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

ARNETIA JOYCE ROBINSON, Plaintiff, v. THE FEDERAL HOUSING FINANCE AGENCY, in its capacity as Conservator of the Federal National Mortgage Association and the Federal Home Loan Mortgage Corporation, MELVIN L. WATT, in his official capacity as Director of the Federal Housing Finance Agency, and THE DEPARTMENT OF THE TREASURY, Defendants.	Civil Action No. 7:15-cv-00109-ART-EBA

REPLY OF DEFENDANTS FHFA AND MELVIN L. WATT TO PLAINTIFF'S RESPONSE TO SUPPLEMENTAL BRIEF IN FURTHER SUPPORT OF DEFENDANTS' MOTION TO DISMISS

Adjudicating Plaintiff's claims would require the Court to review—and, if Plaintiff prevails, nullify—FHFA's regulatory action (separate and apart from the Conservator's execution of the Third Amendment) to suspend capital classifications in light of the Treasury commitment, which provides the Enterprises with the capital support necessary to facilitate the Enterprises' ongoing operations. *See* FHFA Examination Manual at "Capital" p.1, *available at* http://goo.gl/BXpdSU (recognizing that, "[i]n Conservatorship the Enterprises are capitalized via the [PSPAs] with the United States Treasury"). Plaintiff's claims are thus barred by Section 4623(d), which precludes courts from taking any action that will "affect, by injunction or otherwise . . . the issuance or effectiveness" of any regulator action taken under HERA's

provisions concerning regulatory supervision based on capital classifications. 12 U.S.C. § 4623(d). Plaintiff's Response (Doc. # 54) fails to overcome this dispositive jurisdictional bar.

First, Plaintiff argues Section 4623(d) does not apply because the October 2008 Action was not an action taken by FHFA as regulator. Response at 5. Rather, according to Plaintiff, only the FHFA as Conservator has the authority to suspend capital classifications for the duration of the conservatorship. *Id*. (citing 12 C.F.R. § 1237.3(c)). This is wrong. The plain text of FHFA's announcement of the October 2008 Action makes clear the action was taken by FHFA's Director, acting in his regulatory capacity. Indeed, the first sentence of the announcement refers to FHFA's Director as "the safety and soundness *regulator* for Fannie Mae and Freddie Mac," and the announcement goes on to state that "[t]he *Director* is, therefore, announcing several capital-related decisions," and that "[t]he *Director* has determined it is prudent and in the best interests of the market to suspend capital classifications" in light of the PSPAs. *See* Ex. A to FHFA Suppl. Br. (Doc. # 53) (emphases added). Assessing the safety and soundness of the Enterprises by conducting examinations of the Enterprises' capital levels is a regulatory function.

FHFA's Examination Manual, which describes the regulatory examination process, further confirms that the October 2008 Action was a regulatory action. *See generally* FHFA Examination Manual, *available at* http://goo.gl/m8n0Ah. That manual states that: "Given the Conservatorships, FHFA suspended regulatory capital classifications. FHFA has not issued capital classifications since September 2008. Any capital needs (ensuring both Enterprises maintain positive GAAP net worth) are fulfilled by Treasury under the SPSPAs. . . . due to the Conservatorship, examiners need not conduct supervisory activities related to these [preexisting capital] requirements." FHFA Examination Manual at "Capital" p.16, *available at* http://goo.gl/BXpdSU.

Moreover, that the Conservator is empowered to suspend capital classifications for the duration of the conservatorships (12 C.F.R. § 1237.3) does not mean FHFA as regulator did not suspend the capital classification in 2008, three years before the regulation was revised to state the Conservator's power to suspend capital classifications. *See* 76 FR 35733 (June 20, 2011). Indeed, this regulation is expressly derived from provisions of HERA also applicable to FHFA in its regulatory capacity. *See* 12 C.F.R. § 1273.3(c) (describing the "authority to suspend capital classifications" as being "under Section 1364(e)(1) of the Safety and Soundness Act," which is codified within 12 U.S.C. § 4614, a statutory section concerning capital classifications by FHFA as regulator). Accordingly, even if there were no conservatorship, the Director would still be authorized to undertake actions of the type at issue here.

Second, Plaintiff argues that the October 2008 Action allegedly was not a "classification or action" to which Section 4623(d) applies. Response at 5-6. Again, Plaintiff is wrong. Section 4623(d) applies to "any classification or action of the Director under this subchapter," and Subchapter II (in which Section 4623(d) appears) empowers the Director to take a host of supervisory actions over the Enterprises. *See, e.g.*, 12 U.S.C. § 4615 (empowering the Director to, *inter alia*, review capital plans, restrict asset growth, limit acquisitions and new activities of "undercapitalized" entities); *id.* § 4616 (empowering the Director to, *inter alia*, restrict capital distributions, limit increases in obligations, limit growth, limit acquisition of new capital, restrict risky activities, reconstitute the board of "significantly undercapitalized" entities). Subchapter II also includes Section 4617, which empowers the Director to appoint FHFA as conservator or receiver of the Enterprises. *See id.* § 4617(a)(2), (b). The October 2008 Action falls well within the provisions of this Subchapter, as it reflects a determination by the Director that, in light of the Treasury commitment and FHFA's ability as Conservator to operate the Enterprises directly,

"the Enterprises will not be subject to other prompt corrective action requirements" available under Subchapter II, and the capital requirements otherwise applicable under Subchapter II "will not be binding during the conservatorship." Oct. 2008 Action. As FHFA explained to Congress, the Director took the October 2008 Action "based on the fact that the purpose of the [capital] classifications—prompt corrective action—is moot during conservatorship, and because the capital, or GAAP net worth, position of the Enterprise would be supported by the United States Treasury's [PSPAs]." FHFA 2008 Report to Congress at 36, 42, *available at* http://goo.gl/zWnqgu.[1] Accordingly, the October 2008 Action was plainly an "action of the Director" under Subchapter II, and Section 4623(d) thus applies.

Third, Plaintiff argues she is not challenging the October 2008 Action, and that her demand to vacate the Third Amendment "would not reinstate the capital requirements or affect the suspension of those requirements in any way." Response at 6. But Plaintiff's own allegations and arguments in opposition to the motions to dismiss confirm that Plaintiff is, in fact, arguing that the Third Amendment was beyond the Conservator's powers and functions because it allegedly renders the Enterprises unsafe and unsound by limiting the amount of capital they retain. *See* Opp. to Mot. to Dismiss, 34 (Doc. # 32); *see also* Am. Compl. ¶¶ 25, 99, 111-13, 125. This argument is foreclosed by the Director's October 8 Action, which is premised on the conclusion that FHFA as regulator declared that the Enterprises *could* operate with zero capital without being deemed unsafe and unsound, and without being subjected to further supervisory actions based on the Enterprises' capital levels. By asking the Court to declare the

[1] *See also* FHFA Examination Manual at "Capital" p. 16, *available at* http://goo.gl/BXpdSU (noting that "[a]ny capital needs . . . are fulfilled by Treasury under the SPSPAs"); FHFA Advisory Bulletin AB2013-03 at 7 n.6 (May 31, 2013), available at http://goo.gl/fi8k7m ("Regardless of the suspension of ratings and changes to the PSPAs over time, the conservatorships satisfy the Agency's PCA [prompt corrective action] requirements with respect to the Enterprises").

Third Amendment unlawful because it allegedly renders the Enterprises unsafe and unsound, Plaintiff is challenging the Director's conclusion in the October 2008 Action that capital requirements be suspended because, in light of the Treasury commitment, these requirements no longer serve as a determiner of safety and soundness. Such a request is barred by Section 4623(d).[2]

CONCLUSION

For the foregoing reasons—in addition to the bar against challenges to Conservator actions set forth in Section 4617(f), and the succession to all shareholder rights set forth in Section 4617(b)(2)(A)(i)—this Court should dismiss Plaintiff's complaint with prejudice because Plaintiff's challenge to the Director's October 2008 capital determination is precluded by Section 4623(d).

[2] Plaintiff argues that the Treasury commitment should not be viewed as capital because the PSPAs exclude the commitment from their description of the Enterprises' "total assets." Response at 7. But the PSPAs' description of "total assets" applies for the specific purposes of calculating the "deficiency amount" and is not a statement on the purpose of the Treasury commitment. Rather, it simply facilitates the process whereby the Enterprises can draw funds from the commitment. Under the PSPAs, the Enterprises may draw funds from the commitment only if the Enterprises' total liabilities exceed their total assets on a quarterly basis. *See* PSPAs § 1 (defining "Deficiency Amount") and § 2.2 (available at http://goo.gl/nKKlgU). If the Treasury commitment, which at present stands at $258 billion, were included in the calculation of the Enterprises' total assets under the PSPAs, then the Enterprises' total liabilities could not exceed their total assets, and the Enterprises would thus be unable to draw funds from the commitment under the PSPAs. The PSPAs' exclusion of the commitment from the calculation of the Enterprises' total assets is merely a mechanical device to facilitate the proper calculation of a deficiency amount and, if necessary, a draw of funds under the PSPAs.

Dated: July 7, 2016

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that on this 7th day of July, 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/ Howard N. Cayne