

**IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF DELAWARE**

TIMOTHY J. PAGLIARA,
Plaintiff,

v.

FEDERAL NATIONAL MORTGAGE
ASSOCIATION,
Defendant.

C.A. No. 1:16-cv-00193

**MEMORANDUM OF LAW IN SUPPORT OF SUPPLEMENTAL
MOTION TO SUBSTITUTE THE FEDERAL HOUSING FINANCE
AGENCY AS PLAINTIFF**

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The Federal Housing Finance Agency (“FHFA”), Conservator for defendant Federal National Mortgage Association (“Fannie Mae”), respectfully submits this Memorandum in support of its Supplemental Motion to Substitute FHFA as Plaintiff. The supplemental motion memorandum is based on the additional ground of issue preclusion based on a final judgment issued by the Eastern District of Virginia in a copycat suit Pagliara filed contemporaneously with this action. Because the Virginia court only issued its final judgment on August 23, 2016, it was not possible to raise this issue with the Court during the briefing on FHFA’s currently-pending motion to substitute.¹

In this case, Plaintiff Pagliara seeks to exercise his alleged right, pursuant to 8 Del. C. § 220, to inspect books and records of Fannie Mae. *See, e.g.*, Complaint ¶¶ 1, 156-163.² Pagliara filed materially the same complaint against the Federal Home Loan Mortgage Corporation (“Freddie Mac”) in the United States District Court for the Eastern District of Virginia. There, the court entered a final judgment dismissing Pagliara’s complaint, holding that Pagliara has no right to inspection because HERA transferred all such rights to the Conservator. *Pagliara v. Fed. Home Loan Mortg. Ass’n*, No. 16-cv-337, 2016 WL 4441978, at **1, 4-5, 8 (E.D. Va. Aug. 23, 2016) (citing 12 U.S.C. § 4617(b)(2)(A)(i)) (“Virginia Inspection Case”).

Because Pagliara participated fully as plaintiff in the Virginia Inspection Case, he is precluded from relitigating the same issues here. *See, e.g.*, *Burlington N. R.R. Co. v. Hyundai Merch. Marine Co., Ltd.*, 63 F.3d 1227, 1231 (3d Cir. 1995) (“[O]nce an issue is actually and

¹ *See* Mem. in Supp. of Mot. to Substitute FHFA as Pl. (D.I. 9) (“Opening Subst. Br.”).

² As FHFA has previously explained, Fannie Mae is not subject to 8 Del. C. § 220. In order to satisfy federal law requirements, Fannie Mae elected to follow Delaware’s corporate governance procedures, where not inconsistent with Fannie Mae’s federal Charter, Bylaws, and other applicable federal laws. *See* Reply in Supp. of Mot. to Substitute [FHFA] as Pl., at 5-6 (D.I. 15).

necessarily determined by a court of competent jurisdiction, that determination is conclusive in subsequent suits . . . involving a party to the prior litigation.”). Accordingly, the Court should substitute FHFA as Plaintiff.³

NATURE AND STAGE OF THE PROCEEDINGS

Pagliara filed this suit in Delaware Chancery Court on March 14, 2016, seeking “an order permitting him to inspect and copy certain books and records of Fannie Mae.”⁴ On March 25, 2016, Fannie Mae removed the action to this Court. Notice of Removal (D.I. 1). Now pending before the Court are FHFA’s motion to substitute as the proper plaintiff and Pagliara’s motion to remand the suit to Delaware state court.⁵

SUMMARY OF SUPPLEMENTAL ARGUMENT

The doctrine of issue preclusion holds that once an issue is actually and necessarily decided by a court of competent jurisdiction, that determination is conclusive in subsequent suits involving a party to the prior litigation. Under this doctrine, plaintiff Pagliara is bound by the Eastern District of Virginia’s final judgment holding that Congress transferred the inspection rights of shareholders in the “regulated entities”—including both Freddie Mac and Fannie Mae—to FHFA during its conservatorship. Accordingly, this Court should substitute FHFA for Pagliara as the plaintiff in this suit.

³ The procedural posture of the Virginia Inspection Case was different than this one. In the Virginia Inspection Case, the court ruled on Freddie Mac’s and FHFA’s combined motion to dismiss for failure to state claim, or, in the alternative, to substitute FHFA as plaintiff. Because the court dismissed the case on the merits (because HERA transferred Pagliara’s asserted inspection right to FHFA), it did not need to reach the substitution arguments.

⁴ Pl. Timothy J. Pagliara’s Answering Br. in Opp. to Mot. to Substitute [FHFA] as Pl., at 1 (D.I. 13) (“Subst. Opp.”).

⁵ See Opening Subst. Br.; Pl. Timothy J. Pagliara’s Opening Br. in Supp. of his Mot. to Remand to the Delaware Court of Chancery (D.I. 11).

STATEMENT OF FACTS

FHFA’s Director placed both Fannie Mae and Freddie Mac (the “Enterprises”) into statutory conservatorships in September 2008, and they remain in that status today. *See* Compl. ¶ 65. HERA provides that from the inception of conservatorship, FHFA “by operation of law, immediately succeed[ed] to . . . all rights, titles, powers, and privileges of the regulated entity [e.g., Fannie Mae or Freddie Mac], and of any *stockholder*, officer, or director of such regulated entity with respect to the regulated entity and the assets of the regulated entity.” 12 U.S.C. § 4617(b)(2)(A) (emphasis added); *see also* Compl. ¶ 59.⁶ HERA also expressly empowers the Conservator to “[o]perate the [Enterprises] . . . with all the powers of the shareholders, the directors, and the officers” and to “conduct all business of the [Enterprises].” *Id.* § 4617(b)(2)(B).

On January 19, 2016, Pagliara’s counsel sent twin demands to Fannie Mae and Freddie Mac seeking, as a shareholder in each Enterprise, to inspect their books and records. *See* Compl., Exhibit A. When these requests were denied, Pagliara filed this suit against Fannie Mae and a substantially identical suit against Freddie Mac in Virginia state court (which Freddie Mac removed to the Eastern District of Virginia). *See Pagliara*, 2016 WL 4441978.

FHFA challenged Pagliara’s right to pursue both suits, noting that Pagliara’s books-and-records demands were purported *stockholder* rights and that, in HERA, Congress transferred to FHFA “all rights, titles, powers, and privileges . . . of any stockholder” of Fannie Mae or

⁶ Section 4617(b)(2)(A)(i) makes no distinction between Fannie Mae and Freddie Mac, encompassing both within its reference to transferring all “rights, titles, powers, and privileges” of “any stockholder . . . with respect to the *regulated entity* and the assets of the *regulated entity*.” (Emphasis added). Accordingly, the Virginia court’s ruling that Pagliara no longer enjoys a shareholder right to inspect Freddie Mac’s books and records applies with equal force to Plaintiff’s claimed right to inspect Fannie Mae’s books and records.

Freddie Mac. *See* § 4617(b)(2)(A)(i).⁷ FHFA’s motion to substitute is fully briefed and awaits this Court’s decision.

On August 23, 2016, the Eastern District of Virginia ruled that HERA’s “statutory transfer of power to the conservator destroyed the stockholder’s right to inspect corporate records.” *Pagliara*, 2016 WL 4441978, at *1. The court observed that the language “‘all rights, titles, powers, and privileges . . . of any shareholder’ is extremely broad and evidences Congress’s intent ‘to shift as much as possible to the FHFA.’” *Id.* at *5 (citations omitted). The court also rejected the same arguments *Pagliara* simultaneously asserts here, including his assertion that § 4617(b)(2)(A)(i) transferred to FHFA only shareholder *derivative* claims, not their *direct* claims. *Compare id.* **6-8 with Subst. Opp. at 2-3, 10-20. “The derivative-versus-direct distinction . . . has little bearing on the issue in this case,” the court held, because the issue raised by *Pagliara*’s suit was “not whether *Pagliara* may pursue his right through a direct lawsuit, but whether he possesses the right he believes was infringed.” *Pagliara*, 2016 WL 4441978, at *6.

The court, accordingly, issued a final judgment concluding that:

HERA’s plain language evidences Congress’s intent to transfer as much power as possible to the FHFA when acting as Freddie Mac’s conservator. Within that context, the Court may only reasonably read the transfer of “all rights, titles, powers, and privileges” of “any stockholder . . . with respect to the regulated entity and the assets of the regulated entity” to include a stockholder’s right to inspect Freddie Mac’s corporate records. Accordingly, the Court must dismiss this case because *Pagliara* does not possess the right he seeks to enforce.

Pagliara, 2016 WL 4441978, at *8.

⁷ *See* Opening Subst. Br. (D.I. 9); Mem. in Supp. of Mot. to Dismiss or Substitute FHFA as Pl., *Pagliara v. Fed. Home Loan Mortg. Corp.*, No. 16-cv-337 (E.D. Va. filed June 17, 2016) (ECF No. 34).

ARGUMENT

I. THE VIRGINIA INSPECTION CASE’S HOLDING THAT PAGLIARA HAS NO INSPECTION RIGHTS IS BINDING ON HIM IN THIS LITIGATION

“The doctrine of issue preclusion . . . derives from the simple principle that ‘later courts should honor the first actual decision of a matter that has been actually litigated.’” *Burlington*, 63 F.3d at 1231 (quoting 18 C. Wright, A. Miller & E. Cooper, *Federal Practice and Procedure*, § 4416 (1981)). The doctrine ensures that “once an issue is actually and necessarily determined by a court of competent jurisdiction, that determination is conclusive in subsequent suits . . . involving a party to the prior litigation.” *Burlington*, 63 F.3d at 1231 (quoting *Montana v. United States*, 440 U.S. 147, 153 (1979)).

“The prerequisites for the application of issue preclusion are satisfied when: (1) the issue sought to be precluded [is] the same as that involved in the prior action; (2) that issue [was] actually litigated; (3) it [was] determined by a final and valid judgment; and (4) the determination [was] essential to the prior judgment.” *Peloro v. United States*, 488 F.3d 163, 174-75 (3d Cir. 2007) (internal quotation marks and citation omitted) (alterations in original); *see also Burlington*, 63 F.3d at 1232 (same); *LG Elecs. U.S.A., Inc. v. Whirlpool Corp.*, Civil No. 311-GMS, 2011 WL 4543886, at *3 (D. Del. Sept. 29, 2011).⁸

Each of these elements is easily satisfied here.

A. The Identical Question—Whether Congress Transferred Shareholder Book-and-Records Inspection Rights to FHFA—is Dispositive of Both This and the Virginia Inspection Suits

Central to both this suit and the Virginia Inspection Case is whether HERA, § 4617(b)(2)(A)(i), transferred all shareholder books-and-records inspection rights exclusively to

⁸ Fourth Circuit law is the same. *See Ramsay v. U.S. Immigration & Nat’l Svc.*, 14 F.3d 206, 210 (4th Cir. 1994).

FHFA during its conservatorship of Fannie Mae and Freddie Mac. As the Third Circuit has explained, “[i]ssues are identical for [issue preclusion] purposes where ‘the issues presented by [the current] litigation are in substance the same as those resolved’ in the previous litigation.” *Nat’l Med. Imaging, LLC v. Ashland Funding LLC*, No. 15-1996, 2016 WL 1743475, at *5 (3d Cir. May 3, 2016) (quoting *Montana*, 440 U.S. at 155) (third alteration in original). The “facts of the two cases do not need to be identical so long as any factual differences have no ‘legal significance’ in ‘resolving the issues presented in both cases.’” *Nat’l Med. Imaging*, 2016 WL 174375, at *5 (quoting *United States v. Stauffer Chem. Co.*, 464 U.S. 165, 172 (1984)).

Here, both the Virginia Inspection Case and this one turn on a single central question. In Virginia, the court described that issue as follows:

Defendant contends that the Court should dismiss this Complaint for records inspection because Pagliara no longer possesses any right to inspect Freddie Mac’s records. Specifically, Defendant argues that HERA transferred Pagliara’s inspection right to FHFA when FHFA became Freddie Mac’s conservator. Defendant principally relies upon 12 U.S.C. § 4617(b)(2)(A)(i), which declares that FHFA, upon appointment as conservator, immediately succeeds to ‘all rights, titles, powers, and privileges . . . of any stockholder’ of Freddie Mac.

Pagliara, 2016 WL 4441978, at *5.

The dispositive issue resolved by the Virginia Inspection Case is thus identical to the dispositive issue presented by FHFA’s motion to substitute in this court: “The Court should substitute Fannie Mae’s Conservator, FHFA, in place of Plaintiff Pagliara, who brings this suit solely as a shareholder of Fannie Mae. When it became Conservator, FHFA, ‘by operation of law, immediately succeed[ed] to . . . all rights, titles, powers, and privileges of [Fannie Mae] and any stockholder’ of Fannie Mae. 12 U.S.C. §4617(b)(2)(A). This statute, ‘by its unambiguous text, removes the power’ of Fannie Mae’s shareholders to exercise all their rights (including any document-inspection rights) ‘and gives [those rights] to FHFA’ [D]uring conservatorship,

FHFA alone holds and would have standing to pursue the shareholder rights Plaintiff purports to assert here.”⁹

Accordingly, the first element of issue preclusion, that “the issue sought to be precluded [is] the same as that involved in the prior action” is satisfied. *Peloro*, 488 F.3d at 174-75.

B. Whether Shareholders Retain the Right to Inspect During FHFA’s Conservatorship Over Fannie Mae and Freddie Mac Was Actually Litigated

The requirement that the issue be “actually litigated” is also satisfied. The Virginia court held that § 4617(b)(2)(A)(i)’s transfer of “all shareholder rights” could only be read “to include a stockholder’s right to inspect Freddie Mac’s corporate records.” *Pagliara*, 2016 WL 4441978, at *8. Accordingly, the Virginia court ruled, “the statutory transfer of power to the conservator destroyed the stockholder’s right to inspect corporate records.” *Id.* at *1. As noted above, precisely the same issue is fully briefed on FHFA’s motion to substitute in this Court.

C. The Virginia Inspection Case Decision is Valid and Final

The Virginia court’s holding that *Pagliara* enjoys no shareholder inspection rights was issued in a valid and final judgment. The Court dismissed the lawsuit in its entirety and expressly provided that its Order was “FINAL.” *See Order, Pagliara v. Fed. Home Loan Mortg. Corp.*, No. 16-cv-337 (E.D. Va. Aug. 23, 2016) (attached as Exhibit A). The fact that *Pagliara* may appeal the Virginia holding “does not vitiate the preclusive effect of a trial court judgment.” *Tucker v. Bristol-Myers Squibb*, 143 Fed. App’x 411, 412 n** (3d Cir. 2005) (citing *O’Leary v. Liberty Mut. Ins. Co.*, 923 F.2d 1062, 1066 n.6 (3d Cir. 1991)).

This case thus satisfies the third element of issue preclusion, *i.e.*, that the question whether HERA transferred stockholder inspection rights exclusively from shareholders to FHFA

⁹ Opening Subst. Br., at 1 (alterations in original).

during the conservatorship be “determined by a final and valid judgment.” *Peloro*, 488 F.3d at 175.

D. Whether HERA Transferred Stockholder Inspection Rights Exclusively to FHFA Was Essential to the Virginia Inspection Case Judgment

Finally, this case meets the requirement that the question whether HERA transferred Pagliara’s stockholder inspection rights exclusively to FHFA was “essential to the prior judgment.” The Virginia court held that § 4617(b)(2)(A)(i) transferred stockholders’ “right to inspect Freddie Mac’s corporate records” exclusively to FHFA. *Pagliara*, 2016 WL 4441978, at *8. “*Accordingly*,” the court ruled, “the Court *must* dismiss this case because Pagliara does not possess the right he seeks to enforce.” *Id.* (emphasis added).

CONCLUSION

The doctrine of issue preclusion instructs that “once an issue is actually and necessarily determined by a court of competent jurisdiction, that determination is conclusive in subsequent suits . . . involving a party to the prior litigation.” *Burlington*, 63 F.3d at 1231. Here, the Eastern District of Virginia has issued a final ruling, in a case brought and litigated by Pagliara, that shareholders no longer have inspection rights with respect to Fannie Mae and Freddie Mac (both “regulated entities” under HERA). Mr. Pagliara is bound by this ruling. Accordingly, this Court should substitute FHFA for Pagliara as the Plaintiff here, because only FHFA enjoys the shareholder inspection rights Pagliara purports to assert.

[Signature page follows]

Dated: September 2, 2016

Respectfully submitted,

/s/ Robert J. Stearn, Jr.

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Exhibit A

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

Alexandria Division

TIMOTHY J. PAGLIARA,)	
)	
Plaintiff,)	
)	
v.)	Case No. 1:16-cv-337 (JCC/JFA)
)	
FEDERAL HOME LOAN MORTGAGE)	
CORPORATION,)	
)	
Defendant.)	

O R D E R

For the reasons stated in the accompanying Memorandum Opinion, it is hereby ORDERED that:

- (1) Defendant Federal Home Loan Mortgage Corporation's Motion to Dismiss [Dkt. 33] is GRANTED;
- (2) Intervenor Federal Housing Finance Agency's Alternative Motion to Substitute Plaintiff [Dkt. 33] is DENIED as MOOT;
- (3) Plaintiff's complaint is DISMISSED;
- (4) The Clerk of Court shall forward this Order and accompanying Memorandum Opinion to all counsel of record.

It is so ORDERED. This Order is FINAL.

August 23, 2016
Alexandria, Virginia

/s/

 James C. Cacheris
 UNITED STATES DISTRICT COURT JUDGE