UNITED STATES DISTRICT COURT
DISTRICT OF MINNESOTA

Case No. 17-cv-02185 (PJS/HB)

ATIF F. BHATTI, TYLER D. WHITNEY, and MICHAEL F. CARMODY,

Plaintiffs,

-vs-

THE FEDERAL HOUSING FINANCE AGENCY, MELVIN L. WATT, in his official capacity as Director of the Federal Housing Finance Agency, and THE DEPARTMENT OF THE TREASURY,

Defendants.

PLAINTIFFS' FIRST AMENDED COMPLAINT FOR DECLARATORY AND INJUNCTIVE RELIEF

Plaintiffs Atif F. Bhatti, Tyler D. Whitney, and Michael F. Carmody, for their Complaint against Defendants, state and allege as follows:

I.
INTRODUCTION

1. This is an action challenging both past and ongoing policies by a federal agency that operates outside the system of limited and divided government established by the Constitution. This Nation's multi-trillion dollar housing finance market, and familiar features of that market such as readily available 30-year fixed rate mortgages, are built on the foundation of two federally chartered, privately owned entities—the Federal National Mortgage Association and the Federal Home Loan Mortgage Corporation (respectively, "Fannie" and "Freddie," and, together, the "Companies"). Since September 2008, when the Federal Housing Finance Agency ("FHFA") exercised its regulatory authority to

force Fannie and Freddie into conservatorship, FHFA has wielded plenary control over the Companies' operations. FHFA's regulation and operation of the Companies is largely unconstrained by *any* of the three branches of the federal government—FHFA does not depend on congressional appropriations for funding, its Director answers to no one (not even the President), and many of its actions are unreviewable by the courts. FHFA's unbounded authority over Fannie and Freddie and the housing finance market cannot be reconciled with our constitutional system of limited and divided government authority. FHFA has misused its unchecked authority by expropriating tens of billions of dollars of value from private parties for the benefit of the federal government. The provisions of law purporting to allow such actions should be struck down, and the deleterious consequences flowing from those provisions should be undone.

II.
JURISDICTION AND VENUE

2. This action arises under the U.S. Constitution. The Court has subject-matter jurisdiction under 28 U.S.C. §§ 1331 and 2201.

3. Venue is proper in this Court under 28 U.S.C. § 1391(e)(1)(C) because this is an action against agencies of the United States and an officer of the United States in his official capacity, one of the Plaintiffs resides in this judicial district, and no real property is involved in the action.

III.
PARTIES

4. Plaintiff Atif F. Bhatti is a citizen of Minnesota. Mr. Bhatti owns shares of Fannie Mae common stock.

5. Plaintiff Tyler D. Whitney is a citizen of Minnesota. Mr. Whitney owns shares of Fannie Mae common and preferred stock and shares of Freddie Mac common and preferred stock.

6. Plaintiff Michael F. Carmody is a citizen of Missouri. Since September 2008 Mr. Carmody has continuously owned shares of Fannie Mae preferred stock. Mr. Carmody also owns shares of Freddie Mac preferred stock.

7. Defendant FHFA is an independent agency of the United States Government headed by a single Director. FHFA was created on July 30, 2008, pursuant to the Housing and Economic Recovery Act of 2008 ("HERA"). FHFA is located at 400 7th Street, S.W., Washington, D.C. 20024.

8. Defendant Melvin L. Watt is the Director of FHFA. His official address is 400 7th Street, S.W., Washington, D.C. 20024. He is being sued in his official capacity.

9. Defendant Department of the Treasury is an executive agency of the United States Government. Treasury is located at 1500 Pennsylvania Avenue, N.W., Washington, D.C. 20220.

IV.
FACTUAL ALLEGATIONS

Fannie and Freddie

10. Fannie is a for-profit, stockholder-owned corporation organized and existing under the Federal National Mortgage Act. Freddie is a for-profit, stockholder-owned corporation organized and existing under the Federal Home Loan Corporation Act. The Companies' business includes purchasing and guaranteeing mortgages

originated by private banks and bundling the mortgages into securities that can be sold to investors. Fannie and Freddie are owned by private shareholders, and their stock is publicly traded.

11. Both Fannie and Freddie have issued common stock and several series of preferred stock. The various series of preferred stock of the Companies are in parity with each other, but they have priority over the Companies' common stock. The holders of common stock are entitled to the residual economic value of the firms.

12. Before 2007, Fannie and Freddie were consistently profitable. In fact, Fannie had not reported a full-year loss since 1985, and Freddie had never reported a full-year loss since becoming owned by private shareholders. In addition, both Companies regularly declared and paid dividends on their preferred and common stock.

Congress Establishes FHFA as An Independent Agency Headed by a Single Director

13. From 1992 until 2008, the Companies were regulated by the Office of Federal Housing Enterprise Oversight ("OFHEO")—an office within the Department of Housing and Urban Development. OFHEO was not an independent agency; its Director could be removed from office by the President for any reason. *See* Housing and Community Development Act of 1992 § 1312. To fund OFHEO's operations, Congress permitted the office to impose annual assessments on the Companies "to the extent provided in appropriation Acts." Housing and Community Development Act of 1992 § 1316(a). By statute OFHEO's annual spending plans had to be included in the President's budget. *Id.* § 1316(g)(3). The President's control over OFHEO's Director and the fact that OFHEO was subject to the congressional appropriations process ensured that

the office remained accountable to the People through their democratically elected representatives.

14. During the summer of 2008, Congress passed and President Bush signed HERA, which established FHFA as the successor to OFHEO. Unlike its predecessor, FHFA is an "independent" agency, 12 U.S.C. § 4511(a); 44 U.S.C. § 3502(5), and it is headed by a Director who is only removable "for cause by the President," 12 U.S.C. § 4512(b)(2). To further insulate FHFA from presidential influence, HERA also provides that when FHFA acts as conservator it "shall not be subject to the direction or supervision of any other agency of the United States." *Id.* § 4617(a)(7). Also unlike OFHEO, FHFA is funded through assessments that are "not . . . construed to be Government or public funds or appropriated money." *Id.* § 4516(f)(2). As a result, FHFA is neither subject to presidential control nor constrained by the congressional appropriations process.

15. Unlike almost all other independent agencies in our Nation's history, FHFA is headed by a single individual rather than a multi-member board or commission. This highly unusual feature of FHFA's structure violates the separation of powers. In the absence of direct control by the democratically elected President, the usual multi-member leadership structure of independent agencies acts as a substitute check on the excesses of any individual leader of an independent agency. The traditional multi-member structure guards against arbitrary decision making and protects individual liberty by preventing the concentration of power in the hands of any one person. Independent agencies headed by multi-member boards are forced to account for multiple viewpoints, adopt compromises that result in less extreme decisions, and better resist capture by interest groups. FHFA's

unusual structure prevents those affected by its decisions from enjoying the benefits of multi-member leadership, and as a result FHFA has undertaken a series of actions that have significantly harmed the Companies' private shareholders.

16. The fact that FHFA is headed by a single individual also means that the President has less influence over its decisions than the decisions made by independent agencies headed by multi-member commissions. When an independent agency is run by a commission with multiple members who serve staggered terms and with a chairperson who the President designates, the President can influence agency actions by appointing one or more commission members and selecting the chairperson. Many statutes that create multi-member commissions also require bipartisan membership, thus guaranteeing that at least some members will belong to the President's political party. FHFA's Director, in contrast, serves a five-year term and may remain in office indefinitely if the Senate fails to confirm a successor. 12 U.S.C. § 4512(b)(2), (4). As a result, FHFA's Director could remain in office during the entire four-year term of a President from a different political party, all the while pursuing policies directly at odds with those of the incumbent President. As a result of FHFA's unusual structure, it is more insulated from presidential influence than virtually any other independent federal agency.

17. FHFA's status as an independent agency headed by a single Director makes it different from almost every other independent agency in our Nation's history. Indeed, Plaintiffs are aware of only two agencies that were similarly structured when FHFA was created in 2008: the Office of Special Counsel and the Social Security Administration. The structure of both agencies has been constitutionally contested by the Executive

Branch. Furthermore, both agencies are subject to the annual congressional appropriations process, which subjects them to a significant measure of congressional oversight that does not apply to FHFA.

18. Two years after HERA established FHFA, Congress created the Consumer Financial Protection Bureau ("CFPB"), which is also an independent agency headed by a single Director. The Executive Branch has taken the position that the CFPB's structure violates the separation of powers.

19. It is not constitutional for any independent federal agency to operate under the direction of a single individual, but this structure is especially problematic in FHFA's case because it has vast authority over a critical sector of the United States economy. FHFA's current Director has said that his agency is "charged with directing the largest conservatorships in U.S. history in support of the Nation's multi-trillion dollar mortgage finance system." As FHFA's former longtime acting Director has written, "the entire housing system . . . rel[ies] almost entirely on [FHFA's] decisions." Michael Bright & Ed DeMarco, Why Housing Reform Still Matters, Milken Institute Center for Financial Markets 3 (June 2016).

No Statutory Principles Guide FHFA's Claimed
Sweeping Conservatorship Powers

20. HERA empowers FHFA to exercise "general and regulatory authority" over the Companies, 12 U.S.C. § 4511(b)(2); 12 U.S.C. 4501 note, and also authorizes FHFA to place the Companies into conservatorship under certain specified conditions, *see* 12 U.S.C. § 4617(a). While the statute includes a lengthy recitation of powers FHFA

"may" exercise as conservator, FHFA has claimed that it says nothing about what the conservator *should* do. Under this reading of HERA, Congress has failed to articulate an intelligible principle to guide FHFA in the exercise of its conservatorship powers.

21. When it acts as conservator, FHFA has successfully argued that its powers are "extraordinarily broad." *Perry Capital LLC v. Mnuchin*, -- F.3d --, 2017 WL 3078345, at *8 (D.C. Cir. July 17, 2017). Indeed, FHFA has consistently taken the position that as conservator it has "plenary operational authority," Final Opening Brief of Appellees FHFA, Watt, Fannie, and Freddie at 11, *Perry Capital LLC v. Lew*, No. 14-5243 (D.C. Cir. Mar. 7, 2016), and may "operate Fannie and Freddie as it sees fit," FHFA Memorandum in Supp. of Mot. to Dismiss at 15, *Collins v. FHFA*, No. 16-cv-3113 (S.D. Tex. Jan. 9, 2017), ECF No. 24 (quotation marks omitted).

22. Under FHFA's interpretation of HERA, the statute not only gives the conservator sweeping operational authority over the Companies and unbounded discretion to dispose of their assets but also provides that as conservator FHFA "immediately succeed[s] to . . . all rights, titles, powers, and privileges of . . . any stockholder" in the Companies. 12 U.S.C. § 4617(b)(2)(A). With limited exceptions, courts have interpreted this language as making FHFA the successor to derivative claims that shareholders could otherwise file on the Companies' behalf, *Perry Capital*, 2017 WL 3078345, at *23-24, and this provision also makes FHFA the successor to shareholders' rights to inspect the Companies' books and records, *Pagliara v. Federal Home Loan Mortg. Corp.*, 203 F. Supp. 3d 678, 685 (E.D. Va. 2016). As conservator, FHFA thus controls the Companies themselves *and* many of the rights of their private shareholders.

As with its overall authority to manage the Companies, FHFA's interpretation of its statutory authority over shareholder rights does not include an intelligible principle to guide the conservator in its decisions about how to exercise these rights.

23. HERA also says that FHFA "may" exercise the "incidental power" to "take any action authorized by this section, which the Agency determines is in the best interests of the regulated entity *or the Agency*." 12 U.S.C. 4617(b)(2)(J) (emphasis added). FHFA understands this provision to allow it to use its conservatorship powers to advance *its own* interests when those interests conflict with the interests of the Companies and their shareholders. And since the statute does not say how FHFA should go about determining what is in its own interests, FHFA's interpretation of this incidental power effectively empowers it to do anything it wants with the Companies and their assets.

24. Further compounding the lack of an intelligible principle to guide FHFA's exercise of its discretion when it acts as conservator, HERA also severely restricts the availability of judicial review of FHFA's actions as conservator. Most significantly, HERA specifies that "no court may take any action to restrain or affect the exercise of powers or functions of [FHFA] as a conservator." 12 U.S.C. § 4617(f). A number of other provisions of HERA impose additional limitations on judicial review of FHFA's actions as conservator, receiver, or regulator. *See id.* § 4617(b)(2)(A)(i); *id.* § 4617(b)(5)(E); *id.* § 4617(b)(11)(D); *id.* § 4623(d). While none of these provisions bars constitutional claims like those raised in this suit, HERA's restrictions on judicial review further insulate FHFA from the mechanisms the Constitution creates to protect individual rights from arbitrary decisions by the federal government.

Fannie and Freddie Are Forced into Conservatorship

25. Although Congress passed HERA amidst the decline in home prices and financial turmoil of 2008, the Companies were well-positioned to weather those events and were never at any meaningful risk of insolvency. Although both Companies recorded losses in 2007 and the first two quarters of 2008—losses that largely reflected a temporary decline in the market value of their holdings caused by declining home prices—they continued to generate enough cash to easily pay their debts and retained billions of dollars of capital that could be used to cover any future losses.

26. Neither Company was in danger of insolvency in 2008. Indeed, during the summer of 2008, OFHEO Director James Lockhart, who would later become FHFA's first Director, told CNBC that "[b]oth of these companies are adequately capitalized, which is our highest criteria." And on July 13, 2008, Director Lockhart issued a statement emphasizing that "[t]he Enterprises' $95 billion in total capital, their substantial cash and liquidity portfolios, and their experienced management serve as strong supports for the Enterprises' continued operations." An analysis of Freddie's financial condition in August 2008 for FHFA by BlackRock supported these assessments and stated that Freddie's "long-term solvency does not appear endangered – we do not expect Freddie Mac to breach critical capital levels even in stress case."

27. Thanks to the Companies' healthy financial condition in mid-2008, they had the capacity to raise additional capital through the financial markets. Indeed, at this time Fannie had roughly $700 billion in unencumbered liquid assets that were available

to be pledged as collateral for purposes of raising capital, and it had identified a number of private investors who were prepared to provide additional capital.

28. Despite the Companies' strong financial position, FHFA initiated a long-term policy of seizing control of Fannie and Freddie and operating them for the exclusive benefit of the federal government. On September 6, 2008, FHFA directed the Companies' boards to consent to conservatorship. Given that the Companies were not in financial distress and were in no danger of defaulting on their debts, the Companies' directors were confronted with a Hobson's choice: face intense regulatory scrutiny from FHFA as retaliation for rejecting conservatorship, or submit to FHFA's demands and receive a grant of immunity for personal liability under 12 U.S.C. § 4617(a)(6). FHFA ultimately obtained the Companies' consent by threatening to seize them if they did not acquiesce.

29. In publicly announcing the conservatorships, FHFA confirmed that the Companies' private shareholders continued to hold an economic interest that would have value, particularly as the Companies generated profits in the future.

FHFA and Treasury Enter Into the Preferred Stock Purchase Agreements

30. In addition to authorizing FHFA to act as the Companies' conservator, HERA also gave the Treasury Department temporary authority to purchase securities from the Companies. *See* 12 U.S.C. §§ 1455(*l*), 1719(g). HERA expressly stated that Treasury could not exercise this authority without the Companies' consent. 12 U.S.C. §§ 1455(*l*)(1)(A), 1719(g)(1)(A). HERA further provided that Treasury's statutory authority to purchase the Companies' securities would expire at the end of 2009. 12 U.S.C. §§ 1455(*l*)(4), 1719(g)(4).

31. On September 7, 2008, the day after FHFA forced the Companies into conservatorship, Treasury exercised its statutory authority to purchase the Companies' securities. Acting in its capacity as the Companies' conservator, FHFA agreed to Treasury's purchases on the Companies' behalf, and the two federal agencies entered into the Preferred Stock Purchase Agreements (PSPAs).

32. The PSPAs are materially identical for both Companies. Under the original agreements, Treasury committed to provide up to $100 billion to each Company to ensure that it maintained a positive net worth. For quarters in which either Company's liabilities exceed its assets under Generally Accepted Accounting Principles, the PSPAs authorize draws upon Treasury's commitment in an amount equal to the difference between liabilities and assets.

33. In return for Treasury's funding commitment, FHFA agreed to provide Treasury with several forms of consideration that together would entitle Treasury to much—but not all—of the Companies' accumulated capital and future profits. With the Companies still able to raise additional funding in the capital markets and at no risk of failing to generate enough cash to cover their expenses, this was a one-sided agreement that the Companies would not have agreed to had they still been under private management.

34. Under the PSPAs, Treasury received several forms of consideration in return for its funding commitment. First, FHFA agreed to sell Treasury warrants to purchase 79.9% of the common stock of each Company at a nominal price. Exercising these warrants would entitle Treasury to up to 79.9% of all future profits of the

Companies, subject to the Companies' obligation to satisfy their dividend obligations with respect to their preferred stock and to share the remaining 20.1% of those profits with private common shareholders.

35. As further consideration for Treasury's funding commitment, Treasury also received 1 million shares of senior preferred stock ("Government Stock") in each Company. Treasury's Government Stock in each Company had an initial liquidation preference of $1 billion. This liquidation preference increases by one dollar for each dollar the Companies draw on Treasury's funding commitment. In the event that the Companies liquidate, Treasury is entitled to recover the full amount of the liquidation preference before any other preferred or common shareholder receives anything.

36. In addition to payments in the event that the Companies are liquidated, the Government Stock also entitled Treasury to receive, at the Companies' election, either: (i) a cumulative cash dividend equal to 10% of the value of Treasury's outstanding liquidation preference; or (ii) a 12% increase in the amount of Treasury's liquidation preference. If the Companies decided not to pay the dividend in cash, the resulting increase in the size of Treasury's liquidation preference would amount to an in-kind dividend payment of additional Government Stock. After any such in-kind dividend payment, the PSPAs provided that the dividend rate would increase to 12% (payable either in cash or in kind, as just described) until such time as full cumulative dividends were paid in cash, at which point the rate would return to 10%. Thus, the Companies never were required to pay a cash dividend to Treasury but rather had the discretion to pay dividends in kind.

37. FHFA officials repeatedly confirmed their understanding that the PSPAs were designed to allow the Companies to pay the Government Stock dividends in kind—with additional Government Stock—rather than in cash. A document attached to a September 16, 2008, email between FHFA officials expressly states that PSPA dividends may be "paid in-kind." Another FHFA document says that Treasury's Government Stock pays "10 percent cash dividend (12 percent payment-in-kind)." In an internal October 2008 email to Mario Ugoletti—who was then a Treasury official, but later moved to FHFA and was a key point of contact with Treasury in the development of the Net Worth Sweep—another Treasury official indicated that Treasury's consultant wanted to know "whether we expect [Fannie and Freddie] to pay the preferred stock dividends in cash or to just accrue the payments." Following his move to FHFA, Mr. Ugoletti acknowledged the option to pay dividends "in kind" in an email that he sent on the day the Net Worth Sweep was announced.

38. An in-kind dividend payment would not have decreased the amount of Treasury's remaining funding commitment because only when the Companies receive "funding under the Commitment" does the commitment's size decrease. PSPA § 1. Thus, as the Congressional Research Service has acknowledged, under the PSPAs' original terms the Companies could "pay a 12% annual senior preferred stock dividend indefinitely." N. ERIC WEISS, CONG. RESEARCH SERV., RL34661, FANNIE MAE'S AND FREDDIE MAC'S FINANCIAL PROBLEMS (Summary) (Aug. 10, 2012).

39. Finally, the PSPAs provided for the Companies to pay Treasury a quarterly periodic commitment fee "intended to fully compensate [Treasury] for the

support provided by the ongoing Commitment." PSPA § 3.2(a). The periodic commitment fee was to be set for five-year periods by agreement of the Companies and Treasury, but Treasury had the option to waive it for up to a year at a time. Treasury repeatedly exercised this option and never deemed it necessary to receive a periodic commitment fee under the PSPAs. Even if the fee had been charged, the Companies were always free under the express terms of the PSPAs to pay the fee in-kind with additional senior preferred stock rather than in cash, a fact that Freddie's auditor recognized. *See* PSPA § 3.2(c). Furthermore, had a periodic commitment fee been charged, it would have been, at most, a small fraction of the outstanding amount of Treasury's commitment. Freddie forecasted its "sensitivity" to imposition of a periodic commitment fee as follows: "Our sensitivity to a commitment fee based on remaining commitment available beginning in 2013 of $149 billion shows that a 25 bps fee results in a $0.4 billion annual impact on Stockholders' Equity." Indeed, given the Companies' healthy financial condition since 2012, a market-based periodic commitment fee since that time would have been zero.

40. While Treasury's commitment remains outstanding, Fannie and Freddie generally are prohibited from paying down amounts added to the liquidation preference due to draws from Treasury's commitment. *See* Fannie and Freddie Government Stock Certificates § 3(a). The PSPAs also prohibit Fannie and Freddie from declaring and paying dividends on any securities junior to Treasury's Government Stock unless full cumulative dividends have been paid to Treasury on its Government Stock for the then-current and all past dividend periods.

41. On May 6, 2009, FHFA and Treasury amended the PSPAs to increase Treasury's funding commitment to each Company from $100 billion to $200 billion. On December 24, 2009—one week before Treasury's temporary statutory authority to purchase the Companies' securities expired—the agencies again amended the terms of Treasury's funding commitment. Instead of resetting the commitment at a specific dollar amount, the second amendment established a formula to allow Treasury's total commitment to each Company to exceed (but not fall below) $200 billion depending upon any net worth deficiencies experienced in 2010, 2011, and 2012, and any surplus existing as of December 31, 2012.

Director Lockhart Resigns and Mr. DeMarco Serves as
<u>FHFA's Acting Director for Over Four Years</u>

42. As the Director of OFHEO when HERA became law, James Lockhart automatically became the first person to serve as FHFA's independent Director. *See* 12 U.S.C. § 4512(b)(5). Mr. Lockhart forced the Companies into conservatorship and signed the original PSPAs on their behalf in September 2008. On August 5, 2009, Mr. Lockhart publicly announced that he would resign at the end of the month.

43. HERA provides that "[i]n the event of the . . . resignation . . . of the Director, the President shall designate" one of FHFA's three Deputy Directors "to serve as acting Director until . . . the appointment of a successor" who is nominated by the President and confirmed by the Senate. *Id.* § 4512(f). Each of FHFA's Deputy Directors is appointed by FHFA's Director. *Id.* § 4512(c)–(e). In accordance with HERA, on August 25, 2009, President Obama designated Edward DeMarco to serve as FHFA's

acting Director. At the time, Mr. DeMarco was FHFA's Senior Deputy Director for Housing Mission and Goals. Mr. DeMarco had previously been appointed to that post by Mr. Lockhart.

44. Acting agency heads normally serve only temporarily, during the time necessary for the President to nominate and the Senate to confirm someone to permanently fill the position. But it was not until 15 months after Director Lockhart's resignation, on November 15, 2010, when President Obama nominated Joseph A. Smith, Jr. to be FHFA's Director. The Senate failed to confirm Smith, and on December 22, 2010, the nomination was returned to the President. President Obama did not again nominate someone to fill the vacancy created by Mr. Lockhart's resignation until May 2013, when he nominated Congressman Melvin L. Watt. After more than seven months, the Senate confirmed Mr. Watt on December 10, 2013. Mr. Watt was sworn into office on January 6, 2014.

45. From August 2009 until January 2014, Mr. DeMarco led FHFA as the independent agency's acting Director. Mr. DeMarco's 52-month tenure was only eight months shy of the full five-year term that a Senate-confirmed FHFA Director would have served. *See* 12 U.S.C. § 4512(b)(2). And during the great majority of the time Mr. DeMarco was acting Director, there was no pending nomination from the President to fill the important post that Mr. DeMarco occupied. It is highly unusual for an acting agency head to remain in office for even one year. The fact that FHFA did not have a Senate-confirmed Director for over four years, during much of the time when the Nation's housing market was recovering from the 2008 financial crisis, is extraordinary.

46. During his time as acting Director, Mr. DeMarco was responsible for an important shift in FHFA's overall approach to operating the Companies as their conservator. Whereas Mr. Lockhart publicly stated that his goal was to help the Companies rebuild capital and return to private control, Mr. DeMarco undertook a policy aimed at winding down the Companies and doing so in a manner that guaranteed their private shareholders would lose all the value of their investments. Pursuit of this policy ultimately led to the imposition of the Net Worth Sweep on August 17, 2012—three years into Mr. DeMarco's tenure as acting Director.

47. Despite Mr. DeMarco's commitment to operate the Companies for the exclusive financial benefit of the federal government, he resisted some of the Obama Administration's most significant housing finance policies. Most notably, Mr. DeMarco refused to approve the Administration's proposal that the Companies reduce the principal on certain mortgages in an effort to jumpstart the recovery in housing prices. The Obama Administration nevertheless recognized that the President could not fire Mr. DeMarco due to his status as the head of an independent agency. On August 3, 2012, HUD Secretary Shaun Donovan acknowledged that "some ha[d] called for [Mr. DeMarco] to be fired" but told reporters "[t]hat is not authority that the president has." The Obama Administration reached that conclusion despite its desire for new leadership at FHFA. As early as October 2011, Politico reported that Mr. DeMarco had "resisted White House and Treasury Department pressure to step down."

48. Mr. DeMarco also understood that, even though he was FHFA's *acting* Director, he was statutorily empowered to act independently from the President.

Responding to criticism from Obama Administration allies in 2011, Mr. DeMarco described himself as "an independent regulator" who was "not trying to be a friend or foe to anyone." And in March 2012, Mr. DeMarco stated that "the environment of the last number of months have shown substantial attempt to influence or direct an independent regulator."

49. Even if Mr. DeMarco had acceded to the Obama Administration's pressure to resign, Mr. DeMarco could only have been replaced by one of FHFA's three Deputy Directors. 12 U.S.C. § 4512. Mr. DeMarco was himself one of those Deputy Directors, and the other two were appointed by Mr. DeMarco or Mr. Lockhart. Representative Barney Frank, who was at the time the ranking member of the House Financial Services Committee, told a reporter that FHFA's Deputy Directors "support DeMarco's strategies" and "would likely continue the same foreclosure policies that have so angered Democrats and housing advocates."

Under FHFA's Management, the Companies Adopt Unjustified Accounting Policies that Improperly Increase Their Draws on Treasury's Funding Commitment

50. Starting when FHFA took control of the Companies as conservator, the Companies began to make overly pessimistic and unjustified assumptions about their future financial prospects. Those assumptions triggered adjustments to the Companies' balance sheets, most notably write-downs of significant deferred tax assets and the establishment of large loan loss reserves, which caused the Companies to report large non-cash losses. Although reflecting nothing more than faulty accounting assumptions about the Companies' future prospects and having no effect on the cash flow the

Companies were generating, these non-cash losses temporarily decreased the Companies' reported net worth by hundreds of billions of dollars. For example, in the first year and a half after imposition of the conservatorship, Fannie reported $127 billion in losses, but only $16 billion of that amount reflected actual credit-related losses. FHFA was directly involved in the decision to record these excessive non-cash losses.

51. Ultimately, the Companies drew a total of $187 billion from Treasury, in large part to fill the holes in their balance sheets created by these artificial non-cash losses. Including Treasury's initial $1 billion liquidation preference in each Company, Treasury's liquidation preference for its Government Stock amounts to approximately $117 billion for Fannie and approximately $72 billion for Freddie. Approximately $26 billion of these combined amounts were drawn simply to pay the 10% dividend payments owed to Treasury. Thus, Treasury actually disbursed approximately $161 billion to the Companies, primarily reflecting the results of the erroneous accounting decisions.

The Companies Return to Profitability and Stability

52. In 2012, Fannie and Freddie began generating consistent profits notwithstanding their overstated loss reserves and the write-down of their deferred tax assets. Fannie has not drawn on Treasury's commitment since the fourth quarter of 2011, and Freddie has not drawn on Treasury's commitment since the first quarter of 2012. In fact, in the first two quarters of 2012, the Companies posted sizable profits totaling more than $11 billion.

53. By 2012, the Companies were well-positioned to continue generating robust profits for the foreseeable future. Fannie's and Freddie's financial results are

strongly influenced by home prices, which were improving. The improving housing market was coupled with stricter underwriting standards at Fannie and Freddie. As a result—and as FHFA knew—Fannie- and Freddie-backed loans issued after 2008 had dramatically lower serious delinquency rates than loans issued between 2005 and 2008. The strong quality of these newer "vintages" of loans boded well for the Companies' future financial prospects.

54. Together, the Companies' return to robust profitability and the stable recovery of the housing market showed in early 2012 that the Companies could in time redeem Treasury's Government Stock and that value remained in their privately owned preferred and common stock. Furthermore, as a result of Fannie's and Freddie's return to sustained profitability, it was clear that the overly pessimistic accounting decisions weighing down the Companies' balance sheets would have to be reversed. Due to these reversals, by early August 2012, FHFA knew that Fannie and Freddie were poised to generate profits well in excess of the 10% cash dividend the Companies had previously paid Treasury.

FHFA and Treasury Amend the PSPAs To Expropriate
<u>Private Shareholders' Investments</u>

55. On August 17, 2012, days after the Companies had announced their return to profitability and just as it was becoming clear that they had regained the earnings power to redeem Treasury's Government Stock and exit conservatorship, FHFA and Treasury amended the PSPAs for a third time. The third amendment imposed the Net Worth Sweep, under which the Companies are required to pay Treasury a quarterly

dividend starting in 2013 and continuing forever that is equal to their entire net worth, less a small capital buffer that decreases by $600 million every year and reaches zero starting in 2018. Thus, rather than paying Treasury a fixed 10% cash or 12% in kind dividend, the Companies are now required to pay Treasury all of their comprehensive income and retained assets in perpetuity. Since the Net Worth Sweep guarantees that Treasury will receive all of the Companies' comprehensive income anyway, the third amendment suspended the periodic commitment fee.

56. FHFA and Treasury have claimed that the Net Worth Sweep was necessary to restructure the dividend on the Government Stock because the Companies could not afford a cash dividend equal to 10% of Treasury's liquidation preference. Several facts show that the purported problem was not the true reason for FHFA's actions. First, as explained above, the original terms of the PSPAs entitled the Companies to pay Treasury's dividends in kind with additional stock, thus avoiding the need to make draws on Treasury's funding commitment to finance cash dividends they could not otherwise afford.

57. Second, FHFA and Treasury considered an alternative to the arrangement they ultimately adopted that would have had the Net Worth Sweep only kick in if Treasury's remaining funding commitment fell below $100 billion. The only plausible explanation for the decision not to embrace this alternative is that FHFA knew that it would allow the Companies to rebuild capital in contravention of its plans to wipe out private shareholders and wind down the Companies.

58. Third, the structure and timing of the Net Worth Sweep—coming when the Companies were about to add tens of billions of dollars to their balance sheets—had the effect of *reducing* the amount of money available to guarantee that the Companies would maintain a positive net worth. Indeed, during a June 24, 2012 meeting with Secretary Geithner, acting Director DeMarco said that he did not "see[] the urgency of amending the PSPAs this year" because "the GSEs will be generating large revenues over the coming years, thereby enabling them to pay the 10% annual dividend well into the future even with the caps."

59. FHFA's reason for imposing the Net Worth Sweep was to further its objectives of expropriating private shareholders' investments and winding down the Companies. Even before the Net Worth Sweep, FHFA had resolved under acting Director DeMarco's leadership to operate Fannie and Freddie with the aim of "minimiz[ing] losses on behalf of taxpayers," FHFA, A STRATEGIC PLAN FOR ENTERPRISE CONSERVATORSHIPS: THE NEXT CHAPTER IN A STORY THAT NEEDS AN ENDING 7 (Feb. 21, 2012)—a goal that ignores the fact that no such losses have been incurred.

60. The Net Worth Sweep furthered FHFA's goal of enriching the federal government at private shareholders' expense. As FHFA has explained, the Net Worth Sweep "ensures all the [Companies'] earnings are used to benefit taxpayers." FHFA, 2012 REPORT TO CONGRESS at 1. Treasury similarly explained when the Net Worth Sweep was announced that this change would require that "every dollar of earnings that Fannie Mae and Freddie Mac generate will be used to benefit taxpayers." Press Release,

U.S. Dep't of the Treasury, Treasury Department Announces Further Steps to Expedite Wind Down of Fannie Mae and Freddie Mac (Aug. 17, 2012).

61. FHFA also imposed the Net Worth Sweep to further its goal of reforming the Nation's housing finance system by winding down Fannie and Freddie and ensuring that they could not exit conservatorship under private control. In its 2012 report to Congress, FHFA explained that it had begun "prioritizing [its] actions to move the housing industry to a new state, one without Fannie Mae and Freddie Mac." FHFA, 2012 REP. at 13. Mr. DeMarco informed a Senate Committee that the Net Worth Sweep would further this goal, explaining that "recent changes to the PSPAs, replacing the 10 percent dividend with a net worth sweep, reinforce the notion that the [Companies] will not be building capital as a potential step to regaining their former corporate status." Edward J. DeMarco, Acting Director, FHFA, Statement Before the U.S. Sen. Comm. on Banking & Urban Affairs 3 (Apr. 18, 2013).

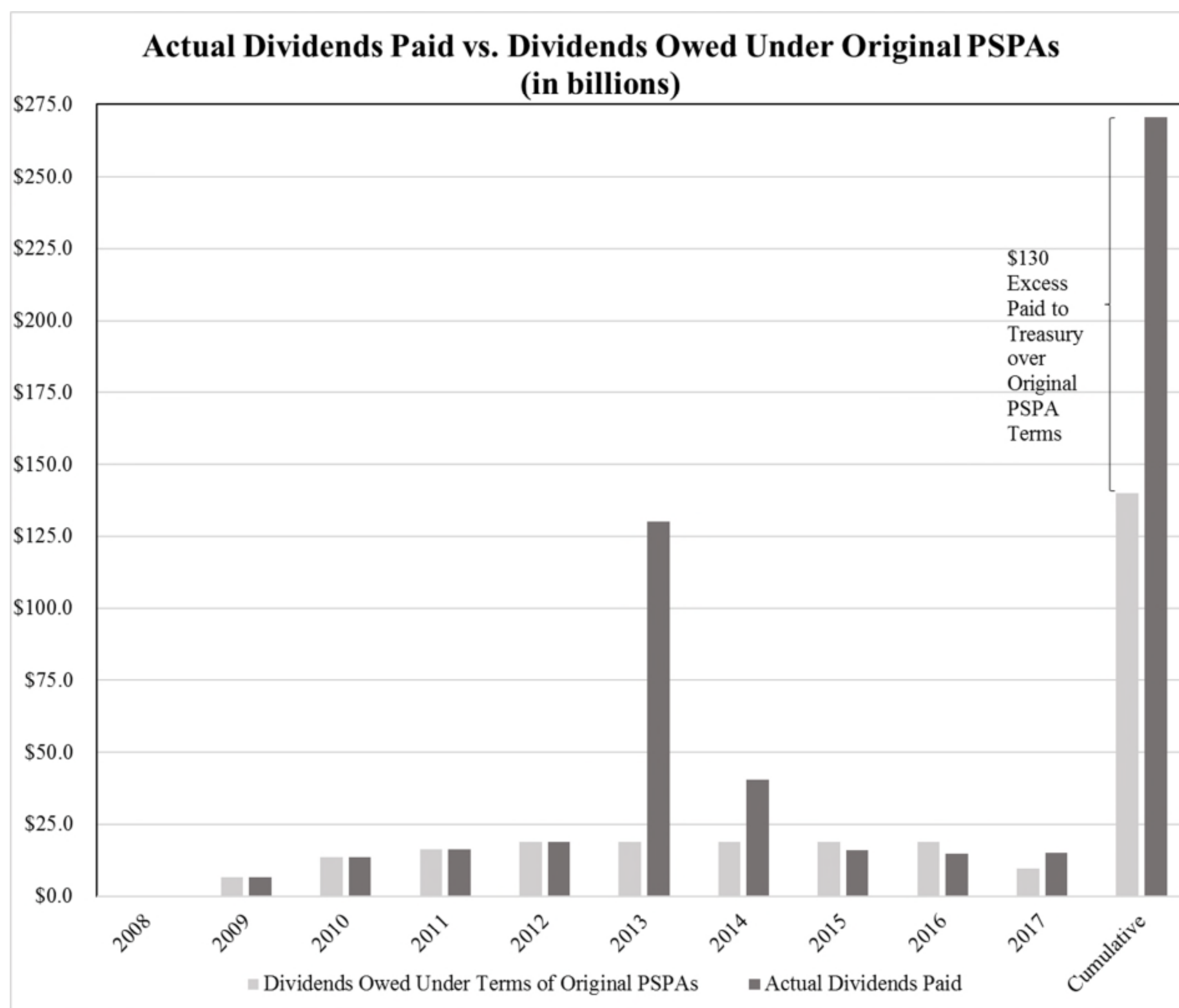
62. The timing of the Net Worth Sweep was driven by the Companies' return to profitability. The "risk" that concerned FHFA was that Fannie and Freddie would recognize extraordinary profits that would allow them to begin rebuilding their capital levels and position themselves to exit conservatorship and deliver value to their private shareholders.

The Federal Government Reaps Windfall Profits from Its Investment
<u>In the Companies Due to the Net Worth Sweep</u>

63. As FHFA anticipated, Fannie and Freddie have been extraordinarily profitable since the imposition of the Net Worth Sweep. From January 2013 through the

end of the second quarter of 2017, the Companies have paid $215.6 billion in Net Worth Sweep "dividends"—over $130 billion more than they would have paid under the prior contractual arrangement. Had they instead been paying 10% cash dividends, they would have paid Treasury approximately $85 billion

64. The following chart shows how imposition of the Net Worth Sweep dramatically increased the size of the Companies' dividend payments to Treasury:



65. Had the Companies used their quarterly profits in excess of Treasury's 10% dividend to partially retire Treasury's senior preferred stock, Treasury's remaining

investment in the Companies would today be roughly $6 billion. Instead, the Net Worth Sweep required the Companies to simply pay these funds over to Treasury in exchange for nothing. As explained above, FHFA knew that the Net Worth Sweep would result in this massive financial windfall for the federal government.

66. The negative impact of the Net Worth Sweep on the Companies' private shareholders is demonstrated by Fannie's results in the first quarter of 2013. At the end of the first quarter Fannie's net worth stood at $62.4 billion. Under the prior versions of the PSPAs, if Fannie chose to declare a cash dividend it would have been obligated to pay Treasury a dividend of only $2.9 billion, and the balance—$59.5 billion—would have been credited to its capital. Private shareholders would have been contractually entitled to dividends before any additional amount of that residual capital could have been paid out to Treasury. The Net Worth Sweep, however, required Fannie to pay Treasury $59.4 billion, while private shareholders were left with nothing.

67. The Net Worth Sweep has become a major revenue source for the United States Government at the expense of Plaintiffs and other private shareholders. For example, the federal government's record-breaking $53.2 billion surplus for the month of December 2013 was driven in large part by the $39 billion swept from Fannie and Freddie. Fannie's and Freddie's outsize dividend payments in 2013 also extended by approximately two months Treasury's ability to meet federal obligations during the debt ceiling crisis.

68. Treasury has disbursed $116.1 billion to Fannie under the PSPAs, and Treasury has recouped a total of $162.6 billion from Fannie in the form of purported

"dividends." Treasury has disbursed $71.3 billion to Freddie under the PSPAs and Treasury has recouped a total of $108.2 billion from Freddie in the form of purported "dividends." Fannie and Freddie have collectively paid Treasury approximately $83.3 billion more than they have received.

69. Yet, under the Net Worth Sweep, these dividend payments do not reduce the liquidation preference or otherwise redeem any of Treasury's Government Stock. Instead, the liquidation preference of Treasury's Government Stock in the Companies remains at approximately $189 billion (due to the Companies' draws and the $1 billion initial valuation of Treasury's Government Stock in each) and will remain at that amount regardless of how many billions of dollars the Companies pay to Treasury in "dividends" going forward.

FHFA Engages in Other Ongoing Conduct that Harms the Companies and Their Private Shareholders

70. Even after it became clear that the Net Worth Sweep had dissipated tens of billions of dollars that the Companies could have otherwise retained as capital, FHFA has used its conservatorship powers to block shareholder suits aimed at overturning the Net Worth Sweep. FHFA has used its status as the successor to most shareholder derivative claims under 12 U.S.C. § 4617(b)(2)(A) to obtain dismissal of shareholder derivative suits brought against FHFA, the Treasury Department, and the Companies' auditors.

71. In entering into and defending the Net Worth Sweep, FHFA has also disregarded the fiduciary duties that state law normally applies to a corporation's

management. If FHFA had fiduciary duties to the Companies or their shareholders, its decision to approve and defend the Net Worth Sweep would be an unlawful act of self-dealing and a violation of the duties of loyalty and care. But when FHFA acts as conservator under HERA, it has successfully argued that it has no duty to prioritize the interests of shareholders above its own interests. In defending the Net Worth Sweep in other cases, FHFA has repeatedly argued that the decision's severe adverse consequences for the Companies and private shareholders do not matter because FHFA was free to pursue *its own* best interests. In adopting and defending the Net Worth Sweep, FHFA has thus disregarded the limits that state law would otherwise impose on the Companies' management.

72. FHFA's approval of the Net Worth Sweep also authorized its contractual counterparty—the Treasury Department—to engage in conduct that would have otherwise violated HERA and the Administrative Procedure Act. In entering into the Net Worth Sweep, Treasury acted arbitrarily and capriciously and it violated HERA, which does not permit Treasury to purchase the Companies' securities after 2009. But on the theory that 12 U.S.C. § 4617(f) not only bars judicial review of *FHFA's* actions as conservator but also the actions of third parties with whom FHFA contracts, courts have dismissed Administrative Procedure Act claims against Treasury. *See Perry Capital*, 2017 WL 3078345, at *16-17. Thus, by contracting with Treasury, FHFA was able to use its conservatorship powers to effectively change the law and empower a federal agency to engage in conduct that would have otherwise violated federal statutes.

73. FHFA's defense of the Net Worth Sweep is just one manifestation of its ongoing policy of seeking to eliminate the investments of the Companies' private shareholders while winding down the Companies and preventing them from rebuilding capital. FHFA is also directing the Companies to develop the Common Securitization Platform—a de facto merger of the information technology systems the Companies use to issue mortgage-backed securities. FHFA has described the Common Securitization Platform as a "cornerstone[]" of housing finance reform that is intended to facilitate the entry of new competitors into the mortgage securitization business. FHFA also has a policy of directing the Companies to enter into uneconomic "credit risk transfer" deals that further FHFA's goal of increasing the role of other financial institutions in the housing finance markets to the Companies' expense and disadvantage.

CLAIMS FOR RELIEF

COUNT I

Violation of the President's Constitutional Removal Authority Against FHFA as Both Regulator and Conservator and Treasury

74. Plaintiffs incorporate by reference the allegations of the preceding paragraphs.

75. The Constitution provides that the "executive Power shall be vested in a President," U.S. CONST. art. II, § 1, cl. 1, and that "he shall take Care that the Laws be faithfully executed," U.S. CONST. art. II, § 3. Those provisions vest all executive power in the President of the United States and give the President the constitutional authority to remove federal agency heads from office at will. Although the Supreme Court has recognized a limited exception to this constitutional principle for certain independent

agencies headed by expert, multi-member commissions, *see generally Humphrey's Executor v. United States*, 295 U.S. 602 (1935), that exception does not apply to FHFA.[1]

76. By making FHFA's head a single Director rather than a multi-member board and eliminating the President's power to remove the Director at will, HERA violates the President's constitutional removal authority.

77. The constitutional defect in FHFA's structure is exacerbated by the fact that FHFA has broad power over the housing sector, a vital part of the economy that represents over 15% of Gross Domestic Product. FHFA has used its conservatorship and regulatory authority in an effort to unilaterally reform this vast sector of the economy to the disadvantage of the Companies and their shareholders.

78. FHFA is subject to the Constitution's separation of powers when it acts as conservator, especially when it exercises its conservatorship powers to expropriate private property.

79. Moreover, even if FHFA were never subject to the Constitution's separation of powers when it acts as conservator, it would still be subject to the separation of powers when it acts as regulator. FHFA acted in its capacity as regulator when it forced the Companies into conservatorship, and that initial decision made it possible for FHFA to later approve the Net Worth Sweep in its capacity as the Companies' conservator. The fact that FHFA was operating in violation of the separation of powers when it initially imposed the conservatorships infects its subsequent decision

[1] Although a ruling in Plaintiffs' favor would be entirely consistent with *Humphrey's Executor*, Plaintiffs believe that the Supreme Court should overrule that decision.

as conservator to agree to the Net Worth Sweep. Furthermore, during conservatorship the Companies remain subject to oversight by FHFA as regulator, and FHFA as conservator could not have agreed to the Net Worth Sweep or ordered the Companies to pay dividends without authorization from FHFA as regulator. *See* 12 C.F.R. § 1237.12(a), (b) (providing that "a regulated entity shall make no capital distribution while in conservatorship" except with authorization from "[t]he Director," i.e., FHFA as regulator).

80. The Net Worth Sweep visits new injuries on the Companies' private shareholders that they did not experience when the conservatorships were initially imposed. It only became clear when FHFA agreed to the Net Worth Sweep that FHFA's operation of the conservatorships would result in the total expropriation of private shareholders' investments. Furthermore, given FHFA's assurances when it initially imposed the conservatorships that it would manage the Companies with the aim of preserving and conserving their assets and rehabilitating them to a sound and solvent condition, the Companies' shareholders did not have adequate notice or incentive to contest the initial decision to impose the conservatorships in 2008.

81. Plaintiffs are suffering ongoing injuries as a result of FHFA's expropriation of the Companies' resources and private shareholders' rights and its continuing efforts to adopt housing-finance policies that disadvantage the Companies and their shareholders. These ongoing injuries are being visited upon Plaintiffs as a result of both decisions by FHFA as conservator and decisions by FHFA as regulator.

82. To remedy the violation of the President's constitutional removal authority alleged in this Count, the Court should: (1) vacate the third amendment to the PSPAs; and (2) declare that henceforth FHFA is no longer an independent agency and strike down the provisions of HERA that purport to make FHFA independent from the President, including 12 U.S.C. §§ 4511(a), 4512(b)(2), and 4617(a)(7).

COUNT II

Violation of the Separation of Powers Against FHFA as Both Regulator and Conservator and Treasury

83. Plaintiffs incorporate by reference the allegations of the preceding paragraphs.

84. Even if it were otherwise constitutional for an independent agency to operate under the leadership of a single individual, this feature of FHFA's structure would still violate the Constitution's structure when combined with other aspects of HERA that further insulate FHFA from oversight by *any* of the three branches of the federal government.

85. In addition to operating without any supervision by the President, FHFA also has no meaningful direction or supervision from Congress. HERA gives FHFA vast power over the Companies and their shareholders, but FHFA has successfully argued for an interpretation of the statute that fails to articulate any overarching policy that FHFA must pursue when it exercises its powers as conservator. HERA also exempts FHFA from the appropriations process by permitting FHFA to self-fund through fees it assesses on the entities it regulates without any oversight from Congress. *See* 12 U.S.C. § 4516(f)(2). Very few independent federal agencies are exempted from the appropriations process,

and FHFA and the CFPB are the only two such agencies headed by a single Director. Exemption from the appropriations process not only diminishes congressional oversight of an independent agency but also reduces the President's influence over the agency since the agency need not seek the President's assistance to obtain funding from Congress.

86. HERA also forbids judicial review of a vast array of actions FHFA takes as regulator or conservator. *See* 12 U.S.C. §§ 4617(b)(2)(A)(i), (b)(5)(E); (b)(11)(D), (f); *id.* § 4623(d). These limitations on judicial review of FHFA's actions are more extensive than those that apply to the CFPB. As a result of the statutory restrictions on judicial review of FHFA's actions, the courts in many circumstances are powerless to ensure that FHFA exercises its authorities in a lawful manner.

87. The purpose of the Constitution's separation of powers is to divide power so as to guard against decisions that diminish the rights of private individuals. The Constitution's structure is also designed to ensure that the organs of the federal government remain accountable to the People. Yet FHFA is not subject to meaningful direction or oversight by *any* of the three branches of government created by the Constitution. The absence of any check on FHFA's actions by the Executive, Legislative, or Judicial Branches makes FHFA the least accountable federal agency in our Nation's history and violates the Constitution's structure and the separation of powers.

88. To remedy the violation of the Constitution alleged in this Count, the Court should: (1) vacate the third amendment to the PSPAs; and (2) declare that henceforth FHFA is no longer an independent agency and strike down the provisions of

HERA that make FHFA unaccountable to any of the three Branches of the federal government.

COUNT III

Violation of the Appointments Clause
Against FHFA as Conservator and Treasury

89. Plaintiffs incorporate by reference the allegations of the preceding paragraphs.

90. The Appointments Clause provides that the President "shall nominate, and by and with the Advice and Consent of the Senate, shall appoint" all principal officers of the United States. U.S CONST. art. II, § 2, cl. 2. The Appointments Clause permits Congress to "vest the Appointment of such *inferior* Officers, as they think proper, in the President alone, in the Courts of Law, or in the Heads of Departments." *Id.* (emphasis added). However, *principal* officers may only assume office by being nominated by the President and confirmed by the Senate.

91. As the head of an independent federal agency, the Director of FHFA is a principal officer of the United States under the Appointments Clause. Accordingly, this office may only be filled by someone who is nominated by the President and confirmed by the Senate.

92. When there is a vacancy in a position that must be filled by a principal officer, the Constitution permits an inferior officer to *temporarily* assume the responsibilities of the position in an acting capacity. However, the Appointments Clause limits the period during which someone who has not been nominated by the President and confirmed by the Senate may serve as an acting principal officer.

93. By the time Mr. DeMarco approved the Net Worth Sweep, he had been FHFA's acting Director for three years. This exceeded the period that was reasonable under the circumstances.

94. Furthermore, it is impossible for someone to serve as a principal officer without Senate confirmation as a recess appointee for more than two years. This shows that it is *per se* unreasonable and unconstitutional for someone to serve as an acting principal officer for more than that length of time.

95. In addition, although Congress may by statute provide that, in the event of a vacancy, the occupant of a specific inferior office will by operation of law become an acting principal officer, the Constitution does not permit the President to *appoint* an acting principal officer. For the same reason, a principal officer may not appoint his acting successor by selecting from among multiple inferior officers. President Obama chose Mr. DeMarco from among three possible candidates to serve as FHFA's acting Director. For this reason as well, Mr. DeMarco's appointment was unconstitutional.

96. To remedy the violation of the Appointments Clause alleged in this Count, the Court should vacate the third amendment to the PSPAs.

COUNT IV

Violation of the Nondelegation Doctrine
Against FHFA as Conservator and Treasury

97. Plaintiffs incorporate by reference the allegations of the preceding paragraphs.

98. Article I, Section 1 of the Constitution vests "[a]ll legislative Powers herein granted . . . in a Congress of the United States." This text permits no delegation of

legislative powers from Congress to any other organ of government. Under the nondelegation doctrine, Congress impermissibly delegates legislative power when it gives a federal agency discretion without articulating any intelligible principle to guide the agency's exercise of discretion.

99. Although HERA broadly defines the boundaries of FHFA's discretion as conservator by enumerating a list of permissive powers the agency may choose to exercise, under the interpretation of the statute that FHFA has successfully advanced in other litigation, Congress failed to articulate an intelligible principle to guide FHFA's exercise of discretion.

100. Similarly, HERA provides that as conservator FHFA "immediately succeed[s]" to "all rights, titles, powers, and privileges . . . of any stockholder . . . with respect to the regulated entity and the assets of the regulated entity." 12 U.S.C. § 4617(b)(2)(A). Under this provision, during conservatorship FHFA has the exclusive authority to decide whether to exercise most shareholder rights, including the authority to decide whether most shareholder derivative suits may go forward. Under FHFA's interpretation of HERA, nothing in the statute provides an intelligible principle to guide FHFA's discretion in the exercise of shareholder rights during conservatorship.

101. This constitutional flaw is exacerbated by the fact that HERA bars any judicial review that would "restrain or affect the exercise of powers or functions of [FHFA] as a conservator." 12 U.S.C. § 4617(f). By foreclosing judicial review of FHFA's exercise of its conservatorship powers or functions, this provision enables FHFA to take actions that would otherwise violate state and federal law. As a result, under

FHFA's understanding of HERA, so long as FHFA is exercising its broadly defined conservatorship powers, it is free to disregard the fiduciary duties that state law would otherwise impose on the Companies' management, to enter into contracts authorizing other federal agencies to violate federal statutes, and generally to ignore *any* law other than the United States Constitution. That FHFA is able to exercise this extraordinary power without any intelligible principle from Congress to guide its exercise of discretion violates the nondelegation doctrine.

102. FHFA abused its undirected discretion as conservator by imposing the Net Worth Sweep, which visited serious harm on the Companies' private shareholders.

103. To remedy the violation of the nondelegation doctrine alleged in this Count, the Court should vacate the third amendment to the PSPAs.

COUNT V

Violation of the Private Nondelegation Doctrine Against FHFA as Conservator and Treasury

104. Plaintiffs incorporate by reference the allegations of the preceding paragraphs.

105. Plaintiffs allege in the alternative and solely for purposes of this Count that when FHFA acts as conservator it is a private entity and not the federal government.

106. The Vesting Clauses award all Legislative power to Congress, U.S. CONST. art. I, § 1, all Executive power to the President, U.S. CONST. art. II, § 1, cl.1, and all Judicial power to the Supreme Court and any inferior federal courts established by Congress, U.S. COST. art. III, § 1, cl.1. Together, these provisions of the Constitution do not permit *any* delegation of Legislative, Executive, or Judicial power to a private entity.

Indeed, authorizing a private entity to exercise any of the sovereign powers of the federal government constitutes "delegation in its most obnoxious form." *Carter v. Carter Coal Co.*, 298 U.S. 238, 311 (1936).

107. Delegations of Executive power to a private entity are no more permissible than delegations of Legislative power to a private entity. "[I]f Congress could act as effectively without the President as with him" by assigning responsibility for executing the laws to a private entity, it would be able to enhance its own powers at the expense of the President. *See Printz v. United States*, 521 U.S. 898, 923 (1997).

108. Delegations of Vesting Clause power to a private entity are *per se* unconstitutional because they invite the use of the federal government's sovereign powers to further private interests. Far from guarding against such misuses of power, FHFA understands HERA to authorize it to do anything it "determines is in the best interests of . . . [FHFA]" when acting as conservator. 12 U.S.C. § 4617(b)(2)(J)(ii). FHFA has specifically relied on this provision of HERA in defending the Net Worth Sweep, arguing that the harmful consequences for the Companies and their private shareholders do not matter because FHFA was authorized to act in its own best interests.

109. Irrespective of whether FHFA's conservatorship powers are characterized as Legislative or Executive, HERA gives Vesting Clause power to FHFA. As conservator, FHFA has successfully argued that HERA grants it the power to ignore otherwise applicable state and federal law and to authorize violations of federal statutes by third parties. FHFA also has sweeping conservatorship powers over the Companies and their private shareholders—powers that FHFA claims it is free to exercise in a

manner that is harmful to the interests of the Companies and their shareholders. FHFA necessarily exercises either Legislative or Executive power when it: (i) displaces state and federal law; and (ii) makes decisions in a non-fiduciary capacity that are binding on the Companies and their shareholders. FHFA did both of those things when it approved the Net Worth Sweep.

110. To remedy the violation of the Constitution alleged in this Count, the Court should vacate the third amendment to the PSPAs.

PRAYER FOR RELIEF

WHEREFORE, Plaintiffs pray for an order and judgment:

1. Vacating and setting aside the third amendment to the PSPAs, including its provision sweeping all of the Companies' net worth to Treasury every quarter;

2. Enjoining Defendants and their officers, employees, and agents from implementing, applying, or taking any action pursuant to the third amendment to the PSPAs, including its provision sweeping all of the Companies' net worth to Treasury every quarter;

3. Enjoining Treasury and its officers, employees, and agents to return to Fannie and Freddie all dividend payments made pursuant to the Net Worth Sweep or, alternatively, recharacterizing such payments as a pay down of the liquidation preference and a corresponding redemption of Treasury's Government Stock rather than mere dividends;

4. Declaring that FHFA's structure violates the separation of powers, that FHFA may no longer operate as an independent agency, and striking down the provisions

of HERA that purport to make FHFA independent from the President and unaccountable to any of the three Branches of the federal government, including 12 U.S.C. §§ 4511(a), 4512(b)(2), 4617(a)(7), and 4617(f);

5. Awarding Plaintiffs their reasonable costs, including attorneys' fees, incurred in bringing this action; and

6. Granting such other and further relief as this Court deems just and proper.

Dated: August 4, 2017.

BRIGGS AND MORGAN, P.A.

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UNITED STATES DISTRICT COURT
DISTRICT OF MINNESOTA

Case No. 17-cv-02185 (PJS/HB)

ATIF F. BHATTI, TYLER D. WHITNEY, and MICHAEL F. CARMODY,

Plaintiffs,

-vs-

THE FEDERAL HOUSING FINANCE AGENCY, MELVIN L. WATT, in his official capacity as Director of the Federal Housing Finance Agency, and THE DEPARTMENT OF THE TREASURY,

Defendants.

WORD COUNT COMPLIANCE CERTIFICATE

I, Scott G. Knudson, certify that Plaintiff's First Amended Complaint for Declaratory and Injunctive Relief complies with the length limitation of no more than 10,000 words imposed by the Honorable Patrick J. Schiltz in his Briefing Order filed on July 18, 2017 as Document 23.

Plaintiffs' First Amended Complaint has been prepared in size 13 font using Microsoft Word 2010.

Plaintiffs' First Amended Complaint consists of 9,994 words total.

I relied on the word count tool in Microsoft Word 2010, applied specifically to include all text, including headings, footnotes and quotations, to determine the number of words contained in Plaintiffs' First Amended Complaint.

Dated: August 4, 2017.

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