IN THE UNITED STATES COURT OF FEDERAL CLAIMS

FAIRHOLME FUNDS, INC., et al.,	)	
Plaintiffs,	)	
v.	)	No. 13-465C
	)	(Judge Sweeney)
THE UNITED STATES,	)	
Defendant.	)	

PLAINTIFFS' MOTION TO AMEND THE COMPLAINT

Pursuant to Rule 15(a)(2) of the Rules of the United States Court of Federal Claims, Plaintiffs Fairholme Funds, Inc., et al., respectfully request that the Court grant Plaintiffs leave to file the proposed Second Amended Complaint submitted along with this motion. Plaintiffs propose to amend their illegal exaction claims to include the theory that the imposition of the Net Worth Sweep and quarterly Net Worth Sweep dividend payments were unauthorized because at all relevant times the Federal Housing Finance Agency ("FHFA") has been operating in violation of constitutional separation of powers principles. The proposed amendment follows a recent decision of the United States Court of Appeals for the Fifth Circuit holding that FHFA is unconstitutionally insulated from Presidential control. *See Collins v. Mnuchin*, 2018 WL 3430826, at *18 (5th Cir. July 16, 2018). Defendant opposes this motion.

QUESTION PRESENTED

Whether Plaintiffs should be permitted to amend their illegal exaction claims to include the theory that FHFA's actions in adopting and implementing the Net Worth Sweep were unauthorized because they were taken while FHFA was operating in violation of constitutional separation of powers principles.

STATEMENT OF THE CASE

1. Plaintiffs are shareholders of Fannie Mae and Freddie Mac (the "Companies"), which since 2008 have been under the control of FHFA as conservator. In August 2012, four years into the conservatorships and at a time when Fannie and Freddie were immensely profitable and poised to begin rebuilding their capital levels, FHFA and the United States Department of the Treasury imposed the "Net Worth Sweep," which had the purpose and effect of eliminating the economic interest of private shareholders in the Companies, transferring that interest to Treasury, and ensuring that Fannie and Freddie could never recapitalize and return value to their private shareholders. Indeed, Treasury itself publicly proclaimed that the Sweep was intended to ensure both that "every dollar of earnings that Fannie Mae and Freddie Mac generate will benefit taxpayers" and that the Companies "will be wound down and will not be allowed to retain profits, rebuild capital, and return to the market in their prior form." Public Redacted Amend. Compl. ¶ 10 (Mar. 11, 2018), Doc. 404. The Sweep accomplished these objectives by requiring Fannie and Freddie to send nearly their entire net worth to Treasury on a quarterly basis. To date, Fannie and Freddie have paid over $220 billion in Net Worth Sweep "dividends" to Treasury. *Id*. ¶ 115.

Plaintiffs filed suit in this Court on July 9, 2013, asserting that the Net Worth Sweep constituted a taking of Plaintiffs' property and that the Constitution therefore required the Government to pay them just compensation. The Government filed a motion to dismiss on December 9, 2013, but in that motion the Government disputed a number of material factual allegations in Plaintiffs' complaint. The Court therefore granted Plaintiffs' motion to suspend briefing on the motion to dismiss to allow Plaintiffs to take necessary discovery. The discovery process generated a number of disputes requiring this Court's intervention, and one of those

disputes led to an interlocutory appeal to the Federal Circuit. Discovery was completed in January 2018.

On March 8, 2018, Plaintiffs filed an amended complaint adding: (a) factual allegations based on discovery materials; (b) a new plaintiff; (c) additional direct claims of illegal exaction, breach of fiduciary duty, and breach of implied-in-fact contract; and (d) derivative claims on behalf of the Companies mirroring the direct claims. The Government filed its renewed motion to dismiss on August 1, 2018, Plaintiffs' response is due October 23, 2018, and the Government's reply is due January 22, 2019.

2. In addition to this action, several additional cases have been filed in this Court and other courts challenging the Net Worth Sweep. In a significant decision in one of those additional cases, the Fifth Circuit in *Collins v. Mnuchin*, 2018 WL 3430826 (5th Cir. July 16, 2018), recently held that FHFA's structure violates Article II of the Constitution because the agency is unconstitutionally insulated from Executive Branch control. The court reached this conclusion "after assessing the combined effect" of a number of FHFA's attributes, including its "single-Director leadership structure" and the Director's "for-cause removal" protection. *Id*. at *18. Rather than undoing the Net Worth Sweep, however, the court simply struck down the for-cause removal limitation prospectively. *Id*. at *26.

On August 1, 2018, a new action was filed in this Court challenging the Net Worth Sweep, *Wazee Street Opportunities Fund IV LP v. United States*, No. 18-cv-1124. The complaint in that action includes direct and derivative illegal exaction claims alleging that the Net Worth Sweep was unauthorized because it was adopted by FHFA, an unconstitutionally structured agency. *See Wazee* Compl. ¶¶ 144, 198-99.

ARGUMENT

This Court's rules provide that the Court "should freely give leave" to amend "when justice so requires," RCFC 15(a)(2), an admonition that the Supreme Court has said "is to be heeded." *Foman v. Davis*, 371 U.S. 178, 182 (1962).[1] That is because "[i]f the underlying facts or circumstances relied upon by a plaintiff may be a proper subject of relief, he ought to be afforded an opportunity to test his claim on the merits." *Id*.

Plaintiffs should be afforded the opportunity to test on the merits the Fifth Circuit's recent separation of powers ruling. While the Fifth Circuit in *Collins* declined to unwind the Net Worth Sweep, its decision indicates that the Net Worth Sweep was adopted at a time when FHFA was operating unconstitutionally and that FHFA has been operating unconstitutionally ever since. This has implications for this case, because this Court has jurisdiction to hear claims "to recover . . . exactions said to have been illegally imposed by federal officials." *Eastport S. S. Corp. v. United States*, 372 F.2d 1002, 1008 (Ct. Cl. 1967). "[T]he Tucker Act's waiver" of sovereign immunity thus "encompasses claims where the plaintiff has paid money over to the Government, directly or in effect, and seeks return of all or part of that sum." *Ontario Power Generation, Inc. v. United States*, 369 F.3d 1298, 1301 (Fed. Cir. 2004) (quotation marks omitted). That is what Plaintiffs seek here. Plaintiffs allege that the Government has, in effect, exacted Plaintiffs' stock and that the Government has Fannie and Freddie's "money in its pocket," *id*., from hundreds of billions of dollars' worth of Net Worth Sweep dividend payments. Plaintiffs seek the return of the value of their stock directly for themselves, *see Casa de Cambio*

[1] The Supreme Court in *Foman* addressed the provision on amendment in Federal Rule of Civil Procedure 15(a), but this Court's rules were designed to be "consistent with the Federal Rules of Civil Procedure." RCFC 83(a). "RCFC 15(a)" in particular "is identical to Federal Rule of Civil Procedure 15(a); thus, case law applying FRCP 15(a) also may be applicable when applying RCFC 15(a)." *Northrop Grumman Sys. Corp. v. United States*, 137 Fed. Cl. 677, 680 n.1 (2018).

Comdiv S.A. de C.V. v. United States, 48 Fed. Cl. 137, 145 (2000) ("Several cases hold that, under the illegal exaction doctrine, a plaintiff may seek the return of the monetary value of property seized or otherwise obtained by the government."), and the return of Fannie's and Freddie's money derivatively on behalf of the Companies. The new theories Plaintiffs propose to add to their illegal exaction claims simply provide additional grounds for finding that the exaction was unauthorized—namely, that FHFA has been operating in violation of the separation of powers.

The Supreme Court has identified factors that may support denying a motion to amend in certain circumstances, "such as undue delay, bad faith or dilatory motive on the part of the movant, repeated failure to cure deficiencies by amendments previously allowed, undue prejudice to the opposing party by virtue of allowance of the amendment, futility of amendment, etc." *Foman*, 371 U.S. at 182. None of these are present here, and the lack of any undue prejudice in particular demonstrates that leave to amend should be granted. "Because RCFC 15 was 'designed to facilitate the amendment of pleadings except where prejudice to the opposing party would result,' the critical factor in determining whether to allow leave to amend is if the amendment will prejudice the non-moving party." *Northrop Grumman Sys. Corp. v. United States*, 137 Fed. Cl. 677, 681 (2018) (quoting *United States v. Hougham*, 364 U.S. 310, 316 (1960)); *see also Advanced Aerospace Techs., Inc. v. United States*, 130 Fed. Cl. 564, 567 (2017) ("The most important factor is prejudice to the opposing party."). Indeed, denying leave to amend in the absence of prejudice to the opposing party "would subvert the basic purpose of the Rule." *Hougham*, 364 U.S. at 317.

Allowing Plaintiffs to amend the complaint will not prejudice the Government. "Undue prejudice may be found when an amended pleading would cause unfair surprise to the opposing

party, unreasonably broaden the issues, or require additional discovery." *Anaheim Gardens v. United States*, 2011 WL 4090899, at *6 (Fed. Cl. 2011) (quotation marks omitted). Undue prejudice has also been described as "a severe disadvantage or inability to present facts or evidence; the necessity of conducting extensive research shortly before trial due to the introduction of new evidence or legal theories; or an excessive delay that is unduly burdensome." *Hanover Ins. Co. v. United States*, 134 Fed. Cl. 51, 61–62 (2017) (quotation marks and brackets omitted). However described, undue prejudice cannot be shown here.

While this case has been pending since July of 2013, procedurally it is still in its infancy, with the Government's motion to dismiss just filed August 1. That is because the merits of this case were essentially on hold from the filing of Plaintiffs' motion for discovery in December of 2013 until the completion of that discovery in January of 2018. The parties jointly proposed that Plaintiffs file their initial amended complaint only after the completion of discovery, Joint Status Report at 10 (Feb. 24, 2017), Doc. 359, and Plaintiffs accordingly filed their first amended complaint on March 8. It has only been a few months since that time, not the "many years" of delay that typically mark the type of excessive delay that can be unduly burdensome. *Northrop Grumman Sys.*, 137 Fed. Cl. at 681.

Because this case is still in its infancy, the proposed amendment will not prejudice the parties or the Court in the least. Indeed, it need not delay resolution of the case at all. As stated above, the Government's motion to dismiss was filed August 1, 2018. We do not propose to make the Government rewrite that motion. Rather, we propose allowing the Government to move forward with its motion to dismiss and to separately move to dismiss the new illegal exaction theories by October 1, 2018. If the Government elects to file such a motion, we propose

setting our response deadline as October 23, 2018, the same date our response to the motion to dismiss is due currently. From there, the schedule can move forward as currently set.

Several other considerations reinforce the lack of any prejudice to the Government here. First, this Court's predecessor held "the need to re-brief [a] motion to dismiss . . . to merely constitute a vexing inconvenience rather than the visitation of measurable prejudice." *Effingham Cty. Bd. of Educ. v. United States*, 9 Cl. Ct. 177, 180 (1985). As just explained, here the Government will not even need to re-brief its motion, but rather will simply need to supplement that motion with another one addressed to the new theories.

Second, while additional briefing is not a substantial burden, the briefing required by Plaintiffs' amendment here will not even rise to the level of a "vexing inconvenience" for the Government. That is because the plaintiffs in *Wazee Street Opportunities Fund IV LP v. United States*, No. 18-cv-1124, are also asserting the illegal exaction theories Plaintiffs propose to add to this case. The Government will therefore be required to brief these issues regardless of whether Plaintiffs' motion is granted. In addition, the Government already has briefed and argued the separation of powers arguments underlying the new illegal exaction theories in *Collins*, 2018 WL 3430826, *Bhatti v. FHFA*, 2018 WL 3336782 (D. Minn. 2018) (currently on appeal), and *Rop v. FHFA*, No. 17-cv-497 (W.D. Mich.).[2]

Third, Plaintiffs are "merely proposing alternative legal theories for recovery on the same underlying facts," not seeking to "fundamentally alter the nature of the case." *King v. United States*, 119 Fed. Cl. 51, 56 (2014). At bottom, this case is a challenge to the Net Worth Sweep, and the proposed amendment does not change that. Indeed, the proposed alternative theories do

[2] One of the theories Plaintiffs seek to add—that Mr. DeMarco's lengthy service as Acting Director violated the Appointments Clause—was not at issue in *Collins* but is present in *Bhatti* and *Rop*.

not implicate any disputed factual issues, as the theories are predicated on the statutory insulation of FHFA from presidential control and the amount of time Acting Director DeMarco was in office when he entered the Net Worth Sweep. While the legal significance of these facts will surely be disputed, the facts themselves should not be.

Fourth, and relatedly, allowing the amendment would not "necessitate substantial and burdensome additional discovery." *Hanover Ins. Co.*, 134 Fed. Cl. at 62–63 (quotation marks omitted). Indeed, because the facts underlying Plaintiffs' new theories are not subject to reasonable dispute the amendment should not require any discovery at all.

Fifth, this is not a case in which Plaintiffs have exhibited a "repeated failure to cure deficiencies by amendments previously allowed." *Foman*, 371 U.S. at 182. To the contrary, Plaintiffs previously have requested and been allowed just a single amendment to date.

CONCLUSION

For the foregoing reasons, Plaintiffs' motion to amend their complaint should be granted. In addition, the Court should order that any motion to dismiss the new theories be filed by October 1, 2018 and that Plaintiffs respond by October 23, 2018.

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Respectfully submitted,

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