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January 20, 2017

BY CM/ECF

The Honorable Gregory M. Sleet
U.S. District Court for the District of Delaware
U.S. Courthouse
844 North King Street
Wilmington, DE 19801

Re: *Jacobs v. Federal Housing Finance Agency*,
C.A. No. 15-708-GMS

Dear Judge Sleet:

I write on behalf of plaintiffs David Jacobs and Gary Hindes in response to the January 9, 2017 correspondence sent by defendant Federal Housing Finance Agency ("FHFA") and nominal defendants Federal National Mortgage Association and Federal Home Loan Mortgage Corporation (together, the "Companies") regarding the Delaware Supreme Court's recent decision in *El Paso Pipeline GP Co., L.L.C. v. Brinckerhoff*, No. 103, 2016, --- A.3d ---, 2016 WL 7380418 (Del. Dec. 20, 2016). D.I. 55.

Defendants failed to mention in their January 9 letter the particular grounds on which the Delaware Supreme Court decided *El Paso*. Critical to the Delaware Supreme Court's decision was the master limited partnership context in which the case arose and the specific language of the limited partnership agreement governing El Paso Pipeline Partners, L.P. (the "Partnership"). The court found that the claims asserted in *El Paso* were derivative because, under the Partnership's limited partnership agreement, "the contractual duty of good faith was owed to the Partnership, not the individual limited partners," and, therefore, the Partnership owned the claims. *El Paso*, 2016 WL 7380418, at *8. In contrast, the statutory and contract claims asserted in this case concern breaches of duties owed directly to the Companies' stockholders under the Delaware and Virginia corporation statutes, which are incorporated into the Companies' respective charters, or under the certificates of designation governing the Companies' preferred stock. With respect to these claims, the Delaware Supreme Court's *El Paso* decision reaffirmed that, where a plaintiff "asserts a claim based upon the plaintiff's own right, such as a claim for breach of a commercial contract," the plaintiff's claim is direct. *Id.* at *9; *see also In re Activision Blizzard, Inc. S'holder Litig.*, 124 A.3d 1025, 1050 (Del. Ch. 2015) ("Stockholders similarly can sue directly to enforce contractual constraints on a board's authority under the charter, bylaws, and provisions of the DGCL . . . [which] together constitute a multi-party contract among the directors, officers, and stockholders of the corporation.") (footnotes omitted); *Gale v. Bershad*, C.A. No. 15714, 1998

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WL 118022, at *2-3 (Del. Ch. Mar. 4, 1998) (holding that preferred stockholder had stated a direct claim against the defendant corporation and its directors for alleged breaches of corporate charter).

Nor does the decision in *El Paso* suggest that plaintiffs' fiduciary duty claims here are solely derivative. As explained by the Delaware Supreme Court, dropdown transactions of the type challenged by the *El Paso* plaintiff "support the typical master limited partnership ('MLP') scheme[.]" *El Paso*, 2016 WL 7380418, at *3. Unlike the dropdown transactions in which MLPs routinely engage with their general partners for legitimate business reasons but which allegedly may involve an "overpayment" by the partnership, the Net Worth Sweep was designed to expropriate the entire economic value of the *minority stockholders'* interest in the Companies and transfer the value of their interest to the government. In this context, and with the Companies in conservatorship, the distinction between direct and derivative claims does not depend on the "voting power [of] the minority stockholders." *Id.* at *12.

Also of importance to the Supreme Court's decision was the fact that the *El Paso* plaintiff had litigated the case through trial solely on a derivative theory. *See id.* at *1-3, *10, *13 ("Finally, Brinckerhoff never presented evidence at trial of specific harm suffered by the limited partners[.] . . . It follows that the General Partner should not be penalized for failing to defend at trial an element of a claim . . . that the plaintiff never attempted to prove."). Conversely, here, plaintiffs have pleaded and pursued direct theories since the filing of their original complaint, *see* D.I. 1 (Counts I-VIII), and they continue to pursue direct claims in their proposed amended complaint, *see* D.I. 48-1 (Counts I-IV).

Regardless, as explained more fully in plaintiffs' opposition to defendants' motion to dismiss, even if plaintiffs' claims were derivative, the Housing and Economic Recovery Act of 2008 ("HERA") permits the Companies' stockholders to bring derivative claims where, as here, FHFA has a manifest conflict of interest. *See* D.I. 23 at 50-53; *accord* 12 U.S.C. § 4617(a)(5) (authorizing Companies to seek judicial review of FHFA's decision to impose conservatorship despite separate HERA provision specifying that, as conservator, FHFA "immediately succeed[s]" to the Companies' rights, titles, powers, and privileges). That has long been the federal courts' interpretation of the Financial Institutions Reform, Recovery, and Enforcement Act ("FIRREA"), and Congress's decision to include substantially identical language in HERA demonstrates that it intended to adopt the judicial interpretations of FIRREA.

Respectfully,



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cc: Counsel of Record – by CM/ECF