No. 17-578

In the Supreme Court of the United States

JOSEPH CACCIAPALLE, et al.,

Petitioners,

v.

THE FEDERAL HOUSING FINANCE AGENCY, et al.,

Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit

REPLY BRIEF FOR PETITIONERS

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REPLY BRIEF FOR PETITIONERS

Two circuits have recognized that shareholders of an entity under federal conservatorship or receivership maintain the right to pursue derivative litigation on behalf of that entity where the federal conservator or receiver would face a "manifest conflict of interest" in pursuing the claim itself. *First Hartford Corp. Pension Plan & Tr. v. United States*, 194 F.3d 1279, 1294-95 (Fed. Cir. 1999); *Delta Savings Bank v. United States*, 265 F.3d 1017, 1021-24 (9th Cir. 2001).

This case fits within this rule. Petitioners are Fannie Mae and Freddie Mac shareholders who filed derivative litigation challenging the transfer of these Companies' entire net worth to a single controlling shareholder. The complaints named as defendants the Companies' federal conservator, the Federal Housing Finance Agency ("FHFA"), who executed this transfer, and the U.S. Department of the Treasury, the controlling shareholder who has reaped (and continues to reap) enormous benefits from it. Since FHFA faces a manifest conflict of interest as to both parties, under *First Hartford* and *Delta Savings*, Petitioners would be permitted to proceed on their derivative claims.

But instead these claims have been cut short. In its opinion below, the D.C. Circuit squarely rejected the rule adopted by its sister circuits, and became the first court of appeals to hold that a federal conservatorship or receivership completely extinguishes shareholders'

right to pursue derivative litigation "even where [the federal conservator or receiver] will not bring a derivative suit due to a conflict of interest."[1] App. 64a.

In this Court, Respondents chose to file a single Opposition – covering this Petition and two others (Nos. 17-580 & 17-591). This brief is designed to bury the circuit split, which is not addressed until its final pages. Br. for the Fed. Resp'ts in Opp. ("Opp.") 31-33. When Respondents finally get around to it, they flatly assert that there is no split here because *First Hartford* and *Delta Savings* addressed a "different statute."[2] Opp. 32.

But this facile distinction cannot withstand scrutiny. As the D.C. Circuit, other courts, and Respondents themselves have each recognized, Congress intended the two nearly identical provisions at issue to "have the same meaning in both statutes."

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[1] The D.C. Circuit remains the only circuit to take this position. Contrary to Respondents' suggestion (Opp. 17), the Sixth Circuit did not follow the D.C. Circuit on the Succession Clause issue. *Robinson v. FHFA*, 876 F.3d 220, 228 n.6 (6th Cir. 2017).

[2] Moreover, by grouping all Petitioners together in a single brief as "GSE shareholders" (Opp. 10), Respondents may also hope to suggest that Petitioners are all sophisticated, well-financed investors, unworthy of this Court's sympathy or time. These factors are obviously irrelevant and should have no bearing on this case. In any event, such a suggestion would be inaccurate. Petitioners represent a putative class that includes tens of thousands of ordinary Americans, many of whom purchased shares in the Companies as a sound and secure investment for retirement.

Smith v. City of Jackson, Miss., 544 U.S. 228, 233 (2005) (plurality opinion). Thus, as the dissenting judge recognized below, the D.C. Circuit's opinion will sow uncertainty regarding the proper construction of *both* the Housing and Economic Recovery Act ("HERA") *and* the Financial Institutions Reform, Recovery, and Enforcement Act ("FIRREA"). *See* App. 111a (Brown, J., dissenting) (explaining that the court's construction of HERA was applicable to FIRREA "by extension"). The legal issues presented in this Petition therefore have far-reaching consequences for the nation's financial system and are not limited to a "unique" or "singular" set of circumstances. *Cf.* Opp. 35. The Court should grant certiorari to resolve this confusion.

I. THE CIRCUITS ARE IN CONFLICT AS TO WHETHER SHAREHOLDERS MAY PURSUE DERIVATIVE CLAIMS ON BEHALF OF ENTITIES UNDER FEDERAL CONSERVATORSHIP OR RECEIVERSHIP WHERE THE CONSERVATOR OR RECEIVER FACES A MANIFEST CONFLICT OF INTEREST.

"There is an apparent circuit split as to whether a statutory succession clause * * * carries with it an implicit conflict-of-interest exception." *Saxton v. FHFA*, 245 F. Supp. 3d 1063, 1079 (N.D. Iowa 2017). The Federal and Ninth circuits both recognize that shareholders maintain the right to bring derivative claims on behalf of an entity under federal conservatorship or receivership where the federal conservator or receiver would face a "manifest conflict of interest" in considering whether to pursue the

claims. *First Hartford,* 194 F.3d at 1294-95; *Delta Savings*, 265 F.3d at 1023-24. The D.C. Circuit has now held the opposite. App. 64a. Petitioners asked this Court to intervene to resolve this conflict among the circuits.

A. The Succession Clauses Of FIRREA And HERA Require A Uniform Interpretation.

It is true that *First Hartford* and *Delta Savings* construed a provision of the FIRREA, Pub. L. No. 101-73, § 212(a), 103 Stat. 183, 225-26 (1989), *codified at* 12 U.S.C. § 1821(d)(2)(A), while the D.C. Circuit construed a provision of HERA, Pub. L. No. 110-289, § 1145(a), 122 Stat. 2654, 2737 (2008), *codified at* 12 U.S.C. § 4617(b)(2)(a). But "when Congress uses the same language in two statutes having similar purposes * * *, it is appropriate to presume that Congress intended that text to have the same meaning in both statutes." *Smith*, 544 U.S. at 233; *see also Northcross v. Bd. Of Ed. Of Memphis City Schs.,* 412 U.S. 427, 428 (1973) (per curiam) (holding that the "similarity of language" in two statutes is "a strong indication that [they] should be interpreted *pari passu*.").

Here, the two provisions are "nearly identical." App. 63a; *accord* App. 151a ("substantially similar"); *Kellmer v. Raines*, 674 F.3d 848, 850 (D.C. Cir. 2012) ("virtually identical"); *In re Fed. Home Loan Mortg. Corp. Derivative Litig.*, 643 F. Supp. 2d 790, 795-96 (E.D. Va. 2009) ("substantially identical"), *aff'd sub nom. La. Mun. Police Emps. Ret. Sys. v. FHFA,* 434 F. App'x 188, 191 (4th Cir. 2011); *see also* Mot. to Dismiss by FHFA 59 (D.D.C. Jan. 17, 2014) ("nearly identical").

This similarity is no accident; Congress modeled HERA's Succession Clause on the one in FIRREA. App. 93a-97a; Congressional Research Service, RL34657, *Financial Institution Insolvency* 1, 3, 19-20 (Apr. 30, 2009). Congress therefore presumably intended the two provisions to "have the same meaning in both statutes." *Smith*, 544 U.S. at 233.

And, as this analysis suggests, Courts have uniformly understood the two provisions as requiring one interpretation. The D.C. Circuit's own construction of HERA's Succession Clause on other issues relied heavily on cases addressing FIRREA's "nearly identical" provision. App. 57a, 61a-62a, 74a-75a. Other courts interpreting HERA's Succession Clause have similarly relied on prior judicial constructions of its twin provision in FIRREA. *La. Mun. Police*, 434 F. App'x 188 (affirming as "well-reasoned" the district court's opinion which "relied on case law interpreting [FIRREA's] * * * similar provisions transferring stockholders' 'rights, titles, powers, and privileges' to federal bank receivers and conservators"); *Kellmer*, 674 F.3d at 850-51; *Esther Sadowsky Testamentary Tr. v. Syron*, 639 F. Supp. 2d 347, 350 (S.D.N.Y. 2009).

In fact, Respondents themselves have relied on cases construing FIRREA's Succession Clause in support of their own proposed interpretation of HERA's identical provision. *See* Final Br. for Treasury 21 (D.C. Cir. Mar. 4, 2016); Treasury's Reply Br. 20 (D.D.C. May 5, 2014); Mot. to Dismiss by FHFA 37-38, 49 n.29, 59 (D.D.C. Jan. 17, 2014).

B. The D.C. Circuit Squarely Rejected The Holdings Of Its Sister Circuits.

The D.C. Circuit's complete analysis of the conflict of interest exception is as follows:

> The class plaintiffs argue that because, as shareholders, they retain rights in the Companies during a conservatorship, the Succession Clause should be read to permit them to sue derivatively to protect those rights when the FHFA has a conflict of interest. They point to the decisions of two other circuits interpreting 12 U.S.C. § 1821(d)(2)(A), a nearly identical provision in FIRREA, to permit such an exception. *See First Hartford* * * *; *Delta Sav.* * ** . Contrary to the class plaintiffs' assertions, two circuit court decisions do not so clearly "settle[] the meaning of [the] existing statutory provision" in FIRREA that we must conclude the Congress intended sub silentio to incorporate those rulings into the Recovery Act. *Merrill Lynch v. Dabit*, 547 U.S. 71, 85 (2006).
>
> Nor are we convinced by the reasoning of those two cases that the Succession Clause implicitly excepts derivative suits where the FHFA would have a conflict of interest. The courts in those cases thought it would be irrational to transfer to an agency the right to sue itself

> derivatively because "the very object of the derivative suit mechanism is to permit shareholders to file suit on behalf of a corporation when the managers or directors of the corporation, perhaps due to a conflict of interest, are unable or unwilling to do so." *First Hartford*, 194 F.3d at 1295; *see also Delta Sav.*, 265 F.3d at 1022-23 (extending the exception to suits against certain agencies with which the conservator or receiver has an "interdependent" relationship and "managerial and operational overlap"). As the district court in this case noted, however, it makes little sense to base an exception to the rule against derivative suits in the Succession Clause "on the purpose of the 'derivative suit mechanism,'" rather than the plain statutory text to the contrary. *See Perry Capital LLC*, 70 F. Supp. 3d at 230-31. We therefore conclude the Succession Clause does not permit shareholders to bring derivative suits on behalf of the Companies even where the FHFA will not bring a derivative suit due to a conflict of interest.

App. 63a-64a. Thus, the court directly rejected the reasoning of *First Hartford* and *Delta Savings* on their own terms; it did not assert that those cases should be disregarded because they address FIRREA's Succession Clause instead of its HERA analogue.

Finding that these cases were "wrongly decided" – and not merely inapposite – is precisely what Respondents had asked the D.C. Circuit to do. *See* Final Br. of FHFA 49 (D.C. Cir. Mar. 7, 2016). Respondents have even acknowledged that the D.C. Circuit rejected *First Hartford* and *Delta Savings* as "contradicting ***FIRREA's*** plain language." Br. of FHFA 57, *Roberts v. FHFA,* No. 17-1880 (7th Cir. Aug. 7, 2017) (emphasis added); Br. of FHFA 52, *Saxton v. FHFA*, No. 17-1727 (8th Cir. Jun. 27, 2017).[3]

The D.C. Circuit's holding that *First Hartford* and *Delta Savings* were wrong creates an unmistakable split among the courts of appeals. The D.C. Circuit did not deny that the two Succession Clauses should receive a single unified interpretation; it disagreed about what that interpretation should be. Indeed, the court characterized "those two cases" as holding that the Succession Clause permits derivative suits "where ***the FHFA*** would have a conflict of interest." App. 64a (emphasis added). Under this logic, if the D.C. Circuit had agreed that the Federal and Ninth Circuits had correctly construed FIRREA, it would have applied the same rule.

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[3] The district court followed the same course, rejecting the reasoning of *First Hartford* and *Delta Savings* on their own terms rather than distinguishing them on factual or legal grounds. App. 153a-154a; *see also* Final Br. of FHFA 49 (D.C. Cir. Mar. 7, 2016) (confirming that the district court held that *First Hartford* and *Delta Savings* were "wrongly decided").

Many other courts have similarly recognized that the two Succession Clauses should be treated the same. For example, numerous courts have applied the *First Hartford* and *Delta Savings* rule in the HERA context. Pet. 22-23 (collecting cases). Tellingly, Respondents do not identify a single HERA case rejecting the application of *First Hartford* and *Delta Savings* based on the fact that those cases addressed a "different statute."

C. Petitioners' Claims Fit Within The Conflict Of Interest Exception Recognized By *First Hartford* And *Delta Savings*.

Respondents also contend that *First Hartford* and *Delta Savings* involved distinct factual circumstances. Opp. 32-33. But none of Respondents' fact issues justify allowing this circuit split to remain unresolved.

For instance, Respondents argue that the conflict of interest exception is unavailable for derivative claims against the conservator or receiver itself, such as Petitioner's derivative claims against FHFA. Opp. 33. But a conservator or receiver, like any other entity, faces a manifest conflict of interest in suing itself – and, indeed, is constitutionally prohibited from doing so. *United States v. ICC*, 337 U.S. 426, 430 (1949) ("no person may sue himself"). Further, Respondents' view flies in the face of *First Hartford*, which applied the conflict of interest exception where "a government contractor with a putative claim of breach by a federal agency is being operated by that very same federal agency." 194 F.3d at 1295; *see also* App. 64a (characterizing *First Hartford* as holding that it would

be "irrational" to transfer to an agency the "right to sue itself").

Similarly, Respondents suggest that allowing derivative claims based on conduct *during* the conservatorship or receivership would be inconsistent with 12 U.S.C. § 4617(f). Opp. 32-33. But this ignores the fact that, as construed by the D.C. Circuit, § 4617(f) does not bar "judicial review through cognizable actions for damages." App. 38a.

Finally, Respondents' assertion that FHFA and Treasury are not truly "interdependent" (Opp. 33) is unconvincing for many reasons, not least of which is the fact that the two parties are represented by the same counsel before this Court.

II. THE COURT OF APPEALS' DECISION IS INCORRECT.

As shown in the Petition, the D.C. Circuit's interpretation cannot be squared with the text and structure of HERA or Congress's ratification of the manifest conflict of interest exception. Pet. 24-27. The decision also raises serious – but avoidable – constitutional questions, and violates common law principles expressly incorporated into HERA. Pet. 28-32.

Respondents attempt to defend the D.C. Circuit's decision. But none of their arguments are correct or justify leaving a circuit split unresolved.

For example, Respondents contend that the D.C. Circuit's opinion is consistent with HERA's "plain language." Opp. 26. But they do not explain how FHFA

can "succeed" to rights that it cannot legally exercise under the Constitution's "Case or Controversy" standard (because FHFA cannot sue itself) (Pet. 24), or how the D.C. Circuit's reading can be squared with HERA's distinction between the *transfer* of rights and their *termination* (Pet. 24-25).

Respondents do not deny that Congress drafted HERA's Succession Clause by copying from FIRREA, and yet they maintain that Congress nevertheless did not intend to incorporate the uncontested and longstanding judicial interpretations of the old provision into the new one. Opp. 27. But when "Congress adopts a new law incorporating sections of a prior law, Congress normally can be presumed to have had knowledge of the interpretation given to the incorporated law" and to have "adopte[d] that interpretation." *Lorillard v. Pons*, 434 U.S. 575, 580-81 (1978).

Respondents' ratification cases are inapposite. *Brown v. Gardner*, 513 U.S. 115, 121 (1994) rejected a ratification argument based on an administrative agency's interpretation, and *Jama v. ICE*, 543 U.S. 335, 351 (2005) rejected one based on an interpretation in a *single* judicial opinion.[4] By contrast, Petitioners' ratification argument is supported by published opinions by the Federal and Ninth Circuits that, for

[4] The Court rejected as irrelevant a second relied-upon judicial opinion because it was "a two-sentence per curiam order" addressing a different issue. *Id.* at 351.

nearly a decade before Congress imported FIRREA's language into HERA, were the sole and uncontested interpretations of the FIRREA provision at issue.[5]

Moreover, *First Hartford* was a seminal decision that helped launch dozens of cases claiming billions of dollars. Those cases were part of the *Winstar*-related litigation that spanned more than two decades, and led to billions of dollars in recoveries from the federal government. Many of those *Winstar* claims were brought derivatively based on the Federal Circuit's decision in *First Hartford*. Congress was necessarily aware of this when it enacted HERA in 2008, and chose to adopt precisely the same language that FIRREA used and that *First Hartford* and *Delta Savings* held must include a manifest conflict of interest exception.

Nor do Respondents provide real answers to the constitutional questions posed by the D.C. Circuit's opinion. For example, Respondents claim that stripping shareholders of derivative claims does not implicate the Fifth Amendment because such a claims "belong[] to the corporation, not to the shareholders." Opp. 28. But both Delaware and Virginia recognize that derivative litigation is a "right" belonging to shareholders. *E.g.*, *Stone ex rel. AmSouth Bancorporation v. Ritter*, 911 A.2d 362, 366 (Del. 2006)

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[5] Lower courts had reached the same conclusion even earlier. *Branch v. FDIC,* 825 F. Supp. 384, 404-05 (D. Mass. 1993); *Suess v. United States*, 33 Fed. Cl. 89, 97 (1995).

(discussing "the right of a stockholder to prosecute a derivative suit"); *Richelieu v. Kirby*, 48 Va. Cir. 260 (1999) (discussing "[t]he right to bring a derivative suit").

Finally, under the D.C. Circuit's interpretation, HERA preempts certain state law claims for breach of fiduciary duties. Pet. 30. Respondents assert that this raises no "meaningful" federalism concerns because "federal preemption of state tort law is a well-established feature of our constitutional system." Opp. 28. But courts are required to "assume[] that the historic police powers of the States were not to be superseded by the Federal Act unless that was the clear and manifest purpose of Congress," and must favor a "narrow interpretation" of federal statutes that minimizes intrusion into areas of traditional State authority. *CTS Corp. v. Waldburger*, 134 S. Ct. 2175, 2188-89 (2014) (citations and quotations omitted). Respondents' reliance on *Riegel v. Medtronic, Inc.*, 552 U.S. 312 (2008) is misplaced because that case involved "an express pre-emption provision." *Id.* at 316, 330 (discussing 21 U.S.C. § 360k(a)). HERA's Succession Clause is not covered by any such provision.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted,

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January 30, 2018

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