UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF PENNSYLVANIA

WAZEE STREET OPPORTUNITIES FUND IV, LP, *et al.*, Plaintiffs, v. THE FEDERAL HOUSING FINANCE AGENCY, *et al.*, Defendants.	Case No. 2:18-cv-03478-NIQA

MOTION OF DEFENDANTS FEDERAL HOUSING FINANCE AGENCY AND MELVIN L. WATT TO DISMISS THE COMPLAINT

Defendants the Federal Housing Finance Agency ("FHFA") and Melvin L. Watt (together, the "FHFA Defendants"), hereby move this Court to dismiss with prejudice the Complaint. The bases for this Motion are set forth in the accompanying Memorandum of Law in support thereof.

WHEREFORE, FHFA Defendants respectfully request that the Court grant their Motion to Dismiss the Complaint. A proposed order is attached.

Dated: November 16, 2018

Respectfully submitted,

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MEMORANDUM OF LAW IN SUPPORT OF FHFA DEFENDANTS' MOTION TO DISMISS

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TABLE OF CONTENTS

INTRODUCTION 1

FACTUAL AND PROCEDURAL BACKGROUND 2

A. Fannie Mae, Freddie Mac, and FHFA 2

B. The Conservatorships and Preferred Stock Purchase Agreements 3

C. The Designation of Edward DeMarco as Acting FHFA Director and Unsuccessful Nomination of Joseph Smith for FHFA Director 4

D. The Third Amendment to the Preferred Stock Purchase Agreements 5

E. The Nomination and Confirmation of FHFA Director Watt 6

F. This Litigation 6

ARGUMENT 8

I. The Court Should Dismiss Plaintiffs' Constitutional challenges to FHFA's Structure 8

A. Plaintiffs Lack Article III Standing 8

1. Plaintiffs' Alleged Injury Is Not Traceable to the Alleged Constitutional Violation 9

2. Plaintiffs Cannot Show That Their Alleged Injury Would Be Redressed by Declaring the Removal Restriction Unconstitutional 12

B. FHFA's Structure as an Independent Agency Is Constitutional 15

1. Longstanding Supreme Court Precedent Endorses Independent Agencies 15

2. Plaintiffs' Efforts to Manufacture an Exception Are Unavailing 16

C. FHFA's Funding Mechanism and Limitations From Judicial Review Raise No Constitutional Issues 20

II. The Court Should Dismiss Plaintiffs' Appointments Clause Claim 22

A. Plaintiffs Lack Standing 24

B. The *De Facto* Officer Doctrine Bars Plaintiffs' Six-Years-Late Appointments Clause Challenges 26

C. Plaintiffs' Appointments Clause Claims Are Meritless 28

III. The Court Should Dismiss Plaintiffs' Nondelegation Claims 32

IV. HERA's Shareholder-Rights Provision Bars Plaintiffs' Claims 36

CONCLUSION 36

CERTIFICATE OF SERVICE 1

TABLE OF AUTHORITIES

Page(s)

Cases

Am. Fed'n of Gov't Emps., AFL-CIO, Local 1647 v. FLRA,
388 F.3d 405 (3d Cir. 2004)....................21

Andrade v. Lauer,
729 F.2d 1475 (D.C. Cir. 1984)....................27

Ass'n of Am. R.Rs. v. U.S. Dep't of Transp.,
721 F.3d 666 (D.C. Cir. 2013), *rev'd on other grounds*, 135 S. Ct. 1225 (2015)....................34

Bhatti v. FHFA,
--- F. Supp. 3d ----, 2018 WL 3336782 (D. Minn. July 6, 2018).................... *passim*

Buckley v. Valeo,
424 U.S. 1 (1976)....................25

In re Burlington Coat Factory Sec. Litig.,
114 F.3d 1410 (3d Cir. 1997)....................12

Campbell v. OPM,
694 F.2d 305 (3d Cir. 1982)....................22

Carter v. Carter Coal Co.,
298 U.S. 238 (1936)....................34

CFPB v. All Am. Check Cashing, Inc.,
No. 3:16-cv-356 (S.D. Miss. Mar. 21, 2018), *interlocutory appeal docketed*, No. 18-60302 (5th Cir.) 16

CFPB v. CashCall, Inc.,
2016 WL 4820635 (C.D. Cal. Aug. 31, 2016), *appeal docketed*, No. 18-55479 (9th Cir.)....................17

CFPB v. D&D Mktg.,
2016 WL 8849698 (C.D. Cal. Nov. 17, 2016), *appeal docketed*, No. 17-55709 (9th Cir.)....................17

CFPB v. Future Income Payments, LLC,
252 F. Supp. 3d 961 (C.D. Cal. 2017), *vacated on other grounds*, No. 17-55721 (9th Cir. Oct. 18, 2018) 16

CFPB v. ITT Educ. Servs., Inc.,
219 F. Supp. 3d 878 (S.D. Ind. 2015) 15, 17, 21

CFPB v. Morgan Drexen, Inc.,
60 F. Supp. 3d 1082 (C.D. Cal. 2014) 17, 21, 22

CFPB v. Nationwide Biweekly Admin., Inc.,
2017 WL 3948396 (N.D. Cal. Sept. 8, 2017), *appeal docketed*, No. 18-15887
(9th Cir.) 16, 21

CFPB v. Navient Corp.,
2017 WL 3380530 (M.D. Pa. Aug. 4, 2017) 16, 18, 20, 21

CFPB v. RD Legal Funding, LLC,
--- F. Supp. 3d ----, 2018 WL 3094916 (S.D.N.Y. June 21, 2018), *appeal docketed*, No. 18-02743 (2d Cir.) 17

CFPB v. Seila Law LLC,
No. 8:17-cv-01081, 2017 WL 6536586 (C.D. Cal. Aug. 25, 2017) 16, 21

CFPB v. TCF Nat'l Bank,
2017 WL 6211033 (D. Minn. Sept. 8, 2017) 16

CFPB v. Think Fin., LLC,
2018 WL 3707911 (D. Mont. Aug. 3, 2018) 16, 21

Collins v. Mnuchin,
--- F.3d ----, 2018 WL 5928985 (5th Cir. Nov. 12, 2018) 7

Collins v. Mnuchin,
896 F.3d 640 (5th Cir. 2018) 7

Comm. for Monetary Reform v. Bd. of Governors of Fed. Reserve Sys.,
766 F.2d 538 (D.C. Cir. 1985) 9

Constitution Party of Pa. v. Cortes,
712 F. Supp. 2d 387 (E.D. Pa. 2010) 8

DiFelice v. Aetna U.S. Healthcare,
346 F.3d 442 (3d Cir. 2003) 4

Doolin Sec. Sav. Bank v. OTS,
139 F.3d 203 (D.C. Cir. 1998) 32

Free Enterprise Fund v. PCAOB,
561 U.S. 477 (2010) 13, 15

Grocery Mfrs. Ass'n v. EPA,
693 F.3d 169 (D.C. Cir. 2012) 12

Herron v. Fannie Mae,
861 F.3d 160 (D.C. Cir. 2017) 14

Humphrey's Executor v. United States,
295 U.S. 602 (1935) 15, 17

Jacobs v. FHFA,
No. 17-3794, --- F.3d ----, 2018 WL 5931515 (3d Cir. Nov. 14, 2018) .... *passim*

John Doe Co. v. CFPB,
849 F.3d 1129 (D.C. Cir. 2017) 13

Lucia v. SEC,
138 S. Ct. 2044 (2018) 25

People of the State of Illinois ex rel. Madigan v. CMK Invs., Inc.,
2015 WL 4038896 (N.D. Ill. June 30, 2015) 17

In re McNeil Consumer Healthcare,
877 F. Supp. 2d 254 (E.D. Pa. 2012) 12

Meridian Invs., Inc. v. Fed. Home Loan Mortg. Corp.,
855 F.3d 573 (4th Cir. 2017) 14

Metro. Wash. Airports Auth. v. Citizens for Abatement of Aircraft Noise, Inc.,
501 U.S. 252 (1991) 8

Milk Indus. Found. v. Glickman,
132 F.3d 1467 (D.C. Cir. 1998) 35

Mistretta v. United States,
488 U.S. 361 (1989) 33, 35

Morrison v. Olson,
487 U.S. 654 (1988) 15

N.J. Physicians, Inc. v. President of U.S.,
653 F.3d 234 (3d Cir. 2011) 8

Nat'l Broad. Co. v. United States,
319 U.S. 190 (1943) 35

NLRB v. SW Gen., Inc.,
137 S. Ct. 929 (2017) 23, 28

Pennsylvania v. New Jersey,
426 U.S. 660 (1976) ... 12

Perry Capital LLC v. Mnuchin,
864 F.3d 591 (D.C. Cir. 2017) ... 3, 7, 14, 35

U.S. ex rel. Petras v. Simparel, Inc.,
857 F.3d 497 (3d Cir. 2017) ... 14

PHH Corp. v. CFPB,
881 F.3d 75 (D.C. Cir. 2018) ... *passim*

Pittston Co. v. United States,
368 F.3d 385 (4th Cir. 2004) ... 34

Roberts v. FHFA,
889 F.3d 397 (7th Cir. 2018) ... 7

Robinson v. CFPB,
2017 WL 497605 (M.D. Pa. Feb. 7, 2017), *aff'd on other grounds*, 689 F. App'x 151 (3d Cir. May 22, 2017) ... 16

Robinson v. FHFA,
876 F.3d 220 (6th Cir. 2017) ... 7

Saxton v. FHFA,
901 F.3d 954 (8th Cir. 2018) ... 7, 14, 35

SW Gen., Inc. v. NLRB,
796 F.3d 67 (D.C. Cir. 2015), *aff'd on other grounds*, 137 S. Ct. 929 ... 27, 28

Swan v. Clinton,
100 F.3d 973 (D.C. Cir. 1996) ... 16

United States v. Berberena,
694 F.3d 514 (3d Cir. 2012) ... 33

United States v. Bozarov,
974 F.2d 1037 (9th Cir. 1992) ... 22

United States v. Eaton,
169 U.S. 331 (1898) ... 23

Wiener v. United States,
357 U.S. 349 (1958) ... 15

Yakus v. United States,
321 U.S. 414 (1944) ... 35

Constitutional Provisions

U.S. CONST. art. II, § 2, cl. 2 ....23, 29

U.S. CONST. art. II, § 2, cl. 3 30

Rules & Statutes

5 U.S.C.
§ 701(a)(1) 22
§ 701(a)(2) 22
§ 3345(a)(2) 28
§ 3345(a)(3) 28

12 U.S.C.
§ 1455(*l*)....................3, 36
§ 1719(g)....................3, 36
§ 4511....................2
§ 4512(b)(1) 2
§ 4512(b)(2) 2, 11, 12, 14
§ 4512(c) 3
§ 4512(d) 3
§ 4512(f).................... *passim*
§ 4516(a) 3
§ 4516(f)(2)....................3
§ 4617(a)(2) 3, 35
§ 4617(a)(7) 3
§ 4617(b)(2)(A)(i)....................36
§ 4617(b)(2)(D)(ii)....................35

15 U.S.C.
§ 41 (1934)....................19

5th Cir. R. 41.3....................7

Federal Vacancies Reform Act, 5 U.S.C. § 3345 *et seq*. 23, 24, 31

Congressional Record

156 Cong. Rec. S11071 (Dec. 22, 2010) 4

156 Cong. Rec. S7911 (Nov. 15, 2010)....................4

159 Cong. Rec. S5799 (July 18, 2013) 6

159 Cong. Rec. S7706 (Oct. 31, 2013)....................6

159 Cong. Rec. S8417 (Nov. 21, 2013)....................6

159 Cong. Rec. S8593 (Dec. 10, 2013) 6

S. Rep. No. 105-250 (1998) 31

Other Authorities

Acting Officers, 6 Op. O.L.C. 119 (1982) 26

Dep't of Energy--Appointment of Interim Officers--Dep't of Energy Org. Act, 2 Op. O.L.C. 405 (1978) 26

Designation of Acting Solicitor of Labor, 2002 WL 34461082 (O.L.C. Nov. 15, 2002) 31

INTRODUCTION

In this case, shareholders of Fannie Mae and Freddie Mac, which are government-chartered financial institutions under the conservatorship of the Federal Housing Finance Agency, seek to undo a 2012 amendment to a preferred stock agreement with the U.S. Department of Treasury through which Treasury has infused hundreds of billions of taxpayer dollars into those companies since the 2008 financial crisis. Plaintiffs allege that the 2012 amendment, known as the Third Amendment, "expropriated" their own investments in the companies—despite the fact that two of the Plaintiffs did not even buy their stock until years thereafter.

Here, Plaintiffs do not assert claims directly attacking the merits of the Third Amendment, a strategy that has already been tried and failed in prior shareholder lawsuits rejected by numerous courts. *See*, *e.g.*, *Jacobs v. FHFA*, No. 17-3794, --- F.3d ----, 2018 WL 5931515 (3d Cir. Nov. 14, 2018). Rather, Plaintiffs bring constitutional claims challenging FHFA's structure as an independent agency and the authority of its leadership to agree to the Third Amendment in 2012.

Plaintiffs' claims are without merit and should be dismissed. Indeed, a district court hearing another Third Amendment lawsuit recently rejected precisely the same claims in a thorough and well-reasoned opinion. *Bhatti v. FHFA*, --- F. Supp. 3d ----, 2018 WL 3336782 (D. Minn. July 6, 2018). Plaintiffs lack Article III standing to bring their primary claim—that FHFA's structure as an independent agency is unconstitutional—for several reasons, not least that prevailing on that claim would not undo the Third Amendment and thus would not redress their purported injury. In any event, FHFA's structure is plainly constitutional under longstanding Supreme Court jurisprudence upholding independent agencies. The Court should reject Plaintiffs' invitation to create new exceptions to that precedent.

Plaintiffs' other counts are equally devoid of merit. Plaintiffs contend that the Third Amendment is invalid because it was approved by an Acting Director of FHFA who Plaintiffs say had served too long in violation of the Appointments Clause. But that claim fails for a multitude of reasons, including that Plaintiffs again lack standing, the *de facto* officer doctrine bars attacks on the validity of a government official's service six years after the fact, and no judicial precedent supports it on the merits. Plaintiffs' claims that Congress unconstitutionally delegated legislative power to FHFA also fail. The Third Amendment was not an exercise of legislative power and, in any event, the statute governing FHFA provides ample intelligible principles to satisfy the Supreme Court's undemanding standard for nondelegation claims. The Court should dismiss all of Plaintiffs' claims with prejudice.

FACTUAL AND PROCEDURAL BACKGROUND

A. Fannie Mae, Freddie Mac, and FHFA

Fannie Mae and Freddie Mac (the "Enterprises") were chartered by Congress to provide liquidity to the mortgage market by purchasing residential loans. (Compl. ¶ 11.) "By buying mortgages and then guaranteeing the resulting securities, Fannie and Freddie make the mortgage market both more liquid and more stable." *Jacobs*, 2018 WL 5931515, at *1.

"In July 2008, in response to the crisis in the housing and mortgage markets," (Compl. ¶ 14), Congress enacted the Housing and Economic Recovery Act of 2008 ("HERA"), Pub. L. No. 110-289, 122 Stat. 2654, 2661 (codified at 12 U.S.C. § 4511 *et seq.*). HERA created a new agency, FHFA, to supervise and regulate the Enterprises. 12 U.S.C. § 4511; *see also* (Compl. ¶¶ 14-15). Congress provided that FHFA would be headed by a Director appointed by the President and confirmed by the Senate to serve "for a term of 5 years, unless removed before the end of such term for cause by the President." 12 U.S.C. § 4512(b)(1)-(2); *see also* (Compl. ¶ 15). Congress also provided that FHFA would be funded through assessments on Fannie Mae

and Freddie Mac rather than congressional appropriations. 12 U.S.C. § 4516(a), (f)(2); *see also* (Compl. ¶ 15).

Congress provided that FHFA would have three Deputy Directors. 12 U.S.C. § 4512(c)-(e). To ensure continuity of agency operations during a vacancy in the office of Director, Congress empowered "the President [to] designate [a Deputy Director] to serve as acting Director until . . . the appointment of a successor pursuant to subsection (b)." *Id.* § 4512(f). Congress did not limit how long a Deputy Director could serve as acting Director, nor did it put any restrictions on the President's power to withdraw such a designation.

Congress authorized FHFA to place the Enterprises in conservatorship "for the purpose of reorganizing, rehabilitating, or winding up [their] affairs." *Id.* § 4617(a)(2). Congress provided that when acting as conservator, FHFA "shall not be subject to the direction or supervision of any other agency of the United States or any State." *Id.* § 4617(a)(7). HERA further authorized Treasury to purchase securities from the Enterprises to "provide stability to the financial markets," "prevent disruptions in the availability of mortgage finance," and "protect the taxpayer." *Id.* §§ 1455(*l*), 1719(g).

B. The Conservatorships and Preferred Stock Purchase Agreements

"In 2008, the collapse of the housing market cost Fannie and Freddie billions of dollars, threatening the U.S. mortgage markets." *Jacobs*, 2018 WL 5931515, at *2. In September 2008, FHFA accordingly placed the Enterprises into conservatorships. (Compl. ¶¶ 16-17.) Simultaneously, Treasury used its new authority under HERA to "commit[]to promptly invest billions of dollars in Fannie and Freddie to keep them from defaulting." *Perry Capital LLC v. Mnuchin*, 864 F.3d 591, 601 (D.C. Cir. 2017). Specifically, Treasury entered into preferred

stock purchase agreements with the Enterprises. *See* Amended & Restated Senior Preferred Stock Purchase Agreements (Sept. 26, 2008) (attached as Exhibit A)).[1] In exchange for senior preferred stock, Treasury committed to advance funds to each Enterprise for each quarter in which that Enterprise's liabilities exceeded its assets, up to a cumulative amount of $100 billion per Enterprise, which cap was later increased by amendment. (Compl. ¶¶ 21, 28.) Each Enterprise committed to pay Treasury a 10% annual dividend, assessed quarterly, based on the total cumulative amount drawn from Treasury (known as the liquidation preference). (*Id.* ¶¶ 21.) In the ensuing years, Treasury would provide the Enterprises with nearly $200 billion under this arrangement. (*Id.* ¶ 40.)

C. The Designation of Edward DeMarco as Acting FHFA Director and Unsuccessful Nomination of Joseph Smith for FHFA Director

In August 2009, the original FHFA Director, James B. Lockhart III, resigned. (Compl. ¶ 63.) At that time, career civil servant Edward DeMarco was serving as one of FHFA's Deputy Directors. (*Id.* ¶ 64.) On August 25, 2009, the President designated Deputy Director DeMarco to serve as FHFA's Acting Director pursuant to 12 U.S.C. § 4512(f). (*Id.*)

On November 12, 2010, President Obama nominated Joseph Smith as FHFA Director. 156 Cong. Rec. S7911 (Nov. 15, 2010); *see also* (Compl. ¶ 65). Although the Senate Banking Committee approved the nomination, opposition blocked a vote in the full Senate, eventually forcing the President to withdraw the nomination. 156 Cong. Rec. S11071 (Dec. 22, 2010).

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[1] Because the preferred stock purchase agreements and Third Amendment are "integral" to the Complaint, (*see, e.g.*, Compl. ¶¶ 1, 21, 22, 24, 35-48, 86, 92, 98, 104, 110, Prayer for Relief), and thereby incorporated into it, the Court may take judicial notice of these documents in resolving this motion to dismiss. *See DiFelice v. Aetna U.S. Healthcare*, 346 F.3d 442, 444 n.2 (3d Cir. 2003). Exhibit A includes both the separate (but substantially identical) preferred stock purchase agreements for Fannie Mae and Freddie Mac. Likewise, Exhibit B includes the Third Amendments to both the Fannie Mae and Freddie Mac preferred stock purchase agreements.

D. The Third Amendment to the Preferred Stock Purchase Agreements

Meanwhile, FHFA, as Conservator for the Enterprises, and Treasury amended the preferred stock purchase agreements twice to increase the amounts Treasury could advance to the Enterprises. By 2012, the cumulative amount of Treasury funding neared $200 billion, requiring the Enterprises to pay almost $20 billion per year in dividends, which exceeded the Enterprises' average historical earnings per year. (*See* Compl. ¶¶ 21(c), 40.) The Enterprises drew more money from Treasury to cover the dividend owed to Treasury, further increasing Treasury's liquidation preferences and the Enterprises' future dividend obligations. (*Id.* ¶¶ 21(d), 31.)

In August 2012, the parties amended the preferred stock purchase agreements for a third time—hence, the "Third Amendment"—to adjust the various forms of consideration paid to Treasury in exchange for its extraordinary funding commitment. (*Id.* ¶ 36.) The Third Amendment modified the formula for the dividend on Treasury's preferred stock from a 10% fixed dividend to a variable dividend equal to each Enterprise's net worth at the end of each quarter (less a buffer), and suspended the Enterprises' obligation to pay Treasury a periodic commitment fee for as long as the Third Amendment remained in effect. Third Amendment to Preferred Stock Purchase Agreements (attached as Exhibit B); *see also* (Compl. ¶ 36). Thus, unless an Enterprise's total net worth in a given quarter exceeds the amount of the buffer (currently $3 billion), it owes no dividend; if an Enterprise's net worth exceeds the $3 billion buffer, it pays the amount of that excess as a dividend, whether greater or less than the prior fixed-percentage dividend obligation. Acting Director DeMarco signed the Third Amendment for FHFA as the Enterprises' Conservator. (*See id.* ¶¶ 66, 67.)

E. The Nomination and Confirmation of FHFA Director Watt

On May 1, 2013, President Obama nominated Rep. Melvin L. Watt as FHFA Director. (*See* Compl. ¶ 65.) The Senate Banking Committee approved the nomination, 159 Cong. Rec. S5799 (July 18, 2013), but it was filibustered in the full Senate, 159 Cong. Rec. S7706 (Oct. 31, 2013). After the Senate abolished the filibuster for certain executive nominees, Rep. Watt was confirmed. 159 Cong. Rec. S8417 at 8417-18 (Nov. 21, 2013); 159 Cong. Rec. S8593 (Dec. 10, 2013). Over eight months after being nominated, Mr. Watt was sworn in as FHFA Director on January 6, 2014 for a five-year term, which automatically ended Mr. DeMarco's tenure as Acting Director. (Compl. ¶ 65.)

F. This Litigation

Plaintiffs filed this action on August 16, 2018, one day short of six years after the Third Amendment was adopted. Lead Plaintiff Wazee Street Opportunities Fund IV, LP is a Delaware limited partnership whose management affiliate describes itself as "a private debt firm" that "seek[s] to exploit financial market fear and uncertainty to purchase securities at deep discounts and then drive successful outcomes through creative restructuring solutions." Wazee Street Capital Management, http://wazeestreetcapital.com/ (last visited Nov. 16, 2018). Wazee purchased 1,605,000 shares of Fannie Mae common stock between December 2016 and November 2017, over four years after the Third Amendment. (Compl. ¶ 5.) A second Plaintiff, Lisa Brown, purchased about 11 shares of Freddie Mac common stock in 2014 (also well after the Third Amendment). (*Id.* ¶ 7.) A third, Douglas Whitley, claims to have acquired 196 Fannie Mae common shares in September 2008, the month Fannie Mae was placed in conservatorship. (*Id.* ¶ 6.)

This case is merely the latest salvo in a long series of shareholder litigations challenging the Third Amendment. An initial wave of cases, beginning in 2013, claimed that the Third

Amendment was outside the Conservator's authority and violated the Administrative Procedure Act ("APA") or other statutes. Every court that considered those arguments rejected them, including the Third Circuit and four other courts of appeals. *See Jacobs*, 2018 WL 5931515; *Saxton v. FHFA*, 901 F.3d 954 (8th Cir. 2018); *Roberts v. FHFA*, 889 F.3d 397 (7th Cir. 2018); *Robinson v. FHFA*, 876 F.3d 220 (6th Cir. 2017); *Perry Capital*, 864 F.3d 591.

In a subsequent wave of cases, other shareholders have brought the same claims alleged in this case. Earlier this year, the federal court in Minnesota recently dismissed a shareholder Third Amendment challenge asserting precisely the same five counts as brought in the complaint here. *Bhatti v. FHFA*, 2018 WL 3336782.[2]

The Complaint here proceeds in five counts. Count I and II allege that FHFA's structure violates the President's constitutional removal authority and the separation of powers. (Compl. ¶¶ 78-92.) Count III alleges that FHFA's former Acting Director, who approved the Third Amendment on behalf of FHFA as Conservator, served in violation of the Appointments Clause at the time of the Third Amendment. (*Id.* ¶¶ 93-98.) Counts IV and V allege that Congress improperly delegated government power to FHFA in violation of the nondelegation doctrine or private nondelegation doctrine, respectively. (*Id.* ¶¶ 99-110.) As relief, Plaintiffs ask the Court to vacate the Third Amendment and to grant injunctive and declaratory relief.

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[2] In a case out of Texas, a panel of the Fifth Circuit held by a two-judge majority that FHFA's structure as an independent agency is unconstitutional, while rejecting unanimously the plaintiffs' argument that that outcome required invalidation of the Third Amendment. *Collins v. Mnuchin*, 896 F.3d 640 (5th Cir. 2018). However, the Fifth Circuit recently ordered that *Collins* will be reheard *en banc* and vacated the panel opinion. *Collins v. Mnuchin*, --- F.3d ----, 2018 WL 5928985, at *1 (5th Cir. Nov. 12, 2018); *see also* 5th Cir. R. 41.3 ("the granting of a rehearing *en banc* vacates the panel opinion and judgment of the court").

ARGUMENT

I. THE COURT SHOULD DISMISS PLAINTIFFS' CONSTITUTIONAL CHALLENGES TO FHFA'S STRUCTURE

Plaintiffs allege in Count I that the Third Amendment should be vacated because HERA "violates the President's constitutional removal authority" by "vesting FHFA's leadership in a single director rather than a multi-member board and eliminating the President's power to remove the director at will." (Compl. ¶ 80.) They allege in Count II that "[e]ven if FHFA's single director does not violate the Constitution's removal requirements" by itself, this structure violates the separation of powers when combined with FHFA's ability to "self-fund through fees it assesses on regulated entities" and with limitations that HERA places on judicial review of certain FHFA actions. (*Id.* ¶¶ 88-90.)

As in *Bhatti*, 2018 WL 3336782, at *4-8, the Court should dismiss both counts for failure to state a claim because (1) Plaintiffs lack standing to assert the claims; (2) Plaintiffs' legal theories are contrary to longstanding Supreme Court precedent upholding the constitutionality of independent agencies; and (3) the funding mechanism and limitations on judicial review Congress chose to adopt for FHFA are irrelevant to the constitutionality of FHFA's structure.

A. Plaintiffs Lack Article III Standing

To have standing to challenge the constitutionality of a statute, Plaintiffs must show an injury-in-fact, "a causal connection between the injury" and the alleged constitutional violation (*i.e.*, traceability), and a likelihood that the injury "will be redressed by a favorable decision" (*i.e.*, redressability). *N.J. Physicians, Inc. v. President of U.S.*, 653 F.3d 234, 238 (3d Cir. 2011); *Constitution Party of Pa. v. Cortes*, 712 F. Supp. 2d 387, 396-98 (E.D. Pa. 2010). These bedrock standing requirements apply to constitutional challenges to agencies' structures with the same force with which they apply to any other kind of claim. *See*, *e.g.*, *Metro. Wash. Airports Auth. v.*

Citizens for Abatement of Aircraft Noise, Inc., 501 U.S. 252, 264 (1991) (applying full traceability and redressability analysis to separation-of-powers claims); *Comm. for Monetary Reform v. Bd. of Governors of Fed. Reserve Sys.*, 766 F.2d 538, 542-43 (D.C. Cir. 1985) (same; dismissing separation-of-powers claim for lack of standing).

In the context of the separation-of-powers claims here, the traceability requirement for Article III standing thus requires Plaintiffs to show a "causal connection" between their injury—the Third Amendment's alleged negative effect on their investments—and FHFA's independence from the President. Redressability requires that Plaintiffs show the same purported injury is likely to be redressed if they are successful in persuading the Court that FHFA's structure is unconstitutional. Plaintiffs cannot make either showing here.

1. Plaintiffs' Alleged Injury Is Not Traceable to the Alleged Constitutional Violation

For three independent reasons, Plaintiffs cannot show that the Third Amendment and its alleged negative effect on their stock are traceable to FHFA's independence from the President.

First, the idea that FHFA's independence could have caused the Third Amendment is in fundamental conflict with Plaintiffs' own allegations and narrative in their Complaint. As the *Bhatti* court put it, and is equally true here,

> At the heart of the claims made by plaintiffs in Counts I and II is their contention that the President lacks sufficient control over FHFA and, as a result, the agency is too independent. The injury that plaintiffs allege is the Third Amendment, which purportedly harms their interests as shareholders in the Companies by being too favorable to Treasury. . . .
>
> The problem with plaintiffs' claims is glaring: There is no causal connection between their injury—a Third Amendment that (in plaintiffs' view) is too favorable to the Executive Branch—and the lack of Executive Branch influence over FHFA.

Bhatti, 2018 WL 3336782, at *4.

Here, as in *Bhatti*, the crux of Plaintiffs' claim is that the President lacks sufficient "influence over the agency's decisions." (Compl. ¶ 56.) Thus, traceability requires Plaintiffs to demonstrate that *more* Presidential influence over FHFA might have spurred FHFA to reject the Third Amendment. But Plaintiffs' own allegations indicate exactly the opposite. The Third Amendment is a contract between FHFA as Conservator and the Secretary of the Treasury. (*Id.* ¶ 36). There is no dispute that the Secretary is removable by the President at will and subject to plenary Presidential control. Had the President not supported the Third Amendment, he of course could have directed Treasury not to enter into it. But he gave no such direction, meaning that "in a very real sense, the President has already approved the Third Amendment." *Bhatti*, 2018 WL 3336782, at *5. Just like the plaintiffs in *Bhatti*, Plaintiffs "have no coherent theory for how their injury—a Third Amendment that, in plaintiffs' view, is unduly favorable to the President—could have resulted from the President having too *little* control over FHFA." *Id.*

Indeed, the Complaint affirmatively alleges that the Third Amendment was not really an "agreement" or "arms-length" at all, but rather "unilateral action" by parties "acting in concert." (Compl. ¶ 36.) According to Plaintiffs, the objective was "to promote the economic and political interests of one stockholder—*the U.S. Treasury*" and "support *the Treasury*'s political goal" of winding down the Enterprises. (*Id.* ¶ 39 (emphasis added).) In Plaintiffs' telling, "*Treasury* enact[ed] the so-called Third Amendment" because "Timothy Geithner was strongly opposed to the rebirth of the old Fannie and Freddie." (*Id.* ¶ 40 (internal quotation marks omitted) (emphasis added).) Plaintiffs rely on statements by "a senior White House advisor" praising the Third Amendment that they characterize as representing the Government's position. (*Id.* ¶ 44.) These allegations are mutually exclusive with the proposition needed for Plaintiffs to have

Article III standing: that *greater* White House control over FHFA might somehow have caused FHFA to *reject* the Third Amendment.

Plaintiffs complain that the Third Amendment transpired because the Conservator did *not* "negotiat[e] at arm's length" with Treasury. (*Id.* ¶ 36.) But Plaintiffs cannot explain how plenary presidential control over both sides of the negotiation would somehow make the transaction *more* arms-length. Here, no less than in *Bhatti*, "there is no doubt that the alleged constitutional violation (too little presidential control over FHFA) did *not* cause the alleged injury (an FHFA action that was too favorable to the President)." *Bhatti*, 2018 WL 3336782, at *5. Counts I and II must be dismissed for this reason alone.

Second, the Third Amendment is also not traceable to HERA's for-cause removal standard because FHFA was led at the time of Third Amendment by an *Acting* Director not covered by that standard. Plaintiffs' challenge centers on 12 U.S.C. § 4512(b)(2), which provides that an FHFA Director appointed by the President and confirmed by the Senate shall serve "for a term of 5 years, unless removed before the end of such term for cause by the President." (Compl. ¶¶ 54, 56.) But the Conservator's decision to enter into the Third Amendment was made by an FHFA *Acting* Director, Edward DeMarco, who was not appointed by the President or confirmed by the Senate to a five-year term. (Compl. ¶¶ 64-67.) As such, § 4512(b)(2) and its for-cause standard did not apply to Mr. DeMarco.

Rather, a separate provision of the statute, not challenged by Plaintiffs on the ground that it restricts presidential power, governs the circumstances in which deputy directors may serve temporarily as acting Director. *See* 12 U.S.C. § 4512(f) ("In the event of the death, resignation, sickness, or absence of the Director, the President shall designate [the Deputy Director of one of three divisions] to serve as acting Director until the return of the Director, or the appointment of

a successor pursuant to subsection (b).”). Section 4512(f) neither sets a fixed term nor contains any “cause” limitations on the President’s authorities. Because § 4512(b)(2)’s cause requirement for removal was inoperative at the time, and the President could freely have designated a different acting director at will and thereby replaced Mr. DeMarco, there cannot have been any connection between that provision and FHFA’s execution of the Third Amendment.

Third, Plaintiffs Wazee and Brown lack Article III standing because they did not purchase their Fannie Mae or Freddie Mac stock until 2016-2017 and 2014 respectively, well *after* the Third Amendment. (Compl. ¶¶ 5, 7.) A hedge fund or individual cannot manufacture Article III standing by knowingly and voluntarily assuming a position subjecting it to the alleged harm. *Grocery Mfrs. Ass’n v. EPA*, 693 F.3d 169, 177 (D.C. Cir. 2012) (such “self-inflicted harm” is “not fairly traceable to the challenged government conduct”); *see also Pennsylvania v. New Jersey*, 426 U.S. 660, 664 (1976) (plaintiff cannot be heard to “complain about damage inflicted by its own hand”); *In re McNeil Consumer Healthcare*, 877 F. Supp. 2d 254, 276 (E.D. Pa. 2012) (denying standing for damages that were “the result of the plaintiffs’ own choices and are not fairly traceable to the actions of the defendants.”). Moreover, to the extent they allege the Third Amendment adversely affected the value of their shares, Plaintiffs Wazee and Brown must have purchased their stock at a discounted price that already took the Third Amendment into account, negating any cognizable injury-in-fact. *See In re Burlington Coat Factory Sec. Litig.*, 114 F.3d 1410, 1425 (3d Cir. 1997) (“[I]nformation important to reasonable investors . . . is immediately incorporated into stock prices.”).

2. Plaintiffs Cannot Show That Their Alleged Injury Would Be Redressed by Declaring the Removal Restriction Unconstitutional

Plaintiffs also lack standing because a holding that § 4512(b)(2) is unconstitutional would not redress their alleged injury. When a limitation on the President’s removal authority crosses

constitutional lines (which is not the case here), the remedy is to declare that limitation prospectively inoperative, not to void past actions by the official who was protected from removal. That is particularly so where, as here, the action challenged was not even "Executive" in nature.

This is demonstrated by the Supreme Court's most recent decision addressing a restriction on the President's removal authority, *Free Enterprise Fund v. PCAOB*, 561 U.S. 477 (2010). In that case, the Supreme Court held a unique set of restrictions on the President's ability to remove PCAOB members unconstitutional. However, neither the Supreme Court nor the lower courts on remand vacated any actions taken by the PCAOB, such as an investigation that caused the plaintiff injury. Rather, the Court "reject[ed]" the plaintiffs' argument that the removal restrictions rendered "all power and authority exercised by [the Board] in violation of the Constitution." 561 U.S. at 508 (internal quotation marks omitted). It was not "the existence of the Board" that "violate[s] the separation of powers," but the particular removal restrictions in the statute. *Id.* at 508-09. "[W]hen confronting a constitutional flaw in a statute, [courts] try to limit the solution to the problem." *Id.* at 508. Thus, the appropriate remedy for such a claim is simply to strike down the problematic provisions so they do not constrain the President's powers going forward. *Id.*; *accord John Doe Co. v. CFPB*, 849 F.3d 1129, 1133 (D.C. Cir. 2017) ("traditional constraints on separation-of-powers remedies" refuted the plaintiffs' position that a removal-restrictions claim could invalidate a CFPB action against them). Although the plaintiffs in *Free Enterprise Fund* sought to invalidate and enjoin the PCAOB's actions as regulator of accounting firms, they were denied that relief.

The nature of the action challenged here provides even greater reason why vacatur of that action is not an available remedy. The doctrinal basis for Plaintiffs' claims is the constitutional

mandate that the President retain "general administrative control of those *executing the laws*," including "some power of removing those for whom he cannot continue to be responsible." *Free Enter. Fund*, 561 U.S. at 492-93 (emphasis added) (internal quotation marks omitted). But those animating concerns have no application to functions, like the Third Amendment, that are not "Executive" in nature and thus not constitutionally reserved for presidential supervision.

When FHFA as Conservator approved the Third Amendment, it was not enforcing the laws in a sovereign executive sense. Rather, "the Third Amendment is an exercise of the Agency's power to take over Fannie and Freddie's assets and operate their businesses," including actions to "secure ongoing access to capital, manage debt loads, control cash flow, and decide whether and how to pay dividends." *Jacobs*, 2018 WL 5931515, at *4; *accord Perry Capital*, 864 F.3d at 605; *Saxton*, 901 F.3d at 960-61 (Stras, J., concurring). Indeed, when government agencies like FHFA serve as conservators or receivers for financial institutions, they are deemed to "step into the shoes" of those institutions and are not acting as the Government at all. *See, e.g.*, *Herron v. Fannie Mae*, 861 F.3d 160, 169 (D.C. Cir. 2017); *Meridian Invs., Inc. v. Fed. Home Loan Mortg. Corp.*, 855 F.3d 573, 579 (4th Cir. 2017); *cf. U.S. ex rel. Petras v. Simparel, Inc.*, 857 F.3d 497, 502-03 (3d Cir. 2017) ("[Small Business Administration] when acting as a receiver . . . was not acting as the Government"). Article II does not mandate that the President have final authority over business operations of financial institutions in conservatorship, such as the transaction here, which was "in essence a renegotiation of an existing lending agreement (albeit with equity rather than debt)." *Jacobs*, 2018 WL 5931515, at *4.

If Plaintiffs here were to succeed on their constitutional claim, the result would therefore be an order striking the "cause" limitation from § 4512(b)(2) and altering the conditions under which a Senate-confirmed FHFA Director might be removed by the President in the future. That

would not help Plaintiffs here, who complain not of any ongoing or anticipated future action by FHFA but rather about entry into the Third Amendment over six years ago.

B. FHFA's Structure as an Independent Agency Is Constitutional

Even if Plaintiffs had standing, their constitutional challenge to FHFA's structure as an independent agency is contrary to well-established Supreme Court precedent. Plaintiffs reach far and wide in an attempt to carve out exceptions to that precedent, but their allegations are unavailing. The Court should dismiss Counts I and II for failure to state a claim.

1. Longstanding Supreme Court Precedent Endorses Independent Agencies

In *Humphrey's Executor v. United States*, 295 U.S. 602 (1935), the Supreme Court held that Congress may "create independent agencies run by principal officers appointed by the President, whom the President may not remove at will but only for good cause." *Free Enter. Fund*, 561 U.S. at 483. The Court "found it 'plain' that the Constitution did not give the President 'illimitable power of removal' over the officers of independent agencies." *Morrison v. Olson*, 487 U.S. 654, 687 (1988) (quoting *Humphrey's Ex'r*, 295 U.S. at 629). The Court has repeatedly reaffirmed this central principle. *See PHH Corp. v. CFPB*, 881 F.3d 75, 86-90 (D.C. Cir. 2018) (*en banc*) (discussing *inter alia Wiener v. United States*, 357 U.S. 349, 352 (1958); *Morrison*, 487 U.S. at 686-87; *Free Enter. Fund*, 561 U.S. at 483, 509). In the modern era, Congress has created dozens of independent agencies, performing a vast array of important functions, based on this judicially approved model. *See PHH*, 881 F.3d at 92; *CFPB v. ITT Educ. Servs., Inc.*, 219 F. Supp. 3d 878, 899 (S.D. Ind. 2015). As *Bhatti* held, "longstanding precedent makes clear that the FHFA director is not unconstitutionally insulated from the President." 2018 WL 3336782, at *6.

Congress created FHFA to regulate and supervise, among select other entities, Fannie Mae and Freddie Mac, financial institutions that play a vital role in housing finance. It has long been recognized that "[i]ndependence from presidential control is arguably important if agencies charged with regulating financial institutions . . . are to successfully fulfill their responsibilities; people will likely have greater confidence in financial institutions if they believe that the regulation of these institutions is immune from political influence." *Swan v. Clinton*, 100 F.3d 973, 983 (D.C. Cir. 1996). Congress's decision that FHFA should be led by a Director removable by the President for cause serves those important interests and was well within the constitutional latitude provided to Congress by *Humphrey's Executor* and its progeny.

2. Plaintiffs' Efforts to Manufacture an Exception Are Unavailing

Plaintiffs ask this Court to create a new exception to *Humphrey's Executor* by holding that it does not apply to agencies, like FHFA, headed by a single individual. (*See* Compl. ¶ 79.) Numerous courts have rejected that argument. The *Bhatti* court rejected it in the context of an Enterprise shareholder claim against FHFA materially identical to Count I. *See* 2018 WL 3336782, at *5-7. And multiple courts, including the *en banc* D.C. Circuit, have rejected similar challenges to the structure of the Consumer Financial Protection Bureau ("CFPB"), which also has a single director removable for cause. *See, e.g.*, *PHH*, 881 F.3d at 96-101; *CFPB v. Think Fin., LLC*, 2018 WL 3707911, at *1-2 (D. Mont. Aug. 3, 2018); Opinion & Order at 4-11, *CFPB v. All Am. Check Cashing, Inc.*, No. 3:16-cv-356 (S.D. Miss. Mar. 21, 2018), *interlocutory appeal docketed*, No. 18-60302 (5th Cir.); *CFPB v. TCF Nat'l Bank*, 2017 WL 6211033, at *6 (D. Minn. Sept. 8, 2017); *CFPB v. Nationwide Biweekly Admin., Inc.*, 2017 WL 3948396, at *10 n.23 (N.D. Cal. Sept. 8, 2017), *appeal docketed*, No. 18-15887 (9th Cir.); *CFPB v. Seila Law, LLC*, 2017 WL 6536586, at *2 (C.D. Cal. Aug. 25, 2017), *appeal docketed*, No. 17-56324 (9th

Cir.); *CFPB v. Navient Corp.*, 2017 WL 3380530, at *9-19 (M.D. Pa. Aug. 4, 2017); *Robinson v. CFPB*, 2017 WL 497605, at *1-2 (M.D. Pa. Feb. 7, 2017), *aff'd on other grounds*, 689 F. App'x 151, 152 (3d Cir. May 22, 2017); *CFPB v. Future Income Payments, LLC*, 252 F. Supp. 3d 961, 970-75 (C.D. Cal. 2017), *vacated on other grounds*, No. 17-55721 (9th Cir. Oct. 18, 2018); *CFPB v. CashCall, Inc.*, 2016 WL 4820635, at *13 (C.D. Cal. Aug. 31, 2016), *appeal docketed*, No. 18-55479 (9th Cir.); *People of the State of Illinois ex rel. Madigan v. CMK Invs., Inc.*, 2015 WL 4038896, at *3 (N.D. Ill. June 30, 2015); *CFPB v. ITT Educ. Servs., Inc.*, 219 F. Supp. 3d 878, 890-99 (S.D. Ind. 2015); *CFPB v. Morgan Drexen, Inc.*, 60 F. Supp. 3d 1082, 1086-92 (C.D. Cal. 2014).[3]

While *Humphrey's Executor* happened to involve an agency structured as a multi-member commission (the Federal Trade Commission ("FTC")), the number of commissioners played no part in the Court's constitutional analysis. *See* 295 U.S. at 626-32; *PHH*, 881 F.3d at 98-99 (explaining that *Humphrey's Executor* did not rely on the existence of a multi-member board); *Bhatti*, 2018 WL 3336782, at *6 ("The Supreme Court has never cited the fact that an agency had multiple leaders as a reason for finding the agency's structure constitutional."). Rather, the relevant issue is simply "'whether the removal restrictions are of such a nature that they impede the President's ability to perform his constitutional duty.'" *PHH*, 881 F.3d at 97 (quoting *Morrison*, 487 U.S. at 691). Here, because Plaintiffs claim not that the removal restriction is problematic by itself, but only when combined with FHFA's single-director structure, Plaintiffs must show that tenure protection for a single agency head impedes the

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[3] *But see CFPB v. RD Legal Funding, LLC*, --- F. Supp. 3d ----, 2018 WL 3094916, at *35-36 & n.7 (S.D.N.Y. June 21, 2018), *appeal docketed*, No. 18-02743 (2d Cir.); *CFPB v. D&D Mktg.*, 2016 WL 8849698 (C.D. Cal. Nov. 17, 2016), *appeal docketed*, No. 17-55709 (9th Cir.).

President's performance of his constitutional duties to a greater degree than if the same tenure protection were provided to multiple members of a commission.

Plaintiffs cannot make that showing. The notion that a President would find it more difficult to supervise a *single* individual removable for cause than a body composed of *numerous* individuals who are each removable for cause defies logic. As the *en banc* D.C. Circuit reasoned, there is no "reason to think that a single-director independent agency is any less responsive than one led by multiple commissioners or board members. If anything, the President's for-cause removal prerogative may allow more efficient control over a solo head than a multi-member directorate." *PHH*, 881 F.3d at 97-98. After all, when an agency is led by a multi-member body, the President might need to "remove multiple Commissioners in order to change the agency's course," whereas "[t]he President need only remove and replace a single officer in order to transform" an agency led by a single director. *Id.* at 98. Furthermore, "[w]ith a multi-member body, it is more difficult to assess or allocate responsibility among the members of the body for policy decisions or actions taken because decision making is made within the group and may be the product of compromise. In contrast, with a single director, it is very clear who made the decision." *Navient*, 2017 WL 3380530, at *17; *see also Bhatti*, 2018 WL 3336782, at *6 ("When a single person is in charge, there is no doubt about who is responsible for any official action that would justify removal for cause.").

The Complaint surmises that a multi-member structure "forces the leadership to account for multiple viewpoints, adopt compromises that result in less extreme decisions, and better resist capture by interest groups." (Compl. ¶ 55.) However, such speculative pronouncements about the merits of collective decision-making are policy issues for Congress—not courts—to weigh. Congress could reasonably conclude, particularly when enacting a statute in a time of economic

emergency, that a single head would be more conducive to the type of firm, immediate decisions and actions that FHFA would need to address. In any case, assessing the wisdom of that call is outside the province of the courts. *See PHH*, 881 F.3d at 109.

Plaintiffs contend that multi-member commissions are constitutionally preferable because they are "often filled with individuals that are serving staggered terms and a chairperson designated by the President, both of which enable the President to influence the agency's actions," and "[m]any" of them "are also required to be bi-partisan, ensuring that at least some members will be filled with persons belonging to the President's political party." (Compl. ¶ 56.) Even if these features are "often" present, they are not inherent characteristics of multi-member commissions, so they cannot be the basis for placing multi-member commissions and single-director agencies on opposite sides of a constitutional line. *PHH*, 881 F.3d at 100 ("We are not aware of any court that has viewed the existence, strength, or particular term of agency chairs or members to be relevant to the constitutionality of an independent agency."). The bipartisanship requirement, if it has any significance, cuts the other way because a requirement that the President appoint members of the *opposition political party* is far more likely to impede presidential control of an agency than facilitate it. Moreover, in 1935 when the Supreme Court decided *Humphrey's Executor*, the FTC statute provided that "[t]he commission shall choose a chairman from its own membership." 15 U.S.C. § 41 (1934). So it is impossible for presidential control over chairmanship to have formed any part of the rationale underlying that seminal decision approving independent agencies.

Plaintiffs point out that, given the five-year term of FHFA's director, "an FHFA director could be in office for the entirety of a President's four-year term, pursuing policies at odds with the President's objectives." (Compl. ¶ 56.) But "[t]he Constitution has never been read to

guarantee that every President will be able to appoint all, or even a majority of, the leaders of every independent agency . . . ." *PHH*, 881 F.3d at 100. Moreover, while it is theoretically possible for an FHFA Director to remain in office during a President's entire four-year term, that is no different than the situation that would apply to a board composed of multiple members selected once every five years or more. *See id.* at 99 (listing examples of agencies led by multi-member commissions with terms longer than four years). In fact, one court has calculated that "eighty percent of presidential terms will enable the President to appoint" a single director with a five year term, whereas only "four-sevenths, or approximately fifty-seven percent, of presidential terms will enable a president to appoint a controlling majority of three or more commissioners" of the FTC (which has five commissioners with staggered seven-year terms). *Navient*, 2017 WL 3380530, at *17; *see also Bhatti*, 2018 WL 3336782, at *7. Based on comparison with those parameters for the FTC, FHFA's single-director structure "actually permit[s] more presidential control over the agency's direction than would a multimember commission." *Bhatti*, 2018 WL 3336782, at *7.

In sum, nothing Plaintiffs offer suggests that having a multi-member structure inherently or systematically enhances an agency's susceptibility to presidential control. Plaintiffs' challenge should be rejected.

C. FHFA's Funding Mechanism and Limitations From Judicial Review Raise No Constitutional Issues

In Count II, Plaintiffs argue that "[e]ven if FHFA's single director does not violate the Constitution's removal requirements," this factor becomes constitutionally problematic when combined with other alleged issues. Specifically, Plaintiffs point to HERA's provision permitting FHFA to fund itself through assessments on the regulated entities (Compl. ¶ 89), and its limitations on judicial review of FHFA actions (Compl. ¶ 90). However, these other factors

add nothing. As the court explained in *PHH,* "two unproblematic structural features" do not "become problematic in combination" unless they "affect the same constitutional concern and amplify each other in a constitutionally relevant way," which the varying issues alleged here do not. *PHH*, 881 F.3d at 96. Multiple courts have thus rejected this mosaic theory of unconstitutionality in the context of challenges to the CFPB. *See, e.g.*, *id.* at 95-96; *Think Fin.*, 2018 WL 3707911, at *1-2; *Nationwide Biweekly Admin.*, 2017 WL 3948396, at *10 n.23; *Seila Law*, 2017 WL 6536586, at *2; *Navient*, 2017 WL 3380530, at *9, *16; *ITT*, 219 F. Supp. 3d at 894-99; *Morgan Drexen*, 60 F. Supp. 3d at 1086-91.

Plaintiffs complain that HERA "exempts FHFA from the appropriations process by permitting FHFA to self-fund through fees it assesses on the entities it regulates without any oversight from Congress." (Compl. ¶ 89 (citing 12 U.S.C. § 4516(f)(2)).) But such "budgetary independence primarily affects Congress, which has the power of the purse; it does not intensify any effect on the President of the removal constraint." *PHH*, 881 F.3d at 96; *accord Bhatti*, 2018 WL 3336782, at *7. In any event, Congress frequently organizes agencies, particularly in the financial regulatory sector, to be funded through fees assessed on regulated entities. *See PHH*, 881 F.3d at 95 (collecting examples, including the Federal Reserve, dating back over a century); *Navient*, 2017 WL 3380530, at *16 (same, and pointing out that Congress "remains free to change how the Bureau is funded at any time"). This common mechanism presents no constitutional issue. "[T]he Constitution does not prohibit Congress from enacting funding structures for agencies that differ from the procedures prescribed by the ordinary appropriations process." *ITT*, 219 F. Supp. 3d at 896; *accord Morgan Drexen*, 60 F. Supp. 3d at 1089. Congress may choose "to loosen its own reins on public expenditure" and "not to finance a

federal entity with appropriations." *Am. Fed'n of Gov't Emps., AFL-CIO, Local 1647 v. FLRA*, 388 F.3d 405, 409 (3d Cir. 2004).

Nor does Congress's decision to exempt certain FHFA actions from judicial review raise any constitutional concerns, either by itself or combined with other issues raised by Plaintiffs. Like exemptions from appropriations, limitations on judicial review do not affect the Executive and are not relevant to whether the President retains sufficient oversight over the agency. *See Bhatti*, 2018 WL 3336782, at *7 (limitations on judicial review are "not a particularly relevant consideration in the context of a separation-of-powers challenge").

Moreover, it is well-established that Congress has "the power to preclude judicial review of non-constitutional challenges to agency actions." *Campbell v. OPM*, 694 F.2d 305, 307 (3d Cir. 1982); *accord Morgan Drexen*, 60 F. Supp. 3d at 1091 n.5. The U.S. Code is replete with statutes limiting judicial review of various agency actions. *See United States v. Bozarov*, 974 F.2d 1037, 1041 (9th Cir. 1992) ("The Supreme Court has upheld a number of statutes that precluded judicial review."). Indeed, reflecting the widespread nature of such provisions, the Administrative Procedure Act expressly withdraws jurisdiction over agency actions for which "statutes preclude judicial review" or that "are committed to agency discretion by law." 5 U.S.C. § 701(a)(1), (2). The judicial-review issue adds nothing to Plaintiffs' separation-of-powers claims. The Court should dismiss those claims.

II. THE COURT SHOULD DISMISS PLAINTIFFS' APPOINTMENTS CLAUSE CLAIM

Plaintiffs contend in Count III that the Third Amendment is invalid because at the time of its adoption, FHFA had an acting director who was not confirmed by the Senate. However, similar to Counts I and II, Plaintiffs lack standing to challenge the validity of FHFA's acting director's service, because the action that they challenge—entry into the Third Amendment—was not the type of sovereign governmental action that can only be taken by an official

confirmed by the Senate. Moreover, the *de facto* officer doctrine bars Plaintiffs' Appointments Clause challenge because they waited far too long to bring it. In any event, longstanding precedent and widespread practices establish that subordinate agency officers may act temporarily as head of an agency without Senate confirmation. Like the similar claims in *Bhatti*, 2018 WL 3336782, at *8-14, Plaintiffs' claims of defects in Mr. DeMarco's designation and tenure should be dismissed.

The Appointments Clause provides that the President must nominate and the Senate must confirm all "principal officers" of the United States. U.S. CONST. art. II, § 2, cl. 2. It has long been understood, however, that to prevent the responsibilities of such an office from "go[ing] unperformed if a vacancy arises and the President and Senate cannot promptly agree on a replacement," the President may "direct certain officials to temporarily carry out the duties of a vacant [principal] office in an acting capacity, without Senate confirmation." *NLRB v. SW Gen., Inc.*, 137 S. Ct. 929, 934 (2017).

The Supreme Court settled the constitutionality of this approach long ago, holding that even though the Appointments Clause requires a full consul to be confirmed by the Senate, such confirmation was not required to enable the vice consul to perform those duties in an acting capacity: "Because the subordinate officer is charged with the performance of the duty of the superior for a limited time and under special and temporary conditions, he is not thereby transformed into the superior and permanent official." *United States v. Eaton*, 169 U.S. 331, 343 (1898).

Congress has conferred authority for inferior officers to serve as acting principal officers through two distinct and complementary routes. First, the Federal Vacancies Reform Act ("Vacancies Act"), 5 U.S.C. § 3345 *et seq.*, generally authorizes the President to designate acting

officers across the government. Second, Congress sometimes includes specific acting-officer provisions within agencies' enabling statutes. FHFA's enabling statute contains such a provision in § 4512(f), which enables the President to designate one of FHFA's Deputy Directors to act temporarily as Director while that office is vacant. In some instances, Congress has imposed a time limit on how long an official can serve in an acting capacity. *See*, *e.g.*, Vacancies Act, 5 U.S.C. § 3346 (210 days, which may be renewed twice for a total of 630 days and is tolled while a nomination is pending). In others, such as § 4512(f), Congress opted *not* to impose any time limit.

Here, the President designated Mr. DeMarco to act as Director under § 4512(f), upon Mr. Lockhart's resignation. (*See* Compl. ¶ 64.) Plaintiffs admit that the designation of Mr. DeMarco was "[i]n accordance with these provisions" of HERA. (*Id.*) However, they argue that Mr. DeMarco's service was deficient on two grounds: (1) that "the Constitution does not permit the President to appoint an acting principal officer," and (2) that "serving as an acting principal officer for more than two years is unconstitutional." (*Id.* ¶¶ 96, 97.) Those claims fail for multiple reasons.

A. Plaintiffs Lack Standing

As a threshold matter, Plaintiffs lack Article III standing for this claim as well. As noted earlier, standing requires an injury-in-fact, a causal connection between the injury and the alleged constitutional violation (*i.e.*, traceability), and a likelihood that the injury will be redressed by a favorable decision (*i.e.*, redressability). *See supra* at 8-9. Just as a holding that FHFA's independent structure is unconstitutional would not be a basis for invalidating the Third Amendment, neither would a holding that Mr. DeMarco was not constitutionally serving as Acting Director in August 2012 justify that relief. Such a holding would amount to an advisory

opinion on a purely historical matter and would leave intact the source of Plaintiffs' alleged injury.

A holding that Mr. DeMarco was not constitutionally serving as Acting Director in August 2012 would not invalidate the Third Amendment because the "renegotiation of an existing lending agreement," *Jacobs*, 2018 WL 5931515, at *4, is not the type of sovereign government function reserved for "Principal Officers" appointed in the manner prescribed by the Appointments Clause, *i.e.*, nominated by the President and confirmed by the Senate. The hallmark of an "Officer[] of the United States" under the Appointments Clause is the "exercise [of] significant authority pursuant to the laws of the United States." *Lucia v. SEC*, 138 S. Ct. 2044, 2051 (2018) (citation and internal quotation marks omitted). For example, in *Lucia*, the Court held that SEC administrative law judges were "Officers of the United States" because they adjudicated "adversarial inquiries" under the public securities laws, in a manner similar to "federal trial judges." *Id* at 2053. On the other hand, there is no impediment to non-"Officers of the United States" performing functions "removed from the administration and enforcement of the public law." *Buckley v. Valeo*, 424 U.S. 1, 139 (1976).

Here, FHFA acted in its Conservator, rather than regulatory, capacity when it entered into the Third Amendment on behalf of the Enterprises. And, as the Third Circuit has already held, "the Third Amendment [was] an exercise of the Agency's power to take over Fannie and Freddie's assets and operate their businesses," including actions to "secure ongoing access to capital, manage debt loads, control cash flow, and decide whether and how to pay dividends." *Jacobs*, 2018 WL 5931515, at *4. Those functions quite plainly evoke "traditional power[s] of corporate officers or directors," *id.*, not "administration and enforcement of the public law." *Buckley*, 424 U.S. at 139. Because the Third Amendment did not need to be approved by an

"Officer of the United States" appointed pursuant to the Appointments Clause in the first place, any alleged issues regarding the consistency of Mr. DeMarco's service with the Appointments Clause would in no way call into question the validity of the Third Amendment. Plaintiffs therefore lack standing to assert Count III.[4]

B. The *De Facto* Officer Doctrine Bars Plaintiffs' Six-Years-Late Appointments Clause Challenges

Even if Plaintiffs had standing, Plaintiffs' Appointments Clause count is barred by the *de facto* officer doctrine. That doctrine "'confers validity upon acts performed by a person acting under the color of official title even though it is later discovered that the legality of that person's appointment or election to office is deficient.'" *Bhatti*, 2018 WL 3336782, at *13 (quoting *Ryder v. United States*, 515 U.S. 177, 180 (1995)). The rationale of the doctrine is to avoid the risk of "chaos" and "multiple and repetitious suits challenging every action taken by every official whose claim to office could be open to question." *Id.* (quoting *Ryder*, 515 U.S. at 180).

The Office of Legal Counsel ("OLC") at the U.S. Department of Justice has explained that the *de facto* officer doctrine is a common "cure[]" for "potential infirmities in the authority" of acting officers. *Acting Officers*, 6 Op. O.L.C. 119, 122 (1982). It applies to challenges not only to the "initial appointment" of an officer but also the officer's "length of service." *Bhatti*, 2018 WL 336782, at *14; *Dep't of Energy--Appointment of Interim Officers--Dep't of Energy Org. Act*, 2 Op. O.L.C. 405, 411 (1978) (*de facto* officer doctrine applies when an "initially valid designation of an acting official" nevertheless was allegedly "vitiated by an excessive delay in

[4] Plaintiffs Wazee and Brown also lack Article III standing to assert Count III because they purchased their Fannie Mae or Freddie Mac stock long after the Third Amendment. *See supra* at 12.

the submission of a nomination."). Thus, it applies to both arguments Plaintiffs make in Count III challenging Mr. DeMarco's service.

To be sure, the *de facto* officer doctrine is not absolute. For example, the D.C. Circuit permits plaintiffs to challenge government action on account of an invalidly serving officer if (1) they bring their action "at or around the time that the challenged government action is taken," and (2) they "show that the agency or department involved has had reasonable notice under all the circumstances of the claimed defect in the official's title to office." *SW Gen., Inc. v. NLRB*, 796 F.3d 67, 81-82 (D.C. Cir. 2015) (internal quotation marks omitted), *aff'd on other grounds*, 137 S. Ct. 929. Thus, the claim in *SW General* was allowed only because it was raised "in the administrative proceedings below" as "a defense to the enforcement action" and "exception to the ALJ decision" of which judicial review was sought. *Id.* at 82; *see also Andrade v. Lauer*, 729 F.2d 1475, 1500 (D.C. Cir. 1984) (*de facto* officer doctrine did not bar DOJ employees' Appointments Clause challenge to reduction-in-force because they sued the "day before the action under attack" as well as "notified the [agency] of their claim of invalid appointment within the month preceding filing of this suit").

That exception to the *de facto* office doctrine does not cover Plaintiffs' Appointments Clause challenge here. Far from bringing this challenge "at or around the time that the challenged government action is taken," as in *SW General* and *Andrade*, Plaintiffs waited until the eve of the six-year anniversary of the Third Amendment—and *nine* years after the designation of Mr. DeMarco as Acting Director that Plaintiffs now insist was void *ab initio*—to bring their claims. In *Bhatti*, the court held that Appointments Clause challenges to the Third Amendment brought in June 2017 could "by no stretch be considered timely" and were therefore

precluded by the *de facto* officer doctrine. 2018 WL 3336782, at *14 (internal quotation marks omitted). Plaintiffs here have outdone even the *Bhatti* plaintiffs in their untimeliness.

Nor can Plaintiffs meet the requirement to "show that the agency or department involved has had reasonable notice under all the circumstances of the claimed defect in the official's title to office." *SW Gen.*, 796 F.3d at 81-82. As discussed below, no court has ever held an acting officer's service or actions unconstitutional based on the novel theories advanced by Plaintiffs. This is a textbook case for application of the *de facto* officer doctrine.

C. Plaintiffs' Appointments Clause Claims Are Meritless

Even if Plaintiffs had standing and their Appointments Claims were not barred by the *de facto* officer doctrine, those claims have no merit.

1. Plaintiffs contend that the designation of Mr. DeMarco to serve as Acting Director was unconstitutional because the President "chose [him] from among three possible candidates to serve as FHFA's acting Director." (Compl. ¶ 97.) Plaintiffs' theory appears to be that it is unconstitutional for the President to have any role in the selection, because they concede that it would be constitutional for Congress to have provided in HERA that "in the event of a vacancy, the occupant of a specific inferior office will by operation of law become an acting principal officer." (*Id.*)

This theory has no support in case law and defies longstanding history and practice. *See Bhatti*, 2018 WL 3336782, at *11. It is the norm for the President to designate acting officials, and nothing in the Constitution prohibits Congress from allowing the President to choose from among several qualified candidates. *See SW Gen.*, 137 S. Ct. at 935 (observing that "[s]ince President Washington's first term, Congress has given the President limited authority to appoint acting officials," including via statutes allowing the President to choose "any person or persons"); 5 U.S.C. § 3345(a)(2), (3) (enabling the President to direct a person, from among a

wide field of options, to act in vacant position). If the President may choose "*any* person or persons" to serve as acting officials regardless of their qualifications, then *a fortiori* there is no constitutional barrier to a statute like HERA that requires the President to choose among three persons with certain specified qualifications.

Plaintiffs also argue that "a principal officer may not appoint his acting successor by selecting from among multiple inferior officers." (Compl. ¶ 97.) It is difficult to understand what Plaintiffs are trying to say here. The outgoing Director and principal officer, Mr. Lockhart, did *not* "appoint" Mr. DeMarco "by selecting from among multiple inferior officers." Rather, as Plaintiffs admit, the President is the one who selected Mr. DeMarco to act as Director. (*Id.*) To the extent Plaintiffs' argument is that it was somehow improper for the "three possible candidates" to consist of "inferior FHFA officers selected by the outgoing Director," (*id.*), that makes little sense. The Appointments Clause expressly permits Congress to vest the appointment of "inferior officers" in "Heads of Departments," and it is of course the norm for heads of departments to choose the deputies who serve under them. U.S. CONST. art. II, § 2, cl. 2. Taking the various contentions in paragraph 97 of the Complaint together, the only way Plaintiffs appear to believe it would be permissible for FHFA to have an acting director during a vacancy is if (a) Congress had specified that the occupant of a specific subordinate office at FHFA would become acting director, and (b) the outgoing FHFA Director somehow had not appointed that person to their subordinate office. It is not surprising that no case law or constitutional principles support such an untenable result.

2. Aside from their theory that his designation as Acting Director was void *ab initio*, Plaintiffs allege that at the time Mr. DeMarco approved the Third Amendment, he had served as Acting Director longer than the Constitution permits. (Compl. ¶¶ 63-66, 95-96.) According to

Plaintiffs, "serving as an acting principal officer for more than two years is unconstitutional" because "[t]he Recess Appointments Clause, which provides for the temporary filling of certain offices, limits the duration of those appoints [sic] to the end of the Senate's session." (Compl. ¶¶ 95-96.) As the court held in *Bhatti*, 2018 WL 3336782, at *11, this theory also is flawed, conflates two separate and analytically distinct constitutional provisions, and lacks any support in precedent.

Under the Recess Appointments Clause, U.S. CONST. art. II, § 2, cl. 3, the President may appoint officers to fill vacancies during Senate recesses without Senate confirmation, and such officers may serve until "the End of [the Senate's] next Session." When that phrase is read together with the Twentieth Amendment (which states that Congress must assemble at least once a year), the combined practical result is that two years is the longest a *recess appointee* can potentially serve.

This analysis has no application to Mr. DeMarco, who was not a recess appointee. As the *Bhatti* court reasoned, "recess appointees are not analogous to acting officers." *Bhatti*, 2018 WL 3336782, at *11. The constitutional recess-appointment power, on the one hand, and the statutory designation of subordinate officials to temporarily act in senior roles, on the other, are two entirely distinct sources of authority, and recess appointees stand in a very different position than subordinate officials temporarily performing the functions of a higher office.

When the Senate takes a recess within the meaning of the Clause, the President's appointing power is absolute (including even Article III judges) and "[t]he *sole* limit on this extraordinary authority over two of the three branches of government is temporal." *Id.* In contrast, the power to designate acting Executive Branch officials is conferred by statute and subject to plenary control by Congress, including whatever time limit Congress deems

appropriate. *Id*. ("Congress has the power to control the President's choice of acting officers" and "if Congress perceives that the President is abusing his limited power to appoint acting officers, Congress has the ability to address the problem through legislation").

OLC has similarly explained that "the constitutionally mandated limit of 'the End of [the Senate's] next Session" for recess appointees has no application to an individual designated under the Vacancies Reform Act to perform the duties of a Senate-confirmed office in an acting capacity. *Designation of Acting Solicitor of Labor*, 2002 WL 34461082, at *3 (O.L.C. Nov. 15, 2002). Plaintiffs' approach "ignore[s] the differences between holding an office and acting in it." *Id.* "An acting official does not hold the office, but only performs the functions and duties of the office," in contrast to a recess appointee, who "is appointed by one of the methods specified in the Constitution itself; he holds the office; and he receives its pay." *Id.*(alteration, citation, and internal quotation marks omitted).

In short, neither constitutional text, jurisprudence, nor the respective policies animating the Recess Appointments Clause, on the one hand, and the necessity for acting officers recognized in cases like *Eaton* and *SW General*, on the other, provides any basis for transplanting limitations between the two very different contexts.

Plaintiffs' proposed two-year limitation is particularly untenable because it would have the instant effect of invalidating not only HERA's acting director provision, but a bevy of provisions throughout the U.S. Code that authorize acting officials without imposing a strict time limit, including the Vacancies Act itself. *See* 5 U.S.C. § 3346 (permitting acting officials to serve over two years if a nomination (which tolls the 630-day time limit) is pending for at least 100 days); S. Rep. No. 105-250, at 17 (1998) (noting that "most" agency-specific acting officer statutes "do not place time restrictions" on the service).

Indeed, there have been many examples of acting officials leading agencies and performing functions associated with offices requiring Senate confirmation for over two years. *See, e.g.*, https://www.ssa.gov/history/commissioners.html (Social Security Administration had one Acting Administrator for nearly four years (Feb. 2013-Jan. 2017) and another for nearly three years (Sept. 1983-June 1986)); *Doolin Sec. Sav. Bank v. OTS*, 139 F.3d 203, 205 (D.C. Cir. 1998) (Acting Director of Office of Thrift Supervision Jonathan Fiechter served nearly four years); https://www.cpsc.gov/About-CPSC/Commissioners (Consumer Product Safety Commission had Acting Chair for two-and-a-half years (July 2006-May 2009)); https://www.atf.gov/about/executive-staff (Acting Director of ATF has served three-and-a-half years, since April 2015).

Plaintiffs' theory would mean all of these instances (and more) were violations of an absolute two-year limit that no one—including Congress, the President, or the Judiciary—realized existed until Plaintiffs discovered it lurking in the shadows of the Recess Appointments Clause and the Twentieth Amendment. The Court should reject Plaintiffs' untenable and implausible argument based on the constitutional text, *Eaton*, and the longstanding consensus of the political branches.[5]

III. THE COURT SHOULD DISMISS PLAINTIFFS' NONDELEGATION CLAIMS

Plaintiffs' Count IV alleges that Congress violated the nondelegation doctrine by improperly delegating "legislative powers" to FHFA as a government agency. (Compl. ¶¶ 99-

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[5] In *Bhatti*, in the alternative to a two-year ceiling derived from the Recess Appointments Clause, the plaintiffs also argued that the Constitution forbids an acting officer from serving longer than "reasonable under the circumstances" and that Mr. DeMarco's tenure violated this standard. The *Bhatti* court rejected this argument as well. *Bhatti*, 2018 WL 3336782, at *8. Here, Plaintiffs' Complaint raises no such claim, so the Court need not address it.

104.) In Count V, Plaintiffs alternatively allege that when FHFA acts as Conservator, it acts as a private entity—not the federal government—and that Congress improperly delegated to this private entity "Legislative or Executive" powers. (*Id.* ¶¶ 105-110.) As the *Bhatti* court held, both claims fail as a matter of law because the powers FHFA as Conservator exercised by entering into the Third Amendment were neither legislative, executive, nor governmental at all in nature. *Bhatti*, 2018 WL 3336782, at *14-16. That holding dovetails with the Third Circuit's recent observation that the Third Amendment was an "exercise of the Agency's power to take over Fannie and Freddie's assets and operate their businesses." *Jacobs*, 2018 WL 5931515, at *4. To the extent FHFA might be deemed to have acted in a governmental capacity, moreover, HERA provides more than sufficient "intelligible principles" to avoid any nondelegation issue. *Bhatti*, 2018 WL 3336782, at *16-17.[6]

Under the conventional nondelegation doctrine, Congress generally cannot delegate legislative power to another branch of government. *See Mistretta v. United States*, 488 U.S. 361, 371 (1989). Cases holding that Congress violated the nondelegation principle are rare: except for two cases in 1935, the Supreme Court "ha[s] upheld, . . . without deviation, Congress' ability to delegate power under broad standards." *Id.* at 373. The Third Circuit has never held that Congress violated the nondelegation doctrine. The modern test for nondelegation challenges merely requires that Congress provide an "intelligible principle" to guide the agency's exercise of discretion. *United States v. Berberena*, 694 F.3d 514, 523 (3d Cir. 2012).

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[6] In addition to the other arguments set forth below, Plaintiffs Wazee and Brown lack Article III standing to assert Counts IV and V because they purchased their Fannie Mae or Freddie Mac stock long after the Third Amendment took effect. *See supra* at 12.

Under the private nondelegation doctrine, Congress generally cannot delegate sovereign legislative or executive power to a private entity. *See Pittston Co. v. United States*, 368 F.3d 385, 394-95 (4th Cir. 2004). Courts have found impermissible private nondelegations in rare instances when statutes authorized private companies to enact regulations that carried the force of law and were binding on the entire industry, including competitors. *See Carter v. Carter Coal Co.*, 298 U.S. 238 (1936); *Ass'n of Am. R.Rs. v. U.S. Dep't of Transp.*, 721 F.3d 666, 673-77 (D.C. Cir. 2013), *rev'd on other grounds*, 135 S. Ct. 1225 (2015).

An essential prerequisite for either form of nondelegation claim is that the powers at issue are sovereign and governmental in nature. For example, in *Pittston*, the Fourth Circuit analyzed a claim that a statute empowering a coal industry pension fund "to invest the premiums it receives from the coal operators" constituted an unconstitutional delegation to a private entity. 368 F.3d at 397. The court held that "the central inquiry" was "whether the *function* of the Combined Fund in preserving and investing money assessed by statute is governmental in nature." *Id.* at 398. Because that function was "not essentially governmental," there simply was no nondelegation problem. *Id.* at 397. Although *Pittston* involved a private nondelegation claim, the same analysis is dispositive of a claim that Congress improperly delegated its legislative powers to another branch—if the functions at issue are not governmental in nature, *a fortiori* they cannot be legislative in nature.

FHFA's entry into the Third Amendment on behalf of the Enterprises, which was "in essence a renegotiation of an existing lending agreement (albeit with equity rather than debt)," *Jacobs*, 2018 WL 5931515, at *4, was "*not* governmental in nature." *Bhatti*, 2018 WL 3336782, at *16 (emphasis in original). Rather, it falls within the heartland of the tasks of a business operator to "secure ongoing access to capital, manage debt loads, control cash flow, and decide

whether and how to pay dividends." *Jacobs*, 2018 WL 5931515, at *4; *accord Perry Capital*, 864 F.3d at 605; *Saxton*, 901 F.3d at 960-61 (Stras, J., concurring). FHFA's action was an exercise of "business judgment," not the type of legislative or executive function the Constitution commits to Congress or the President. *Perry Capital*, 864 F.3d at 615. The Third Amendment is thus the type of activity "that any conservator would typically undertake, not [an] exercise[] of governmental power." *Bhatti*, 2018 WL 3336782, at *15.

To the extent that the Conservator might be deemed to have functioned in a legislative capacity when it entered into the Third Amendment, Plaintiffs' nondelegation claim would fail because Congress provided intelligible principles to guide FHFA's discretion. *See Bhatti*, 2018 WL 33367872, at *16-17. It is well-established that Congress can "obtain[] the assistance of its coordinate Branches" in carrying out the law. *Mistretta*, 488 U.S. at 372. The requisite intelligible principle may be a "broad standard[]," *id.* at 373, including to act in the "public interest," *Nat'l Broad. Co. v. United States*, 319 U.S. 190, 216 (1943); *see also Yakus v. United States*, 321 U.S. 414, 448-49 (1944) ("generally fair and equitable"); *Milk Indus. Found. v. Glickman*, 132 F.3d 1467, 1475 (D.C. Cir. 1998) ("compelling public interest").

HERA's provisions are "more than sufficient to meet the 'intelligible principle' standard" to avoid any unconstitutional delegation of legislative power. *Bhatti*, 2018 WL 3336782, at *17. In HERA, Congress empowered FHFA as Conservator "take such action as may be . . . appropriate to carry on the business of the [Enterprises] and preserve and conserve the[ir] assets and property." 12 U.S.C. § 4617(b)(2)(D)(ii). Additionally, HERA states the "purpose" of FHFA's appointment as conservator is to "reorganiz[e], rehabilitat[e], or wind[] up the affairs" of the Enterprises. *Id.* § 4617(a)(2). Congress thus "empower[ed] FHFA to 'take such action' as may be necessary or appropriate to fulfill several goals." *Perry Capital*, 864 F.3d at 608.

Congress also provided an explicit roadmap in HERA's amendments to the Enterprises' statutory charters, which specifically authorized securities transactions between the Enterprises and Treasury in order to "provide stability to the financial markets," "prevent disruptions in the availability of mortgage finance," and "protect the taxpayer." 12 U.S.C. §§ 1455(*l*), 1719(g). These provisions offer far more detail than has been present in statutes previously upheld against nondelegation challenges. *See Bhatti*, 2018 WL 3336782, at *17. Thus, even if the powers the Conservator exercised when entering into the Third Amendment could be considered legislative, Plaintiffs' nondelegation claims nevertheless would fail.

IV. HERA'S SHAREHOLDER-RIGHTS PROVISION BARS PLAINTIFFS' CLAIMS

FHFA adopts and incorporates by reference Treasury's arguments in its motion to dismiss that Plaintiffs' claims are derivative in character and barred by HERA's transfer-of-shareholder-rights provision. 12 U.S.C. § 4617(b)(2)(A)(i); *see* Treasury Mem. 8-13 (ECF No. 15-1).

CONCLUSION

For the foregoing reasons, the Court should dismiss this case with prejudice.

Dated: November 16, 2018

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that on November 16, 2018, I filed and served via the Court's ECF system a true and correct copy of the foregoing documents.

/s/ Leslie M. Greenspan
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