter-party] to modify the Sellback Agreement."). A right, as plaintiff asserts, Opp. 52, is a "legal, equitable, or moral entitlement to do something," and to "exercise" means to "make use of; to put into action" or "[t]o implement the terms of." Black's Law Dictionary 916 (10th ed. 2014). When Treasury and FHFA agreed to the Third Amendment, they "ma[d]e use of" their "legal . . . entitlement" to amend the original PSPAs.[9]

Plaintiff cannot revive her textually deficient "purchase" argument by relying on the "fundamental change" doctrine. Plaintiff concedes that many courts – including the Sixth Circuit – have never recognized the "fundamental change" doctrine even in the securities fraud context in which it arose, while others have expressly declined to adopt it. *See Isquith by Isquith v. Caremark Int'l, Inc.*, 136 F.3d 531, 535 (7th Cir. 1998);[10] *see also Katz v. Gerardi*, 655 F.3d 1212, 1221 (10th Cir. 2011).[11] Yet she insists that the doctrine's rejection "cast[s] no doubt on

[9] Plaintiff cites *United States v. Petty Motor Co.*, 327 U.S. 372 (1946), for the assertion that a contractual "right" cannot entail mutual agreement. Opp. 52. *Petty Motor* was a takings case that concerned the amount of just compensation the government owed to tenants of a property that the government had appropriated. The Supreme Court determined that the tenants were entitled to damages equal to the value of the remainder of their lease. *Id.* at 380. In a footnote, the Court noted that plaintiffs were not entitled to damages based on the expected renewal of their leases, even though the building's landlord had often extended their leases through "mutual consent." *Id.* at 380 n.9. It was the terms of the lease, not the parties' informal expectations, that delineated the tenants' "rights" to compensation. *Id.*

[10] Plaintiff's attempt to distinguish *Isquith*, Opp. 55, simply misreads the case: The Seventh Circuit rejected "the 'fundamental change' doctrine," which "began life as the 'forced seller' doctrine." *Isquith*, 136 F.3d at 535.

[11] Further, *SEC v. Nat'l Securities, Inc.*, 393 U.S. 453 (1969), does not stand for the proposition that "holders of a fundamentally changed security are considered purchasers of new securities," Opp. 55. That case did not rely on the "purchase" language of section 10(b), but rather on the "broad antifraud purposes" of section 10(b) which were "furthered" by their application to an

it" as an interpretive tool for HERA. Opp. 55. However, "[E]soteric and dubious judge-made doctrine[s]," *Isquith*, 136 F.3d at 535, from disparate legal contexts are not used to shed light on the meaning of terms in entirely different statues, particularly where there is sharp disagreement over the validity of that interpretation. *Cf. Bruesewitz v. Wyeth*, 562 U.S. 223, 243 (2011); *Jama v. Immigration & Customs Enf't*, 543 U.S. 335, 349 (2005). And plaintiff does not even attempt to answer Treasury's point that the "fundamental change" doctrine cannot apply where the supposed "purchaser" does not claim to have been defrauded. *See* Treasury Mem. 22.

B. HERA Does Not Impose Fiduciary Duties on Treasury.

Plaintiff's claim that the Third Amendment was arbitrary and capricious because it is not consistent with Treasury's fiduciary duties under state corporate law fails because Treasury has no such fiduciary duties to the GSEs shareholders. Plaintiff argues that these duties arise under Delaware and Virginia state corporate law, *see* Opp. 58, but ignores two fundamental related components of the Supremacy Clause: intergovernmental immunity and preemption. The Supreme Court has repeatedly held that state law does not apply of its own force to the activities of the federal government. *See Hancock v. Train*, 426 U.S. 167, 179 (1976) ("[W]here Congress does not affirmatively declare its instrumentalities or property subject to regulation, the federal function must be left free of regulation."); *Lamb v. Martin Marietta Energy Sys., Inc.*, 835 F. Supp. 959, 963 (W.D. Ky. 1993) ("The Supreme Court has long held that the Supremacy Clause forbids state regulation of the federal government's activities.") (citing *McCulloch v. Maryland*, 4 Wheat. 316, 426 (1819)).

Congress did not create a fiduciary duty between Treasury and the GSEs' shareholders in

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alleged deceptive scheme in which shareholders exchanged their stock as part of a merger. 393 U.S. at 467.

HERA. To the contrary, 12 U.S.C. § 1719(g) and 12 U.S.C. § 1455(*l*) expressly state that the emergency authority to provide funding to the GSEs was granted to "provide stability to the financial markets," "prevent disruptions in the availability of mortgage finance," and "protect the taxpayer." 12 U.S.C. § 1719(g)(1)(B). Consequently, even if state law could be applied to the federal government (and it cannot), HERA would preempt any state law that imposes requirements incompatible with the federal statute. *See Arizona v. United States*, 132 S. Ct. 2492, 2501 (2012) (state law is preempted where it "stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress.").

Nothing in HERA establishes a fiduciary duty between Treasury and the GSEs' shareholders (the words "fiduciary duty" do not appear in either section 1719(g) or 1455(*l*)), and such a duty is inconsistent with Treasury's statutory mandates to provide funding to the GSEs to stabilize the housing market, and to structure its investment "to protect the taxpayers." 12 U.S.C. §1719(g)(1)(C). Further, Congress instructed the Secretary to consider a number of factors that are flatly inconsistent with the notion that Treasury owes a fiduciary duty to the GSEs' shareholders, including "the need for preferences or priorities regarding payments to the Government," and "[r]estrictions on the use of corporation resources, including limitations on the payment of dividends and executive compensation . . . ." *Id.* § 1719(g)(1)(C)(i), (vi).

Plaintiff cites two other considerations in section 1719(g)(1)(C) in support of her argument: "[t]he corporation's plan for the orderly resumption of private market funding or capital market access," and "[t]he need to maintain the corporation's status as a private shareholder-owned company." *Id.* § 1719(g)(1)(C)(iii),(v). However, plaintiff neglects to mention that all of the factors listed are to be considered "*[t]o protect the taxpayers*." *Id.* § 1719(g)(1)(C) (emphasis added). Congress did not require Treasury to consider the interests of

private shareholders in a way that would prioritize them over or conflict with protecting the taxpayers' interests, and indeed HERA actually instructs Treasury to consider factors that are directly contrary to the interests of shareholders. *Id.* § 1719(g)(1)(C)(i),(vi). Finally, Plaintiff cites no authority holding that a federal agency extending emergency funding is bound by state law fiduciary duties, and previous cases have rejected this argument. *See Starr Int'l Co., Inc. v. Fed. Reserve Bank of New York*, 742 F.3d 37, 41–42 (2d Cir. 2014) ("Delaware fiduciary duty law cannot be applied to FRBNY's rescue activities consistently with adequate protection of the federal interests at stake in stabilizing the national economy.").[12]

C. Treasury Is Not a Controlling Shareholder Under State Law.

Even if state law could be applied to the activities of Treasury, a fiduciary relationship would not arise because Treasury is not a "controlling shareholder" under state law. Plaintiff counters that she has *alleged* that Treasury is a controlling shareholder, and therefore the Court must treat this allegation as true. Opp. 58. That is wrong. Pleading "labels and conclusions" simply "will not do," *Ashcroft v. Iqbal*, 556 U.S. 662, 678 (2009) (quoting *Bell Atl. Corp. v. Twombly*, 550 U.S. 544, 555 (2007)), and the existence of a controlling shareholder relationship is a question of law.[13] *See Starr Int'l Co. v. Fed. Reserve Bank of New York*, 906 F. Supp. 2d 202, 216–30 (S.D.N.Y. 2012). Plaintiff makes no attempt to answer the arguments of the

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[12] *Cobell v. Norton*, 240 F.3d 1081 (D.C. Cir. 2001), is of no help to plaintiff. The fiduciary duties of the United States as a trustee of tribal land and property, discussed in that case, "can only arise from a statute, treaty, or executive order." *Id.* at 1098 (citation omitted). Where, as here, Congress has not imposed such a fiduciary duty, none exists.

[13] *Gradient OC Master, Ltd v. NBC Universal, Inc.*, 930 A.2d 104 (Del. Ch. 2007), which plaintiff cites elsewhere, *see* Opp. 70 & 72, undermines her position. There, the court held that plaintiffs failed to show that either defendant constituted "a *de facto* or controlling shareholder" in the absence of evidence that defendants had "close to a majority of shares," regardless of allegations concerning NBCU's "impact on the Board's decisions" as a "result of contractual obligations between NBCU and ION." *Id.* at 130–31.

opening brief that her allegations are simply insufficient as a matter of law to establish that Treasury is a controlling shareholder.[14] Treasury Mem. 35–36.

IV. PLAINTIFF'S CLAIMS ARE BARRED BY ISSUE PRECLUSION.

Plaintiff attempts to escape issue preclusion by primarily arguing that because her claims are direct, not derivative, she should not be bound by the final judgment in *Perry Capital*. *See* Opp. 77–80. This argument fails because, as explained above, her claims are derivative.

Plaintiff argues that issue preclusion does not apply to her claims because the APA claims in *Perry Capital* "were indisputably asserted and prosecuted as direct claims," and that the plaintiffs in that case thus could not adequately represent her interests. Opp. 78, 79. Plaintiff ignores that *Perry Capital* also addressed expressly derivative claims. *See Perry Capital*, 70 F. Supp. 3d at 229 ("The class plaintiffs have brought . . . derivative claims for breach of fiduciary duty."). The court held these derivative claims were barred because: (a) they sought equitable relief, including rescission of the Third Amendment, and such relief is barred by Section 4617(f), *see id.* at 224–29; and (b) HERA's succession of rights provision, 12 U.S.C. § 4617(b)(2)(A)(i), bars derivative claims notwithstanding allegations that the conservator faced a conflict of interest. *Perry Capital*, 70 F. Supp. 3d at 230–32. Issue preclusion bars "successive litigation of an issue of fact or law actually litigated and resolved in a valid court determination essential to the prior judgment, *even if the issue recurs in the context of a different claim*." *Taylor v. Sturgell*, 553 U.S. 880, 892 (2008) (emphasis added); *see also Stryker Corp. v. Nat'l Union Fire*

[14] Her lone argument, a citation to the CBO's budgetary treatment of the GSEs, Opp. 58, is unavailing. CBO includes the GSEs' operations in the federal budget because they are under the conservatorship of a federal agency and the taxpayers' commitment of funds has provided them with all of their operating capital in conservatorship. Congressional Budget Office, CBO's Budgetary Treatment of Fannie Mae and Freddie Mac 7 (2010). Whether or not Treasury is a "controlling shareholder" under state law plays no part in the CBO's analysis. *Id.*

Ins. Co. of Pittsburgh, PA, 681 F.3d 819, 824 (6th Cir. 2012) (same). Because the issues of whether HERA bars all claims seeking equitable relief and all shareholder derivative claims, notwithstanding an alleged conflict of interest, were actually litigated in *Perry Capital* and were necessary for that court's dismissal of the derivative claims, she is barred from re-litigating those issues here, even under the guise of a different derivative claim.[15]

Plaintiff also complains in passing that she "cannot be presumed to have been on notice that her rights were at issue" in *Perry Capital*. Opp. 79. But there is no "notice" requirement for issue preclusion to apply to subsequent derivative actions. Courts routinely apply issue preclusion in subsequent derivative actions without considering notice. *See Arduini v. Hart*, 774 F.3d 622, 637–38 (9th Cir. 2014); *In re Sonus Networks, Inc, S'holder Derivative Litig.*, 499 F.3d 47, 64 (1st Cir. 2007).

Finally, the Court should reject plaintiff's request for a "special circumstances" exception to the normal rules of preclusion. Opp. 80. The ever-growing number of follow-on shareholder suits concerning the Third Amendment illustrates the need for application of the issue preclusion doctrine; they are not a reason for an exception to the normal rules.

CONCLUSION

For the foregoing reasons, and for those stated in FHFA's reply brief, the Court should grant the motions to dismiss.

[15] Plaintiff's reliance on the D.D.C.'s *Rafter* order, Opp. 78 n.24, is inapt: whether the court's conclusion in *Perry Capital* that the contract claims were derivative can be characterized as a holding vs. *dicta* is irrelevant since the court also considered and dismissed expressly derivative claims as barred by HERA. That holding precludes plaintiff's derivative claims here.

Dated: March 14, 2016

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that on this 14th day of March, 2016, I electronically filed the foregoing through the Court's ECF system, which will send a notice of electronic filing to all parties to this action.

/s/ Thomas D. Zimpleman