UNITED STATES COURT OF FEDERAL CLAIMS

LOUISE RAFTER, *et al.*,	)	
	)	
Plaintiffs,	)	
	)	No. 14-740C
v.	)	(Chief Judge Sweeney)
	)	
THE UNITED STATES,	)	
	)	
Defendant.	)	
	)	

PLAINTIFFS' SUPPLEMENTAL BRIEF IN OPPOSITION TO DEFENDANT'S AMENDED MOTION TO DISMISS

Dated: November 2, 2018

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PRELIMINARY STATEMENT[1]

The claims in this case all revolve around the same question: Do the Constitution and the laws of this country provide relief when the Government takes private property from profitable companies and their shareholders without compensation? The answer must be yes. Once Congress issues a charter to a corporation, it does not have the power "to take away property already acquired under the operation of the charter, or to deprive the corporation of the fruits actually reduced to possession lawfully made." *Bowen*, 477 U.S. at 55. The Government cannot hide behind the Third Amendment to the PSPAs to evade the law. *See Dimare Fresh, Inc. v. United States*, 808 F.3d 1301, 1307 (Fed. Cir. 2015) ("what is important is the nature or substance of the government's action," not "the precise form it may take").

This Supplemental Brief addresses the *Rafter* Plaintiffs' contract claims. It is beyond dispute that the Net Worth Sweep eviscerated the *Rafter* Plaintiffs' contract rights. The Net Worth Sweep turned HERA on its head, using legislation designed to support investors' confidence in the Companies as a weapon to destroy their investments. The implications of the Government's end run around its contractual (as well as its statutory and constitutional) obligations to the Companies and their shareholders are enormous. If the Government can use preferred share dividends to nationalize Fannie and Freddie without compensation, it can use the same expedient to nationalize other institutions that it regulates. In the next financial crisis, no investors will be duped into putting, or keeping, private capital in troubled financial institutions when they know that the Government can take their assets with impunity.

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[1] The *Rafter* Plaintiffs file this brief, as a supplement to the accompanying Brief in Opposition to the Defendant's Omnibus Motion to Dismiss ("**Omnibus Opposition**," or "**OB**")—which addresses the *Rafter* Plaintiffs' takings and illegal exaction claims—to address arguments that are specific to *Rafter* Second Amended Verified Complaint, filed on March 8, 2018 ("***Rafter* Complaint**" or "**¶_**"). Unless otherwise indicated, defined terms have the meaning in the OB, and short form citations are used for cases in the OB. Emphasis is added to, and internal citations and quotes are omitted from, quotations throughout this brief.

The Government leans heavily on *Perry II*, which affirmed FHFA's "stunningly broad view of its own power," characterized by the dissent as "insist[ing] its *authority is entirely without limit* and argu[ing] for a complete ouster of federal courts' power to grant injunctive relief to redress *any action* it takes while purporting to serve in the conservator role." 864 F.3d at 635 (Brown, J., dissenting). In response to the dissent's protest that "a nation governed by the rule of law cannot transfer broad and unreviewable power to a government entity to do whatsoever it wishes with the assets of these Companies," *id*., the majority maintained that its ruling did "not prevent either constitutional claims" or "cognizable actions for damages like breach of contract." *Id*. at 613-14. These are the very claims the Government now argues are unreviewable.

The Government's motion to dismiss the *Rafter* Plaintiffs' contract claims is devoid of merit. *First*, the PSPA, as amended, should be reformed to excise the Net Worth Sweep because it is unlawful (Claim IV). *Second*, the Net Worth Sweep breached the Companies' Charters, each a contract with the United States specifying the terms of the stock that investors purchased (Claims VI and VII). *Third*, the Net Worth Sweep violates Delaware corporate law, which Fannie's bylaws incorporate and which forms part of the contract between Fannie's investors and the Government (Claim V). Because these are valid contractual claims, predicated on contracts with the Government, the Government's motion to dismiss them must be denied. Having invited private investors to take ownership of the Companies, the Government cannot take away their property and breach their contractual rights without compensating them.

SUPPLEMENTAL STATEMENT OF THE CASE[2]

Plaintiffs. Louise Rafter is a retired nurse who owns 36,000 shares of Fannie common stock, some of which she purchased with her late husband over 25 years ago and has since continuously held. ¶18. Josephine and Stephen Rattien (with Louise Rafter, the "**Individual Plaintiffs**"), also retirees (she a former inner-city school counselor, he a former science and technology policy manager) jointly own 1,000 shares of Fannie common stock, which they purchased approximately 15 years ago and have since continuously held. ¶19. Pershing Square, L.P., Pershing Square II, L.P., Pershing Square Holdings, Ltd., and Pershing Square International, Ltd. ("**Funds**" and with their investment advisor Pershing Square Capital Management, L.P., "**Pershing**"), are private investment funds that together hold approximately 10% of the common stock of each Company. Each Fund began purchasing that common stock in October 2013. ¶20.

This Action. In 2008, this country faced a financial crisis, and the Government took drastic action to stabilize the housing markets. Congress passed HERA to give investors confidence to continue to invest in the Companies by demonstrating the Government's support. ¶32. Under HERA, the Government placed the Companies into conservatorship, ostensibly to restore them to "safety and soundness," and Treasury exercised its temporary authority to make the Companies draw billions from Treasury under the PSPAs. ¶¶3, 43, 45.

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[2] This Supplemental Statement of the Facts is based on allegations in the *Rafter* Complaint and documents incorporated by reference therein, which establish the factual basis of jurisdiction "by a preponderance of the evidence." *McNutt v. Gen. Motors Acceptance Corp. of Ind.*, 298 U.S. 178, 189 (1936). Because the Government disputes the sufficiency of the allegations and inferences to be drawn from them under RCFC 12(b)(1) and (6), but not the truth of the allegations, *see* MTD 21 (relying on "the amended and newly filed complaints" to argue lack of jurisdiction"), the well-plead allegations are assumed to be true for the purposes of the Government's Motion. *See Kalos v. United States*, 368 F. App'x 127, 129 (Fed. Cir. 2010).

This lawsuit does not challenge those decisions. Rather, it focuses on the Government's actions four years after the crisis, *when the housing markets were recovering and the Companies returning to profitability*. In 2012, the Government took an unprecedented action: using the fig leaf of a Third Amendment to the PSPAs, Treasury and FHFA effected the Net Worth Sweep, which gave all of the Companies' profits to Treasury forever. Although the Government has represented in court that the Net Worth Sweep was necessary to prevent a "death spiral" of increasing dividend obligations and draws under the PSPAs, discovery in the coordinated cases before this Court has shown that the Government took this action knowing the Companies were so profitable they no longer needed to borrow from Treasury (¶12) based on its own public policy preferences: to ensure "existing common equity holders" will not receive "positive earnings from [the Companies] in the future," and that the Companies can never "recapitalize," "escape" conservatorship or repay Treasury. ¶¶12, 14. The Executive Branch effectively nationalized two of the world's largest companies without asking Congress—although the statutes in place provide for the private ownership of the Companies—because the White House was afraid that any legislation to achieve its goals would be "voted down" by Congress. ¶14.

The Government's Misleading Characterization of the *Rafter* Complaint. Striving to present the Net Worth Sweep as appropriate under HERA, the Government misrepresents numerous allegations demonstrating the irreconcilability of the Net Worth Sweep and the Government's exercise of authority over the Companies in conservatorship. For example, the Government mischaracterizes the Companies' debt as debilitating. MTD 11. In fact, "by the end of 2012, both Companies were sufficiently profitable to pay the Government dividends from available cash" (¶56), and the Government's own documents and testimony confirm its acute

awareness, *before* the Third Amendment, that the Companies' profits would exceed dividends payable to Treasury. ¶67 (anticipating "convincing return to profitability"); *see also* ¶¶68-69.

The Government misrepresents the Net Worth Sweep as a benign measure to let the Companies "pay whatever dividend they could afford—however little, however much …. If Fannie and Freddie made profits, Treasury would reap the rewards; if they suffered losses, Treasury would have to forgo payment entirely." MTD 12 (ellipses in original). But replacing the PSPAs' 10% dividend with the Net Worth Sweep does not benefit the Companies "however little" or "however much" they earn: the Sweeps *always* require the Companies to pay their entire net worth to Treasury, and never permit them to build capital or repay Treasury. ¶72.

The *Rafter* Complaint refutes the Government's claim that Treasury and FHFA acted independently in negotiating the Third Amendment. MTD 25-27. Treasury was the "architect" of the Third Amendment and imposed it on the Companies (¶75), and FHFA did not advocate any alternative terms, much less secure any meaningful consideration for the Net Worth Sweep. *See* ¶¶72-77. FHFA's acquiescence in Treasury's plan was no surprise, since Treasury "had already effectively nationalized the GSEs [ ], and could decide how to carve up, dismember, sell or restructure those institutions." ¶75. Any pretense that the Net Worth Sweep and 10% dividend differ only in degree as a fair "exchange for Treasury's capital commitment" (MTD 9) is shattered by the billions more paid to Treasury under the Net Worth Sweep. ¶¶78-81.

ARGUMENT: ALL THE *RAFTER* CONTRACT CLAIMS SHOULD PROCEED

The Government's jurisdictional and substantive challenges to the *Rafter* Plaintiffs' contract claims—purported lack of privity, failure to plead a valid contract, lack of standing, or supposedly barred by HERA's succession clause—are meritless. The derivative reformation claim is based on a valid contract—the PSPA—to which the derivative plaintiff, Fannie, is party, and which was breached by conduct that exceeded the Government's authority under HERA.

The direct contract claims are likewise based on valid contracts to which the Government and shareholders are party: each Company's Charter or the contract formed by the Fannie's Charter, By-laws, and the Delaware General Corporation Laws ("**DGCL**") (the "**Fannie Contract**"). The *Rafter* Plaintiffs all have standing to assert contract claims, which do not depend on when they acquired their contractual rights. Nor does the HERA succession clause foreclose any derivative claim (including the *Rafter* Plaintiffs' derivative reformation claim) or any direct claims (including the *Rafter* Plaintiffs' direct contract claims), which the Government purports to recharacterize as derivative. All of the *Rafter* Plaintiffs' contract claims should proceed.

I. THE *RAFTER* COMPLAINT STATES A DERIVATIVE REFORMATION CLAIM

The reformation claim (Claim IV) is a derivative claim against the United States brought on behalf of Fannie by the Individual Plaintiffs based on a breach of the PSPA. ¶¶134-37. The *Rafter* Complaint alleges that the Third Amendment was unlawful, and thus void, because the Net Worth Sweep exceeded FHFA and Treasury's authority under HERA and its regulations. ¶¶135-36. The Individual Plaintiffs seek the reformation of the PSPA to excise the unlawful amendment and restitution of funds paid to the United States under the Net Worth Sweep. ¶137.

A. The Derivative Reformation Claim on behalf of Fannie Is Based on the PSPA, a Valid Contract to Which Fannie Is Party

The Government does not, and cannot, dispute this Court's well-established authority to reform an illegal contract, void an unlawful amendment, or award restitution. *See United States v. Miss. Valley Generating Co.*, 364 U.S. 520, 566 (1961) (government contract "infected by an illegal conflict" unenforceable); *Council for Tribal Emp't Rights v. United States*, 112 Fed. Cl. 231, 249 & n.17 (2013), *aff'd*, 556 F. App'x 965 (Fed. Cir. 2014) (amendments "violative of the statute ... void *ab initio*," and reforming contract). Instead, the Government argues that "the Court lacks jurisdiction" over the reformation claim or fails to plead "a valid contract between

the parties" because the *Rafter* Plaintiffs are not in contractual privity with the Government. MTD 41-42, 75. This argument misses its mark because the reformation claim is derivative, not direct, and Fannie, on whose behalf the claim is asserted, is a party to the PSPA with Treasury, and thus in contractual privity with the Government. *See First Hartford*, 194 F.3d at 1292 (where a shareholder files a derivative claim on behalf of contracting corporation, the "entity stands within privity"); RCFC Rule 23.1.

B. The Reformation Claim Is Supported by Allegations That Treasury and FHFA Acted Beyond Their HERA Authority

Alternatively, the Government argues (MTD 77) that the reformation claim fails because the *Rafter* Plaintiffs' cannot establish that the Net Worth Sweep exceeded the Government's legal authority. Not so. Allegations demonstrating exactly how the Treasury and FHFA exceeded their authority—under HERA, its rules, and the Constitution—are detailed in the Omnibus Opposition, including allegations not addressed by the non-controlling, non-binding authorities that the Government cites. *See* OB 58-66; *see, e.g.*, ¶¶34-39, 44, 55, 60-62, 127-29.

II. THE DIRECT BREACH OF CHARTER CLAIMS ARE BASED ON VALID CONTRACTS (CLAIMS VI AND VII)

The *Rafter* Plaintiffs assert claims for breach of the implied covenant of good faith and fair dealing in the Company's Charters. ¶¶154-69. The Charters are contracts between the Government, the Companies, and their shareholders, including the *Rafter* Plaintiffs. *See Trs. of Dartmouth Coll. v. Woodward*, 17 U.S. 518, 595 (1819). Shareholders invested in the Companies' stock in reliance on the Charters, which vested common stockholders with a right to share in the Companies' earnings and their residual value. ¶¶156, 164; 12 U.S.C. §§1453(a), 1718(a), 1719(g)(1)(C)(v). Those investments allowed the Government to advance its goal, enumerated in the Charters, of ensuring that the secondary residential mortgage market "shall be financed by private capital to the maximum extent feasible." *Id.* §1716. *See id.* §1451 (note).

But the Government has not honored its bargain. Instead of permitting common stockholders to enjoy their contractual interest in the Companies' net worth, the Government breached those rights by diverting all of the Companies' capital to Treasury. *See Centex Corp. v. United States*, 395 F.3d 1283, 1305, 1311 (Fed. Cir. 2005) ("government breached the implied covenant" by enacting an amendment which "depriv[ed] its contracting partners of … the fruits of the contract and appropriat[ed] those fruits, *pro tanto*, to itself"); *United States v. Winstar Corp.*, 518 U.S. 839, 868-70 (1996) (government contract impliedly promised that the government would "insure the promise against loss" from a breach due to change in law).

The Government's sole substantive challenge to these claims is to invoke the rebuttable "presumption," described in *Moda Health Plan, Inc. v. United States*, 892 F.3d 1311, 1329 (Fed. Cir. 2018) (MTD 41, 76), that "a law is not intended to create private contractual or vested rights." To be sure, that presumption exists—but it does not apply to corporate charters. On the contrary, as the Supreme Court's seminal *Dartmouth College* decision held, a charter is a constitutionally protected contract between the chartered entity's owners and the issuing government. 17 U.S. at 595 ("the charter ... is a contract ... mutual in its considerations, express and formal in its terms").[3]

That this well-established rule applies to the Charters has been confirmed by the United States itself. In a 1977 opinion, the Office of Legal Counsel answered in the affirmative the question, "Did the charter granted to [Fannie] by the Government create contractual rights

[3] *See also The Sinking-Fund Cases*, 99 U.S. 700 (1878) (construing railroad charter as a contract); *D.C. v. Metro. R.R. Co.*, 8 App. D.C. 322, 340-41 (D.C. Cir. 1896) (railroad charter is "a contract between the government and the grantee"); *Helvering v. N.W. Steel Rolling Mills, Inc.*, 311 U.S. 46, 51 (1940) ("an act of incorporation is a contract between the state and the stockholders"); *In re Binghamton Bridge*, 70 U.S. 51, 73 (1865) ("an unbroken course of decisions" hold "an act of incorporation [is] a contract between the State and the stockholders;" "every successful enterprise is undertaken, in the unshaken belief that it will never be forsaken").

between the Government, [Fannie], and the stockholders?" 1 Op. Off. Legal Counsel 126, 126-27, 1977 WL 18036 (June 3, 1977) (citing *Dartmouth College*). Although such opinions are "binding on the Department of Justice," *Tenaska Wash. Partners II, L.P. v. United States*, 34 Fed. Cl. 434, 440 (1995), the Government now argues that Fannie's Charter is not a contract but without explaining its departure from the 1977 opinion or *Dartmouth College*.

None of the cases cited by the Government (MTD 76) to argue that the Charters are not contracts deal with corporate charters. *Moda*, 892 F.3d at 1330, concluded that programs described in the Affordable Care Act and implemented by regulations did not create contracts. *Brooks v. Dunlop Manufacturing Inc.*, 702 F.3d 624, 630-32 (Fed. Cir. 2012), declined to treat a *qui tam* provision as a contract. And *National Rail Road Corp. v. Atchison Topeka & Santa Fe Railway. Co.*, 470 U.S. 451, 470 (1985), concluded that the legislation that created Amtrak did not create a contract between the United States and *other* private railroads that contracted with Amtrak. That these authorities have no bearing on corporate charters is confirmed by *Bowen*, which expanded on *National Rail Road* by contrasting amendments to the Social Security Act (which did not create contracts) with corporate charters, which expressly create rights "held to constitute 'property' within the meaning of the Fifth Amendment." 477 U.S. at 53-56.

Because the Charters are valid, enforceable contracts, the Government's motion to dismiss claims based on the Charters should be denied.

III. THE *RAFTER* PLAINTIFFS' CLAIM FOR BREACH OF THE FANNIE CONTRACT SHOULD PROCEED BECAUSE THE UNITED STATES IS A PARTY (CLAIM V)

Rafter Claim V asserts a breach of the Fannie Contract, which is an agreement formed by Fannie's Charter, By-laws, and the DGCL. Not only is Fannie's Charter a contract between the Government, Fannie, and Fannie's shareholders (¶140; *supra* §II), but the Charter, By-laws, and the DGCL also form an enforceable contract among Fannie, its directors, officers and

shareholders under Delaware law, which is applicable to Fannie under its By-laws. *See* ¶141; *Boilermakers Local 154 Ret. Fund v. Chevron Corp.*, 73 A.3d 934, 940 (Del. Ch. 2013) ("bylaws, together with the certificate of incorporation and the broader DGCL, form part of a flexible contract between corporations and stockholders") (citing *Centaur Partners, IV v. Nat'l Intergroup, Inc.*, 582 A.2d 923, 928 (Del. 1990)). Thus, the Government, Fannie, and its directors, officers and shareholders all are party to the Fannie Contract.

The Government does not dispute the existence of the Fannie Contract. Nor does the Government challenge Claim V's allegations (¶¶143-51) that it breached the Fannie Contract by agreeing to the Net Worth Sweep, which gives one shareholder (Treasury) all of Fannie's net worth and residual value and pays it dividends that are not "at [ ] rates" and "in … relation to" dividends payable to other shareholders. *Contra* 8 DEL. C. §§151(c), 159. Rather, the Government's motion to dismiss Claim V depends on its argument that the United States is not party to the Fannie Contract. MTD 41, 75. That argument should be rejected. The Government became party to the Fannie Contract when FHFA succeeded to "all rights, titles, powers, and privileges" of Fannie under HERA's succession clause. 12 U.S.C. §4617(b)(2). Further, as set forth in the Omnibus Opposition at 10-19, FHFA exercised its succession powers on behalf of the United States to bind Fannie, as a federal instrumentality, to the Net Worth Sweep. Moreover, the Fannie Charter, to which the Government is party under *Dartmouth College*, 17 U.S. at 595, is part of the Fannie Contract. *See Boilermakers Local 154*, 73 A.3d at 940; *supra* §II. Because the Government is party to the Fannie Contract, Claim V states a claim.

IV. THE *RAFTER* PLAINTIFFS HAVE STANDING TO BRING THEIR DIRECT CONTRACT CLAIMS (CLAIMS V, VI AND VII)

The Government disputes that any Plaintiffs who purchased Company stock "after the Third Amendment" have standing to bring contract claims. This argument has no application to

the direct contract claims (Claims V and VI) brought by the Individual Plaintiffs who have owned Fannie stock since long before the Net Worth Sweep. *See* ¶¶18-19. Nor, as a matter of law, does the argument warrant dismissal of the corresponding claims by Pershing (Claims V, VI and VII), which acquired its shares of Fannie and Freddie on and after October 7, 2013. *See* ¶20.

Delaware law—which is applicable to Fannie under its By-laws (¶141), and which guides Virginia law applicable to Freddie under its By-laws[4]—makes it clear that "a Charter Violation claim transfers to a later purchaser because the injury is to the stock and not the holder." *Schultz v. Ginsburg*, 965 A.2d 661, 667-68 (Del. 2009) ("[U]nder a Charter Violation claim, the Buyer [of the stock] would suffer the injury."). The contract rights at issue are embedded in the securities pursuant to 6 Del. C. § 8-302, which provides that the "purchaser … acquires all rights in the security that the transferor had or had power to transfer." *See In re Activision Blizzard, Inc. Stockholder Litig.*, 124 A.3d 1025, 1050 (Del. Ch. 2015) ("When a share of stock is sold, the property rights associated with the shares … travel with the shares.").

Delaware's rule is consistent with federal law, such as the statute addressed in *Whitney v. Butler*, 118 U.S. 655, 657-58 (1886), under which "all the rights and liabilities" associated with shares transfer to current shareholders. It is also the general rule applied by other states. *E.g.*, *Zahn v. Transamerica Corp.*, 162 F.2d 36, 49 (3d Cir. 1947) (Kentucky, like "other States," follows Delaware in not requiring a stockholder with a direct claim to "allege ownership of his shares at the time … of the events complained of"); *FDIC v. Citibank N.A.*, 2016 WL 8737356, at *5 (S.D.N.Y. Sept. 30, 2016) (New York law follows Delaware: "claims and rights travel with

[4] Freddie By-laws §1.1, *available at* http://www.freddiemac.com/governance/pdf/bylaws.pdf. Courts interpreting Virginia corporate law often look to Delaware corporate law for guidance. *See Milstead v. Bradshaw*, 43 Va. Cir. 428 (1997) (noting Delaware law is "persuasive authority").

the shares"); 12B FLETCHER CYC. CORP. §5936.10 (2018) (modern "cases generally hold" that shareholders with direct claims are "not required to have owned stock at the time").

There is a strong public policy animating the rule that claims travel with shares: it aligns the interests of current shareholders—who benefit indirectly from any company recovery—and the company. If claims remained with former shareholders, their interests would be pitted against the company's competing claims to recover for the same misconduct. This Court rejected such a rule in *Slattery v. United States*, which concluded under a federal receivership statute—which HERA tracks, *compare* 12 U.S.C. §1821(d)(11)(A)(v) *with* 12 U.S.C. §4617(c)(1)(D)—that a damages award for breach of contract should be distributed to current shareholders, not those who held shares at the time of the breach. 102 Fed. Cl. 27, 29-30 (2011), *aff'd*, 710 F.3d 1336 (Fed. Cir. 2013). The public policy considerations are even greater here: since the Net Worth Sweep is an ongoing harm, every new dividend affects current shareholders.

The Government identifies no authority supporting its position that contract claims do not travel with the shares. Most of the Government's cases deal with takings claims, not breach of contract (MTD 46-47), addressed in the Omnibus Opposition at 39-40. The Government cites only one contract case, *Scott Timber Co.*, 692 F.3d at 1372 (MTD 47), which stands for the uncontroversial—but irrelevanOBt—proposition that a covenant of good faith and fair dealing would not take effect "where a valid contract has not yet been formed." Because the contractual property rights under the Charters and the Fannie Contract "traveled with" the shares, Pershing has standing to assert its contract claims.

V. THE SUCCESSION CLAUSE CANNOT BAR THE *RAFTER* PLAINTIFFS' DIRECT CONTRACT CLAIMS (CLAIMS V, VI, AND VII)

Finally, the Government strains to extend its flawed argument that HERA's succession clause bars all derivative claims to all of the Plaintiffs' direct claims—including *Rafter* Claims

V, VI, and VII—which the Government deems "[s]ubstantively derivative." MTD 29. Under binding Federal Circuit precedent, the succession clause does not even bar derivative claims because FHFA is subject to a well-plead and disabling conflict of interest. *See First Hartford*, 194 F.3d at 1294-95; OB 25-31. But even assuming the succession clause did bar derivative claims (it does not), each of the direct *Rafter* contract claims "can prevail without showing an injury to the corporation," *Agostino v. Hicks*, 845 A.2d 1110, 1122 (Del. Ch. 2004), and is therefore direct, not derivative, under applicable federal, Delaware and Virginia law.

Although federal and Delaware law have established tests for distinguishing between direct and derivative claims,[5] the Virginia Supreme Court has reserved on that issue. *See Remora Invs., LLC v. Orr*, 673 S.E.2d 845, 848 (Va. 2009). But all three bodies of law agree that "a suit by a party to a commercial contract to enforce its own contractual rights is not a derivative action under Delaware law." *El Paso Pipeline GP Co. v. Brinckerhoff*, 152 A.3d 1248, 1259 (Del. 2016).[6]

The *Rafter* Plaintiffs' direct contract claims are exactly that. These claims can prevail even if the Court concludes that the Net Worth Sweep did *not* harm the Companies because they are based on injuries to shareholders arising from the dividends paid to Treasury. Claim V seeks to vindicate the *Rafter* Plaintiffs' own contractual rights regarding how Fannie's profits are distributed between different groups of shareholders under DGCL §§151(c) and 159. ¶¶138-54.

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[5] *See Starr II*, 856 F.3d at 966 ("federal and Delaware law distinguish between derivative and direct actions" based on whether the corporation or the shareholder has a "direct interest"); *Franchise Tax Bd. v. Alcan Aluminium Ltd.*, 493 U.S. 331, 336 (1990) ("a shareholder with a direct, personal interest in a cause of action [is allowed] to bring suit even if the corporation's rights are also implicated").

[6] *See Fairholme Funds, Inc.*, 2018 WL 4680197, at *10 (class plaintiff-shareholders stated a direct "claim for breach of the implied covenant" in the stock certificates); *Remora*, 673 S.E.2d at 848 (dismissing direct shareholder claims for breach of duties not within the operating agreement, but recognizing that shareholders and corporations "are free to" "vary commercial rules by contract").

Claims VI and VII likewise seek to vindicate the *Rafter* Plaintiffs' own implied contractual rights under the Charters benefit from the Companies' net worth and residual value. ¶¶154-69.

The *Rafter* Claims V-VII do not seek relief that is identically beneficial to the Companies or all shareholders proportionally. The Companies' controlling preferred shareholder, Treasury, cannot be entitled to recover for the Government's breach of contractual duties owed exclusively to common shareholders and which benefitted Treasury alone. *See Lipton v. News Int'l, Plc,* 514 A.2d 1075, 1078 (Del. 1986) ("a plaintiff … may maintain an individual action if he complains of an injury distinct from that suffered by other shareholders"). The *Rafter* Plaintiffs' direct contract claims seek only to recover for their separate and distinct injuries as individual common shareholders for the consequences of these breaches. *See Rafter* Complaint p. 66 (seeking "[o]n Claims V, VI, and VII, … damages, disgorgement, restitution or appropriate other relief").

The Government cites cases challenging the Net Worth Sweeps on other theories in other jurisdictions, trying to show that claims by the Companies' shareholders are uniformly treated as derivative (MTD 27-32)—but the cases are to the contrary. *Perry II* held that "contract-based claims are obviously direct ... because they assert that the Companies breached contractual duties owed to the [shareholder] class plaintiffs by virtue of their stock certificates." 864 F.3d at 626, 628 (but holding fiduciary claim "that did not seek relief that would accrue directly" was derivative). *Roberts* concluded that a rescission claim was derivative, but that claim—unlike *Rafter* Claims V, VI, and VII—concerned "a contract between the *companies* and Treasury." 889 F.3d at 409 (emphasis in original). Similarly, *Saxton* lumped contract claims based on the "expropriation of stock value" in with other claims it held were derivative, but only after noting that the plaintiffs sought relief that "accrues [only] to the GSEs." 245 F. Supp. 3d at 1072-73.

The other cases cited by the Government (MTD 27-32) do not involve claims by shareholders seeking to vindicate their *own* rights for their *own* injuries under their *own* contracts—and, tellingly, they do recognize that such claims are direct and give rise to individual damages. *See, e.g.*, *Holland v. United States*, 59 Fed. Cl. 735, 737, 741 (2004) (shareholder plaintiffs "asserting *their* contract rights" can "directly pursue" damages from an injury "separate and distinct" from the corporation's) (emphasis in original); *Hometown Fin. Inc. v. United States*, 56 Fed. Cl. 477, 486 (2003) (shareholder plaintiffs could recover restitution on contract claim, but not "expectancy damages" that "must flow through the corporation"); *Tooley*, 845 A.2d at 1034-35 (claim based on the directors' breach of fiduciary duties was "purely derivative" where plaintiffs had "no … contractual right that had ripened"); *Cowin v. Bresler*, 741 F.2d 410, 416 (D.C. Cir. 1984) (distinguishing derivative mismanagement claims from direct claims by "a stockholder with a *contractual right*") (emphasis in original); *In re Ionosphere Clubs, Inc.*, 17 F.3d 600, 604-05 (2d Cir. 1994) (claims from injuries to the corporation are derivative; declining to consider "potentially direct" claims based breach of agreements not raised below).[7]

None of the *Rafter* Plaintiffs' direct contract claims are "substantively derivative," and the Government's motion to dismiss them as derivative claims barred by the succession clause—despite FHFA's conflict of interest—must be denied.

CONCLUSION

For the reasons set forth above and in the Omnibus Opposition, the *Rafter* Plaintiffs respectfully request that Government's motion to dismiss their claims be denied.

[7] The remaining authorities cited by the Government (MTD 27-32) are otherwise unavailing. *See, e.g.*, *NAF Holdings, LLC v. Li & Fung (Trading) Ltd.*, 118 A.3d 175, 176 (Del. 2015) (claim based on a commercial contract direct, not derivative); *El Paso*, 152 A.3d at 1255, 1261 (claim commenced as a derivative action but extinguished by merger held "exclusively derivative" because plaintiff "presented evidence of harm *only* as to the partnership, not to the individual unitholders"); *Pareto*, 139 F.3d at 699 (allegations that "directors breached their duties of care" to the bank "describe a direct injury to the bank," not stockholders).

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