No. 17-20364

In the United States Court of Appeals for the Fifth Circuit

PATRICK J. COLLINS; MARCUS J. LIOTTA;
WILLIAM M. HITCHCOCK,
Plaintiffs-Appellants
v.

STEVEN T. MNUCHIN, SECRETARY, U.S. DEPARTMENT OF TREASURY;
DEPARTMENT OF THE TREASURY; FEDERAL HOUSING FINANCE AGENCY;
MELVIN L. WATT,
Defendants-Appellees

ON APPEAL FROM THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF TEXAS, No. 4:16-cv-03113

REPLY BRIEF OF PLAINTIFFS-APPELLANTS

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CERTIFICATE OF INTERESTED PERSONS

Patrick J. Collins, *et al.* v. *Steven T. Mnuchin*, *et al.*, No. 17-20364

The undersigned counsel of record certifies that the following listed persons and entities as described in the fourth sentence of Rule 28.2.1 have an interest in the outcome of this case. These representations are made in order that the judges of this court may evaluate possible disqualification or recusal.

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Plaintiffs originally named Jacob J. Lew in his official capacity as Secretary of the Treasury as a defendant in this case. Secretary Mnuchin was substituted for Secretary Lew pursuant to Federal Rule of Civil Procedure 25(d). In addition to the named parties listed above, all Fannie Mae and Freddie Mac shareholders have a financial interest in the outcome of this case.

Dated: September 22, 2017

s/ Charles J. Cooper
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INTRODUCTION

A ruling in Defendants' favor would make the Director of FHFA one of the least accountable federal officials in our Nation's history—able to nationalize two massive and highly profitable insurance companies without any oversight by the President, guidance from Congress, or review by the Courts. The separation of powers does not permit an administrative agency to be so wholly insulated from *all three* branches of government, and Congress did not intend to create an agency with unchecked powers when it enacted the Housing and Economic Recovery Act ("HERA"). To the contrary, in HERA Congress merely gave FHFA the same conservatorship and receivership powers that the FDIC and its predecessors had already exercised on hundreds of occasions over the decades without ever doing anything remotely like the Net Worth Sweep. This unprecedented action must be enjoined because it was doubly unlawful: imposed without statutory authorization by an agency that was unconstitutionally insulated from influence by the elected President.

ARGUMENT

I. The Net Worth Sweep Must Be Vacated Because FHFA's Leadership Structure Violates the Separation of Powers.

A. Treasury's Approval of the Net Worth Sweep Does Not Defeat Plaintiffs' Standing.

FHFA is badly mistaken when it argues that Treasury's approval of the Net Worth Sweep deprives Plaintiffs of standing to challenge FHFA's structure. *See*

FHFA Br. 40-41. It is well settled that a plaintiff's standing in a separation of powers case cannot be defeated by speculation about what decision the government might have reached had it followed the procedures the Constitution requires. *Free Enter. Fund v. PCAOB*, 561 U.S. 477, 512 n.12 (2010); *Landry v. FDIC*, 204 F.3d 1125, 1131 (D.C. Cir. 2000); *see also Lujan v. Defenders of Wildlife*, 504 U.S. 555, 572 n.7 (1992). This rule applies with particular force where, as here, the challenged action is the product of negotiations. *Metropolitan Washington Airports Auth. v. Citizens for Abatement of Aircraft Noise, Inc.*, 501 U.S. 252, 264-65 (1991). FHFA says nothing about these precedents and cites no authority for its argument to the contrary.

B. FHFA Is Unconstitutionally Insulated From Presidential Oversight.

Most of FHFA's arguments in defense of its structure were thoroughly and correctly rebutted in Judge Kavanaugh's opinion for the panel in *PHH v. CFPB*, 839 F.3d 1 (D.C. Cir. 2016), but two additional points deserve emphasis.

First, there is a floor beneath which the President's influence over an independent agency headed by a bipartisan, multi-member commission cannot fall; for such commissions, members of the President's party and the President's own appointees are guaranteed to have a voice in the decision-making process. While this minimum degree of Presidential influence may not in all circumstances be constitutionally sufficient, *cf. Meyers v. United States*, 272 U.S. 52, 164 (1926), the

Supreme Court ruled in *Humphrey's Executor v. United States* that it is enough for purposes of an independent agency like the FTC, 295 U.S. 602, 629 (1935).

FHFA's novel structure presents a different question than the one the Supreme Court decided in *Humphrey's Executor* because it eliminates this floor and makes possible something that could never occur with an agency headed by a bipartisan, multi-member commission: someone opposed to the President's policies exercising exclusive and long-term control over a significant component of the Executive Branch. The Oval Office is today occupied by a Republican, but FHFA is run by a Democratic appointee. Acting Director DeMarco, who signed the Third Amendment during the tenure of a Democratic President, attained his position because he was previously made Deputy Director by Republican-appointed FHFA Director James Lockhart. *See* 12 U.S.C. § 4512(f). In both instances, FHFA's structure reduced the incumbent President's influence to a nadir that could never be reached with a multi-member bipartisan commission. It is no answer to say, as FHFA does, that in some *other* situations the President might prefer that an independent agency be led by a single individual. The President must at all times have at least as much influence over an independent agency as was guaranteed with the bipartisan multi-member commission at issue in *Humphrey's Executor*. FHFA's structure reduces Presidential influence beneath this constitutional minimum.

Second, the "most telling indication of the severe constitutional problem with [FHFA] is the lack of historical precedent for this entity." *Free Enter. Fund*, 561 U.S. at 505. FHFA's argument that this history does not matter runs headlong into a long line of Supreme Court separation of powers cases. *See PHH*, 839 F.3d at 21-25. FHFA is also wrong when it argues that the Comptroller of the Currency provides historical support for its structure. The Comptroller does not enjoy for-cause removal protection, *id.* at 20 n.6, and operates "under the general direction of the Secretary of the Treasury," who selects the Comptroller's Deputies, 12 U.S.C. §§ 1, 4. Also unlike FHFA, the Comptroller does not benefit from statutory provisions that insulate him from Congressional and judicial as well as Presidential oversight. *See* Pls. Br. 19-20.[1]

C. Mr. DeMarco's Status as an Acting Director Does Not Affect Plaintiffs' Claims.

When a senior Obama Administration official was asked about the possibility of firing acting Director DeMarco over a policy disagreement, he told reporters "[t]hat is not authority the president has." *See* Rob Blackwell, *HUD Chief: Obama Can't Fire FHFA's DeMarco*, NAT'L MORTGAGE NEWS (Aug. 3, 2012), http://goo.gl/Ql039i. The Obama Administration was correct. HERA says that

[1] FHFA invokes the presumption in favor of constitutionality, FHFA Br. 50, but that presumption does not apply in separation of powers cases. *See NLRB v. New Vista Nursing & Rehab.*, 719 F.3d 203, 240-41 (3d Cir. 2013).

FHFA is an "independent" agency without any hint that its status changes during the tenure of an acting Director, 12 U.S.C. § 4511(a); 44 U.S.C. § 3502(5), and Defendants have never disputed that an acting Director succeeds to the full powers of the Director in all other respects. "The most reliable factor for drawing an inference regarding the President's power of removal . . . is the nature of the function that Congress vested in" the officer in question. *Wiener v. United States*, 357 U.S. 349, 353 (1958). With Congress having vested in the acting Director the very same responsibility for running an independent agency that is otherwise assigned to the Director, the only reasonable inference is that Congress intended for the acting Director to enjoy the Director's removal protections.

That Congress did not think it necessary to repeat in 12 U.S.C. § 4512(f) what it had already said in 12 U.S.C. § 4512(b)(2)—that the Director enjoys "for cause" removal protection—does not support a different conclusion. Section 4512(f) does not comprehensively enumerate the rights and powers of the acting Director because such acting officers are presumed to "succeed[ ] to all the powers of the office" except as otherwise specified. *United States v. Guzek*, 527 F.2d 552, 560 (8th Cir. 1975).

Furthermore, even if the President could have fired Mr. DeMarco without cause, that would not have cured the constitutional defect in the agency's structure. Mr. DeMarco could have only been replaced by one of the agency's other Deputy

Directors—individuals selected by Mr. DeMarco or his Republican-appointed predecessor. *See* 12 U.S.C. § 4512(c)-(f). That prevented the President from using any removal power he had to effect a policy change at the agency. Mike Lillis, *Rep. Frank joins calls for top Fannie, Freddie regulator to be replaced*, THE HILL (Mar. 11, 2012), https://goo.gl/kK9YrF (recounting observation by House Financial Services Committee ranking member that President could not force change in policies at FHFA by firing Mr. DeMarco because FHFA's Deputy Directors "support DeMarco's strategies" and "would likely continue the same" policies).

D. FHFA's Unconstitutional Structure Requires Vacatur of the Net Worth Sweep.

1. As the Department of Justice recently acknowledged in other litigation, a "second proceeding [is] necessary" when an agency official is "unconstitutionally insulated from presidential control at the time of the initial proceeding." Brief of the SEC 37, *Laccetti v. SEC*, No. 16-1368 (D.C. Cir. Mar. 31, 2017). Accordingly, the Net Worth Sweep must be vacated so that it can be reconsidered by FHFA after it is restructured to comply with the separation of powers. *See IBS, Inc. v. Copyright Royalty Board*, 684 F.3d 1332, 1340-42 (D.C. Cir. 2012) (vacating Copyright Board decision "[b]ecause the Board's structure was unconstitutional at the time it issued its determination").

Free Enterprise Fund, 561 U.S. at 509, and *John Doe Co. v. CFPB*, 849 F.3d 1129 (D.C. Cir. 2017),[2] are not to the contrary. The plaintiffs in both cases challenged *ongoing* agency investigations, and vacatur was not needed for the restructured agencies to decide whether to continue investigating. *See FEC v. Legi-Tech, Inc.*, 75 F.3d 704, 708 (D.C. Cir. 1996) (declining to dismiss civil enforcement action first brought by unconstitutionally composed FEC because enforcement action was later ratified by constitutionally restructured agency). The Net Worth Sweep, in contrast, must be vacated before a constitutionally restructured FHFA can reconsider it. FHFA quotes *Free Enterprise Fund* and *John Doe Co.* out of context, but neither supports FHFA's novel theory that removal cases should be treated differently from appointments cases when fashioning a remedy for a violation of the separation of powers.

2. For the first time on appeal, Treasury argues that vacating the Net Worth Sweep while leaving the original PSPAs in place would improperly allow Plaintiffs to "benefit from agency action they now insist is unlawful." Treas. Br. 52-53. But Plaintiffs did not benefit from the original PSPAs. To the contrary, the Complaint alleges that the Companies never needed Treasury's financial support and only drew

[2] In *John Doe*, a D.C. Circuit panel refused to issue an emergency injunction over a well-reasoned dissent. *See* 849 F.3d at 1135-37 (Kavanaugh, J., dissenting). Notably, under very similar circumstances the Ninth Circuit recently issued a stay pending appeal, albeit without explanation. *CFPB v. Future Income Payments, LLC*, 2017 WL 2622774 (9th Cir. June 1, 2017).

on its funding commitment due to erroneous accounting decisions imposed under FHFA's leadership. ROA.26-28, 41-44. To the extent the Court deems it appropriate, Plaintiffs have no objection to vacatur of the PSPAs in their entirety. Furthermore, even if Treasury's argument were not both forfeited and contrary to the allegations in the Complaint, Plaintiffs can hardly be faulted for focusing their constitutional claim on the actions by FHFA that have been most harmful to shareholders.

3. It is impossible to read the Complaint and come away with the conclusion that the Net Worth Sweep was "an action that private fiscal managers typically undertake for the benefit of the financial institutions they oversee." Treas. Br. 50; *see also* FHFA Br. 46 (mislabeling Net Worth Sweep as generic "financing transaction"). To the contrary, the Complaint alleges that Defendants "imposed the Net Worth Sweep to expropriate for the federal government the value of Fannie and Freddie shares held by private investors." ROA.15. Presented with very similar allegations, the Federal Circuit allowed Fifth Amendment takings claims to go forward against the FDIC as receiver in *Slattery v. United States*, 583 F.3d 800, 828 (Fed. Cir. 2009). None of the cases Defendants cite involved a similar expropriation for the benefit of the federal government by a conservator or receiver, and this Court previously refused to attribute a receiver's action to the federal government precisely because the proceeds would "not go to the United States Treasury." *United States v. Beszborn*, 21 F.3d 62, 68 (5th Cir. 1994).

Treasury argues that FHFA's imposition of the Net Worth Sweep is not attributable to the federal government in light of the "historical practice" of appointing private conservators, Treas. Br. 48, but FHFA says in its brief that Plaintiffs' statutory claims fail because "HERA's conservatorship powers 'bear[] no resemblance to the type of conservatorship measures that a private common-law conservator would be able to undertake.'" FHFA Br. 22 (quoting *Perry Capital*, 864 F.3d at 613). Defendants cannot have it both ways. Either Plaintiffs' statutory claims may go forward because FHFA is required to pursue the duties of a common law conservator or the historical treatment of common law conservators is irrelevant to Plaintiffs' constitutional claim.

In all events, Defendants do not dispute that FHFA's actions as regulator are attributable to the federal government or that FHFA exercised its regulatory powers by imposing and overseeing the conservatorships. Defendants protest that the Complaint does not assert claims against FHFA "as regulator," but doing so was unnecessary because the constitutional flaw in FHFA's leadership structure infects all of its decisions as conservator—including the Net Worth Sweep. To the extent the Court disagrees and concludes that this issue is dispositive, it should remand to permit Plaintiffs to amend the Complaint.

II. Plaintiffs May Sue FHFA and Treasury for Violating HERA and the APA.

A. Section 4617(f) Does Not Bar Claims that the Conservator Exceeded Its Statutory Powers and Functions.

Every court to examine the issue has ruled that Section 4617(f) and its FIRREA analogue only apply when the conservator or receiver is "exercising an authorized power or function." *Carney v. RTC*, 19 F.3d 950, 956 (5th Cir. 1994); *see* Pls. Br. 24-25. Thus, FHFA may be enjoined from taking actions that are "beyond the powers granted" to it by statute. *231-300 Joint Venture v. Onion*, 938 F.2d 35, 39 (5th Cir. 1991).

Despite the precedents, FHFA argues that even provisions of HERA that set out the conservator's mandatory duties are not "judicially enforceable." FHFA Br. 20-21, 30. Although it is possible to imagine a statute that would "bar[ ] courts from *policing*" the bounds of FHFA's conservatorship powers, FHFA Br. 30, that is not what Section 4617(f) or its predecessors say or how they have been interpreted. Instead, when FHFA purports to exercise a power it does not have, equitable relief is available because FHFA has failed to "exercise [its] powers or functions . . . as a conservator." 12 U.S.C. § 4617(f); *see Coit Indep. Joint Venture v. Federal Sav. & Loan Ins. Corp.*, 489 U.S. 561, 572-79 (1989).

Citing isolated language from *Ward v. RTC*, 996 F.2d 99 (5th Cir. 1993), Treasury argues that Section 4617(f) permits relief "if at all" only when FHFA's actions as conservator fall "clearly" outside its statutory powers and functions. Treas. Br. 16. But *Ward* simply affirmed that federal courts *do* have the ability to restrain a conservator or receiver acting "clearly outside its statutory powers," 996 F.2d at 102, and it cannot be read to mean that FHFA may exceed its authority under HERA so long as its conduct is not *too obviously* unlawful. *Ward*, at any rate, was nothing like this case. It concerned a plaintiff's attempt to thwart the sale of a single property as part of a larger group sale—an action the Court determined was clearly authorized by statute. *Id.* at 103-04. Here, by contrast, Plaintiffs challenge FHFA's decision to dissipate all of the Companies' net assets and future profits—the very antithesis of FHFA's statutory mission as conservator.

FHFA is wrong when it contends that Section 4617(f) requires the Court to blind itself to the purpose of the conservator's actions when determining whether it has exceeded its powers and functions. FHFA Br. 22-23. As FHFA acknowledges, HERA defines the scope of FHFA's powers in part by reference to the "purpose" of conservatorship and receivership. 12 U.S.C. § 4617(a)(2); *see* FHFA Br. 29. To be clear, the Court need not examine the Net Worth Sweep's purpose to determine that this action exceeded FHFA's powers as conservator; regardless of purpose, "divesting the Companies of their near-entire net worth is plainly antithetical" to FHFA's conservatorship mission. *Perry Capital LLC v. Mnuchin*, 848 F.3d 1072, 1124-25 (D.C. Cir. 2017) (Brown, J., dissenting). Nevertheless, judicial inquiry into the Net Worth Sweep's purpose would be entirely appropriate.

B. FHFA May Not Abandon Its Conservatorship Mission To Preserve and Conserve the Companies' Assets and Restore the Companies to a Sound and Solvent Condition.

1. Like FIRREA, HERA "states explicitly that a conservator only has the power to take actions necessary to restore a financially troubled institution to solvency." *McAllister v. RTC*, 201 F.3d 570, 579 (5th Cir. 2000). FHFA's senior leadership has repeatedly acknowledged that pursuing this rehabilitative statutory mission is mandatory. *See* Pls. Br. 31-32.

FHFA responds that the repeated statements by its senior leadership that contradict its legal position merely "reflect the Conservator's efforts to balance various, potentially competing, high-level goals and priorities set forth by Congress." FHFA Br. 21. FHFA never says what other "goals and priorities" HERA requires it to pursue or how the Net Worth Sweep furthered them, but it makes a telling concession when it acknowledges that the goals specified in 12 U.S.C. § 4617(b)(2)(D)—preserving and conserving assets and restoring the Companies to soundness and solvency—are among those it is required by statute to balance. This understanding of Section 4617(b)(2)(D) cannot be reconciled with the *Perry Capital* majority's conclusion that the provision's use of the word "may" renders pursuit of the goals it specifies "permissive rather than obligatory." *Perry Capital*, 848 F.3d at 1088.

2. Defendants likewise miss the mark when they invoke FHFA's "[i]ncidental power[ ] . . . as conservator" 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). This provision authorizes FHFA to act in its own interests "as conservator," and FHFA does not advance its conservatorship interests when it permanently dissipates assets it is charged with preserving and conserving and makes it impossible for the Companies to operate in a sound manner. Any other interpretation of the general incidental powers provision would nullify the specific rehabilitative mission assigned to the conservator in Section 4617(b)(2)(D). *See RadLAX Gateway Hotel, LLC v. Amalgamated Bank*, 132 S. Ct. 2065, 2071 (2012) ("It is a commonplace of statutory construction that the specific governs the general."). That the power in Section 4617(b)(2)(J) is labeled "[i]ncidental" further reinforces this conclusion. Confronted with a similarly structured statute in *Brannan v. Stark*, 342 U.S. 451, 463 (1952), the Supreme Court rejected an interpretation of an "incidental" powers provision that would have swallowed much of the rest of the statute: "We do not think it likely that Congress, in fashioning this intricate . . . machinery, would thus hang one of the main gears on the tail pipe."

Defendants' position is also at odds with the longstanding interpretation of materially identical provisions of FIRREA and its predecessors. The Supreme Court has said that when "the FDIC is acting only as a receiver of a failed institution" "it is *not* pursuing the interest of the Federal Government as a bank insurer," *Atherton v. FDIC*, 519 U.S. 213, 225 (1997) (emphasis added), despite FIRREA's similar authorization of the receiver to pursue "the best interests of . . . the [FDIC]," 12 U.S.C. § 1821(d)(2)(J). Indeed, even though the FDIC may consider its own best interests when it acts as conservator, FIRREA elsewhere refers to "the conservator's fiduciary duty to minimize the institution's losses." 12 U.S.C. § 1831f(d)(3). And despite hundreds of federal conservatorships and receiverships that have occurred over the decades, Defendants cannot identify a single instance in which another conservator or receiver has drained its ward's assets for the exclusive benefit of the federal government. That is not surprising, for legislative history makes clear that when Congress first authorized federal receivers to take their own "best interests" into account, it anticipated that they would "give due consideration to the interest of all the claimants upon the assets of the association, including general creditors, uninsured depositors, *and association stockholders*." H.R. Rep. No. 1263, at 10 (1968) (emphasis added).

Defendants' interpretation of Section 4617(b)(2)(J) would also mean that the imposition of conservatorship itself nullifies the economic rights of shareholders, thus exposing the federal government to takings liability. Congress plainly did not intend for the federal government to pay just compensation every time a financial institution is placed into conservatorship, and constitutional avoidance strongly counsels against that result. *See American Cont'l Corp. v. United States*, 22 Cl. Ct. 692, 698 (1991) (FIRREA receivership was not a taking because incidental powers provision does not "sanction arbitrary action" or nullify receiver's obligation "ultimately to turn all remaining proceeds over to . . . shareholders after making payments to depositors, creditors, and other claimants and after paying expenses").

3. Defendants' interpretation of HERA would also leave FHFA with no intelligible principle to guide its exercise of discretion when it acts as conservator, thus rendering the statute unconstitutional under the nondelegation doctrine. Pls. Br. 36-37. Under Defendants' interpretation, neither FHFA's power to "carry on the business of the [Companies]" pursuant to their charters nor its power to pursue the Companies' "best interests" provides the necessary intelligible principle because these are powers that FHFA "may" but is not required to exercise. *See* 12 U.S.C. § 4617(b)(2)(D), (b)(2)(J).

Defendants also emphasize that it has been many years since the Supreme Court struck down a statute under the nondelegation doctrine. But that is because under the cannon of constitutional avoidance courts strive to interpret statutes in a manner that *avoids* a nondelegation issue. *See Mistretta v. United States*, 488 U.S.

361, 373 n.7 (1989). The Supreme Court took that approach in *Fahey v. Malonee*, 332 U.S. 245, 250-53 (1947), and FHFA admits that it is arguing for conservatorship powers that go far beyond those of the conservator in that case, FHFA Br. 22 n.4.

4. An essential part of FHFA's conservatorship "mission[ ]" is "to carry on the business of the institution[s]" under its care, *RTC v. CedarMinn Bldg. Ltd. P'ship*, 956 F.2d 1446, 1453 (8th Cir. 1992), and FHFA may not do the opposite by winding up the Companies without first placing them into receivership. FHFA's contrary interpretation of HERA is based almost entirely on 12 U.S.C. § 4617(a)(2), which gives FHFA's Director discretion to appoint the agency as "conservator or receiver for the purpose of reorganizing, rehabilitating, or winding up the affairs of [the] regulated entity." The *Perry Capital* dissent explained why FHFA's reading of this provision is wrong: "Between the conservator and receiver roles, FHFA surely has the power to accomplish each of the enumerated functions; nonetheless, a conservator can no more 'wind[ ] up' a company than a receiver can 'rehabilitat[e]' it." *Perry Capital*, 848 F.3d at 1119 n.2 (Brown, J., dissenting).

Recognizing that a necessary implication of its position is that as receiver it may "rehabilitate" the Companies, FHFA seeks support for that conclusion in provisions of HERA that instruct the receiver to establish a "limited-life regulated entity." FHFA Br. 27 (citing 12 U.S.C. § 4617(i)(2)(A)). But as its name suggests, this receivership entity has a limited life; a provision of HERA that FHFA ignores requires the receiver to "wind up the affairs" of the entity within five years. 12 U.S.C. § 4617(i)(6). Indeed, the limited time within which FHFA is required to *complete* "wind up" of the entity shows that HERA uses this term as a synonym for "liquidate."

Treasury attacks a straw man when it declares that a "premise" of Plaintiffs' position is that FHFA must "return the enterprises to the same state that existed prior to the conservatorship." Treas. Br. 21. To say that FHFA is required as conservator to seek to "preserve and conserve" the Companies' assets and restore them to a "sound and solvent condition" is not to deny the discretion FHFA enjoys when pursuing those ends. 12 U.S.C. § 4617(b)(2)(D). And if FHFA deems it appropriate to wind up the Companies, it has that authority as well—so long as it lawfully places the Companies into receivership and follows the procedures HERA specifies for distributing the Companies' assets. Whatever the scope of FHFA's authority to change the Companies' business model during conservatorship, this authority does not encompass the power to permanently dissipate assets the conservator is charged with preserving and conserving.

5. Treasury is wrong when it argues that a 2016 appropriations rider ratified the Net Worth Sweep. Treas. Br. 20. When interpreting a federal statute, the actions of subsequent Congresses have "little probative value because a post-enactment legislative body has no special insight regarding the intent of a past legislative body."

Laborers' Local 265 Pension Fund v. iShares Tr., 769 F.3d 399, 409 (6th Cir. 2014); *see also Solid Waste Agency of N. Cook Cty. v. United States Army Corps of Eng'rs*, 531 U.S. 159, 169 (2001) (emphasizing need for "extreme care" before crediting arguments that Congress acquiesced in an agency's decision by failing to overturn it). And here, the statute the subsequent Congress enacted says nothing about the validity of the Net Worth Sweep. Notably, several Senators—including Senator Corker, the driving force behind this provision—expressly stated that the Act "does not prejudice" Plaintiffs' claims or "have any effect on the court cases . . . challenging the validity of the [Net Worth Sweep]." 161 CONG. REC. S8857 (daily ed. Dec. 18, 2015) (statement of Sen. Brown); *see* 161 CONG. REC. S8760 (daily ed. Dec. 17, 2015) (statement of Sen. Corker).

C. The Net Worth Sweep Is a Permanent Abandonment of FHFA's Conservatorship Mission.

Defendants cannot deny that but for the Net Worth Sweep the Companies would today have $130 billion in additional capital to absorb any future losses, and they openly acknowledged when they announced the Net Worth Sweep that it was a step toward winding up the Companies. *See* Pls. Br. 38-40. Indeed, since the Net Worth Sweep went into effect, FHFA has described the Companies as "effectively balance sheet insolvent" and "a textbook illustration of financial instability." Defs. Mot. to Dismiss 19, *Samuels v. FHFA*, No. 13-cv-22399 (S.D. Fla. Dec. 6, 2013), ECF No. 38. Permanently dissipating the Companies' assets and income and requiring them to operate with no capital is the opposite of "preserv[ing] and conserv[ing]" their assets and rehabilitating them to soundness and solvency. *See* 12 U.S.C. § 4617(b)(2)(D).

Defendants nevertheless attempt to reconcile the Net Worth Sweep with FHFA's conservatorship mission. As the following examples illustrate, Defendants' arguments directly contradict allegations in the Complaint, which must be taken as true at this stage of the litigation:

Defendants' Assertion	**Complaint's Allegation**
"The enterprises were on the precipice of failure in 2008 . . . ." Treas. Br. 22.	"Neither Company was in danger of insolvency" in 2008, and both were able "to easily pay their debts and retained billions of dollars of capital that could be used to cover any future losses." ROA.26.
"By late 2008, the Enterprises' liabilities exceeded their assets under GAAP; Treasury thus began infusing billions of dollars into the Enterprises." FHFA Br. 8.	"[T]he 'losses' Fannie and Freddie experienced under conservatorship were driven primarily by temporary and unrealistically pessimistic accounting decisions" made under FHFA's supervision, and "throughout the conservatorship they have had more than enough cash reserves and operational revenues to cover their expenses." ROA.45.
"In 2013 and 2014, . . . the enterprises' net worth was substantially higher than expected." Treas. Br. 11.	"[T]he Agencies knew that the Net Worth Sweep would result in [a] massive financial windfall for the federal government." ROA.67.
The Companies "anticipated that they would not be able to pay their 10% dividends to Treasury without drawing on Treasury's funding commitment in the future." Treas. Br. 10.	When the Net Worth Sweep was announced, Defendants "fully understood that the Companies were on the precipice of generating huge profits,

	far in excess of the dividends owed" under the prior arrangement. ROA.15.
The Net Worth Sweep "relieved the enterprises of their obligation to pay a fixed 10% cash dividend to Treasury." Treas. Br. 27.	The Companies "never were required to pay a cash dividend to Treasury but rather had the discretion to pay dividends in kind." ROA.36.
Prior to the Net Worth Sweep, dividend payments "threatened to erode Treasury's unused funding commitment." Treas. Br. 26.	"[T]here was never any risk that payment of dividends would render the Companies insolvent," ROA.36, and in August 2012 the risk that the Companies would exhaust Treasury's funding commitment "was at its lowest point since the start of the conservatorships," ROA.55.
The Net Worth Sweep " 'ensures continued access to vital capital,' *Perry Capital*, 848 F.3d at 1091, and has been crucial to preserving the GSEs' financial stability and solvency." Treas. Br. 26.	"[T]he Net Worth Sweep's reduction and eventual elimination of the Companies' capital reserves *increases* the likelihood" that the Companies will need money from Treasury. ROA.68.

D. Section 4617(f) Does Not Apply When Treasury Violates Its Own Obligations Under HERA and the APA.

Unilaterally amending the PSPAs is not among FHFA's powers or functions. FHFA was powerless to impose the Net Worth Sweep without Treasury's consent, and insisting that Treasury comply with its own independent legal obligations under HERA and the APA before consenting does not restrain or affect FHFA's exercise of its powers. Pls. Br. 45-48.

Treasury does not deny that under its broader reading of Section 4617(f), FHFA could suspend the application of *any* statute to *any* federal agency by entering into a contract requiring the other agency to violate the law. Given the presumption in favor of judicial review of administrative action, Congress should not be lightly understood to have authorized suspensions of its laws through "agreements" between executive agencies. Furthermore, the result that Treasury urges is especially anomalous because Plaintiffs allege that Treasury violated HERA. Section 4617(f) does not apply when FHFA violates HERA, and Treasury cannot explain why it should enjoy broader protection from judicial review than the conservator itself.

Dittmer Props., L.P. v. FDIC, 708 F.3d 1011 (8th Cir. 2013), and the other FIRREA cases cited by Treasury do not support a different conclusion. *See* Treas. Br. 28-29. In none of those cases was the "third party" another federal agency subject to the presumption in favor of judicial review, and none of the cases involved a claim that the third party had violated a provision of federal law unrelated to the conduct of the receivership. Just as this Court previously declined to extend the analogous provision of FIRREA to bar judicial review of claims against the FDIC in its corporate capacity, it should likewise hold that Section 4617(f) does not apply to Treasury. *See Sierra Club v. FDIC*, 992 F.2d 545, 548-51 (5th Cir. 1993).

III. HERA's Succession Clause Does Not Bar Plaintiffs' Claims.

A. The Succession Clause Applies Only to Derivative Claims, and Plaintiffs' Claims Are Direct.

"No federal court has read" Section 4617(b)(2)(A) or the analogous provision of FIRREA to transfer *direct*—as opposed to derivative—shareholder claims to the conservator or receiver. *Levin v. Miller*, 763 F.3d 667, 672 (7th Cir. 2014). As the

Perry Capital court explained, to do so would be contrary to the statute's plain meaning, which terminates shareholder rights "against the assets or charter of the regulated entity" only during receivership. *Perry Capital*, 848 F.3d at 1105 (quoting 12 U.S.C. § 4617(b)(2)(K)(i)). Numerous other appellate courts have likewise held that shareholders may pursue direct claims during conservatorship or receivership. *See Barnes v. Harris*, 783 F.3d 1185, 1193, 1195 (10th Cir. 2015); *In re Beach First Nat'l Bancshares, Inc.*, 702 F.3d 772, 778, 780 (4th Cir. 2012); *Lubin v. Skow*, 382 F. App'x 866, 870-71 (11th Cir. 2010).

Whether a shareholder is asserting claims "with respect to" the Companies within the meaning of Section 4617(b)(2)(A) is thus a question of federal law that depends on application of the shareholder standing rule. Congress has the power to relax that rule, and it did so when it directed the courts to take an especially generous approach to deciding who may sue in APA cases. Pls. Br. 49-50; *FAIC Sec., Inc. v. United States*, 768 F.2d 352, 357 (D.C. Cir. 1985). The APA gives Plaintiffs a direct, personal interest in this case because they are within the zone of interests protected by HERA. No more is required for Plaintiffs to sue directly.

Treasury responds by declaring that this argument "fundamentally misunderstands the distinction between direct and derivative suits," Treas. Br. 36, but the only cases it cites in rebuttal concern shareholder standing under RICO. These cases are very far afield because, while the APA relaxes the usual standards for determining who may sue, RICO imposes *heightened* requirements. *See Liquidation Comm'n of Banco Intercontinental, SA v. Renta*, 530 F.3d 1339, 1350 n.14 (11th Cir. 2008); *Motorola Credit Corp. v. Uzan*, 388 F.3d 39, 58 (2d Cir. 2004).

Furthermore, even if state law were relevant, Plaintiffs' APA claims would still be direct without regard to the test set out in *Tooley v. Donaldson, Lufkin & Jenrette, Inc.*, 845 A.2d 1031, 1033 (Del. 2004). Where, as here, the substantive law that provides the plaintiffs' cause of action also gives the plaintiffs a direct interest in the claim, the plaintiffs' claim is direct without regard to *Tooley*. *Citigroup Inc. v. AHW Inv. P'ship*, 140 A.3d 1125, 1138 (Del. 2016); *NAF Holdings, LLC v. Li & Fung (Trading) Ltd.*, 118 A.3d 175, 180 (Del. 2015). Treasury argues that these cases show only that a court has "no need to apply the *Tooley* test where a plaintiff's claim is self-evidently direct," Treas. Br. 33 n.9, but that is not correct. In *Citigroup*, it was not "self-evident" whether the plaintiffs' claims were derivative under *Tooley* and its progeny, and that is why the Second Circuit certified the question to the Delaware Supreme Court. The Delaware Supreme Court responded that *Tooley* was "not relevant" because "under the laws governing those claims . . . the claims belong to the stockholder." *Citigroup*, 140 A.3d at 1126-27.

Plaintiffs' claims are also direct under *Tooley*. Far from being "dependent on an injury to the corporation," *Tooley*, 845 A.2d at 1036, Plaintiffs were harmed by the transfer of their economic rights to Treasury even if one assumes—contrary to the allegations in the Complaint—that this action somehow helped the Companies. Treasury's corporate overpayment cases, including *Starr International Co. v. United States*, 856 F.3d 953, 965-66 (Fed. Cir. 2017), and *El Paso Pipeline GP Co. v. Brinckerhoff*, 152 A.3d 1248, 1259 (Del. 2016), are not to the contrary. None of Treasury's cases concerned the transfer of *all* minority shareholder economic rights to a single, majority shareholder. *See In re Medtronic, Inc.*, 2017 WL 3496401, at *7 (Minn. Aug. 16, 2017) (claim was direct where shareholder alleged "loss of certain rightful incidents of his ownership interest" "rather than a simple loss of economic value"). Minority shareholders were directly and uniquely harmed by the expropriation of their rights, and an order restoring those rights would benefit Plaintiffs directly without regard to its effect on Fannie and Freddie.

B. The Succession Clause Does Not Apply When FHFA Is Conflicted and Would be Unconstitutional if Used To Nullify Constitutional Rights.

Irrespective of whether Plaintiffs' claims are direct or derivative, HERA's Succession Clause does not bar these claims in light of FHFA's manifest conflict of interest.

1. Defendants argue for the first time on appeal that the Succession Clause bars not only Plaintiffs' statutory claims but also their constitutional claim. This argument was not pressed or passed upon in the district court and is therefore

forfeited. *LeMaire v. Louisiana Dep't of Transp. & Dev.*, 480 F.3d 383, 387 (5th Cir. 2007).

In any event, Defendants' acknowledgement that their interpretation of the Succession Clause would effectively nullify the Companies' constitutional rights by making FHFA the successor to constitutional claims *against itself* provides a powerful additional reason to reject the Defendants' position. Congress may not use its power to regulate federal jurisdiction "to deprive a party of a right created by the Constitution," *Bartlett v. Bowen*, 816 F.2d 695, 705 (D.C. Cir. 1987), but that is what Defendants' interpretation of the Succession Clause would do since no court could hear a case in which FHFA sued itself for violating the Constitution, *see United States v. ICC*, 337 U.S. 426, 430 (1949). Neither does due process permit Congress to pass a law requiring the Companies to accept FHFA, a government agency, as their representative in pursuing claims against itself. *Cf. Richards v. Jefferson Cty.*, 517 U.S. 793, 802 (1996); *Phillips Petroleum Co. v. Shutts*, 472 U.S. 797, 812 (1985). The Supreme Court has repeatedly read statutes "to avoid the 'serious constitutional question' that would arise if a federal statute were construed to deny any judicial forum for a colorable constitutional claim," *Webster v. Doe*, 486 U.S. 592, 603 (1988), and for similar reasons this Court should follow the Federal and Ninth Circuits in concluding that shareholder derivative suits may go forward when the conservator is conflicted.

2. Defendants' efforts to distinguish *First Hartford Corp. Pension Plan & Trust v. United States*, 194 F.3d 1279, 1283 (Fed. Cir. 1999), and *Delta Savings Bank v. United States*, 265 F.3d 1017, 1024 (9th Cir. 2001), are unpersuasive. FHFA notes that both cases involved receiverships, FHFA Br. 35, but the same rule should also apply to conservatorships. Unlike the appointment of a receiver, the appointment of a conservator does not "terminate" shareholder claims and relegate them to a statutory claims process. *See* 12 U.S.C. § 4617(b)(2)(K)(i). And without the protections of this statutory claims process, there is an even greater need for a conflict-of-interest exception to protect the interests of shareholders during conservatorship.

Treasury argues that *First Hartford* and *Delta Savings* only apply where a derivative claim concerns conduct that occurred prior to the conservatorship or receivership. Treas. Br. 44. But neither court's analysis turned on when or how the alleged misconduct occurred, but rather focused on the conflict faced by the receiver when determining whether to bring suit. *First Hartford*, 194 F.3d at 1295; *Delta Savings*, 265 F.3d at 1023-24.

3. Treasury argues that issue preclusion forecloses Plaintiffs' interpretation of the Succession Clause because the D.C. Circuit rejected it in *Perry Capital*, but a prior judgment that other plaintiffs *lacked the capacity* to sue on behalf of the Companies cannot bind the Companies or shareholders who were not parties to the

prior suit. *See* WRIGHT & MILLER, FEDERAL PRACTICE & PROCEDURE § 1840 (a judgment "that is not on the merits but that relates to the representative's capacity to bring the suit . . . will not bar other stockholders from bringing a derivative action"). To be sure, there is a division of authority over this question in the demand futility context. *Compare In re Wal-Mart Stores, Inc. Del. Derivative Litig.*, 2017 WL 3138201 (Del. Ch. July 25, 2017), *with In re Sonus Networks*, 499 F.3d 47, 64 (1st Cir. 2007). But the Supreme Court has held, partly for due process reasons, that where a putative class action is dismissed prior to certification, issue preclusion cannot bar an absent class member from relitigating the same issues in a subsequent suit. *Smith v. Bayer Corp.*, 564 U.S. 299, 314-18 (2011). In the same way here, due process does not permit the Companies and their absent shareholders to be bound by the *Perry Capital* court's ruling that the plaintiffs in that case could not sue on the Companies' behalf.

CONCLUSION

The district court's judgment should be reversed.

Date: September 22, 2017

Respectfully submitted,

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CERTIFICATE OF COMPLIANCE

Pursuant to FED. R. APP. P. 32(g), I certify the following:

This brief complies with the type-volume limitation of Rule 32(a)(7)(B) of the Federal Rules of Appellate Procedure because this brief contains 6,491 words, excluding the parts of the brief exempted by Rule 32(f) of the Federal Rules of Appellate Procedure.

This brief complies with the typeface requirements of Rule 32(a)(5) of the Federal Rules of Appellate Procedure and the type style requirements of Rule 32(a)(6) of the Federal Rules of Appellate Procedure because this brief has been prepared in a proportionately spaced typeface using the 2016 version of Microsoft Word in 14-point Times New Roman font.

Dated: September 22, 2017

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CERTIFICATE OF SERVICE

I hereby certify that I electronically filed the foregoing with the Clerk of Court for the United States Court of Appeals for the Fifth Circuit on September 22, 2017 by using the appellate CM/ECF system. I certify that service will be accomplished on September 22, 2017 by the appellate CM/ECF system on the following:

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