Nos. 2020-1912, 2020-1914

IN THE UNITED STATES COURT OF APPEALS
FOR THE FEDERAL CIRCUIT

FAIRHOLME FUNDS, INC., ACADIA INSURANCE COMPANY, ADMIRAL INDEMNITY COMPANY, ADMIRAL INSURANCE COMPANY, BERKLEY INSURANCE COMPANY, BERKLEY REGIONAL INSURANCE COMPANY, CAROLINA CASUALTY INSURANCE COMPANY, CONTINENTAL WESTERN INSURANCE COMPANY, MIDWEST EMPLOYERS CASUALTY INSURANCE COMPANY, NAUTILUS INSURANCE COMPANY, PREFERRED EMPLOYERS INSURANCE COMPANY, THE FAIRHOLME FUND, ANDREW T. BARRETT,

Plaintiffs-Appellants,

v.

UNITED STATES,

Defendant-Cross-Appellant.

Appeal Nos. 2020-1912, 2020-1914, on appeal from the Court of Federal Claims in No. 1:13-cv-00465-MMS, Chief Judge Margaret M. Sweeney

CROSS-APPEAL REPLY BRIEF FOR THE UNITED STATES

BRIAN M. BOYNTON
Acting Assistant Attorney General

MARK B. STERN
ABBY C. WRIGHT
GERARD SINZDAK
KYLE T. EDWARDS
Attorneys, Appellate Staff
Civil Division, Room 7235
U.S. Department of Justice
950 Pennsylvania Avenue NW
Washington, DC 20530
(202) 514-1597

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INTRODUCTION AND SUMMARY

Our principal brief explained that when the Federal Housing Finance Agency (FHFA) acts as conservator it is not acting in a governmental capacity and its actions cannot be the basis of a Tucker Act suit against the United States. The brief also explained that implying a conflict-of-interest exception to the Housing and Economic Recovery Act's (HERA) unambiguous transfer of shareholder rights would frustrate Congress's unambiguous intent with respect to the central transactions authorized by the statute.

The Court of Federal Claims erred in ruling to the contrary on both issues, and plaintiffs' response brief makes little effort to defend the court's reasoning as to either holding. With respect to the conservator's governmental status, plaintiffs embark on an extended discussion of principles that demonstrate only that FHFA is a government agency, a point that no one disputes. Plaintiffs' argument ultimately reduces to the contention that since FHFA is a government agency, it remains a government agency even when it steps into the shoes of a private entity. Plaintiffs make only the most cursory attempt to square this argument, which does not turn on any consideration unique to FHFA or HERA, with the array of decisions holding that FHFA, the Federal Deposit Insurance Corporation (FDIC), and other agencies lose their governmental character when they act as receiver or conservator of a private corporation.

Plaintiffs also offer no plausible defense of the Court of Federal Claims' conclusion that this Court's decision in *First Hartford Corp. Pension Plan & Trust v. United States*, 194 F.3d 1279 (Fed. Cir. 1999), dictated that it should read a conflict-of-interest exception into HERA's Succession Clause. Plaintiffs identify nothing in the language, history, or purpose of HERA to support that proposition, and the Court in *First Hartford* stressed that its ruling with respect to the analogous provision in the Financial Institutions Reform, Recovery, and Enforcement Act (FIRREA) permitted shareholders to sue in a "very narrow range of circumstances," *id.* at 1295, circumstances that are entirely absent here. Moreover, in sharp contrast to the circumstances in *First Hartford*, Congress enacted HERA's Succession Clause with full knowledge that, as a centerpiece of the statutory scheme, the conservator, if necessary, would contract with Treasury for the funds necessary to sustain the enterprises. Plaintiffs do not explain how a court could properly nullify the bar on derivative suits with respect to the very transactions authorized by the statute.

Plaintiffs also offer no basis for permitting their implied contract claim to go forward. As discussed in the government's principal brief, the claim rests on a series of wholly conclusory legal assertions and improbable speculation.

ARGUMENT

I. The Facts Relevant to This Appeal Are Not Disputed.

Plaintiffs begin their response brief by criticizing the government for purportedly declining to accept as true the allegations contained in their complaints.

Jt.Reply.Br.6-10. As plaintiffs themselves concede, Jt.Reply.Br.10, even if their criticism were accurate, it would "not matter" to this Court's resolution of the various threshold issues presented in these appeals. For example, plaintiffs identify no factual dispute relevant to determining whether HERA contains an implied conflict-of-interest exception or whether FHFA should be deemed the United States when entering into contracts on behalf of the enterprises as conservator.

The apparent purpose of plaintiffs' extended discussion is not to identify any issue relevant to these appeals but to restate instead their account of the events surrounding the Third Amendment. Even in that regard, none of the facts cited in the government's principal brief regarding the background of the Third Amendment is subject to dispute, as the courts of appeals have recognized in resolving challenges to the Third Amendment that were based on the same allegations and evidence plaintiffs cite here. None of the following facts, for example, are contested: the Federal National Mortgage Association (Fannie Mae) and the Federal Home Loan Mortgage Corporation (Freddie Mac) lost more money in 2008 than they had made in the previous 37 years combined. Following FHFA's appointment as conservator, Treasury committed $200 billion in taxpayer funds to the enterprises, a commitment that Treasury eventually increased to over $400 billion. Appx4-5. In exchange for that commitment, Treasury received a right to a 10% dividend payment, periodic commitment fees, warrants to purchase nearly 80% of the enterprises' common stock, and priority over other stockholders in recouping Treasury's investment if the

enterprises were later liquidated. Appx5. By 2012, those dividend payments totaled nearly $19 billion per year, more than the enterprises had made in all but one year of their existence. *See* Gov't.Br.9-10. Between 2008 and 2012, the enterprises regularly drew on Treasury's commitment to pay those dividends. *Id.*

There is likewise no dispute that the Third Amendment, under which Treasury agreed to forgo the 10% dividend and periodic commitment fees in exchange for a variable dividend equal to the enterprises' net worth (less a capital buffer), eliminated the possibility that the enterprises would have to draw on Treasury's commitment to pay future dividends. Appx6. Thus, as court after court has held, the Third Amendment involved the "quintessential conservatorship tasks" of "[r]enegotiating dividend agreements, managing heavy debt and other financial obligations, and ensuring ongoing access to vital yet hard-to-come-by capital." *Perry Capital LLC v. Mnuchin*, 864 F.3d 591, 607 (D.C. Cir. 2017); *see also, e.g.*, *Jacobs v. FHFA*, 908 F.3d 884, 890 (3d Cir. 2018).

II. Plaintiffs' Claims Are Not Against the United States.

A. FHFA's Actions as Conservator Are Not Attributable to the Government.

1. The Court of Federal Claims rejected most of plaintiffs' contentions with respect to why FHFA's actions as conservator are attributable to the United States. The court concluded, for example, that FHFA as conservator was not Treasury's agent and was not coerced by Treasury. Appx16-19. The court also acknowledged

that FHFA would not be the United States when acting as receiver. Appx24-25. The court nevertheless concluded that FHFA is the United States when it acts as conservator, relying on the district court's decision in *Sisti v. FHFA*, 324 F. Supp. 3d 273, 279 (D.R.I. 2018) (appeal pending). Appx24-25.

The government's principal brief explained that the distinction between conservators and receivers was without basis, Gov't.Br.36-39, and plaintiffs make little effort to defend the court's reasoning and no effort at all to grapple with the many appellate decisions holding that a federal agency is not the United States when acting as conservator or receiver. Instead, they baldly declare that such precedent does not exist. Jt.Reply.Br.32.

But plaintiffs cannot dispose of holdings with which they disagree by insisting that they do not exist. Courts have expressly held that FHFA as conservator "steps into [the private enterprises'] shoes, shedding its government character and becoming a private party." *Meridian Invs., Inc. v. Freddie Mac*, 855 F.3d 573, 579 (4th Cir. 2017); *see also, e.g.*, *Herron v. Fannie Mae*, 861 F.3d 160, 169 (D.C. Cir. 2017) ("[A]s conservator," FHFA "stepped into [Fannie Mae's] shoes" and thereby "shed[] its government character and . . . became a private party."); *United States ex rel. Adams v. Aurora Loan Servs., Inc.*, 813 F.3d 1259, 1261 (9th Cir. 2016); *see also* Gov't.Br.33-34 (citing additional cases). The Court of Federal Claims itself recognized that, "[i]n other jurisdictions, courts have held (with near unanimity) that the FHFA loses its government status" when it acts as conservator. Appx20. And the district court in

Sisti similarly acknowledged that its conclusion that FHFA retains its governmental character when acting as conservator was "contrary to every other court to reach the issue." 324 F. Supp. 3d at 277.

Plaintiffs suggest that *Sisti* accords with precedent by noting *Sisti*'s footnote citation to an unpublished district court discovery order. Jt.Reply.Br.32-33; *see also Sisti*, 324 F. Supp. 3d at 282 n.8 (citing *FHFA v. Royal Bank of Scot. Grp. PLC*, No. 11-cv-01383, 2012 WL 3580522 (D. Conn. Aug. 17, 2012)). That the *Sisti* court could find support for its conclusion only in a footnote in an unpublished discovery order underscores the absence of authority for plaintiffs' position. Nor do the holding or reasoning of *Royal Bank of Scotland* buttress plaintiffs' argument. The issue in that case was whether the Private Securities Litigation Reform Act's discovery stay provision applied to a suit brought by FHFA as conservator. 2012 WL 3580522, at *1. Moreover, the court simply declared without elaboration or citation that "the fact that a federal agency has stepped into the shoes of a person who would be a private plaintiff . . . simply makes it a federal agency standing in the shoes of a person who would be a private plaintiff." *Id.* at *4. In their mistaken attempt to suggest that *Sisti* reflects a widely held view, plaintiffs also note a citation to *Sisti* in *Phoenix Bond & Indemnity Co. v. FDIC*, No. 18 C 6897, 2020 WL 7223710 (N.D. Ill. Dec. 8, 2020). But *Phoenix Bond* concerned FDIC's actions as receiver, and the court simply cited *Sisti* for the proposition that FDIC as receiver is not the government. *Id.* at *3.

Plaintiffs' citation to *DeKalb County v. FHFA*, 741 F.3d 795, 804 (7th Cir. 2013), is likewise misplaced. Jt.Reply.Br.33. The Seventh Circuit's holding in that case was not concerned with the status of the conservator—indeed, FHFA filed suit in its regulatory capacity, *see* ECF.74, 3:12-cv-50230 (N.D. Ill., Sept. 27, 2012) at 10 (explaining that FHFA initiated the suit as an agency of the federal government)—but with the question whether Fannie Mae and Freddie Mac could be subject to state and local taxation and whether the Tax Injunction Act barred the suit. The Seventh Circuit explained that "[t]he Tax Injunction Act 'does not constrain the power of federal courts if the United States sues to protect itself or its instrumentalities from state taxation," 741 F.3d at 804 (citations omitted), and concluded that the presence of FHFA meant that the Act did not bar the suit. That holding has no bearing on the question whether FHFA acting as conservator is the United States.

The government's principal brief furthermore explained that no basis exists for the Court of Federal Claims' underlying rationale in distinguishing between conservators and receivers—that conservators, unlike receivers, purportedly owe fiduciary duties to the entities they oversee. Gov't.Br.36-37. Even assuming FHFA as conservator owes fiduciary duties to the enterprises, that fact would not distinguish it from the enterprises' officers and directors, who also owe fiduciary duties to the enterprises, and whose private power FHFA exercises as conservator.

Plaintiffs respond by stating, without elaboration, that the Court of Federal Claims' conservator/receiver distinction is "not inconsistent" with the principle that

corporate officers and directors owe fiduciary duties to the corporation. Jt.Reply.Br.33. This cursory response disregards the court's reasoning and the reasoning of the *Sisti* district court. Both courts reasoned that because FHFA as conservator (assertedly) owes fiduciary duties to the enterprises its actions must be governmental. Appx24. But insofar as the conservator has such fiduciary duties, it stands on the same footing as officers and directors of the corporation.

2. Presumably because they recognize that the reasoning of the Court of Federal Claims is untenable, plaintiffs primarily urge that FHFA is a government agency (which is uncontested) and, as such, it never loses its governmental character (a contention at odds with established precedent). Jt.Reply.Br.11-23.

Plaintiffs fail to come to grips with the uniform precedent establishing that government agencies are generally not governmental actors when functioning as conservators or receivers. *See* Gov't.Br.33-34. Instead, they dismiss these decisions on the theory that they concerned the "status of *the Companies*" not the "status of the Agency." Jt.Reply.Br.27. This assertion is wrong in every respect. These decisions expressly addressed the status of the agency when it becomes a conservator or receiver, concluding that it "shed[s] its government character and . . . becom[es] a private party." *Meridian Investments*, 855 F.3d at 579; *see also Herron*, 861 F.3d at 169.

Thus, as the D.C. Circuit stated unambiguously, upon its appointment as conservator, "FHFA's status changed" from a government actor to a private one. *Herron*, 861 F.3d at 169. And when FHFA (or FDIC or another agency) takes action

as conservator or receiver, it does so on behalf of the private enterprise in conservatorship or receivership, not in its capacity as a government regulatory agency.

The Purchase Agreements themselves underscore the nature of the conservator's role. Those contracts are agreements between Treasury and the enterprises, not between Treasury and FHFA. *See, e.g.*, SAppx1 (This Stock Purchase Agreement is an agreement "between the UNITED STATES DEPARTMENT OF THE TREASURY ('Purchaser') and FEDERAL NATIONAL MORTGAGE ASSOCIATION ('Seller')."); SAppx25. FHFA signed the agreements on the enterprises' behalf "as [their] duly appointed conservator." SAppx1. The enterprises are the contractual counterparties that have rights and obligations under the Purchase Agreements, not FHFA. In other words, it is the enterprises that agreed to the Purchase Agreements and Third Amendment. Thus, the question presented in this case, as in all of the cases cited by the government, is whether actions taken by a private entity under the control of a federal conservator or receiver are government action. As almost every court to consider the question has concluded, they are not.

The D.C. Circuit's decision in *Auction Co. of America v. FDIC*, 132 F.3d 746 (D.C. Cir. 1997), on which plaintiffs seek to rely, Jt.Reply.Br.29, reflects the errors underlying their argument. In *Auction Co.*, the court held that a breach-of-contract claim brought against FDIC as receiver was a claim "against the United States." 132 F.3d at 748-51. But, as the court emphasized, the contract at issue was between the plaintiff and FDIC, not between the plaintiff and the financial institution in

receivership. *Id.* at 751. Thus, the plaintiffs' breach-of-contract claim was against the United States because the plaintiff was "not suing to enforce a contract with a defunct depository but to enforce one made initially and exclusively with" FDIC. *Id.* The transaction at the heart of these appeals, by contrast, is "exclusively" between the enterprises and Treasury.

Plaintiffs' extended reliance (Jt.Reply.Br.12-15) on the Supreme Court's decision in *Lebron v. National Railroad Passenger Corp.*, 513 U.S. 374 (1995), also underscores the flaws in their analysis. *Lebron* stated as a general rule that a corporation will qualify as a government actor for constitutional purposes where: "[(1)] the Government creates [the] corporation by special law, [(2)] for the furtherance of governmental objectives, and [(3)] retains for itself permanent authority to appoint a majority of the directors of that corporation." *Id.* at 400. Plaintiffs argue that FHFA meets each of these criteria and thus qualifies as a government actor. Jt.Reply.Br.13. But, again, no one disputes that FHFA is, as a general matter, a federal government agency. The question is whether FHFA's actions as conservator on behalf of the enterprises are governmental.

Courts applying *Lebron* have uniformly concluded that FHFA's conservatorship does not transform actions taken on the enterprises' behalf into those of the government. In *Herron*, for example, the D.C. Circuit held that the conservatorship did not convert Fannie Mae into a government actor because, among other things, the conservatorship was "temporary" and thus, even assuming FHFA remained the

government as conservator, its control was not "permanent." 861 F.3d at 169. The Fourth Circuit, "applying the reasoning of *Lebron*" to FHFA as conservator of Freddie Mac, similarly concluded that neither FHFA as conservator nor Freddie Mac is "a federal instrumentality." *Meridian Investments*, 855 F.3d at 579; *see also Aurora Loan Servs., Inc.*, 813 F.3d at 1261 ("Even assuming that *Lebron* outlines the correct analytical framework," relators' "argument still fails, because relators do not allege that the conservatorship represents the federal government's retention of permanent authority to control Fannie Mae and Freddie Mac.").

For similar reasons, plaintiffs' citations (Jt.Reply.Br.15-22) to various HERA provisions that establish FHFA as a federal agency are beside the point. Congress, of course, created FHFA as an "agency of the Federal Government." Jt.Reply.Br.16 (quoting 12 U.S.C. § 4511(a)). Congress likewise created FDIC and the Small Business Administration (among others) as independent federal agencies. Equally clearly, these entities do not retain their government status when they operate as a conservator or receiver of a private financial institution.

Plaintiffs' reliance on 12 U.S.C. § 4617(a)(7) similarly misses the mark. Jt.Reply.Br.16-17. Plaintiffs note that § 4617(a)(7) provides that "[w]hen acting as conservator or receiver, the Agency shall not be subject to the direction of any other agency of the United States or any State." Jt.Reply.Br.17-18 (brackets in original) (quotation marks and emphasis omitted). But, in nearly identical language, Congress provided that "the Corporation"—*i.e.*, the FDIC—"shall not be subject to the

direction or supervision of any other agency or department of the United States or any State" when "acting as conservator or receiver." 12 U.S.C. § 1821(c)(2)(C). Congress's mandate that FHFA, when "acting as conservator or receiver," is not "subject to the direction of any other agency of the United States" does not suggest that FHFA or FDIC is the government when acting as a conservator. And, moreover, the *Sisti*-based analysis plaintiffs and the Court of Federal Claims adopted would deem *conservators but not receivers* governmental. That conclusion cannot be squared with the language of Sections 4617(a)(7) and 1821(c)(2)(C), which each apply regardless of whether FHFA or FDIC is acting as conservator or receiver.

Three other HERA provisions cited by plaintiffs are equally unavailing. Jt.Reply.Br.19. Section 4617(a)(5) provides that the enterprises may bring an action in district court to challenge FHFA's appointment as conservator within 30 days of that appointment. Such a suit would have challenged the decision of FHFA acting as regulator to place the enterprises into conservatorship. The provision has no bearing on FHFA's status when it takes action as conservator.

Plaintiffs' reliance on HERA's anti-injunction provision, 12 U.S.C. § 4617(f), and its Succession Clause, *id.* § 4617(b)(2)(A), is similarly misplaced. The first provision bars courts from entering injunctions that would restrain or affect a conservator's actions, while the second bars shareholders from bringing derivative suits during conservatorship. These "special protections" do not, as plaintiffs contend (Jt.Reply.Br.19), suggest that FHFA as conservator is a government actor.

Congress may preclude suits against private entities when it concludes that litigation would not further the public interest. As one recent example, Congress has provided numerous "special protections" to vaccine manufacturers that limit the parties who may bring vaccine-related tort suits against those companies and the remedies available in such suits. *See, e.g.*, 42 U.S.C. § 247d-6d (providing immunity from suit to private parties providing "pandemic and epidemic" related products); *id.* §§ 300aa-10 to 300aa-23 (limiting liability of vaccine manufacturers). Such protections and limitations do not convert the private parties receiving the protection into government actors.

Indeed, HERA's Succession Clause "evinces Congress's intention to have the FHFA step into Fannie Mae's private shoes." *Herron*, 861 F.3d at 169; *see* Gov't.Br.37-38. It provides that FHFA as conservator succeeds to the "rights, titles, powers, and privileges" of the enterprises' officers, directors, and shareholders. 12 U.S.C. § 4617(b)(2)(A)(i). The provision thus establishes that Congress intended FHFA as conservator to assume the role of the enterprises' officers and directors. Plaintiffs make no attempt to reconcile their position with the statute's text.

Plaintiffs' insistence that the conservator should be deemed the government is also at odds with the types of activities FHFA undertakes as conservator, which are not governmental in nature and instead involve the day-to-day operation of private companies. *See* Gov't.Br.34-36. The Third Amendment itself, for example, involved the renegotiation of the enterprises' financial obligations and lending arrangements,

actions "within the heartland of powers vested in the officers or board of directors of any corporation." *Saxton v. FHFA*, 901 F.3d 954, 960-61 (8th Cir. 2018).

Plaintiffs do not dispute that the actions FHFA takes as conservator track those of the enterprises' officers and directors. They suggest, however, that FHFA as conservator possesses "extraordinary statutory powers" that the enterprises' officers and directors do not possess. Jt.Reply.Br.20-21. Despite this extravagant language, the only "extraordinary statutory power" that plaintiffs identify is FHFA's authority "to take into account 'public' policy." *Id.* And that authority does not distinguish FHFA as conservator from the enterprises' pre-conservatorship officers and directors. Although Fannie Mae and Freddie Mac are private companies, their statutory charters require them to pursue federal policy goals and objectives. *See* 12 U.S.C. § 4501; *id.* § 1451 note; *id.* § 1716; *see also American Bankers Mortg. Corp. v. Federal Home Loan Mortg. Corp.,* 75 F.3d 1401, 1406-07 (9th Cir. 1996). Those public missions do not make either the enterprises or the conservator government entities.[1]

As noted, plaintiffs' reasoning does not turn on characteristics unique to FHFA and would have potentially far-reaching consequences for not only FHFA, but also

[1] In explaining that conservators perform non-governmental functions, the government also noted (Gov't.Br.35-36) that "[f]ederal regulators appointed private entities to be conservators and receivers of troubled financial institutions until the advent of the FDIC." Plaintiffs' mistakenly challenge the accuracy of that statement, (Jt.Reply.Br.22), relying on *Ex parte Chetwood*, 165 U.S. 443, 444 (1897), in which the Comptroller of Currency in fact appointed "one S. P. Young," a private individual, as receiver.

FDIC and other federal agencies that serve as conservators or receivers. Plaintiffs' only response is to suggest that FDIC is not a federal agency. Jt.Reply.Br.31-32. Such groundless assertions do not advance plaintiffs' argument.

3. Plaintiffs mistakenly urge that it is immaterial whether FHFA as conservator is a private actor, because FHFA as regulator purportedly approved all agreements, including the Third Amendment, and their suit can proceed against the United States on this basis. Jt.Reply.Br.22-23. As the Purchase Agreements and Third Amendment themselves make clear, FHFA agreed to the Agreements and Amendment on behalf of the enterprises in its capacity as conservator. It was not required to and did not obtain FHFA's approval as regulator when it entered into those transactions. Indeed, the regulation that plaintiffs cite in support of their contention—12 C.F.R. § 1237.12, which governs capital distributions during the conservatorship—is contained in a chapter outlining FHFA's powers as "conservator or receiver" of the enterprises, *id.* § 1237.1. The provision explains that the *conservator* may authorize capital distributions during a conservatorship under certain conditions. It nowhere suggests that such distributions require regulatory approval.

Plaintiffs similarly miss the mark in suggesting that FHFA's alleged failure to "silo its conservatorship and regulatory functions" indicates that FHFA's actions as conservator and regulator are one and the same. Jt.Reply.Br.22-23. The law has long recognized a distinction between actions taken by an agency in its regulatory capacity and those taken by an agency in its conservator or receiver capacity. *See supra* pp. 5-

10; *see also*, *e.g.*, *County of Sonoma v. FHFA*, 710 F.3d 987, 992 (9th Cir. 2013). Plaintiffs provide no basis for their supposition (Jt.Reply.Br.23) that FHFA "policymakers" have failed to adhere to that distinction.

B. Treasury's Involvement as a Contractual Counterparty Does Not Provide a Basis for the Court's Jurisdiction.

Plaintiffs do not dispute the Court of Federal Claims' conclusions that Treasury did not coerce FHFA into agreeing to the Third Amendment and that FHFA was not acting as Treasury's agent. *See* Appx18-19; Gov't.Br.40-42. Accordingly, plaintiffs have waived any challenge to those conclusions. *See Advanced Magnetic Closures, Inc. v. Rome Fastener Corp.*, 607 F.3d 817, 833 (Fed. Cir. 2010). Any such challenge would be meritless in any event. *See* Gov't.Br.40-42.

Plaintiffs nonetheless assert that their claims should be deemed to be against the United States on the ground that the Third Amendment was "accomplished by two government entities acting in coordination and by agreement." Jt.Reply.Br.24. This assertion depends on the mistaken premise that FHFA is a government entity wielding governmental power when acting as conservator. Because that premise is incorrect, it is immaterial that Treasury is a government entity.

Plaintiffs are also wrong in seeking to analogize the contract here to the circumstances of *Hendler v. United States*, 952 F.2d 1364 (Fed. Cir. 1991), in which California employees, as well as federal employees, entered the plaintiffs' land as part of a joint federal/state clean-up of a Superfund site. In concluding that the plaintiffs

could proceed against the United States for actions taken by California employees, the Court emphasized that employees of the State as well as the federal government acted under the authority of an order of the Environmental Protection Agency issued under federal law. *See id.* at 1378-79. The decision has no bearing on the contracts between the enterprises and Treasury.[2]

III. The Court of Federal Claims Erred in Declining to Dismiss Plaintiffs' Derivative Claims.

A. Issue Preclusion Bars Plaintiffs from Re-Litigating the Question Whether HERA's Succession Clause Contains a Conflict-of-Interest Exception.

Plaintiffs recognize that HERA's Succession Clause, 12 U.S.C. § 4617(b)(2)(A), by its plain terms bars enterprise shareholders from bringing derivative suits during a conservatorship. *See, e.g.*, Jt.Reply.Br.19. Our principal brief explained that the Court of Federal Claims erred in concluding that *First Hartford* dictated that it should imply a "conflict-of-interest" exception that would render HERA's Succession Clause nugatory with respect to the crucial transactions specifically authorized by the

[2] Plaintiffs assert (Jt.Reply.Br.25) that questions regarding whether FHFA was acting as Treasury's agent or was coerced by Treasury into agreeing to the Third Amendment go "to the merits . . ., not jurisdiction." That is incorrect. Indeed, plaintiffs relied on these theories in attempting to persuade the Court of Federal Claims that it could properly exercise jurisdiction. While this Court has on occasion considered such issues as part of a merits inquiry where jurisdictional arguments were not pressed, *see A&D Auto Sales, Inc. v. United States*, 748 F.3d 1142 (Fed. Cir. 2014), it has recognized that issues of agency and coercion implicate the jurisdictional question whether a plaintiffs' suit is "against the United States," *see, e.g., Texas State Bank v. United States*, 423 F.3d 1370, 1376-77 (Fed. Cir. 2005); *Lion Raisins, Inc. v. United States*, 416 F.3d 1356, 1362-63 (Fed. Cir. 2005). That is clearly the case here.

legislation. Plaintiffs address none of the critical flaws in the court's reasoning and do not explain how its holding can be reconciled with the statute's text and purpose.

As an initial matter, however, the question of whether a court may imply a conflict-of-interest exception was "ful[ly] and fair[ly]" litigated, *In re Freeman*, 30 F.3d 1459, 1467 (Fed. Cir. 1994), in a derivative action by shareholders in *Perry Capital LLC v. Lew*, 70 F. Supp. 3d 208, 229-30 (D.D.C. 2014), and cannot be re-litigated here.

Plaintiffs acknowledge that when a derivative suit is brought by a shareholder the judgment may bind "the corporation and all its shareholders." Jt.Reply.Br.92. They urge, however, that a different result should obtain when a court resolves the suit by concluding that no shareholder can meet a threshold requirement. To support this assertion, they invoke the principle of "hornbook law" that when "the plaintiff lacks 'capacity to bring the suit,' the plaintiff cannot adequately represent the interests of the corporation and the dismissal 'will not bar other stockholders from bringing a derivative action.'" Jt.Reply.Br.92 (quoting 7C Charles Alan Wright & Arthur R. Miller*, Federal Practice & Procedure* § 1840 (3d ed.)). The "hornbook law" explicated in that treatise is that a shareholder lacks "capacity" to bring a derivative suit when the shareholder does not adequately represent the interests of the other shareholders or the corporation and is instead "seeking to protect only personal interests." Wright & Miller, *supra*, § 1840. Thus, a "particular stockholder who institutes a stockholder's derivative suit" will lack capacity where, for instance, he "participated in the wrong complained of," "ratified the wrong complained of or acquiesced in it." *Id.* (quotation

marks omitted); *see also In re Nine West LBO Sec. Litig.*, No. 20 MD. 2941, 2020 WL 7090277, at *8 (S.D.N.Y. Dec. 4, 2020) (citied by plaintiffs at Jt.Reply.Br.94) (stating that issue preclusion did not apply because the interests of shareholders in prior derivative litigation "were directly opposed" to the interest of the litigation trustee in the later litigation). Where, on the other hand, there is no reason "to doubt the quality, extensiveness, or fairness" of a particular shareholder's litigation of a prior derivative suit, *In re Freeman*, 30 F.3d at 1467, the results of that suit are binding on other shareholders.

Plaintiffs do not assert that the shareholders in *Perry Capital* did not represent adequately the interests of all enterprise shareholders; that they were pursing their own personal interests; or that there are reasons to doubt the quality, extensiveness, or fairness of their representation. Any such claim would be surprising since plaintiffs here are represented by many of the same counsel as the plaintiffs in *Perry Capital* and advance the same arguments they advanced there. *See* Gov't.Br.76.

Instead, plaintiffs falsely equate the question of capacity with the question of whether prior litigation was decided on a threshold ground. That equivalence finds no basis in law. In *In re Sonus Networks, Inc,* 499 F.3d 47 (1st Cir. 2007), for example, the First Circuit first held that issue preclusion applied to the threshold question whether shareholders "should be permitted to bring suit on behalf of the corporation," *id.* at 64, and then conducted a separate inquiry into the adequacy of representation in the prior suit, *id.* at 64-66.

Plaintiffs' analogy to class-action lawsuits that are dismissed before class certification, Jt.Reply.Br.94-95, disregards the fundamental ways in which class action suits differ from shareholder derivative suits. "Unlike a class action, the shareholder-plaintiff [in a derivative suit] is not seeking to enforce an individual right belonging to each of the shareholders; the shareholder is suing on behalf of the corporation." Wright & Miller, *supra*, § 1840. Thus, whereas absent class members are not parties to a class action until the class is certified, *see Smith v. Bayer Corp.*, 564 U.S. 299, 317-18 (2011), all shareholders and the corporation are parties to every derivative suit, because the corporation is "the real party in interest," *In re Sonus Networks*, 499 F.3d at 63.

Plaintiffs also err in asserting that the question of whether HERA's Succession Clause bars derivative constitutional claims, as opposed to derivative non-constitutional claims, is a "distinct issue" that was not litigated in *Perry Capital*. Jt.Reply.Br.95. They argue that the issue is "distinct" because it "implicates the serious constitutional question that would arise if a federal statue were construed to deny any judicial forum for a colorable constitutional claim." Jt.Reply.Br.95 (quoting *Webster v. Doe*, 486 U.S. 592 (1988)).

Whether HERA's Succession Clause bars shareholders from pursuing derivative constitutional claims is not "distinct" from the question whether it bars other derivative claims. Plaintiffs' argument to the contrary proceeds from an incorrect premise. The Succession Clause does *not* bar "Mr. Barrett's constitutional

claims," as plaintiffs contend. Jt.Reply.Br.95-96. The relevant constitutional claims belong to the enterprises. *See Koster v. (American) Lumbermens Mut. Cas. Co.*, 330 U.S. 518, 522 (1947) (In a derivative suit, "[t]he cause of action which . . . a plaintiff [stockholder] brings before the court is not his own but the corporation's."). The Succession Clause merely precludes shareholders as third parties from bringing constitutional claims on behalf of the enterprises.

Whether a plaintiff can pursue a third party's constitutional rights in litigation does not raise any constitutional concerns. Indeed, plaintiffs are generally barred from raising constitutional claims on behalf of third parties. *See, e.g.*, *Kowalski v. Tesmer*, 543 U.S. 125, 134 (2004). And courts, including this one, have routinely concluded that shareholders lack standing to pursue derivative constitutional claims belonging to the corporation. *See, e.g.*, *Starr Int'l Co. v. United States*, 856 F.3d 953, 964-67 (Fed. Cir. 2017) (holding that shareholders were barred from bringing derivative Due Process illegal exaction claim); *Gregory v. Mitchell*, 634 F.2d 199, 202 (5th Cir. 1981); *Pagán v. Calderón*, 448 F.3d 16, 28-29 (1st Cir. 2006). In evaluating whether a shareholder may bring a derivative constitutional claim, moreover, courts apply the same rules that apply to any derivative claim. *See, e.g.*, *Starr Int'l*, 856 F.3d at 964-66.

Plaintiffs similarly err in asserting that the application of the Succession Clause to plaintiffs' derivative claims would "deny any judicial forum for a colorable constitutional claim." Jt.Reply.Br.95 (quotation marks omitted). FHFA as conservator remains free to pursue any constitutional claims belonging to the

enterprises, including takings and illegal exaction claims. *See* Gov't.Br.82-83. FDIC as receiver has brought such claims. *See, e.g.*, *First Hartford Corp. Pension Plan & Tr. v. United States*, 42 Fed. Cl. 599, 616 (1998).

Plaintiffs also contend as a final matter that preclusion will purportedly "freeze the development of the law in this area by making it impossible for anyone to question the D.C. Circuit's construction of the statute." Jt.Reply.Br.97-98. This would not be a basis for setting aside principles of issue preclusion; but in any event, three courts of appeals have addressed the same issue and one of those decisions is currently on review before the Supreme Court in *Collins v. Mnuchin*, No. 19-422 (U.S. *cert. granted* July 9, 2020).

B. HERA's Succession Clause Does Not Include a Conflict-of-Interest Exception That Permits Plaintiffs' Derivative Claims to Proceed Here.

1. Plaintiffs do not claim that a conflict-of-interest exception is consistent with the Succession Clause's text or with Congress's purpose in enacting the provision. They instead argue that, in the absence of a conflict-of-interest exception, the Succession Clause would run afoul of the "clear statement" rule set forth in *Webster*. Jt.Reply.Br.103. *Webster* is inapplicable here; the Succession Clause does not foreclose any constitutional claims; it simply bars shareholders from pursuing constitutional claims belonging to the enterprises.

Plaintiffs' reference to the presumption in favor of judicial review of agency action is equally misplaced. Jt.Reply.Br.104. The Succession Clause does not

preclude judicial review of any claims. It limits who may bring them and does so in clear terms. And a presumption is not a license for disregarding unambiguous statutory text.

The only HERA provision that plaintiffs cite (Jt.Reply.Br.105) in support of their contention is § 4617(a)(5), which permits a challenge to FHFA's appointment as conservator, provided it occurs within 30 days. Plaintiffs assert (Jt.Reply.Br.105) that § 4617(a)(5) demonstrates that "Congress understood a shareholder derivative suit against the conservator to be consistent with the Succession Clause's transfer of shareholder rights."

Their contention is wrong in every respect. First, a suit under § 4617(a)(5) would be brought against FHFA as regulator, not against FHFA as conservator. Second, plaintiffs' contention gets principles of statutory interpretation backwards. The existence of an "express exception . . . implies that there are no other" implicit ones. *Jennings v. Rodriguez*, 138 S. Ct. 830, 844 (2018). That Congress permitted shareholders to sue derivatively in limited circumstances thus indicates that they cannot otherwise do so.

2. Plaintiffs' principal argument in favor of an implicit conflict-of-interest exception is not based on HERA's text, structure, or purpose. Rather, plaintiffs primarily argue (Jt.Reply.Br.100-101) that this Court is compelled to interpret HERA's Succession Clause to permit their derivative claims, because this Court in *First Hartford*

concluded that FIRREA's analogous provision contains a "very narrow" exception. This argument, too, is mistaken on many grounds.

In *First Hartford*, this Court emphasized that the exception it was implying permitted shareholders to sue in a "very narrow range of circumstances." 194 F.3d at 1295. Specifically, this Court concluded that shareholders could pursue derivative litigation where the alternative would have required FDIC as receiver to bring suit to challenge actions the FDIC as regulator took before the receivership. *See id.* No such conflict exists here. Nothing would prevent FHFA as conservator from bringing claims on behalf of the enterprises against the United States, as FDIC as receiver has done.

Plaintiffs declare that "the notion that FHFA faces no conflict when deciding whether to challenge a joint FHFA-Treasury action cannot be taken seriously" and further assert that FHFA cannot be expected to file suit as a "practical and legal reality." Jt.Reply.Br.102, 104-105. But there is no "practical and legal reality" that precludes a suit. As noted, there would be no legal impediment to filing suit. And, as a practical matter, there is no reason to assume that subsequent FHFA Directors would be unwilling to question the judgment of the Acting Director who agreed to the Third Amendment—particularly if, as plaintiffs assert, Treasury coerced FHFA into agreeing to the Third Amendment, in which case the current FHFA Director would have every incentive to challenge the transaction.

Plaintiffs also disregard crucial distinctions between HERA and FIRREA that bear on the interpretation of HERA's Succession Clause. As *First Hartford* illustrates, FIRREA applied to a wide range of financial institutions and lawsuits arising from a similarly broad range of potential circumstances. HERA, by contrast, concerns the conservatorship or receivership only of a few crucial institutions. In enacting the Succession Clause, Congress understood that the most important transactions that the conservator would enter would be the agreements with Treasury by which it would obtain the capital commitment necessary for the conservator to keep the enterprises afloat. Nothing in the text or history of HERA suggests that Congress believed that these transactions created a conflict of interest or that courts could nullify the Succession Clause with regard to the very transactions that the statute authorized.[3]

Although plaintiffs insist that the Court should imply a conflict-of-interest exception, they do not dispute the far-ranging impact that would result from accepting their position. Because FHFA's status as a contractual counterparty is, in plaintiffs' view, sufficient evidence of a disabling conflict, under plaintiffs' theory, *every* transaction FHFA as conservator enters would be subject to challenge by shareholders in a derivative action. Plaintiffs do not explain how that result can be

[3] Plaintiffs declare (Jt.Reply.Br.101) that Congress implicitly intended to enact this Court's interpretation of FIRREA's succession provision when it enacted HERA, but they provide nothing to support that assertion. The Supreme Court has also made clear that *stare decisis* does not necessarily compel a court to import an interpretation of one statute into a second statute with similar language. *See, e.g.*, *Irwin v. Department of Veterans Affairs*, 498 U.S. 89, 94 (1990).

squared with this Court's emphasis on the "very narrow range of circumstances" in which the conflict-of-interest exception it adopted in *First Hartford* applies. 194 F.3d at 1295.

IV. Plaintiffs Fail to State an Implied-in-Fact Contract Claim.

Plaintiffs assert that FHFA and the enterprises' boards entered into an implied-in-fact contract under which FHFA promised to operate the conservatorships for the benefit of its shareholders in exchange for the boards' consent to conservatorship. *See* Appx47. Plaintiffs' claim that FHFA as conservator breached that contract fails for the threshold reasons discussed above and in our principal brief.

Even apart from the threshold grounds for dismissal, the complaints are devoid of any legally sufficient allegations that would support the existence of an implied contract. Gov't.Br.88-89, 91. They merely offer conclusory recitals of the elements of a contract—for example, that "[t]he Agency offered, and the boards of Fannie Mae and Freddie Mac accepted, a conservatorship." Appx530.

Although plaintiffs insist that these allegations are sufficient, "[t]hreadbare recitals of the elements of a cause of action, supported by mere conclusory statements," are not entitled to the assumption of truth. *Ashcroft v. Iqbal*, 556 U.S. 662, 678-79 (2009). That is particularly the case here, because a plaintiff claiming the existence of an implied-in-fact contract with the government must allege more than "[a]n agency's performance of its regulatory or sovereign functions," which "does not create contractual obligations." *Mola Dev. Corp. v. United States*, 516 F.3d 1370, 1378

(Fed. Cir. 2008) (quotation marks omitted). Such a plaintiff must allege facts supporting "a clear indication of intent to contract," which is "something more than a cloud of evidence that could be consistent with a contract." *Id.* (quotation marks omitted). Here, FHFA asked for and received the boards' consent to conservatorship pursuant to its statutory authority, just as the government agency in *Mola* and other *Winstar* cases considered and approved bank mergers pursuant to its statutory authority. *See* 12 U.S.C. § 4617(a)(3)(I). While plaintiffs attempt to distinguish *Mola* by claiming that FHFA here "chose to negotiate an agreement," Jt.Reply.Br.71, plaintiffs again offer no factual allegations of negotiations to support that claim. Plaintiffs also note that *Mola* was decided at summary judgment, Jt.Reply.Br.70, but this Court has applied the same standard in concluding that allegations were insufficient to state an implied-in-fact contract claim at the motion to dismiss stage, *see Cain v. United States*, 350 F.3d 1309, 1316-17 (Fed. Cir. 2003).

The absence of any legally sufficient allegations is unsurprising because the contract that plaintiffs assert FHFA agreed to is entirely implausible. HERA mandates that FHFA ensure the enterprises operate in a manner consistent with the "public interest," 12 U.S.C. § 4513(a)(1)(B)(v), and FHFA could not disregard that mandate by promising to operate the enterprises in conservatorship with solely the shareholders' interests in mind. *See* Gov't.Br.89. Plaintiffs suggest (Jt.Reply.Br.72) that FHFA could have agreed to the terms of their asserted contract because HERA grants the conservator broad discretion in operating the conservatorships. Whatever

the scope of the conservator's powers, FHFA, acting as regulator, could not have agreed to a constraint that would contravene the statute's mandate.

Moreover, FHFA had no need to bargain with the enterprises for their consent to conservatorship, because it could have appointed the conservator under several other statutory provisions that did not require the boards' consent. *See* Gov't.Br.89. Indeed, plaintiffs' complaints quote from the FHFA Director's public statement upon imposing the conservatorships, which clearly states that other bases were available. *See* Appx499 (quoting FHFA, *Statement of FHFA Director James B. Lockhart at News Conference Announcing Conservatorship of Fannie Mae and Freddie Mac* (Sept. 7, 2008)). Plaintiffs are driven to assert that FHFA was motivated to bargain for the boards' consent by a desire to avoid litigation, Jt.Reply.Br.70, 71, adding yet another layer of speculation to their argument. But the complaints allege that the boards—not FHFA—feared litigation if they did not consent. *See* Appx413 ("[T]he Companies' directors were confronted with a Hobson's choice: agree to conservatorship, or they would face 'nasty lawsuits'"); 12 U.S.C. § 4617(a)(6) (providing that directors are immune from suit if they consent to conservatorship).

CONCLUSION

This Court should direct the Court of Federal Claims to dismiss the derivative claims it permitted to go forward and affirm the dismissal of plaintiffs' other claims.

Respectfully submitted,

BRIAN M. BOYNTON
Acting Assistant Attorney General

/s/ Abby C. Wright
MARK B. STERN
ABBY C. WRIGHT
GERARD SINZDAK
KYLE T. EDWARDS
Attorneys, Appellate Staff
Civil Division, Room 7252
U.S. Department of Justice
950 Pennsylvania Avenue NW
Washington, DC 20530
(202) 514-0664
Abby.Wright@usdoj.gov

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CERTIFICATE OF COMPLIANCE

This brief complies with the type-volume limit of Federal Rule of Appellate Procedure 28.1(e)(2)(B) because it contains 6,995 words. This brief also complies with the typeface and type-style requirements of Federal Rule of Appellate Procedure 32(a)(5)-(6) because it was prepared using Microsoft Word 2016 in Garamond 14-point font, a proportionally spaced typeface.

/s/ Abby C. Wright
Abby C. Wright

CERTIFICATE OF SERVICE

I hereby certify that on March 26, 2021, I electronically filed the foregoing brief with the Clerk of the Court for the United States Court of Appeals for the Federal Circuit by using the appellate CM/ECF system. Participants in the case are registered CM/ECF users, and service will be accomplished by the appellate CM/ECF system.

/s/ Abby C. Wright
Abby C. Wright