IN THE UNITED STATES DISTRICT COURT
FOR THE EASTERN DISTRICT OF PENNSYLVANIA

WAZEE STREET OPPORTUNITIES FUND IV LP, *et al.*,

Plaintiffs,

v.

THE FEDERAL HOUSING FINANCE AGENCY, *et al.*,

Defendants.

Civil Action No. 2:18-cv-3478-NIQA

MEMORANDUM IN OPPOSITION TO PLAINTIFFS' MOTION FOR SUMMARY JUDGMENT AND IN SUPPORT OF TREASURY'S MOTION TO DISMISS

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INTRODUCTION

In 2012, the Department of the Treasury ("Treasury") and the Federal Housing Finance Agency ("FHFA"), acting as conservator for Fannie Mae and Freddie Mac (collectively, the "GSEs" or the "enterprises"), amended the Preferred Stock Purchase Agreements between Treasury and FHFA (the "Third Amendment"). For years, GSE shareholders have engaged in near constant litigation directly attacking the Third Amendment. Unable to obtain their desired relief – an injunction invalidating the Third Amendment – the shareholders have changed course and attacked the Third Amendment indirectly through collateral challenges to FHFA's structure and authority. Like the first round of attacks, which have been uniformly rejected by the courts to have addressed them – including the Third Circuit, *see Jacobs v. FHFA*, 908 F.3d 884 (3d Cir. 2018) – this action should be dismissed.

Try as Plaintiffs might to argue otherwise, they assert quintessentially derivative claims, alleging that the Third Amendment has harmed the GSEs and seeking relief – invalidation of the Third Amendment – that would require transfer of funds to the GSEs. These derivative claims properly belong to the GSEs and the Housing and Economic Recovery Act's ("HERA") transfer-of-shareholder-rights provision (also referred to as the "shareholder succession provision") prevents Plaintiffs from asserting the rights of the corporation in this action.

Even if Plaintiffs' claims are not barred by HERA, their claims provide no basis for invalidating the Third Amendment. FHFA executed that agreement in its capacity as conservator for the GSEs and thus did not exercise governmental power. The separation-of-powers concerns raised by restrictions on the removal of persons exercising significant governmental authority do not apply where, as here, a government-appointed conservator steps into the shoes of private entities. Moreover, HERA's "for-cause" removal provision did not actually apply to Edward

DeMarco, FHFA's Acting Director at the time of the Third Amendment. And, finally, even if Plaintiffs were correct, the result would not be to turn back the clock more than six years and selectively vacate only the Third Amendment among the many acts FHFA has taken as conservator – with all the disruptive effects such remedial action would entail.

The fact that FHFA executed the Third Amendment in its capacity as conservator similarly dooms Plaintiffs' Appointments Clause claim. But even were that not the case, the argument fails on its merits. The Supreme Court has never suggested that the Constitution imposes a specified and judicially enforceable time limit on the service of a person exercising duties in an acting capacity, rendering inquiry into whether DeMarco's tenure as an Acting Director was "too long" non-justiciable. And in any event, the length of DeMarco's service was reasonable. Plaintiffs, moreover, offer nothing to rebut the argument that they waited too long – nearly six years – to bring this claim and that, given the development of significant reliance interests, equitable doctrines should bar this claim.

Plaintiffs' non-delegation claims also fail in light of the fact that FHFA, as conservator, does not exercise governmental authority. And contrary to Plaintiffs' contention, HERA, with its extensive delineation of FHFA's authority as conservator, is not the first statute in more than eighty years to fail to provide the requisite intelligible principle to guide FHFA's discretion.

Finally, and even more fundamentally, Plaintiffs' claims against Treasury fail because they simply do not allege that Treasury is liable on the causes of action asserted in the Complaint. Accordingly, this case can be resolved (and dismissed) on the Complaint. Should the Court decide this case on the basis of Plaintiffs' summary judgment papers, the result is the same. Nothing in those papers provides any basis for invalidating the Third Amendment, and Treasury is entitled to

judgment as a matter of law.[1]

ARGUMENT

I. PLAINTIFFS' CLAIMS ARE BARRED BY HERA'S TRANSFER-OF-SHAREHOLDER-RIGHTS PROVISION

As explained in Treasury's motion to dismiss brief, Mem. in Supp. of Treasury Mot. to Dismiss at 8-13, ECF No. 15-1 ("Treasury MTD"), Plaintiffs' claims, which are derivative in nature, are barred by HERA's transfer-of-shareholder-rights provision, 12 U.S.C. § 4617(b)(2)(A)(i). In opposition, Plaintiffs argue that their claims are direct as a matter of federal law because treating them otherwise would "frustrate" the "federal policy underlying Plaintiffs' constitutional claims." Mem. in Supp. of Pls.' Mot. for Summ. J. & in Opp'n to Defs.' Mot. to Dismiss at 33, ECF Nos. 18 & 19-1 ("Pls.' Mem."). But both federal law and applicable Delaware law have long "distinguish[ed] between derivative and direct actions." *Starr Int'l Co. v. United States*, 856 F.3d 953, 966 (Fed. Cir. 2017). Federal common law – which presumptively incorporates state law on issues, like this one, that "affect[] the allocation of governing power within the corporation," *Kamen v. Kemper Fin. Servs., Inc.*, 500 U.S. 90, 100 (1991) – recognizes that whether a plaintiff's federal claim is direct or derivative turns on the nature of the plaintiff's harm and the relief sought. Thus, if Plaintiffs are only indirectly affected, as a result of harm to the GSEs, by the alleged constitutional violations, and seek relief that accrues to the GSEs, their

[1] Plaintiffs filed a "statement of material facts" with their summary judgment motion. *See* ECF Nos. 18-1 & 19-3. No provision of either the Federal Rules of Civil Procedure or this Court's Local Rules authorize or require either that such a statement be filed or that the opposing party respond to such a statement. In any event, the parties' motions present purely legal issues related to the structure of FHFA, and many of the "material facts" that Plaintiffs reference are irrelevant to the resolution of those legal issues. *See, e.g.*, ECF No. 18-1 ¶ 25 (characterizing a Treasury press release describing the Third Amendment). Accordingly, Treasury is not filing herewith a response to Plaintiffs' statement of facts. Treasury can, of course, provide such a response should the Court deem it necessary.

claims are derivative. *See Starr Int'l Co.*, 856 F.3d at 966 ("Only 'shareholder[s] with a direct, personal interest in a cause of action,' rather than 'injuries [that] are entirely derivative of their ownership interests' in a corporation, can bring actions directly." (citation omitted)); *In re Kaplan*, 143 F.3d 807, 811-12 (3d Cir. 1998) (Alito, J.) ("The derivative injury rule holds that a shareholder . . . may not sue for personal injuries that result directly from injuries to the corporation.").

Plaintiffs' opposition brief provides no support for setting aside these well-established principles. Instead, Plaintiffs, attempting to draw an analogy to the doctrine of third-party standing, argue that the Court should relax its standing analysis because "if Plaintiffs cannot bring this suit, then no one can." Pls.' Mem. at 33. This argument, however, misses the mark. As discussed below and in Treasury's motion to dismiss, Plaintiffs assert claims based on harm suffered, in the first instance, by the GSEs. By definition, these are derivative claims that belong to the GSEs. Enforcing traditional limitations on shareholders' ability to assert such derivative claims does not prevent Plaintiffs (or anyone else) from suing to remedy direct, personal harm resulting from the constitutional violations that Plaintiffs allege here. Indeed, it is fully consistent with the rule that "[a] stockholder of a corporation does not acquire standing to maintain an action in his own right, as a shareholder, when the alleged injury is inflicted upon the corporation." *Kauffman v. Dreyfus Fund, Inc.*, 434 F.2d 727, 732 (3d Cir. 1970); *see also Potthoff v. Morin*, 245 F.3d 710, 716 (8th Cir. 2001) ("actions to enforce corporate rights or redress injuries to the corporation cannot be maintained by a stockholder in his own name.") (citation omitted). If a party could allege *direct* injury as a result of FHFA's actions, it could bring a suit challenging FHFA's alleged constitutional violations. *See Cty. of Sonoma v. FHFA*, 710 F.3d 987 (9th Cir. 2013); *Leon Cty. v. FHFA*, 700 F.3d 1273 (11th Cir. 2012). Because Plaintiffs cannot do so, their claims are appropriately treated as derivative and dismissed under HERA's shareholder succession provision.

See Burke v. Ford, Civ. A. No. 92-5811, 1993 WL 483585, at *1 (E.D. Pa. Nov. 17, 1993) (applying shareholder standing rule to dismiss due process and equal protection claims where "the corporation . . . suffered the harm alleged in the complaint").

Plaintiffs also contend that applying the shareholder succession provision here would "violate the Due Process Clause" to the extent that such application would "require the [GSEs] and their stockholders to accept FHFA as their exclusive representative to pursue claims alleging that FHFA itself is unconstitutional." Pls.' Mem. at 32. But even if it were the case that completely precluding the GSEs from bringing a constitutional challenge to FHFA's structure would implicate the GSEs' due process rights, HERA did not do so. One of its provisions, 12 U.S.C. § 4617(a)(5), permits challenges to the appointment of FHFA as conservator within a limited time frame. A scheme funneling constitutional claims in this manner satisfies due process. *See, e.g.*, *Yakus v. United States*, 321 U.S. 414, 435 (1944) (concluding that a statutory scheme that channeled all challenges, including constitutional challenges, to wartime price regulations into an administrative process with a sixty-day filing deadline did not violate due process). Plaintiffs cite no authority for the proposition that the GSEs, much less GSE shareholders on the GSEs' behalf, possess a free-floating due-process right to bring a challenge to FHFA's structure in connection with FHFA's actions as conservator at the time of their choosing.

Unable to establish that their claims are direct as a matter of federal law, Plaintiffs turn to state law, attempting to fit the round peg of their claims into the *Tooley* test's square hole. Plaintiffs assert that their claims are direct because the Third Amendment allegedly altered the value of their shares in relation to Treasury's, arguing that their economic rights as shareholders were "wrongfully expropriated." Pls.' Mem. at 35-36. But such claims for equity dilution are generally treated as derivative, *see, e.g.*, *Feldman v. Cutaia*, 956 A.2d 644, 655 (Del. Ch. 2007), and

Delaware law only allows a shareholder to bring a direct claim based on the diversion of share value from one shareholder to another in the narrow circumstance where:

> (1) a stockholder having majority or effective control causes the corporation to issue 'excessive' shares of its stock in exchange for assets of the controlling stockholder that have a lesser value; and (2) the exchange causes an increase in the percentage of the outstanding shares owned by the controlling shareholder, and a corresponding decrease in the share percentage owned by the public (minority) shareholders.

El Paso Pipeline GP Co. v. Brinckerhoff, 152 A.3d 1248, 1263 (Del. 2016) (quoting *Gentile v. Rossette*, 906 A.2d 91, 100 (Del. 2006)). Absent allegations that a controlling shareholder extracted voting power from minority shareholders, and received an "exclusive benefit of increased equity ownership and voting power," *Feldman*, 956 A.2d at 657, the "expropriation" of "solely economic value" does not inflict direct injury. *El Paso Pipeline*, 152 A.3d at 1264.

None of these circumstances are present here. Treasury is not a controlling shareholder, the Third Amendment did not involve the issuance of new shares, and Plaintiffs allege no injury to their voting power. Accordingly, Plaintiffs' economic dilution claims are derivative. *See Roberts v. FHFA*, 889 F.3d 397, 409 (7th Cir. 2018) (shareholder claims that Third Amendment was the result of "mismanagement" and resulted in the "depletion of corporate assets through overpayment" were "classic derivative claims," and thus barred by the shareholder succession provision); *Saxton v. FHFA*, 245 F. Supp. 3d 1063, 1072 (N.D. Iowa 2017) (allegations that Third Amendment expropriated the value of shares in the GSEs did not state direct claim "absent additional allegations that [the shareholders'] voting rights have been diluted").[2] In arguing that

[2] In addition to a footnote in an unpublished, non-controlling Delaware Chancery Court opinion addressing a shareholder's right to compel inspection of corporate books and records, Plaintiffs cite a Ninth Circuit decision that, in the end, concluded that claims for "injury to [the corporation] itself, which ultimately reduced the value of the stock," were derivative. *See Pareto v. FDIC*, 139 F.3d 696, 699 (9th Cir. 1998) (cited in Pls.' Mem. at 34). Neither case supports Plaintiffs' contention that their claims asserting purely economic harm in diluted share value are direct.

the Third Amendment has impacted their "rights to dividends and liquidation distributions," Pls.' Mem. at 35 – *i.e.*, decreased the economic value of Plaintiffs' GSE shares – Plaintiffs assert no injury and claim no entitlement to relief that would not accrue to the GSEs in the first instance.

Finally, Plaintiffs attempt to avoid the shareholder succession provision's clear command by emphasizing that they have Article III standing to bring this action. *See* Pls.' Mem. at 37. This point is irrelevant. Defendants do not dispute that Plaintiffs would be injured, for constitutional standing purposes, by the equity dilution and decline in share value they allege the Third Amendment imposes. But, as explained above, those injuries are derivative, and where shareholders suffer harm only as a result of injuries experienced by the corporation in which they hold equity, the claims to remedy that harm properly belong to the corporation. Indeed, although codified in HERA, shareholder standing is typically a prudential rule, recognizing that although a shareholder might suffer a concrete injury through her ownership in corporate shares, the shareholder is nevertheless "generally prohibit[ed] . . . from initiating actions to enforce the rights of the corporation." *Franchise Tax Bd. of Cal. v. Alcan Aluminum Ltd.*, 493 U.S. 331, 336 (1990). The shareholder succession provision thus bars Plaintiffs' claims whether or not Plaintiffs are able to establish Article III standing.

II. HERA'S FOR-CAUSE REMOVAL PROVISION DOES NOT REQUIRE THAT THE THIRD AMENDMENT BE SET ASIDE

A. FHFA's Execution of the Third Amendment Does Not Implicate the Separation of Powers

As discussed above, application of the shareholder succession provision can resolve this case without further inquiry. But even if the Court were to consider Plaintiffs' merits arguments, they provide no basis to set aside the Third Amendment. Plaintiffs contend, relying on the now-vacated panel decision in *Collins* and *Freytag v. Commissioner*, 501 U.S. 868 (1991), that it is

immaterial whether FHFA was exercising executive power when it adopted the Third Amendment because the removal restriction is a structural violation that the separation of powers, as a "prophylactic device," is designed to remedy. Pls.' Mem. at 14 (citation omitted). But *Freytag* is inapposite. There, the Supreme Court considered whether special trial judges of the Tax Court were inferior officers or mere employees, and it simply rejected the proposition that the special trial judges were "inferior officers for purposes of some of their duties . . . , but mere employees with respect to other responsibilities." 501 U.S. at 882. In other words, for Appointments Clause purposes, when individuals are exercising governmental authority in *all* their duties, they cannot be officers when performing some governmental functions and mere employees when performing other governmental functions. *Freytag*'s reasoning has no application here, because FHFA as conservator is exercising no executive authority. Indeed, the distinction between the two entities – FHFA-regulator and FHFA-conservator – is made plain by the fact that when Congress created FHFA and its Director in 2008, the Director acted only as regulator; it was not until the enterprises were placed in conservatorship that FHFA became conservator, as well.

Plaintiffs fare no better in their various contentions that FHFA was in fact exercising executive power even when acting as conservator. For example, Plaintiffs argue that FHFA's agreement to the Third Amendment was not the act of a private party because the agreement "expropriate[s] property in furtherance of federal interests." Pls.' Mem. at 15. The agreement, however, involved an action that private fiscal managers typically undertake for the benefit of the financial institutions they oversee – the renegotiation of an institution's financial obligations to its most significant investor. As the Third Circuit has recognized, the "Third Amendment is in essence a renegotiation of an existing lending agreement," which is a "traditional power of corporate officers or directors" that FHFA, as conservator, inherited. *Jacobs*, 908 F.3d at 890.

Plaintiffs counter that *Jacobs* actually supports their position because, in upholding the Third Amendment against a direct challenge to its lawfulness, the Third Circuit found that HERA grants FHFA powers beyond those available to a traditional common-law conservator. *See* Pls.' Mem. at 14-15. But the mere fact that FHFA was acting pursuant to authorities granted to it under federal law does not make its actions governmental, let alone executive, in nature. *See, e.g.*, *Flagg Bros., Inc. v. Brooks*, 436 U.S. 149, 164-66 (1978) (a private actor's actions are not "properly attributable" to the government simply because a statute "has authorized" those actions). And of course, Congress can authorize private parties to take actions that they would otherwise be unable to take under state law, *see In re Fosamax Prods. Liability Litig.*, 852 F.3d 268, 282 (3d Cir. 2017) (noting general proposition that federal rules preempt state requirements when a private party cannot comply with both) without transforming those private acts into government acts. In holding that the FHFA inherited statutory powers above and beyond the powers it inherited from the GSEs, and that the Third Amendment was consistent with these statutory powers, *Jacobs*, 908 F.3d at 894, the Third Circuit did not undermine the traditional rule that actions taken as a conservator are not governmental acts or suggest that the Third Amendment itself – which, again, the court recognized as a "traditional power of corporate officers or directors," *id*. at 890 – was an exercise of executive power.[3]

Similarly unavailing is Plaintiffs' assertion that the private nature of a conservator's actions is irrelevant because the Third Amendment "was made possible and has been implemented by

[3] Nor does the Federal Circuit's decision in *Slattery v. United States*, 583 F.3d 800, 826-29 (Fed. Cir. 2009) (cited in Pls.' Mem. at 15), counsel a different result. *Slattery* emphasized that the challenged FDIC action—its refusal to turn over the monetary surplus it obtained from a bank liquidation—did not fall within "the standard receivership situation in which the receiver is enforcing the rights or defending claims and paying the bills of the seized bank." *Id.* at 827-28. By contrast, FHFA's negotiation of, and agreement to, the Third Amendment were "quintessential conservatorship tasks." *Perry Capital LLC v. Mnuchin*, 864 F.3d 591, 607 (D.C. Cir. 2017).

FHFA's exercise of its regulatory powers." Pls.' Mem. at 15-16. But the statutory provisions invoked merely authorize FHFA to regulate the enterprises and set forth FHFA's general duties as regulator. *See, e.g.*, 12 U.S.C. § 4511(b)(2) ("The Director shall have general regulatory authority over each regulated entity . . . ."); *id.* § 4513(a)(1)(B)(i)-(ii) (FHFA's Director shall "ensure that . . . each regulated entity operates in a safe and sound manner" and that "the operations and activities of each regulated entity foster liquid, efficient, competitive, and resilient national housing finance markets"). And the regulation Plaintiffs cite, 12 C.F.R. § 1237.12, is contained in a chapter concerning the operations of FHFA as conservator or receiver; it does not convert the quarterly dividend payment from the action of FHFA as conservator (which it indisputably is) into a regulatory act.

In any event, as explained in the motion to dismiss, *see* Treasury MTD at 15-16, the Third Amendment was executed by an FHFA Acting Director who *was* revocable at will, thus defeating Plaintiffs' claim. Because the President could "hold[] his subordinate[] accountable," *Free Enter. Fund v. Pub. Co. Accounting Oversight Bd.*, 561 U.S. 477, 496 (2010), he had the control the Constitution requires over FHFA's adoption of the Third Amendment. In response, Plaintiffs repeat the uncontroversial proposition that FHFA is an independent agency, but do not explain why, contrary to the plain text of the statute, HERA should be read to extend the for-cause removal protection for the FHFA Director to a Deputy Director serving as Acting Director. At the very least, Plaintiffs do not demonstrate that Treasury's reading – which would avoid any doubts about the constitutionality of the statute – is not "fairly possible." *See* Treasury MTD at 16 (quoting *Commc'ns Workers of Am. v. Beck*, 487 U.S. 735, 762 (1988)). Moreover, as explained above, the Third Amendment itself was an action indisputably taken by FHFA in its capacity as conservator. While Plaintiffs contend that the Third Amendment was "sustained, implemented, and defended"

by FHFA's eventual permanent Director, Melvin Watt, Pls.' Mem. at 16, they do not identify any specific act taken by Watt that has injured them beyond the injuries allegedly suffered as a result of DeMarco entering into the Third Amendment.

B. Invalidating the Third Amendment is Not the Proper Remedy for the Separation of Powers Violation Plaintiffs Have Identified

Plaintiffs contend that vacating past decisions is "common practice in separation of powers cases." Pls.' Mem. at 17. While that may be true in some circumstances, the general rule is that "vacatur of past actions is not routine." *John Doe Co. v. CFPB*, 849 F.3d 1129, 1133 (D.C. Cir. 2017). Indeed, in a case raising similar structural challenges as Plaintiffs raise to HERA's for-cause removal provision, the D.C. Circuit recognized "traditional constraints on separation-of-powers remedies" and noted that it is "[o]ften" the case in separation-of-powers cases that "severance of the unconstitutional provision is the chosen remedy." *Id.* To the extent any remedy is appropriate here based on Plaintiffs' Complaint, that remedy should, consistent with this traditional practice, be limited to severing HERA's for-cause removal provision. This is fully consistent with the Supreme Court's guidance that equitable relief "does not follow from success on the merits as a matter of course" but rather is subject to "equitable discretion," *Winter v. NRDC, Inc.*, 555 U.S. 7, 32 (2008), and that any injunctive relief must comport with "what is necessary, what is fair, and what is workable," *North Carolina v. Covington*, 137 S. Ct. 1624, 1625 (2017) (per curiam) (citation omitted).

Traditional equitable principles demonstrate that invalidation of the Third Amendment would be inappropriate here. In the six years since the Third Amendment, a host of individuals and corporations – including the GSEs, their customers, and their lenders – have conducted their affairs in reliance on the Third Amendment, and invalidating that provision would cause a substantial and unwarranted disruption not only in the GSEs' operations, but also in the housing

market generally. The Third Amendment was a "risk-averse" measure that assured the GSEs' ongoing operation, *Jacobs*, 908 F.3d at 893-94, and market participants such as lenders, investors, and others relied on the Third Amendment and the safeguards it placed on the GSEs' financial future in structuring their relationships with the GSEs over the past several years. A judicial order setting aside the Third Amendment now would undo those safeguards, undermine all of the transactions that presumed those safeguards' existence, and potentially cast the market into turmoil. Moreover, as Treasury has pointed out, *see* Treasury MTD at 19 n.4, Plaintiffs' remedial preference would render invalid not only the Third Amendment, but also the original PSPAs between FHFA and Treasury and prior amendments that rescued the GSEs and continue to provide them with hundreds of billions of dollars of funding. *See, e.g. Perry Capital*, 864 F.3d at 601.

All of this despite the fact that, on the other side of the equitable balance, the constitutional violation at issue was quite likely harmless. Plaintiffs speculate otherwise, Pls.' Mem. at 27, but it is highly implausible that HERA's for-cause removal provision had any actual effect on FHFA's decision to enter into the Third Amendment, given that the counter-party was the Treasury Department, headed by a Secretary who was removable at will by the President. Although courts may, upon finding a separation-of-powers violation, vacate *an individual adjudication* without regard to harmless error so that a proper adjudicator can reconsider the case, *see, e.g.*, *Landry v. FDIC*, 204 F.3d 1125, 1130-32 (D.C. Cir. 2000) (cited in Pls.' Mem. at 28), it would be quite another thing for this Court to unwind a complex commercial contract implicating important third-party reliance interest years after the fact even though the alleged structural violation had no demonstrated effect whatsoever on the contract's enactment.

Nonetheless, Plaintiffs assert that the Supreme Court's decision in *Bowsher v. Synar*, 478 U.S. 714 (1986), is "controlling" as to the remedy this case. Pls.' Mem. at 17. Not so. Neither

that case nor any other controlling precedent dictates the invalidation of an agency's past actions whenever the agency was unconstitutionally structured at the time it took those actions. In *Bowsher*, the Court held on the merits that vesting executive functions in an officer (the Comptroller General) whose removal was subject to congressional control was unconstitutional. 478 U.S. at 726, 732. But, as a remedial matter, the Court held that, rather than converting the Comptroller General into an executive officer removable at the President's will, the executive functions (certain reporting and budgetary obligations) should be invalidated, thus triggering a statutory "fallback" provision that provided an alternative budget process if the executive functions were invalidated. *Id*. at 733-35. In short, *Bowsher* is inapposite because the Court was limited to the binary remedial question of whether to sever the removal restriction or the executive functions, as the statute itself resolved the question of whether the past actions should be set aside.

Nor are Plaintiffs correct that the Administrative Procedure Act ("APA") compels their desired remedy. *See* Pls.' Mem. at 18. Even assuming that the conservator's actions constituted "agency action" for purposes of the APA, a court "do[es] not lightly assume that Congress has intended to depart from established principles" regarding equitable discretion, *Weinberger v. Romero-Barcelo*, 456 U.S. 305, 313 (1982), and the APA's general instruction that unlawful agency action "shall" be "set aside," 5 U.S.C. § 706(2), is insufficient to mandate such a departure. *See Hecht Co. v. Bowles*, 321 U.S. 321, 329-30 (1944) (in a decision issued only a few years before the APA was enacted, finding that a statute that provided, upon a specified showing, that an injunction or "other order" "shall be granted" did not strip courts of their traditional discretion to deny relief on equitable grounds). To the contrary, the APA makes clear that, absent a special review statute, "[t]he form of proceeding for judicial review" is simply the traditional "form[s] of legal action," 5 U.S.C. § 703, and that the statutory right of review does not affect "the power or

duty of the court to . . . deny relief on any . . . appropriate legal or equitable ground," *id*. § 702(1). Recognizing this principle, courts finding error under the APA do not uniformly vacate challenged agency action. *See, e.g., Allied-Signal, Inc. v. U.S. Nuclear Regulatory Comm'n*, 988 F.2d 146, 150-51 (D.C. Cir. 1993).

III. THE APPOINTMENTS CLAUSE DOES NOT REQUIRE THAT THE THIRD AMENDMENT BE SET ASIDE

In their Appointments Clause claim, Plaintiffs argue that the Constitution itself requires that any temporary position "becomes permanent after two years." Pls.' Mem. at 20. This is simply not the case. As explained in Treasury's motion to dismiss, *see* Treasury MTD at 20-22, neither the Appointments Clause nor any other constitutional provision places any express limit on the length of time during which an individual may be designated to act as a principal officer. Plaintiffs' only response is to point to the Recess Appointments Clause, where the Constitution itself imposes an effective two-year limitation on any recess appointee. But once again, the Recess Appointments Clause addresses a completely different circumstance than is presented here – to reflexively import its temporal limitation to determine how long an officer can serve in an acting capacity would be an unprecedented step that "finds no support in the Constitution." *Bhatti v. FHFA*, 332 F. Supp. 3d 1206, 1221 (D. Minn. 2018), *appeal filed*, No. 18-2506 (8th Cir. July 16, 2018). Indeed, Plaintiffs have identified no case in which a court has even considered whether the length of time before confirmation of a permanent officer has exceeded any constitutional limitation, let alone any case in which a court actually held that the length of an acting official's tenure actually became unconstitutional (and even less an instance in which a court found the tenure to be unconstitutional based on application of the Recess Appointments Clause).

Eventually, Plaintiffs recognize, as they must, that the Constitution does not answer the question. Plaintiffs attempt to rely on two opinions from the Office of Legal Counsel ("OLC") to

create a standard for this Court to apply in determining whether an acting director's tenure has continued for too long. Pls.' Mem. at 22-23 (relying on Designation of Acting Director of OMB, 2003 WL 24151770, at *1 n.2 (June 12, 2003), and Status of the Acting Director, Office of Management and Budget, 1 Op. O.L.C. 287 (1977)). But the fact that OLC advised an executive agency that the length of service in an acting role should be "reasonable under the circumstances," Status of the Acting Director, Office of Management and Budget, 1 Op. O.L.C. 287, 287 (1977)), hardly provides a sufficient basis for a court to invalidate the tenure of Acting Director DeMarco as constitutionally excessive.

As the court in *Bhatti* recognized in response to an identical argument, the OLC opinion opinions upon which Plaintiffs rely provide no "judicially discoverable or manageable standard" a court could use to determine when an acting director has served too long. *Bhatti*, 332 F. Supp. 3d at 1218; *cf. Baker v. Carr*, 369 U.S. 186, 217 (1962). Determining whether an individual's length of service in an acting role is "reasonable" would require a court to make numerous evaluations of political actions. *See Bhatti*, 332 F. Supp. 3d at 1218 (noting that applying this standard "would require a judge to assess the functioning of the entire Executive Branch and the changing state of the nation (actually, the world) throughout the length of the acting officer's tenure to determine at what point, if ever, the length of the officer's service became unreasonable"). "These assessments are far outside the competency of the judiciary and would require delving into areas – such as 'the President's ability to devote attention to the matter' and his 'desire to appraise the work of an Acting Director' – that are not normally the subject of judicial inquiry." *Id.*

The type of evaluation contemplated by Plaintiffs is thus plainly committed to the political

branches.[4] The President may take such action as he deems necessary in the face of an extended designation as Acting Director, and Congress – which has the greatest equities in the service of an Acting Director who is not Senate-confirmed – may impose statutory time limitations on the length of time an individual may serve in an acting capacity. For example, in the report accompanying the Federal Vacancies Reform Act, S. Rep. No. 105-250 (1998), the Senate Committee on Governmental Affairs noted that "[m]ost" agency-specific statutes "do not place time restrictions on the length of an acting officer," and suggested that Congress might want to "reexamine whether these positions should continue to be filled through the existing procedure." *Id*. at 17.

But even assuming a court may inquire into the reasonableness of an acting officer's tenure, the length of time DeMarco served as Acting Director was reasonable. DeMarco had served as Acting Director for a little more than one year when the President nominated Joseph Smith to be FHFA's Director. *See* Compl. ¶ 65; *see also* 156 Cong. Rec. S7911 (Nov. 15, 2010). After the Senate returned Smith's nomination to the President, DeMarco continued to serve as Acting Director for less than two years before the Third Amendment was signed in August 2012. *See* Compl. ¶ 65. The President then nominated Melvin Watt to be Director in May 2013, the Senate confirmed him, and Mr. Watt was sworn in as FHFA Director on January 6, 2014. *Id*. Thus, during DeMarco's tenure, the President took steps to replace DeMarco with a permanent Director.

[4] Plaintiffs meekly contend that Treasury has waived this argument. *See* Pls.' Mem. at 23 n.9. But Plaintiffs' Complaint did not allege that DeMarco's tenure violated the Appointments Clause because it was unreasonably long or rely on the OLC opinions to fashion a standard; Plaintiffs argued only that it violated the temporal limitation imposed by the Recess Appointments Clause. Treasury, in turn, argued that the Recess Appointments Clause is inapposite and noted that because Plaintiffs offered no other standard for assessing how long is "too long," they presented a non-justiciable political question. *See* Treasury MTD at 22 n.5. Now that Plaintiffs have attempted to offer the OLC opinions as a standard, Treasury appropriately responds herein, and it has not waived its ability to argue that this standard highlights the non-justiciable nature of the question presented.

Moreover, DeMarco signed the Third Amendment less than two years after the President's initial nomination for a permanent Director failed, and given that failure, it is not surprising that it took time to nominate a second candidate who both met the President's qualifications and obtain Senate confirmation. And if Congress looked unfavorably upon the length of time FHFA did not have a Senate-confirmed permanent Director, Congress could have amended HERA to limit the tenure of the Acting Director.[5]

In any event, even if Plaintiffs' Appointments Clause claim was reviewable and meritorious, the proper remedy would not be invalidation of the Third Amendment. This is true for the same reasons, and based on the same "traditional equitable principles," discussed above in relation to Plaintiffs' challenge to HERA's restriction on the President's removal power. *See supra* pp. 11-12. Moreover, as discussed in Treasury's motion to dismiss, equitable doctrines bar Plaintiffs' six-years-later challenge to the Third Amendment. *See* Treasury MTD at 23-24. Plaintiffs offer nothing in response, other than to note that their claims were brought within the applicable limitations period. *See* Pls.' Mem. at 24. But traditional equitable doctrines provide a court flexibility to "protect defendants against unreasonable, prejudicial delay in commencing suit." *In re Bressman*, 874 F.3d 142, 149 (3d Cir. 2017) (citations omitted). It is not the case then, as Plaintiffs argue, that their claim is timely merely because it was brought (barely) within the six-

[5] Plaintiffs opaquely argue that DeMarco's "tenure" violates the Appointments Clause because, although the President appointed him according to the procedure Congress explicitly set forth in HERA, "the President cannot appoint acting principal officers." Pls.' Mem. at 24. To the extent Plaintiffs are attempting to suggest that the President lacks the authority, without Senate confirmation, to direct an individual in an acting capacity to temporarily perform the functions of a principal officer, they are wrong. *See, e.g.*, *United States v. Eaton*, 169 U.S. 331 (1898); *NLRB v. SW General, Inc.*, 137 S. Ct. 929, 934 (2017) (noting that Congress repeatedly has "authoriz[ed] the President to direct certain officials to temporarily carry out the duties of a vacant PAS office [*i.e.*, one requiring Presidential Appointment and Senate confirmation] in an acting capacity, without Senate confirmation").

year statute of limitations, without any further inquiry into the question of whether it would be equitable to grant them the relief they seek. Given the significant disruption that would follow from invalidation of the Third Amendment, and the prejudice this would entail for both the government and third parties, *see supra* pp. 11-12; Treasury MTD at 24, the Third Amendment should not be set aside even if the Court were to find Plaintiffs' Appointments Clause claim meritorious.

IV. PLAINTIFFS' NON-DELEGATION CLAIMS FAIL

As explained above, FHFA entered into the Third Amendment in its capacity as conservator and did not exercise any governmental power – executive or otherwise – in doing so. For those reasons, Plaintiffs' contentions that the Third Amendment represented an unlawful delegation of governmental powers to a private entity should be rejected. *See, e.g.*, *Bhatti*, 332 F. Supp. 3d at 1227 (because "FHFA's actions as a conservator are *not* governmental in nature," "the private non-delegation doctrine is not implicated"). Plaintiffs are left arguing, then, that, for the first time since 1935, *see United States v. Cooper*, 750 F.3d 263, 268 (3d Cir. 2014), Congress has impermissibly delegated its authority without the requisite "intelligible principle." In support, they rely on the dissenting opinion in *Perry Capital* and the fact that HERA uses the word "may" in certain instances to grant FHFA "permissive, discretionary authority," Pls.' Mem. at 26 (quoting *Perry Capital*, 864 F.3d at 607). But the mere fact that Congress gave FHFA broad discretion does not mean that Congress did not provide an intelligible principle to guide the exercise of FHFA's authority. *See Mistretta v. United States*, 488 U.S. 361, 373 (1989) (documenting Supreme Court case law recognizing "Congress' ability to delegate power under broad standards"). *Perry Capital* does not suggest that HERA left FHFA with no guiding principles on how to exercise its statutory authority, and indeed the majority opinion recognized that the statute

"charged FHFA's Director with overseeing the prudential operations of [the GSEs] and ensuring that they operate in a safe and sound manner" – a grant of authority that the court found was furthered by the Third Amendment. *Perry Capital*, 864 F.3d at 599, 607 (citations and internal alterations omitted); *see also Bhatti*, 332 F. Supp. 3d at 1228 (finding that HERA's delineation of the actions FHFA "may" take as conservator to achieve its statutory goal is "more than sufficient to meet the 'intelligible principle' standard").

V. PLAINTIFFS FAIL TO STATE A CLAIM AGAINST TREASURY

Plaintiffs' Complaint alleges that FHFA, in its structure, operations, and legal authority, violates the separation of powers, the Appointments Clause, and non-delegation doctrines. Plaintiffs do not allege that Treasury itself violated these constitutional doctrines or in any respect facilitated FHFA's alleged violations. Because Plaintiffs fail to allege any of the elements of a separation of powers, Appointments Clause, or non-delegation claim against Treasury, Plaintiffs have failed to state a claim against Treasury. In their opposition brief, Plaintiffs emphasize that their Complaint includes various allegations implicating Treasury's behavior in agreeing to the Third Amendment. But to allege that Treasury "is a party to the PSPAs at issue and a central actor in the harm" that Plaintiffs allege to have suffered as a result of the Third Amendment, Pls.' Mem. at 38, is not to allege that Treasury is liable for any of the actual legal claims that Plaintiffs assert. Plaintiffs have not chosen, in this action (as opposed to previously filed suits), to attack the Third Amendment directly or allege that Treasury violated any provision of law in agreeing to it. Manifestly, then, Plaintiffs have not stated a claim against Treasury because they have not alleged that any action by Treasury violated the separation of powers, the Appointments Clause, or the non-delegation doctrines.

Plaintiffs further contend that Treasury is an appropriate party to this case because their

lawsuit challenges a contract to which Treasury is a party and seeks relief that may implicate Treasury. Pls.' Mem. at 39. But Plaintiffs have not sought to join Treasury as a necessary party; they have named it as a defendant and alleged, with respect to each count in the Complaint, that Treasury is liable for a constitutional violation to the same extent as FHFA. Having attempted to state clams for relief against Treasury, Plaintiffs must allege how Treasury is liable. And having failed to do so, Plaintiffs should have their claims against Treasury dismissed.

CONCLUSION

For the foregoing reasons, and those stated in Treasury's brief supporting its motion to dismiss, the Court should grant Treasury's motion to dismiss and deny Plaintiffs' motion for summary judgment.

Dated: February 15, 2019

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that on February 15, 2019, a true and correct copy of the foregoing memorandum was filed electronically and is available for viewing and downloading from the Court's CM/ECF system, which will send notification of such filing to counsel of record in this matter who are registered on the CM/ECF system.

Executed on February 15, 2019.

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