IN THE UNITED STATES COURT OF FEDERAL CLAIMS

ARROWOOD INDEMNITY CO., *et al.*,	)	
Plaintiffs,	)	No. 13-698C
	)	(Chief Judge Sweeney)
v.	)	
THE UNITED STATES,	)	
Defendant.	)	

DEFENDANT'S RESPONSE TO PLAINTIFFS' SUPPLEMENTAL BRIEF

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Defendant, the United States, respectfully submits this response to the supplemental brief filed by plaintiffs, Arrowood Indemnity Co., *et al*. (Pl. Br.). Based on the Court's reasoning in *Fairholme Funds, Inc. v. United States*, No. 13-465C (Fed. Cl. Dec. 6, 2019, reissued Mar. 9, 2020) (Op.), the Court should enter the attached proposed order and dismiss the complaint.

I. The *Fairholme* Decision Requires Dismissal Of The *Arrowood* Complaint

Because the *Arrowood* and *Fairholme* plaintiffs raised the same "direct" taking, illegal exaction, breach-of-fiduciary-duty, and breach-of-implied-contract claims, submitted virtually-identical complaints, and filed the same response to our omnibus motion to dismiss, the Court's dismissal of those claims in *Fairholme* requires dismissal of those claims here.

The *Fairholme* and *Arrowood* plaintiffs both allege that the Third Amendment "nationalized the Companies and [took] all the value of the Companies, thereby depriving the private shareholders of all their economic rights." *Arrowood* 2d Am. Compl. ¶ 10; *Fairholme* 2d Am. Compl. ¶ 10. Both allege that "the quarterly sweep of the Companies' net worth ensures that there never will be sufficient funds for the Companies to pay a dividend to private shareholders. It also ensures that private shareholders will receive nothing in the event of liquidation." *Arrowood* 2d Am. Compl. ¶ 97; *Fairholme* 2d Am. Compl. ¶ 117. And both allege that, as a result of the Third Amendment, Fannie Mae and Freddie Mac (Enterprises) pay far more in dividends than they would have paid under the fixed-dividend arrangement. *Arrowood* 2d Am. Compl. ¶ 106; *Fairholme* 2d Am. Compl. ¶ 126.

Moreover, in response to our omnibus motion to dismiss, the *Arrowood* plaintiffs submitted the same opposition brief as the *Fairholme*, *Cacciapalle*, *Rafter*, *Fisher*, and *Reid* plaintiffs (Omnibus Opposition), and joined in the argument that their complaint asserted "direct" claims against the United States arising from the Third Amendment. *See* Pl. Opp. to

U.S. Mot. to Dismiss at App'x A, ECF No. 49. The Court addressed the factual and legal arguments raised in the Omnibus Opposition in *Fairholme*, and dismissed the "direct" taking and illegal exaction claims for lack of standing because those claims were substantively derivative:

> Plaintiffs focus on the expropriation of the Enterprises' assets via compulsory payments of all profits. The gravamen of each claim is the same: The government, via the PSPA Amendments, compelled the Enterprises to overpay Treasury . . . . Plaintiffs cannot transform their substantively derivative claims into direct claims by merely alleging that, as a result of overpayments, they were deprived of their stockholder rights to receive dividends or liquidation payments. The claims remain derivative because plaintiffs' purported "harms are 'merely the unavoidable result . . . of the reduction in the value of the corporate entity."

Op. at 40 (quoting *Protas v. Cavanagh*, No. CIV. A. 6555-VCG, 2012 WL 1580969, at *6 (Del. Ch. May 4, 2012)). Given that the *Arrowood* and *Fairholme* plaintiffs made the same factual and legal arguments in their response to our omnibus motion to dismiss, and the Court considered those arguments in *Fairholme*, the same reasoning that compelled dismissal of the "direct" taking and illegal exaction claims in *Fairholme* compels dismissal of those claims in *Arrowood.*

II. The *Arrowood* Plaintiffs Identify No Relevant Distinction Between Their Case And *Fairholme* That Warrants Survival Of *Arrowood*'s Taking And Illegal Exaction Claims

In its order lifting the stay, the Court directed the *Arrowood* plaintiffs to explain, with "reference to specific paragraphs in [their] complaint," why their claims should survive our omnibus motion to dismiss when the Court dismissed the same claims in *Fairholme*. Order at 1-2, Mar. 30, 2020, ECF No. 64. The *Arrowood* plaintiffs identify only two differences, neither of which warrants survival of their "direct" taking and illegal exaction claims: (1) the *Arrowood* plaintiffs only seek damages for themselves, while the *Fairholme* plaintiffs seek damages for

themselves and for the Enterprises; and (2) the *Arrowood* plaintiffs all owned Enterprise stock before the Third Amendment, while only one of the *Fairholme* plaintiffs did. Pl. Br. at 2-4.

First, that the *Arrowood* plaintiffs only seek damages for themselves is irrelevant to whether their claims are direct or derivative. The allegations' substance controls whether a claim is direct or derivative, not the plaintiffs' requested relief. *Compare* Pl. Br. at 3-4, *with* Op. at 35 (citing *Starr Int'l Co. v. United States*, 856 F.3d 953, 966-67 (Fed. Cir. 2017)). Nearly all of the substantive allegations underlying the *Arrowood* and *Fairholme* complaints are—word-for-word—the same. *Compare, e.g.*, *Arrowood* 2d Am. Compl. ¶¶ 39-79, 81-86, 88-112, 114-126, 130-35, 139-42, *with Fairholme* 2d Am. Compl. ¶¶ 58-99, 101-06, 108-32, 134-46, 166-71, 193-96. And because the Court already determined in *Fairholme* that those allegations reflected substantively-derivative claims, no basis exists for the Court to reach a different decision here simply because the *Arrowood* plaintiffs only seek damages for themselves.

Second, the *Arrowood* plaintiffs contend that their taking and illegal exaction claims should survive because, unlike most of the *Fairholme* plaintiffs, all of the *Arrowood* plaintiffs owned Enterprise stock before the Third Amendment. Pl. Br. at 3-4. But the timing of plaintiffs' stock purchases has no bearing on whether their claims are direct or derivative. Indeed, the Court already determined that a *Fairholme* plaintiff who, like the *Arrowood* plaintiffs, owned Enterprise stock before the Third Amendment, lacked standing to bring his substantively-derivative claims as direct claims. Op. at 36-41. The *Arrowood* plaintiffs fail to show how application of the Court's reasoning in *Fairholme* would justify a different result in their case.

Finally, the *Arrowood* plaintiffs contend that the Court should reconsider its ruling that *Fairholme*'s "direct" claims were substantively derivative; the *Arrowood* plaintiffs base this

contention on an argument made by the *Owl Creek* plaintiffs—namely, that their claims are "direct" because the Federal Circuit recognized that a shareholder may pursue a direct claim for a portion of a failed bank's liquidation surplus as part of FIRREA's statutory claims process. *See* Pl. Br. at 3, 4 n.3; *Owl Creek* Supp. Br. at 1, 5 (citing *Owl Creek* Opp. to U.S. Mot. to Dismiss at 38; *First Hartford Corp. Pension Plan & Tr. v. United States*, 194 F.3d 1279, 1296 (Fed. Cir. 1999)).

As an initial matter, the Court did not invite plaintiffs to relitigate the motion to dismiss or raise arguments that they had not raised in the past; on the contrary, the Court explicitly cautioned that the opportunity to address the effect of the *Fairholme* opinion "is not an invitation to challenge the legal conclusions reached in [that opinion]." Order at 1 n.2, Mar. 19, 2020, ECF No. 65. Indeed, the entire point of certifying the *Fairholme* decision was to obtain authoritative guidance from the Federal Circuit on the legal issues the Court decided. Thus, it would waste judicial resources for the Court to reconsider rulings that are currently at issue in interlocutory-appeal petitions before the Federal Circuit. In any event, the *Arrowood* plaintiffs' argument for reconsideration is irrelevant. Although HERA, like FIRREA, provides for shareholder participation in the statutory claims process in the event of the Enterprises' liquidation in receivership, HERA provides no analogous right that could support a direct claim when the Enterprises operate in conservatorship.

Simply put, given that the *Arrowood* and *Fairholme* complaints are virtually identical and both sets of plaintiffs advanced the same factual and legal arguments in response to our omnibus motion to dismiss, the *Arrowood* plaintiffs fail to show that the reasoning in *Fairholme* would merit any result other than dismissal of their "direct" taking and illegal exaction claims. Accordingly, the Court should dismiss counts I and II of the complaint.

III. The *Arrowood* Plaintiffs Acknowledge That The Reasoning In The *Fairholme* Decision Warrants Dismissal Of Their Breach-Of-Fiduciary-Duty And Breach-Of-Implied-Contract Claims (Counts III And IV)

The *Arrowood* plaintiffs concede that the Court's analysis of *Fairholme*'s "direct" breach-of-fiduciary-duty and breach-of-implied-contract claims warrants dismissal of *Arrowood*'s analogous claims. Pl. Br. at 5. Accordingly, the Court should dismiss counts III and IV of the complaint.

CONCLUSION

For these reasons, the Court should enter the attached proposed order and dismiss the complaint.

Respectfully submitted,

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PROPOSED ORDER

I. Defendant's motion to dismiss plaintiffs' taking and illegal exaction claims (counts I and II) is GRANTED pursuant to Rule 12(b)(1) because plaintiffs lack standing to pursue those claims. Although plaintiffs purport to bring direct taking and illegal exaction claims, their complaint reflects injuries to Fannie Mae and Freddie Mac (Enterprises), not to plaintiffs, such that those claims are substantively derivative. Because "[a] shareholder lacks standing to litigate nominally direct claims that are substantively derivative in nature," counts I and II are dismissed. *See Fairholme Funds, Inc. v. United States*, No. 13-465C, slip op. at 35, 38-40 (Fed. Cl. Dec. 6, 2019, reissued Mar. 9, 2020).

II. Defendant's motion to dismiss plaintiffs' breach-of-fiduciary-duty claim (count III) is GRANTED pursuant to Rule 12(b)(1) because the Court lacks subject-matter jurisdiction to entertain claims sounding in tort. Accordingly, count III is dismissed. *Id.* at 29-33.

III. Defendant's motion to dismiss plaintiffs' breach-of-implied-contract claim (count IV) is GRANTED pursuant to Rule 12(b)(1) because plaintiffs are not parties to the alleged implied contract and fail to plausibly allege that they are intended third-party beneficiaries of that contract. Accordingly, count IV is dismissed. *Id*. at 33-35.