Nos. 14-5243 (L), 14-5254 (con.), 14-5260 (con.), 14-5262 (con.)

IN THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

IN RE FANNIE MAE/FREDDIE MAC SENIOR PREFERRED STOCK PURCHASE AGREEMENT CLASS ACTION

On Appeal from the United States District Court
For the District of Columbia, No. 13-mc-01288
(Royce C. Lamberth, District Judge)

BRIEF OF CLASS PLAINTIFFS IN REPLY TO SUPPLEMENTAL BRIEFS OF APPELLES ON QUESTIONS OF IMMUNITY AND SUBJECT MATTER JURISDICTION

Hamish P.M. Hume
BOIES, SCHILLER & FLEXNER LLP
5301 Wisconsin Ave., NW, Suite 800
Washington, DC 20015
Tel: (202) 237-2727
Fax: (202) 237-6131

Interim Co-Lead Class Counsel for Appellants American European Insurance Company, Joseph Cacciapalle, John Cane, Francis J. Dennis, Marneu Holdings, Co., Michelle M. Miller, United Equities Commodities, Co., 111 John Realty Corp., Barry P. Borodkin and Mary Meiya Liao

[*Additional Appearances on Inside Cover*]

BERNSTEIN LITOWITZ BERGER& GROSSMAN LLP
David L. Wales
1251 Avenue of the Americas
New York, NY 10020
Tel: (212) 554-1409
Fax: (212) 554-1444
dwales@blbglaw.com

Blair A. Nicholas
David R. Kaplan
Lucas E. Gilmore
12481 High Bluff Drive, Suite 300
San Diego, CA 92130
Tel: (858) 793-0070
Fax: (858) 793-0323
blairn@blbglaw.com
davidk@blbglaw.com

GRANT & EISENHOFER P.A.
Michael J. Barry
123 Justison Street
Wilmington, DE 19801
Tel: (302) 622-7000
Fax: (302) 622-7100
gjarvis@gelaw.com
mbarry@gelaw.com

KESSLER TOPAZ MELTZER & CHECK, LLP
Eric L. Zagar
Matthew A. Goldstein
280 King of Prussia Road
Radnor, PA 19087
Tel: (610) 667-7706
Fax: (610) 667-7056

Interim Co-Lead Class Counsel for Appellants American European Insurance Company, Joseph Cacciapalle, John Cane, Francis J. Dennis, Marneu Holdings, Co., Michelle M. Miller, United Equities Commodities, Co., 111 John Realty Corp., Barry P. Borodkin and Mary Meiya Liao

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GLOSSARY

Term	**Abbreviation**
American European Insurance Company, Joseph Cacciapalle, John Cane, Francis J. Dennis, Marneu Holdings, Co., Michelle M. Miller, United Equities Commodities, Co., 111 John Realty Corp., Barry P. Borodkin and Mary Meiya Liao	Class Plaintiffs
Federal National Mortgage Association ("Fannie") and Federal Home Loan Mortgage Corporation ("Freddie")	The Companies
Class Plaintiffs' Consolidated Amended Class Action and Derivative Complaint, filed in the District Court on December 3, 2013	Consolidated Class Complaint or Complaint
United States District Court for the District of Columbia (Lamberth, J.)	District Court
Citations to the Docket in *In re Fannie Mae/Freddie Mac Senior Preferred Stock Purchase Agreement Class Action Litigations*, Misc. Action No. 13-mc-1288 (RCL)	Dkt. ___
Federal Housing and Finance Agency	FHFA
The Housing and Economic Recovery Act of 2008, Pub. L. 110-289, 122 Stat. 2654 (2008)	HERA
The Third Amendment to the Senior Preferred Stock Purchase Agreements between the United	The Net Worth Sweep, or Third Amendment

States Department of the Treasury and the Federal Housing Finance Agency, as conservator to Fannie Mae and Freddie Mac, dated August 17, 2012, and the declaration of dividends pursuant to the Third Amendment beginning January 1, 2013	
Senior Preferred Stock Purchase Agreements	PSPAs, or Government Stock Agreements
United States Department of Treasury	Treasury

I. REPLY TO FHFA.

FHFA admits:

- "Sovereign immunity is not applicable to the Enterprises, which are government-sponsored but private entities subject to their own 'sue-and-be sued' clauses."
- FHFA "has not asserted sovereign immunity" for itself.
- FHFA's "execution of the Third Amendment" was "the Conservator's" action.
- "in the absence of HERA's jurisdiction-withdrawal provisions" – provisions that have been extensively briefed and were not the subject of the Court's briefing order – "the charters of Fannie Mae and Freddie Mac would provide subject-matter jurisdiction over this action."

Doc. #1624902, at 3-4. These admissions addressed the Court's questions, and should have been the end of FHFA's brief.

Instead, FHFA devotes the bulk of its brief to 12 U.S.C. § 4623(d).

Section 4623(d) states that "no court shall have jurisdiction to affect, by injunction or otherwise, the issuance or effectiveness of any classification or action of the Director under this subchapter." 12 U.S.C. § 4623(d). This statute limits court jurisdiction only for claims that may affect actions by the "Director" – meaning *regulatory* actions taken "under this subchapter." Doc. #1610113, at 2-6. It does not limit jurisdiction over claims based on FHFA actions taken in its role as conservator or receiver.

FHFA concedes that § 4623(d) limits a court's jurisdiction only with respect to claims that affect "FHFA regulatory actions." Doc. #1624902, at 2.[1] In addition, FHFA has made clear it "is ***not*** claiming the Third Amendment is a regulatory action…" Doc. #1610211, at 4 n.4 (emphasis added). Logically, this concedes that since Class Plaintiffs seek damages caused only by the Third Amendment, their claims do not affect any regulatory action and therefore are not barred by § 4623(d).

To evade that logical result, FHFA says plaintiffs' claims are "essentially" a challenge to FHFA's decision in October 2008 to "suspend" all "capital classifications" for the two Companies ("October 2008 Suspension"). FHFA argues that unlike the Third Amendment, the October 2008 Suspension *was* a regulatory action, and that a victory for plaintiffs will somehow "nullify" or "affect the effectiveness" of that regulatory action, and hence is barred by §4623(d). Doc. #1624902, at 8-9.

Throughout its briefing in the District Court and on appeal before the oral argument, FHFA never once suggested that any plaintiff claims would affect the October 2008 Suspension. FHFA never even mentioned that suspension of capital classifications, let alone argued that plaintiffs' claims would somehow nullify it. Overlooking the statute it now invokes as the centerpiece of its defense is bad

[1] *See also* Doc. #1610113, at 6 n.8-9.

enough; but now FHFA asserts that plaintiffs' claims are a direct threat to "nullify" a decision announced in October 2008 that FHFA never even mentioned in prior briefing.

Moreover, FHFA's prior brief on § 4623(d) focused on the APA claim by the Institutional Plaintiffs, claiming it seeks to impose "sound and solvent" capitalization standards on the Companies that are inconsistent with the October 2008 Suspension. Doc. #1610211 at 4. That FHFA argument has no bearing on the Class Plaintiffs' claims. It is only now that the Court has focused FHFA on the Class Plaintiffs' claims (to which FHFA has no good defense) that FHFA reaches out, beyond the questions posed by the Court, to try to stretch § 4623(d) to somehow cover Class Plaintiffs' claims. Its effort to do so is meritless.

A. FHFA's Regulations Say The Suspension of Capital Classifications Is An Act Of The Conservator.

FHFA's regulations state: "the authority to suspend capital classifications.... during the duration of the conservatorship" is one held by "[t]he Agency, as conservator." 12 C.F.R. § 1237.3(c). FHFA's prior brief on § 4623(d) cited this provision as authorizing the October 2008 Suspension. Doc.#1610211 at 2. This is inconsistent with FHFA's current claim that the October 2008 Suspension was regulatory action protected by §4623(d).

B. Section 4623(d) Does Not Apply Because Class Plaintiffs Seek Damages Caused By The Third Amendment, Not By The October 2008 Suspension of Capital Classifications.

Awarding damages to Class Plaintiffs would not affect the October 2008 Suspension in any way. FHFA says the October 2008 Suspension created a "new capital paradigm" and "new capital regime" in which "balance sheet capital no longer served as the controlling measure of safety and soundness." Doc. #1624902, at 2, 6. Class Plaintiffs do not challenge any of that. We simply seek compensation for the economic harm inflicted on private shareholders by the Third Amendment. FHFA and the Companies can pay damages to Class Plaintiffs without changing a thing in their "new capital paradigm." It can still be the case that "balance sheet capital" will "no longer serve[] as the controlling measure of safety and soundness." None of that changes because Class Plaintiffs are awarded damages based on the breach of their common law rights.

Class Plaintiffs' common-law claims do not depend on any finding that stripping Fannie and Freddie of their capital on a quarterly basis conflicts with FHFA's conservatorship responsibilities. Rather, those claims depend only on whether FHFA's elimination of Class Plaintiffs' economic interest in the Companies constituted a breach of contract, breach of the implied covenant of good faith, and/or breach of fiduciary duties.

For example, it is apparently FHFA's position that from August 2012 to April 2015, the "new capital paradigm" called for the Companies to pay out dividends that were $130 billion more than they would have been had the Companies simply paid Treasury its 10% senior preferred dividend set forth in the original PSPAs. Whether that can fairly be called "a new capital paradigm" or not is irrelevant to the claims by Class Plaintiffs. The fact remains that the Fannie and Freddie shareholder contracts as they existed before the Third Amendment – meaning both the PSPAs and the private shareholder contracts – unambiguously required the Companies: (a) to pay preferred dividends to the junior (private) preferred shareholders before paying Treasury anything more than its 10% senior preferred stock dividend (*i.e.*, Treasury could receive more than that 10% senior dividend for any period only by exercising its nominal warrants to acquire 80% of the Companies' common stock, on which dividends could be paid only *after* paying the junior, private preferred shareholders); and (b) to pay dividends on privately held common stock on a pro rata basis with dividends paid on Treasury's common stock – meaning the private common shareholders would receive 20% of any dividends paid out after all of the senior preferred dividends were paid. J.A. 235, 311-15, 467-69, 470-84, 485-93, 504-18, 519-27. That is what the contracts unambiguously required. By executing the Third Amendment, FHFA (and the Companies) breached those contracts, as well as their implied covenants of good

faith and FHFA's fiduciary duties. Awarding damages for those breaches does not change the ability of FHFA to dictate that the "new capital paradigm" requires the Companies to be stripped of all their capital each quarter. At most, it may change who receives some of that capital.

FHFA may be suggesting that if it were required to pay private shareholders some of the capital it is stripping from the Companies each quarter, then it would never strip out that extra capital – and therefore, according to FHFA's logic, a win for Class Plaintiffs' "affects" the "new capital paradigm." That argument fails on its face. If Class Plaintiffs' claims "affect" FHFA's decision to pay all dividends to Treasury and none to private shareholders, then it affects the decision made in the Third Amendment, not the decision made in the October 2008 Suspension. There is nothing in the decision to "suspend capital classifications" that dictated where any future dividends might be paid. Instead, the decision to direct 100% of all dividends to Treasury was made solely in the Third Amendment. J.A. 220-21, 2394-2401, 2402-09. And FHFA admits that decision was taken by it as "conservator," not as "regulator."

C. Section 4623(d) Does Not Bar Any Damages Claims.

We previously demonstrated that the provision on which § 4623(d) is modeled, 12 U.S.C. § 1818(i)(1), has been held not to bar damage claims. Doc. #1610113, at 7 n.10. FHFA responds by pointing to a one word difference in the

statute: §1818(i)(1) bars jurisdiction to "affect . . . *the issuance or enforcement*" of a bank regulator's notices or orders; §4623(d) bars jurisdiction to "affect . . . *the issuance or effectiveness*" of the Director's classifications under Subchapter II. Doc. #1624902, at 9 (underline added). FHFA claims the difference between "enforcement" and "effectiveness" is the difference between barring damage claims and not. Nothing supports that.

The minor difference in language is explained by the fact that §1818(i)(1) addresses the authority of bank regulators to apply for "district court . . . *enforcement*" of their notices and orders. Section 4623(d) does not. The two statutes are otherwise completely parallel in structure and intent. There is no basis for construing §4623(d) as barring damage claims when §1818(i) has been held not to.

FHFA never argued to the District Court that *any* provision of HERA barred plaintiffs from seeking damages based on their direct claims. And the District Court expressly held that HERA §4617(f) did *not* bar plaintiffs from seeking damages. Dkt. 51 at 33. FHFA did not challenge that ruling as an alternate basis for affirmance. Its attempt to invoke § 4623(d) as new bar to damage claims is waived; at a minimum, it is not credible.

Moreover, HERA expressly contemplates breach of contract damage claims in a provision addressing the conservator's authority to repudiate contracts. 12 U.S.C. § 4617(d)(3)(A).[2]

Finally, any interpretation of §4623(d) that would preclude Class Plaintiffs from asserting their common-law damage claims would raise serious constitutional questions and should be avoided. *See Coit Independence Joint Venture v. Fed. Savings & Loans Ins. Corp.*, 489 U.S. 561, 578-79 (1989) (avoiding interpretation of receivership statute that would have raised "serious constitutional difficulties" by eliminating *de novo* judicial consideration of "breach of fiduciary duty claims" and "contract disputes").

II. REPLY TO TREASURY.

1. Treasury concedes that if there is an applicable waiver of sovereign immunity for Class Plaintiffs' claims against Treasury, then "their claims would properly be brought in federal court, not state court." Doc. #1624476, at 3, n.2. This concedes the subject matter jurisdiction points made by Class Plaintiffs.

2. In response to the question whether any statute other than the FTCA provided an immunity waiver for Class Plaintiffs' fiduciary breach claims, we invoked this Court's holdings that the immunity waiver in 5 U.S.C. § 702 "applies

[2] FHFA failed to repudiate Class Plaintiffs' contracts "within a reasonable period" following its appointment as conservator, and so cannot invoke the limitations of §4617(d)(3)(A); *see* 12 C.F.R. 1237.5(b) (the "reasonable period" is "18 months").

to any suit whether under the APA or not."[3] Class Plaintiffs showed that this Court has held that § 702's immunity waiver applies claims seeking declaratory and injunctive relief *based on a tort*. Doc. #1623314, at 4-5 (citing *U.S. Info. Agency v. Krc*, 989 F.2d 1211, 1216 (D.C. Cir. 1993)); *see also Treasurer of New Jersey v. U.S. Dept. of Treasury*, 684 F.3d 382, 396-400 & n.19 (3d Cir. 2012).

In response, Treasury says "plaintiffs assert that they could bring a breach of fiduciary claim against Treasury under the APA." Doc. #1624476, at 3. That is a mischaracterization. Class Plaintiffs demonstrated that this Court has repeatedly held that § 702's immunity waiver is *not* limited to claims brought "under the APA." Doc. #1623314, at 4 (citing cases). Treasury's suggestion that Class Plaintiffs are now trying to bring an APA claim is incorrect.

Treasury also suggests that Class Plaintiffs failed to raise § 702 before the District Court, and expresses surprise that we seek any equitable relief based on the fiduciary breach claim. But our Complaint adequately seeks equitable relief based on any and all of our claims. J.A. 278. Section 702 was not raised in the District Court because Treasury's motion to dismiss did not assert sovereign immunity as a bar to the fiduciary breach claims. Dkt. No. 19-1 at 43-49.

Treasury invokes Judge Kavanaugh's concurrence in *El-Shifa Pharmaceuticals Industries Co. v. United States*, 607 F.3d 836 (D.C. Cir. 2010) (*en*

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[3] Doc. #1623314, at 4 (citing cases).

banc), arguing it stands for the proposition that "the APA does not subject the United States to suits asserting state law claims, whether based on common law or state." Doc. #1624476, at 5. *El-Shifa* was a case brought by a plaintiff whose pharmaceutical factory was destroyed by United States missile attacks based on the belief the plaintiff had ties to Osama bin Laden and international terrorism. The majority of the *en banc* Court held the case should be dismissed under the political question doctrine. *El-Shifa*, 607 F.3d at 842-51. Judge Kavanaugh's concurrence opined that the case should instead have been dismissed under a doctrine allowing dismissal of claims that are "so insubstantial, implausible, foreclosed by prior decisions of this Court, or otherwise completely devoid of merit as not to involve a federal controversy." *Id.* at 852 (citation omitted). In the course of explicating this proposed ruling, Judge Kavanaugh wrote that: (a) "there is no federal cause of action for defamation available against the United States," *id.* at 853; (b) "no customary international law norm… require[s] compensation by the United States under the Alien Tort Statute for mistaken war-time bombings," *id*; (c) "the APA contains no cause of action for defamation," *id.*; and (d) while "plaintiffs might also be alleging a purported *state* common-law cause of action," their "complaint never quite says as much," and "Even so, any such state-law cause of action may not be brought against the United States absent congressional authorization to that effect." *Id.* at 854.

Only the last of these four points could have any conceivable relevance here. In making that point, Judge Kavanaugh never addresses § 702 (cited nowhere in his concurrence), and does not discuss this Court's holding in *Krc* (his concurrence cites to *Krc*, but in a prior discussion without any reference to its holding that § 702 waives immunity for state tort claims).

Regardless, Judge Kavanaugh's concurrence does not trump this Court's square holding in *Krc* that the immunity waiver in § 702 allows declaratory and injunctive claims against United States agencies based on their violation of state common law rights.

3. Treasury repeatedly argued in the District Court that Class Plaintiffs' fiduciary breach claim was "founded on a contractual relation, and thus is subject to the jurisdictional limits of the Tucker Act" – *i.e.*, it had to brought in the Court of Federal Claims as a Tucker Act claim.[4] Treasury now takes the opposite position.[5]

<u>CONCLUSION</u>

The Court should reject the arguments made by FHFA and Treasury.

[4] Doc.#1623314, at n.6.

[5] Doc.#1624476, at 2-3.

Dated: July 20, 2016

Respectfully submitted,

/s/ *Hamish P.M. Hume*

Hamish P.M. Hume
BOIES, SCHILLER & FLEXNER LLP
5301 Wisconsin Ave., NW, Suite 800
Washington, DC 20015
Tel: (202) 237-2727
Fax: (202) 237-6131

CERTIFICATE OF COMPLIANCE

Pursuant to Fed. R. App. P. 32(a)(7)(C) and this Court's Order dated June 21, 2016, I hereby certify that this brief complies with the word limitation because the text of the brief is not in excess of 2,500 words, excluding the parts exempted by Fed. R. App. P. 32(a)(7)(B)(iii).

I further certify that this brief complies with the typeface requirements of Fed. R. App. P. 32(a)(5) and the typeface style requirements of Fed. R. App. P. 32(a)(6) because the brief was prepared in 14-point Times New Roman font using Microsoft Word.

Dated: July 20, 2016

/s/ *Hamish P.M. Hume*

CERTIFICATE OF SERVICE

I hereby certify, pursuant to Fed. R. App. P. 25(c), Cir. R. 25 and this Court's Order dated June 21, 2016, the foregoing was hand-delivered to the Court and electronically filed with the Clerk of the Court using the CM/ECF system, which will send a notification to the attorneys of record in this matter who are registered with the Court's CM/ECF system.

DATED: July 20, 2016

/s/ *Hamish P.M. Hume*
Hamish P.M. Hume