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Proceedings recorded by mechanical stenography;  
transcript produced by computer.



1 you.

2 You know, I don't even know how to get a foothold  
3 on this. I feel like I have about five lawsuits here, and a  
4 lot of the claims are kind of -- and the arguments are kind  
5 of tangled with each other. So I guess I'd like to try to  
6 just march through this one count at a time and hear from  
7 all the parties on one count and then hear from all the  
8 parties on the other count just to try to break it up a  
9 little bit.

10 I think it would probably go more smoothly if I  
11 talked to plaintiffs first. So, Mr. Knudson, could I have  
12 you at the podium to talk about Counts One and Two, the  
13 removal of authority and separation of powers argument.

14 MR. KNUDSON: Very good, Your Honor.

15 THE COURT: Just let me know when you're ready to  
16 go there.

17 MR. KNUDSON: We believe that the separation of  
18 powers argument is a structural problem. With respect to  
19 how the agency is formed, it's set up with a single director  
20 with for-cause removal protection.

21 THE COURT: Let's talk about the standing issue  
22 first, if we could. I just want to tell you what bothers me  
23 about the -- my concern about the standing argument from  
24 30,000 feet and then let you take it where you are.

25 So my understanding of -- the heart of your

1 argument here is that the structure of the FHFA violates  
2 separation of powers because a single director is more  
3 insulated from presidential influence, less accountable to  
4 the President than a multi-director board would be. And yet  
5 what you're complaining about here is that this board  
6 essentially entered into a contract with the President, with  
7 Treasury, which is an executive agency.

8 There's just something -- I'm having a hard time  
9 grasping the logic here -- again, this is at the 30,000-foot  
10 level -- that if this board was properly constituted, the  
11 President would have had more influence over it and,  
12 therefore, they wouldn't have entered a contract with the  
13 President. I mean, it's like if -- the subject of the  
14 controversy here is a contract between A and B, and the  
15 thing your clients are mad about is they think the contract  
16 was too favorable to A, Treasury, and not favorable enough  
17 to B, the GSEs, and I don't follow the logic that if A had  
18 more influence over B, then the contract would have been  
19 more favorable to B and less favorable to A. I'm really  
20 having trouble connecting your theory with your harm.

21 MR. KNUDSON: Well, I'd like to address the  
22 standing question sort of in a general sense here because  
23 what you're zeroing in on is would it have been different if  
24 the President had the power to fire DeMarco when the Net  
25 Worth Sweep Rule was adopted.

1 I think the fact Treasury's approval of a Net  
2 Worth Sweep doesn't deprive us, the plaintiffs, of standing,  
3 this still is a structural problem, a violation of the  
4 separation of powers. My clients have been injured by that  
5 and, therefore, they have an injury that's traceable to  
6 government conduct, and it's redressable by this Court  
7 through its equitable powers. So I think, at a general  
8 level, we have standing to pursue this claim.

9 I think it's also clear from the Supreme Court  
10 precedent, *Lujan* and *Free Enterprise*, that we don't have to  
11 speculate about what might've been done had DeMarco, the  
12 acting Director, been subject to presidential removal power  
13 at the President's discretion.

14 THE COURT: Well, what about if you're not -- it's  
15 one thing to be speculating about if Mr. Humphrey would have  
16 still been on the FTC, would the FTC have taken different  
17 actions with his vote versus somebody other's vote or if  
18 this senator had been in the Senate, would the Senate would  
19 have done something different than it did without the  
20 senator. Here it's just irrational to think that if the  
21 President had more influence over DeMarco, DeMarco would not  
22 have entered into a contract that was, in your client's  
23 view, unduly favorable to the President. It completely just  
24 doesn't make sense. It's not us sitting here and  
25 speculating what would one vote on a commission -- one vote

1 different have made. There's just no logic to it.

2 MR. KNUDSON: Well, the fact is we're sitting in a  
3 situation today where the Net Worth Sweep Rule is still in  
4 place, has been confirmed by the Senate, and he is  
5 authorizing payments of dividends to the Treasury. So we  
6 have an ongoing harm that is irrespective of whether or not  
7 DeMarco could've been fired by the President. Apparent  
8 circumstances create an ongoing injury to my clients.

9 In 2012 when DeMarco --

10 THE COURT: But it's the same logical problem. So  
11 the constitutional violation here is that the President  
12 doesn't have enough influence over Watt, Watt is not  
13 sufficiently accountable to the President, and therefore the  
14 argument is that if the President had more influence over  
15 Watt, Watt would act less favorably toward the President by  
16 making -- I mean, because what you're really complaining  
17 about are payments to the Treasury, is the Treasury  
18 enriching itself at the cost of the GSEs and their  
19 shareholders. But, again, I'm just having trouble -- there  
20 seems to be a mismatch between your constitutional theory,  
21 which is the President doesn't have enough influence over  
22 this agency, and your harm, which is the agency is ripping  
23 us off to benefit the President. There's just this  
24 mismatch.

25 MR. KNUDSON: Well, we have to take the facts as

1 they are, and that's basically what *Free Enterprise* says, so  
2 that we don't need to speculate about what might have been  
3 had it be constitutionally set up. It wasn't  
4 constitutionally set up. We have to deal with the  
5 circumstances that existed in 2012. Those circumstances  
6 violated the separation of powers because the President  
7 didn't have removal power. In 2012, what DeMarco did was  
8 consistent with what the administration wanted to do. It  
9 might not be the case today, but we'd have to remove the  
10 for-cause removal protection in order to give the President  
11 proper supervisory authority over the director of the  
12 agency.

13 So the circumstances in 2012 are the circumstances  
14 before the Court today. We have a structural problem with  
15 the separation of powers. DeMarco had for-cause removal  
16 protection according to the Obama administration, according  
17 to DeMarco, so he could act as he wanted to in adopting the  
18 Net Worth Sweep Rule. If we took away that removal power  
19 today, we would have Watt subject to presidential control.  
20 We would still have the Net Worth Sweep Rule in place, and  
21 we need to strike that down because it was adopted under an  
22 unconstitutional structure. That's what *Free Enterprise* is  
23 saying.

24 THE COURT: Well, let me ask you about that. So  
25 the logic of your theory isn't restrained, isn't restricted



1 to the Third Amendment. The logic of your theory is that  
2 every action taken by this agency since its founding has  
3 been invalid. Correct?

4 MR. KNUDSON: If you follow it through, yes.

5 THE COURT: I mean, basically, what has happened  
6 here is we had a bunch of lawsuits where they tried to  
7 excise the growth from the organism (the Third Amendment)  
8 and they failed, and now this new wave of lawsuits you're  
9 trying to kill the organism. You're trying to kill the  
10 host. But killing the host means not just that the Third  
11 Amendment dies, it means everything the agency has done  
12 dies.

13 I'm trying to figure out what this would look  
14 like. So your complaint -- the relief you ask for is that I  
15 declare not only that the agency is invalid -- or that the  
16 removal power is invalid, but that the Third Amendment is  
17 invalid. So what does that look like then? Do we go back  
18 to the Second Amendment -- the world under the Second  
19 Amendment? That's invalid, too. Do we go back to the First  
20 Amendment? I don't even know what it is. That's invalid,  
21 too. Do we go back to the P -- what do you call them,  
22 PSPAs? Those are invalid. Literally what do -- so I say  
23 you win, Mr. Knudson has convinced me this was an  
24 unconstitutionally constituted agency. Now let's all go and  
25 do what?

1 MR. KNUDSON: Well, I think we look to what  
2 happened with *Noel Canning*, which was a determination by the  
3 Supreme Court that the NLRB was improperly constituted, the  
4 recess appointments were invalid. So any decision made by  
5 the NLRB by that majority of the board would be  
6 unconstitutional. So they had to go back and re-set. So  
7 there are ways --

8 THE COURT: I apologize because, as I'm sure you  
9 realize, there was not only lots of briefs to read, but it  
10 seemed like dozens and dozens of cases cited, and a lot of  
11 them are D.C. circuit opinions, which means they are very,  
12 very long, but I didn't read -- but my recollection of that  
13 case is that it was an appeal from an action and they  
14 basically said that the action was invalid. I don't recall  
15 them saying that everything the NLRB did during that time  
16 was invalid. Now, correct me if I'm wrong. I didn't have a  
17 chance to read that.

18 MR. KNUDSON: It was an enforcement proceeding, so  
19 the specific action was overturned. But also the foundation  
20 upon which the board was acting was upset, therefore, what  
21 the board did then once they got properly appointed and  
22 therefore was constitutionally formed, went back and  
23 reaffirmed what had been done before taking --

24 THE COURT: Did the board go back and revisit  
25 every single decision they'd made at the time when the

1 unlawfully-appointed member was participating?

2 MR. KNUDSON: If I recall correctly, they had  
3 basically blanket ratification of administrative-type  
4 decisions, basically what contracts went into it for  
5 supplies and things of that nature, and then re-examined  
6 adjudications on a case-by-case basis. So they went back,  
7 re-set the clock, and started over. It was not a  
8 catastrophic decision to tell the board go back, get  
9 yourself fixed, and then go back and re-examine these  
10 adjudications on a case-by-case basis.

11 Here we're challenging the Net Worth Sweep Rule,  
12 particular action by the agency. If there are other actions  
13 that could be challenged because the agency was  
14 unconstitutionally formed at the beginning, in 2008, there  
15 are other people who might have standing to bring claims on  
16 that basis. They face a statute of limitations problem, but  
17 if they can get over the limitations period and they have a  
18 problem, then they can bring an action. But it's not going  
19 to be very many. And if the agency is properly constituted,  
20 in other words, we have a director that can be removed at  
21 the pleasure of the President, then they can go back -- the  
22 director can go back and re-affirm what has been decided  
23 before under a constitutionally-correct structure.

24 THE COURT: Well, there's a couple of things that  
25 occur to me. One is, is that it's kind of impossible to go

1 back and re-make these decisions under the conditions they  
2 were made. For example, let's say that a director was  
3 ordered to rethink the PSPAs. Well, the PSPAs were reached  
4 at a time when, in the view of at least some, the GSEs were  
5 on the verge of insolvency. This would be like somebody  
6 negotiating for the spare parachute on a plane that was  
7 about to crash or the spare lifeboat on the Titanic. You  
8 can't go back and recreate the conditions and renegotiate  
9 and rethink whether it was a good idea. The conditions  
10 don't exist anymore. It's literally impossible for someone  
11 to sit there now and say, well, geez, is entering the PSPAs  
12 under the conditions that existed in whenever they were  
13 entered, 2008 or 2009 -- it's almost impossible to recreate  
14 the decisions. It's almost impossible for the director now,  
15 who is accountable to the President, to go back and say,  
16 geez, in 2008 would it have made sense for me as conservator  
17 to have entered this deal. It's very hard to do.

18 And I still don't quite know what you want -- so  
19 you're saying, well, logically our argument means everything  
20 this agency has done is unconstitutional and invalid, but  
21 we're, like, complaining about the Third Amendment. Okay.  
22 So I strike down the Third Amendment. So then what do we do  
23 then? If the new director says -- not the new director but  
24 the director whose for-cause restriction is struck down, can  
25 he just say I hereby ratify retroactively the Third

1 Amendment and we're all just where we started?

2 MR. KNUDSON: Well, let me first say that the  
3 exigent circumstances of 2008 don't justify an  
4 unconstitutional agency.

5 THE COURT: Yeah. You still have to act  
6 constitutionally; I know. All I'm saying is you kind of  
7 blithely say in your briefs, well, they just can go back and  
8 decide again whether to do this and do that. Well, they  
9 can't really decide it again under the conditions that  
10 existed at the time. It's really a different decision now.

11 MR. KNUDSON: They would have to make a decision  
12 based on current circumstances; I agree, Your Honor. Now,  
13 whether Director Watt could re-adopt the Net Worth Sweep  
14 Rule would be an issue subject to discussion between the  
15 agency and the Treasury Department and would involve the  
16 executive branch determining whether or not that particular  
17 rule made sense in today's circumstances.

18 So the President then would have the authority  
19 under Article II to be sure that the laws were faithfully  
20 enforced, the due care provision. The Treasury could then  
21 examine under the current circumstances whether or not it  
22 makes sense to run the capital of the entities -- Fannie Mae  
23 and Freddie Mac -- down to zero leaving them subject to  
24 market forces or would it make more sense to allow them to  
25 rebuild their capital structure so they can participate in

1 the market the way they were intended to participate, build  
2 up their capital, which would mean it would make no sense to  
3 re-adopt a Net Worth Sweep Rule. It would be a question  
4 decided by the Director subject to discussions with the  
5 Treasury to determine what made sense or the agency to act  
6 as conservator. It may, in fact, decide that it doesn't  
7 need to be conservator after a certain point in time. The  
8 current circumstances would run the capital of these two  
9 entities down essentially to zero by the end of this year.

10 THE COURT: All of this, of course, they can do --  
11 everything you described to me they can do now, albeit with  
12 the for-cause removal, but any of that stuff he can do now,  
13 right?

14 MR. KNUDSON: Well, as currently constituted with  
15 Director Watt having for-cause removal protection, yes. The  
16 broad powers under the *Perry Capital* decision gives the  
17 agency unfettered control over Fannie Mae and Freddie Mac as  
18 conservator.

19 THE COURT: So by striking down the for-cause  
20 removal provision -- so right now we have a director who can  
21 do all the things you just described and he can think about  
22 whether this makes sense for the GSEs and can -- all that  
23 stuff he can do. He can negotiate changes to the deal with  
24 Treasury if he wants; nothing that keeps him from doing it  
25 now. So your lawsuit, if you win, that same director can

1 still think through the same things about this deal that you  
2 say is too favorable to Treasury with more power -- with the  
3 President having more power over him rather than less.

4 Why would there be any reason that a director who  
5 now is more influenced by the President would renegotiate  
6 deals to make them less favorable to the President who now  
7 has more influence over him?

8 MR. KNUDSON: Well, we're getting into sort of  
9 what --

10 THE COURT: I'm getting back to the standing  
11 issue, I know. It's just a struggle I'm having.

12 MR. KNUDSON: It's a hypothetical question in  
13 terms of what would Director Watt do today if he is subject  
14 to removal by the President for any reason whatsoever. He  
15 would have to negotiate with Treasury as to what to do with  
16 the profits Fannie Mae and Freddie Mac are making, where  
17 should those profits go, what makes most sense in terms of  
18 -- what role will these two entities play in the housing  
19 market. And those are executive-level decisions that under  
20 the Article II take care clause the President should have  
21 the power to influence. That's how the framers set up the  
22 separation of powers. That's why a single director with  
23 for-cause removal protection is particularly problematic and  
24 in especially this particular agency, which is outside of  
25 executive, legislative, for all practical purposes judicial

1 control.

2 THE COURT: Before we get to the merits of that,  
3 let me just ask one more thing about standing. I'm still  
4 not entirely clear. You want me to declare the -- so if you  
5 get what you want, I would declare that the agency is  
6 unconstitutionally structured. I would strike the for-cause  
7 removal provision. I would also declare just one of the  
8 agency's actions over the last ten years invalid, that being  
9 the Third Amendment. And then what happens? So the next  
10 day is the world at the time the Third Amendment was  
11 adopted, is that what's restored? So now the GSEs owe the  
12 ten percent dividend again, the ten percent quarterly  
13 dividend? Is that what the world would look like at that  
14 point?

15 MR. KNUDSON: Well, what we're looking for in  
16 terms of relief would be to pay down the liquidation  
17 preference the Treasury currently has in terms of the remedy  
18 as a result of striking down the Net Worth Sweep Rule. We  
19 aren't challenging the other provisions that have been  
20 imposed on the entities during conservatorship. We're just  
21 challenging the Net Worth Sweep Rule.

22 THE COURT: So does that mean yes? So the day  
23 after my order comes out, we would be basically going back  
24 to an hour before the Third Amendment was agreed to, and you  
25 would be back with the ten percent -- I'm going to be really



1 bad at the vocabulary here, but the ten percent dividend on  
2 the liquidation preference? That's the world you would be  
3 back into, where the GSEs had to borrow from Treasury every  
4 quarter just to pay the dividend to Treasury? That's the  
5 world we'd be back into then?

6 MR. KNUDSON: Well, that would be the provision  
7 that would be in place. The world has changed since then in  
8 terms of the economics of the --

9 THE COURT: I don't mean world, but that's what  
10 the --

11 So your clients would benefit from that. As  
12 shareholders of the GSEs, your clients would benefit from  
13 going back to a world where the GSEs had to borrow every  
14 quarter just to pay the dividend to Treasury? That would be  
15 better for them than the world under the Third Amendment?

16 MR. KNUDSON: Well, under current conditions I  
17 think they wouldn't be borrowing. But, again, I'm  
18 speculating on that particular point. But they would be  
19 better off.

20 THE COURT: But the answer is we would go back to  
21 the arrangement as it existed a minute before the Third  
22 Amendment was -- even though that arrangement was  
23 unconstitutional, too?

24 MR. KNUDSON: That is correct.

25 THE COURT: Okay. So we would exchange one

1 unconstitutional regime for another unconstitutional regime.

2 MR. KNUDSON: Well, we would have a director then  
3 subject to presidential removal at the President's  
4 discretion, and we could then --

5 THE COURT: I have no problem with the idea going  
6 forward. I don't have a problem if I agree with you on the  
7 merits striking the for-cause removal provision and,  
8 therefore, this director going forward would make  
9 constitutional decisions.

10 What I'm having trouble with is the wind back.  
11 And it's really hard -- I was not able to look at a lot of  
12 the decisions that both parties cite -- the three parties  
13 cite, but it's just hard to find an example in history.  
14 *Buckley v. Valeo* is the closest that I could see to my  
15 situation where the Supreme Court at the end of its,  
16 whatever, 400-page opinion has one paragraph basically  
17 saying and as to all the things that these commissioners  
18 have done, we're just going to let them stand without a  
19 whole lot of explanation. Then we follow that with *Ryder*,  
20 which says, well, we're not going to extend that beyond its  
21 facts, which I don't know what that means either. It's not  
22 a real satisfactory group of law. It's hard to find  
23 examples where a judge essentially says that everything an  
24 agency has done for X number of years is unconstitutional.  
25 I just can't find those cases.

1 MR. KNUDSON: Well, we are in a relatively  
2 unchartered area of the law, Your Honor. I agree with that.  
3 But I would point the Court then to -- the *Nguyen* and *Ryder*  
4 cases do cite a *de facto* officer doctrine, which was applied  
5 in *Buckley*, but really doesn't apply to constitutional  
6 violations. So they boxed in *Buckley* to its facts because  
7 of its unusual nature of its case.

8 Then if you look at *Noel Canning*, when they took a  
9 hard look at the recess appointments of the board, then  
10 basically they said that was not constitutional and the  
11 board had to go back and re-examine what it had done when it  
12 was unconstitutionally formed.

13 The same would pertain here, Your Honor, that if  
14 we have to revisit everything the agency has done, so be it.  
15 But it's not going to be a catastrophic event. I think what  
16 the NLRB did was relatively straightforward. We don't see  
17 an agency here that's in a busy adjudicative mode, so there  
18 aren't a lot of decisions -- enforcement actions that are  
19 going to have to be revisited.

20 THE COURT: But it's different, you know, to  
21 revisit an adjudication than it is to essentially declare  
22 everything an agency has done for 10 years to be  
23 unconstitutional. I mean, even the Third Amendment --  
24 there's been five years since the Third Amendment has gone.  
25 Billions of dollars have changed hands in reliance on the

1 Third Amendment. People have made decisions. Your clients  
2 have made decisions. The GSEs have made -- well, the FHFA  
3 as conservator has made decisions. The people who contract  
4 with them have made decisions. Congress has made decisions.  
5 Treasury has made decisions. There's been five years of  
6 people engaging in billions of dollars of economic activity  
7 based upon the Third Amendment. This isn't like a videotape  
8 that you can just rewind and bring everybody back to five  
9 years ago. And I just can't find -- it might exist. As I  
10 said, I've worked on this for a couple of days, but there's  
11 a lot left to go. I just can't find an example -- I've seen  
12 where the Supreme Court has made kind of do-overs on  
13 adjudications or on discrete decisions. But that kind of a  
14 turning back of the clock, it would be almost unprecedented  
15 as far as I can tell.

16 MR. KNUDSON: Well, the circumstances surrounding  
17 the formation of the agency are unique. There is really  
18 only one paradigm, that's CFPB, and that was done after the  
19 formation of FHFA. So we are here in a situation where  
20 there isn't much precedent to look at.

21 I urge the Court to look at *Noel Canning*. That is  
22 really the reset mode that would have to be undertaken. I  
23 would suggest it's not as catastrophic as perhaps you're  
24 concerned with.

25 The fact is if they unconstitutionally imposed the

1 Net Worth Sweep Rule and the funds transferred under that  
2 rule, it should be undone. We're asking for a relatively  
3 straightforward accounting fix to that problem.

4 THE COURT: Well, the accounting would be, among  
5 other things, the transfers under the Third Amendment would  
6 be reversed. But then we would have to figure out what the  
7 GSEs would have owed under the Second Amendment regime,  
8 right?

9 MR. KNUDSON: It would follow, yes, if that's  
10 still in force.

11 THE COURT: I mean, that's what you said we would  
12 do. We would go back to the legal arrangement a minute  
13 before the Third Amendment was signed, and that required  
14 these payments and borrowing. So, you know, one factor in  
15 the equation would be to reverse the Third Amendment  
16 payments, but there have been times -- I think I remember  
17 reading in one of the cases that there was at least once  
18 when Freddie Mac didn't owe anything because it didn't have  
19 any positive net worth for a quarter. Is that right?

20 MR. KNUDSON: That seems to be correct, Your  
21 Honor. But the point would be if we go back to ex ante,  
22 before the imposition of the Net Worth Sweep Rule, we would  
23 have to look at what happened in terms of actual economic  
24 performance and what the ten percent dividend requirement  
25 would have meant. And I don't know what the numbers would

1 be. That was simply something that the agency could work  
2 through.

3 THE COURT: Is it possible that at the end of the  
4 day the result of unwinding the Third Amendment and bringing  
5 us back to what I call the Second Amendment world would be  
6 that -- that sounds like it has to do with guns -- right  
7 before the Third Amendment the possibility would be that the  
8 GSEs would owe Treasury money and so I would at the end of  
9 the day have to be ordering the GSEs to pay money to  
10 Treasury?

11 MR. KNUDSON: You wouldn't be ordering the GSEs to  
12 do that. We would be looking at what would be the  
13 contractual provisions as between the entities and Treasury  
14 with respect to the circumstances under the Second  
15 Amendment. But I don't think we'd be here today if we  
16 expected that it would be a negative result.

17 We believe that the harm caused by the Net Worth  
18 Sweep Rule is so large that the capital structure of the  
19 entities would be dramatically different today.

20 THE COURT: Has anybody just ballparked this, that  
21 if they had never signed the Third Amendment, if they had  
22 just gone with the regime that existed before the Third  
23 Amendment, what the dollars would look like today?

24 MR. KNUDSON: I have not seen that calculation,  
25 Your Honor.

1 THE COURT: Okay.

2 MR. SAWERS: Pardon me, Your Honor.

3 THE COURT: Feel free to interrupt.

4 MR. KNUDSON: Well, I think the suggestion here is  
5 we unwind the Third Amendment. Our preference is to reduce  
6 the liquidation preference. Another alternative is to pay  
7 back the dividends paid to Treasury. That's \$130 billion  
8 without interest calculated to it. So that's a big number.

9 THE COURT: Yeah. Okay.

10 Let's turn to the merits of your  
11 separation-of-powers argument. I want to put off discussing  
12 whether the FHFA was exercising governmental power or  
13 non-governmental power. We'll just put that discussion off  
14 for now. Let's just assume they were exercising  
15 governmental power and the separation of powers applies to  
16 them.

17 You're really riding *PHH*. *PHH* is kind of what  
18 you're advocating here today. I did read all, however many  
19 pages, of *PHH* last night. I wasn't persuaded by it, and  
20 I'll tell you why. Despite my respect for Judge Kavanaugh  
21 and the obviously very scholarly opinion that he wrote, at  
22 the end of the day, I just wasn't persuaded. Let me tell  
23 you why and then tell me why I should've been persuaded.

24 It seemed to me what Judge Kavanaugh did is first  
25 he said the purpose of separation of powers is to protect

1 individual liberty. Then he kind of describes how, well,  
2 good decisions protect individual liberty better than bad  
3 decisions, and a multi-member board makes better decisions  
4 because they're accountable to each other, and they're a  
5 check on each other, and they don't make extreme decisions,  
6 and they get each other's input. It seemed to me as I was  
7 reading that that none of that has anything to do with  
8 separation of powers.

9 To me -- and my understanding might be wrong --  
10 the accountability that matters for separation of powers is  
11 accountability to the President of the United States, not to  
12 other people who are not the President of the United States.  
13 In other words, separation of powers doesn't protect  
14 individual liberty in the abstract. It protects it in a  
15 particular way, by making executive officers accountable to  
16 the President and the President accountable to the voters.

17 So to write this decision about how, well, when  
18 you have multi members of a commission, they can talk to  
19 each other and persuade each other, none of that has  
20 anything to do with being accountable to the President. If  
21 you read *Free Enterprise Fund*, the theme in *Free Enterprise*  
22 *Fund* again and again and again is the degree of the  
23 President's control over the board, the actors, the degree  
24 of accountability to the President.

25 So it seems to me what our case turns on is



1 whether the President has more control over a multi-member  
2 board than he does over a single -- you know what I mean,  
3 multi-member head versus a single-member head, and that that  
4 should be our focus. It's in the *PHH* opinion, but there's a  
5 ton of other stuff in the *PHH* opinion that seems to me to  
6 have nothing really to do with separation of powers.

7 So if I'm right about that -- tell me if you don't  
8 think I am, but if I'm right about that, why is it that the  
9 President has less control over a single-member head than he  
10 does over a multi-member head?

11 MR. KNUDSON: Well, the point we're making with  
12 respect to the structural problem does go with agency, who's  
13 insulated from presidential power, and that's the  
14 Appointments Clause: President shall appoint principal  
15 officers. The removal right is kind of a corresponding part  
16 of the appointments power.

17 So the fact that *PHH* addressed it under the  
18 context of single member and then justified the decision in  
19 part because the multi-member decisionmaking process is a  
20 better decision-making process for reaching the correct  
21 result, therefore, it's probably a permissible structure in  
22 the separation-of-powers analysis, is reflecting the fact  
23 that we are looking at the *Humphrey Executor's* decision  
24 where the court affirmed the multi-member FTC and the  
25 rationale, in part, being that they have this deliberative

1 process that's more effective in reaching the right result.  
2 You might remember on a multi-member commission you could  
3 have staggered terms. The President would have some  
4 influence who is on that commission during the  
5 administration. The President may pick the chairman of that  
6 commission. So there are circumstances set up that make the  
7 multi-member model more reflective of the President's  
8 executive choices.

9 THE COURT: When you're asking how much control a  
10 president has over an agency, are you asking like on average  
11 or are you asking at any particular time? I mean, for  
12 example, let's suppose that the current President, President  
13 Trump, was able to appoint the head of the FHFA on his first  
14 day in office. Well, then the President would have a lot  
15 more control over the FHFA than he would have if it had been  
16 a multi-member agency and he was able to appoint only one of  
17 seven members during his first term or two of seven members,  
18 a lot more control. He got to appoint the one and only  
19 person running the agency. But it's also possible that if a  
20 new head of the FHFA had been confirmed the month before  
21 President Trump took office, he would never get to appoint  
22 anybody who's running the FHFA, and he would have had zero  
23 control.

24 So under one scenario he has much more control  
25 than if it had been a multi-member board. Under another

1 scenario, he has much less control than if it's a  
2 multi-member board. If you look at it over history -- 20,  
3 30, 40 years, if the agency lasts that long, maybe on  
4 average presidents, as a group, would have exercised as much  
5 control over the agency as they would have if it had been  
6 multi-member. It's just a different kind of control. You  
7 see what I'm getting at?

8 When you're measuring the amount of presidential  
9 control over an agency, what's the time frame we're looking  
10 at? A day? A year? Ten years?

11 MR. KNUDSON: I think with respect to the -- I  
12 think we're dealing with a context here where we're not  
13 asking this Court to overturn *Humphrey's Executor*.

14 THE COURT: That's good, because that might be a  
15 loser if you argued it.

16 MR. KNUDSON: I totally agree. That's the  
17 backdrop to the distinction between a single director versus  
18 a multi member.

19 THE COURT: It was the FTC in *Humphrey's Executor*.  
20 It was a multi-membered board. Other than describing in the  
21 fact section, the Supreme Court doesn't cite it -- in fact,  
22 as I was saying to my law clerk, there's just not a whole  
23 lot of reasoning in *Humphrey's Executor*. Right? It's sort  
24 of independent agencies are okay with us, next case. That's  
25 kind of the -- it's hard to glean a lot. A lot of this --

1 like Judge Kavanaugh's opinion, a lot of this is kind of  
2 reading things backwards onto *Humphrey's Executor* that  
3 *Humphrey's Executor* didn't actually say.

4 I think the critical question is whether the  
5 President exercises an unconstitutionally limited amount of  
6 control -- I'm putting this terribly, but whether a single  
7 member agency is insulated from presidential control more  
8 than a multi-member agency; and not only is there less  
9 influence, but that makes it constitutionally infirm.

10 You say in your brief that if you kind of take the  
11 *Humphrey's Executor* level of influence, control, it can't  
12 dip below that. Well, that's not a numerical value. Right?  
13 You kind of look at the FTC, which at that time was five  
14 members. There was certain restrictions about who the chair  
15 was going to be and the bipartisanship, and you kind of  
16 would have to come up with a presidential control score.  
17 And then you'd have to look at the FHFA and you would have  
18 to, like -- it's just very hard to do. These are not  
19 precise numerical values. They're controlled in different  
20 ways by the President. I just don't know what to do with  
21 that.

22 MR. KNUDSON: Well, I agree that the more modern  
23 cases on separation of powers have looked back and come up  
24 with just rationale for explaining *Humphrey's Executor* that  
25 wasn't in the opinion itself.

1           If we take *Humphrey's Executor* as the floor, then  
2 when you have a single director with for-cause removal  
3 protection, you drop below that floor. The president's  
4 appointment power, his removal power has been excised out of  
5 that structure. And that's the violation that by itself is  
6 unconstitutional.

7           THE COURT: But why? Why is it that here's the  
8 *Humphrey* floor and when you take and you switch the agency  
9 from multi member to single member you're below the floor?  
10 Why does the President have less control over a  
11 single-member agency than a multi-member agency?

12           MR. KNUDSON: Well, it comes back to trying to  
13 explain why *Humphrey's Executor* is still good law. In a  
14 multi-member set-up, you have checks and balances built into  
15 the decision-making process both among the members in terms  
16 of their deliberations.

17           THE COURT: Which I believe to be irrelevant for  
18 separation-of-powers concerns or considerations.

19           MR. KNUDSON: Well --

20           THE COURT: The accountability of members of a  
21 board to other people who aren't the President to me has  
22 nothing to do with separation of powers, which is your  
23 accountability to the President. You can be accountable all  
24 day long to each other, but that doesn't make you any more  
25 or less accountable to the President of the United States,

1 and that's what separation of powers is concerned about, the  
2 ability of the -- that's what *Free Enterprise Fund* was all  
3 about, is what is the control of the President, the  
4 accountability of the President, the President's  
5 responsibility for the agency. They can have the most  
6 wonderful pact in the world about how us seven commissioners  
7 are going to be really accountable to each other and hold  
8 each other accountable. That's great, but they are not the  
9 President. The President is the President.

10 MR. KNUDSON: If you set up a multi-member  
11 commission that was something that the President would have  
12 no influence over who was on that commission, then you would  
13 have a similar problem as you do today with the  
14 single-member head of this agency who has a five-year term,  
15 can't be removed during that term unless there's cause, so  
16 that person could serve completely outside one  
17 administration. So, therefore, I think this particular  
18 arrangement should be a straightforward separation-of-powers  
19 analysis. This has isolated the President from removing the  
20 director during the term of the director. That is a  
21 straightforward separation-of-powers problem.

22 Whether or not multi-member commissions are the  
23 problem or not isn't before this Court. What is before this  
24 Court is this agency and how it's set up. Because it's a  
25 single director with a five-year term, isolated from

1 presidential removal power, isolated from legislative  
2 appropriation process, isolated from judicial review, you've  
3 got a situation here where you create an agency that's  
4 outside the structure the framers set up in the  
5 Constitution.

6 THE COURT: Okay. Is there anything more you want  
7 to say on the separation-of-powers issue? I'll have you  
8 back on the Appointments Clause, and on res judicata, and  
9 the other things that we need to talk about.

10 MR. KNUDSON: Just to add that in terms of trying  
11 to justify this single head there really isn't any history  
12 or tradition that would support that as a constitutional  
13 practice. Thank you, Your Honor.

14 THE COURT: All right. Thank you, Mr. Knudson.  
15 Let's see. Mr. Katerberg.

16 MR. KATERBERG: Thank you, Your Honor.

17 THE COURT: Let me ask you first off about the  
18 standing argument. Is your standing argument -- are you  
19 raising it only as a defense to the separation of powers or  
20 are you raising it as a defense to all the claims in the  
21 Complaint?

22 MR. KATERBERG: Well, I guess, Your Honor, there's  
23 different sort of forms of standing arguments. Our primary  
24 standing argument, which is really anchored in traceability,  
25 which is causation and redressability, is as to Count One

1 and, I guess, I sort of view Count Two as sort of an  
2 appendage --

3 THE COURT: I kind of consider the two together.

4 MR. KATERBERG: -- onto Count One.

5 Count Three, we don't make strictly a standing  
6 challenge to that count, but some of the considerations --  
7 de facto officer doctrine, I mean, I think there's maybe  
8 some overlap with the standing doctrine. We don't make --  
9 we're assuming arguendo here. There is an injury in fact,  
10 not conceding that, but we can start with traceability and  
11 redressability. But for the acting director claim, you  
12 know, he did sign the Third Amendment, acting Director  
13 DeMarco, on behalf of the conservator as acting director, so  
14 we don't have a lot to say about traceability there. It's  
15 just that it's really an unprecedented claim. There's a lot  
16 of other reasons, including the non-justiciability, the  
17 political questions that would be engendered why the Court  
18 shouldn't reach the merits.

19 THE COURT: Okay. So as to the standing on  
20 separation of powers, one of the things that I'm struggling  
21 with on this is it kind of seems like I have to reason  
22 backwards from the remedy and that's, I guess, what  
23 redressability makes you do. You look at, well, if the  
24 plaintiff wins, what happens? And if what happens doesn't  
25 affect the plaintiff, leaves the plaintiffs exactly where



1 they were or makes it worse for them, then there's no  
2 standing. Right?

3 MR. KATERBERG: That's exactly right, Your Honor.  
4 It's maybe a little counterintuitive, and I guess I would  
5 say if there's any discomfort with couching it as standing,  
6 you could just look at it as they are not entitled to relief  
7 if the relief that they are seeking wouldn't address what  
8 causes their injury. I mean, we framed it as standing, but  
9 they're here also asking for summary judgment today. They  
10 have a cross-motion for summary judgment. And so if you  
11 can't grant -- if their constitutional theory doesn't get  
12 them to the relief that they're seeking, then that's a  
13 reason not to grant the relief.

14 Just for an example -- this is fairly typical in  
15 Article III standing jurisprudence -- that, for example,  
16 *Franklin v. Massachusetts*, which is a 1992 Supreme Court  
17 plurality opinion, the Court looked at -- it was a challenge  
18 to certain actions in connection with a 1990 census, and  
19 Massachusetts challenged actions with the census because it  
20 reduced Massachusetts' congressional representation in  
21 Congress. One of the issues was would the court have the  
22 power to enjoin the President, enjoin the President to  
23 handle the results of the census differently, and  
24 redressability ultimately turned on that. Now, the court  
25 found that there was redressability, but only because the

1 Massachusetts injury could be addressed by enjoining lesser  
2 officials because everybody sort agreed that you couldn't  
3 enjoin the President.

4 There's other cases I could cite, but that sort of  
5 illustrates this principle that, you know, if a ruling on  
6 the constitutional issue wouldn't get them what they are  
7 looking for in terms of assuaging their injury, then really  
8 the game is not worth the candle, and the Court doesn't need  
9 to reach out to decide novel constitutional questions.

10 THE COURT: And so what in your view -- I wasn't  
11 asking Mr. Knudson questions about this rhetorically; I  
12 sincerely struggle with this. Suppose I agreed with him  
13 that the agency as it has been constituted from the  
14 beginning is unconstitutional because of the for-cause  
15 removal protection. So let's say that's my ruling on the  
16 merits. Okay? Now what? In your view, now what?  
17 Obviously, what they want is for the Third Amendment to go  
18 away and for us to go back to a different unconstitutional  
19 time, the unconstitutional time before the Third Amendment,  
20 as opposed to the unconstitutional time after the Third  
21 Amendment. What do I do?

22 MR. KATERBERG: So I think if I can just dispute  
23 the premise, because I think it's completely wrong, and I  
24 think we can be guided here by *Free Enterprise Fund*, which,  
25 of course, is the Supreme Court's most recent pronouncement

1 of this area -- this was a live issue in *Free Enterprise*  
2 *Fund*. If you look at the end of Chief Justice Roberts's  
3 opinion, the issue he addressed is the plaintiffs in that  
4 case, which was an accounting firm challenging the PCAOB,  
5 they wanted relief that would include total invalidation,  
6 declare everything --

7 THE COURT: I couldn't tell -- and I read it last  
8 night, but I didn't have time to go look at the briefs.  
9 There was this -- there is this line in there. He says  
10 you're referring to petitioner's complaint, arguing that the  
11 board's "freedom from presidential oversight and control"  
12 rendered it "and all power and authority excised it" in  
13 violation of the Constitution. We reject such a broad  
14 holding. Now, I couldn't tell, that could mean that what  
15 they were arguing is that basically the board has to shut  
16 down and it can't do anything going forward or it could mean  
17 everything the board has ever done should be invalidated. I  
18 mean, it's a little ambiguous what Chief Justice Roberts is  
19 characterizing an argument, and it wasn't clear to me what  
20 exactly the party was arguing.

21 MR. KATERBERG: I understand, and we may be able  
22 to shed some light on that. We have copies of the *Free*  
23 *Enterprise* complaint, which we would be happy to hand up to  
24 Your Honor. What you will see is that they show that what  
25 was sought in that case was an injunction and voiding of

1 past actions --

2 THE COURT: Okay.

3 MR. KATERBERG: -- against this accounting firm,  
4 including the investigation. So that was a live issue.  
5 That was rejected in that case.

6 And I think even *PHH* -- I mean, I don't want to  
7 say too much about *PHH* because I don't think --

8 THE COURT: You're exactly right, and that  
9 occurred to me when I was reading *PHH*, is Judge Kavanaugh --  
10 it would have been very easy for him to say since the  
11 decision was made by an unconstitutionally-constructed  
12 agency, it doesn't stand period. But instead he spent pages  
13 and pages going through the merits and then remanded it for  
14 more action consistent with the opinion. So even Judge  
15 Kavanaugh didn't seem to think that everything that had  
16 happened to date was wiped out. That would have been -- he  
17 could've cut 50 pages off his opinion if he had done that.

18 MR. KATERBERG: That's exactly right, Your Honor.  
19 In fact, I think he said that explicitly. At the end of the  
20 opinion, he said basically what happens, the  
21 unconstitutional violation, if there is one, is that the  
22 President's power of removal is limited. So the remedy for  
23 that is that you excise that. So going forward if the  
24 President wants to renew the director of the CFPB or the  
25 director of the FHFA if, in fact, for-cause removal is

1 unconstitutional, the President is not going to be limited  
2 by that anymore. And that is the remedy in this situation.

3 I think *Free Enterprise* stands for that  
4 proposition. I think the *PHH* panel opinion, as much as I  
5 disagree with it in many other ways, I think that also  
6 supports that proposition. And also more recently in the  
7 *John Doe Company v. CFPD* case from earlier this year, this  
8 is 839 F.3d at 1133, the D.C. Circuit said vacature of past  
9 actions is not routine. And the position of that company in  
10 that case, which was essentially somebody trying to come in  
11 and piggy backing on the *PHH* panel opinion and get an action  
12 vacated, so that ignores traditional constraints on  
13 separation-of-powers remedies.

14 We don't generally burn down the house, just kind  
15 of lay waste to everything that has happened if there is a  
16 removal restrictions issue. The way that these removal  
17 restrictions cases developed in the first instance, most of  
18 the early cases were actually about suits for back pay. So  
19 *Myers v. United States Postmaster General*, the issue was  
20 whether -- it's like a Title VII case -- could the President  
21 remove him, because if he couldn't, he should get pay for  
22 that time. *Humphrey's Executor* --

23 THE COURT: Historically did it ever come up --  
24 like in *Humphrey's Executor*, obviously, he's suing for the  
25 back pay of Humphrey, the deceased Humphrey. But the

1       implication of the opinion is that President Roosevelt acted  
2       wrongly in removing Humphrey, that Humphrey should have been  
3       a member of the FTC, that he should have been exercising the  
4       authority and his vote on the FTC. There is, obviously, no  
5       hint in the opinion itself that the FTC needed to go back  
6       and re-do anything because one of its members had been  
7       unconstitutionally removed.

8               Do you know just historically whether anybody  
9       looked back at all at that point or did it never even occur  
10      to anybody that any of the actions taken in Humphrey's  
11      absence were invalid?

12             MR. KATERBERG: I couldn't say that I have scoured  
13      for exhaustive research, but I have seen nothing -- and I  
14      have studied this area quite extensively -- I have seen  
15      nothing to indicate that past actions by the FTC were called  
16      into question in connection with the issue in that case.

17             There is another one in the 1950s, *Wiener v.*  
18      *United States*, which is the War Claims Commission, a Supreme  
19      Court case, and there again it was back pay.

20             I think where this notion of going back and  
21      invalidating really first came up -- the first removal  
22      restrictions case I'm aware of where it really came up is  
23      *Morrison v. Olson*. Okay. But that is a very different  
24      situation than what we have here because Ted Olson was  
25      essentially held in contempt by the independent prosecutor.

1 And I don't think it's that far of a reach to say that if  
2 you are held in contempt for not complying with the subpoena  
3 and you challenge the validity of the subpoena and you're  
4 right that the independent counsel is unconstitutional, you  
5 can probably, you know, get your contempt lifted and get the  
6 subpoena voided.

7 I think it's a very different situation than what  
8 we have here, which is a transaction between the conservator  
9 and another party that is alleged to have an incidental  
10 effect on somebody and they sue five years later.

11 THE COURT: But what makes this so hard, as I read  
12 the cases on remedies, is there's nothing quite like this.  
13 We have some cases on remedies that arise out of  
14 adjudications, like what is the -- the case that limited  
15 *Buckley* to its facts?

16 MR. KATERBERG: I think Your Honor is thinking of  
17 *Ryder*.

18 THE COURT: I was going to say Ryan and I knew  
19 that wasn't right. *Ryder*. That's like an adjudication.  
20 You know, when you're before somebody who you don't think  
21 has the authority to adjudicate your claim, you appeal your  
22 claim up and if you win, you win. The action against you  
23 doesn't stand. But this isn't an adjudication that we have  
24 before me today.

25 It's also not like pure rulemaking where you

1 strike down a rule. Essentially I'm being asked to strike  
2 down a contract, but the route through that is first to  
3 declare that the agency doesn't have -- everything it has  
4 done is illegitimate because of its structure, and then I'm  
5 being asked to strike down a contract by people who weren't  
6 parties to the contract but who say they're affected by the  
7 contract. There's really just nothing like that that I can  
8 find or that I saw discussed in the cases. It's a real  
9 unusual situation.

10 MR. KATERBERG: It's very different than any of  
11 the cases, Your Honor. And there is a presumption of  
12 regularity that attaches to government action. That's kind  
13 of one of the policies animating the de facto officer  
14 doctrine, is that when actions get taken if they're not sort  
15 of challenged in real-time and folks depend on those actions  
16 and rely on them, we don't generally go back and upend the  
17 past actions.

18 I want to say a couple of things about the  
19 adjudications case, because I think it's very important.  
20 First, as Your Honor mentioned, *Ryder* limited *Buckley*, but I  
21 would also emphasize *Ryder* limited itself and the other  
22 Supreme Court cases in that same line.

23 So there's a case call *Nguyen*. They talk about  
24 this policy being really specific to cases involving judges.  
25 So if you are criminally convicted and you're up on appeal



1 and then it turns out one of the judges on your panel is  
2 actually an Article IV judge of a territorial court that  
3 can't constitutionally sit, that's a problem. I think what  
4 the court is saying in those cases is, basically, we're not  
5 going to do harmless error analysis. Right? So if your  
6 trial judge or your appellate panel was not properly  
7 constituted because there was somebody that didn't enjoy the  
8 life tenure that Article III judges get, that is sort of per  
9 se invalidation. But the Court is very careful to limit it  
10 to that context. Okay, that's point number one.

11 Point number two is I believe you won't find any  
12 case that does that in the context of a removal restriction.  
13 So those cases all involve -- the nature of the challenge  
14 was an Appointments Clause challenge or a challenge under  
15 the statutes that govern the terms under which people have  
16 to be appointed.

17 Let's talk about *Noel Canning*. Counsel referred  
18 extensively to *Noel Canning*. *Noel Canning* involved a  
19 problem with recess appointments that deprived the NLRB of  
20 the quorum that it needed to act. So if the body that's  
21 taking action against you -- specifically against you, not  
22 the incidental effect of a contract, specific adjudicative  
23 exercise of sovereign authority against you, but it didn't  
24 have the power to act because it didn't have a quorum, it's  
25 logical in that instance that that would be voidable. I

1 don't think that at all supports extending that principle to  
2 --

3 THE COURT: Did the board do what Mr. Knudson  
4 said, which was it didn't just reconsider the case in *Noel*  
5 *Canning*, but it went back and had to re-adjudicate all the  
6 cases it had at the time it didn't have a quorum?

7 MR. KATERBERG: I am a little unclear on that.  
8 There may have been some kind of ratification that was done  
9 after the fact. Those kinds of things are sometimes done as  
10 cures for this.

11 But there's another standing point that I want to  
12 talk about just briefly because I don't think it has been  
13 touched on, which is the action here was taken by an acting  
14 director who didn't actually enjoy the for-cause removal --

15 THE COURT: I want to get back to that in just a  
16 second. Don't let me forget about that. But before we  
17 leave the broader topic, of all the cases out there, which  
18 do you think -- on this remedies issue what do you do if --  
19 again, supposing I agree with the plaintiffs here that the  
20 for-cause removal restriction is unconstitutional, the  
21 question then being what do I do? What, of all the cases,  
22 do you think is the closest ones to -- recognizing there is  
23 nothing exactly like this, what's the closest one, do you  
24 think, to these facts?

25 MR. KATERBERG: I would throw in my lot with *Free*

1        *Enterprise Fund* and say as far as the remedy there, I think  
2        what that would look like is Your Honor would issue a  
3        declaratory judgment that the for-cause limitation won't be  
4        operative and, you know, that could go up on appeal.  
5        Obviously, we would resist that very strongly in terms of  
6        the remedial import. That's what it would be. And that  
7        would not help them at all.

8                As Your Honor noted, this is a two-way contract,  
9        so the President through his plenary control over the  
10       Secretary of the Treasury -- everybody agrees the Secretary  
11       of the Treasury is removable, at will, serves at the  
12       pleasure of the President. So if the President had wanted  
13       to resist this transaction at any time, he had a plenary  
14       veto power all along, never interrupted. All he had to do  
15       was tell the Secretary of Treasury, hey, let's not do this.

16               So the notion that by being sort of made to be  
17       more subservient to the President because that's deemed  
18       constitutionally required -- the notion that the FHFA  
19       director being more subservient to the President would  
20       result in a more independent look at the transaction just  
21       makes no sense. I think it's completely and utterly  
22       logically backwards.

23               If their claim were different, if their claim were  
24       that the FHFA was not independent enough from the President,  
25       the opposite of the claim they're making today -- and I

1 don't want to suggest that that claim would have any legal  
2 or factual basis because then we'll see that in the next  
3 wave of complaints, but that at least would make some  
4 logical sense. Right? But the claim that they had today --

5 THE COURT: As I said, from 30,000 feet it's a  
6 very odd lawsuit. I mean, the constitutional violation here  
7 is the President didn't have enough influence over the  
8 agency. And the complaint is if he'd had more influence,  
9 the agency would have not done this thing that so favored  
10 the President. It just doesn't make logical sense.

11 MR. KATERBERG: You don't need to look further  
12 than their own Complaint because in paragraph 60 they talk  
13 about how Treasury trumpeted this transaction and Treasury  
14 supported it. Paragraph 65 they said it's a massive  
15 financial windfall.

16 THE COURT: Right. Treasury is the President.

17 On the issue of whether the acting director was  
18 removable for cause, I was more inclined toward the  
19 plaintiffs on that issue than toward you. I mean, the  
20 implication of your argument is that an independent agency  
21 goes from being an independent agency to not independent  
22 agency to an independent agency to not an independent agency  
23 depending on whether there is an acting director. That  
24 seems really hard for me to believe that that's what  
25 Congress intended. Given the way the statute is written,

1 given that the acting director has all the same authority,  
2 responsibilities, powers, it would be an odd circumstance  
3 that an agency when it has a confirmed director is an  
4 independent agency, but when it has an acting director, it's  
5 not an independent agency. That's whether an agency is  
6 dependent turns on, is basically the President's authority  
7 over its head. It's hard for me to believe that that's what  
8 Congress intended.

9 MR. KATERBERG: So let me try to clarify that  
10 because I don't want Your Honor to have the impression that  
11 we're saying that it wasn't independent at the time of  
12 DeMarco being acting director. It's an independent agency  
13 all along. But being independent in a vacuum, sort of that  
14 label, is not something that constitutional significance  
15 attaches to. An independence is simply being described that  
16 way. That description, there's no basis for saying that  
17 violates Article II.

18 Where an Article II issue potentially comes up is  
19 a specific manifestation of independence, which is the  
20 President having only limited power to control the agency or  
21 to supervise the agency and, more specifically, the power to  
22 remove. There we have a statute, and it's about as clear an  
23 illustration of the *Russello* presumption, that you attribute  
24 significance to the fact that Congress puts certain words in  
25 one part of the statute but not in another. And for the

1 permanent director after Senate confirmation they serve for  
2 a five-year term, unless removed before the end of such term  
3 for cause by the President.

4 THE COURT: But 4512 says the acting director  
5 serves until the return of the director or the appointment  
6 of a successor. So that sounds like -- I mean, on its face  
7 that's even more protection than the -- literally speaking  
8 here, the President couldn't remove this person at all.

9 MR. KATERBERG: Well, so I want to be careful  
10 about this because with removal -- so I want to explain sort  
11 of the mechanics of how the acting directorship works.

12 So what you have with an acting directorship, and  
13 this is laid out in a number of OLC opinions, is essentially  
14 you are deputizing a subordinate employee to temporarily  
15 perform the functions of the higher office. Okay?

16 So when we talk about removing DeMarco, could  
17 DeMarco have been removed, we're not talking about removing  
18 him from his permanent civil service spot. That's not the  
19 issue. The issue is could he be required to cease acting as  
20 the director. I guess maybe "removal" is not quite the  
21 right term for it. I mean, one way to put it -- I think the  
22 way Treasury puts it in their brief is accurate. It's an  
23 issue of the President revoking his designation.

24 So the President designates a deputy director to  
25 serve as acting director, but there's nothing limiting the

1 President's power to revoke that designation. The President  
2 could revoke it at any time, designate somebody else to act  
3 as director. And so there's several ways in which an acting  
4 director could cease to act in that capacity: switch to a  
5 new acting director or somebody gets appointed -- nominated  
6 by the President, confirmed by the Senate. But in all  
7 events, they don't enjoy the protection that a full director  
8 enjoys, which is --

9 THE COURT: Well, doesn't that de facto then mean  
10 that the agency isn't independent? The word "independent"  
11 in the phrase "independent agency" means independence from  
12 the President, and the independence from the President comes  
13 from the restriction on the ability of the President to  
14 remove the head of the agency. If the President doesn't  
15 have that authority or if the President isn't so restricted,  
16 the agency doesn't seem to be independent to me.

17 MR. KATERBERG: So there are other ways that the  
18 independence is manifested. This is the particular one that  
19 has constitutional significance. I don't know that they're  
20 really challenging the other ways that the agency's  
21 independence is operationalized. Unfortunately, I can't  
22 sort of catalog them very specifically, but there's issues  
23 about sort of how you report to Congress, you know, how you  
24 are sort of situated vis-a-vis the President and the White  
25 House staff and that sort of thing. Those kinds of things

1 would be constant throughout, whether it's a director or an  
2 acting director.

3 So, again, I want to be clear that we're not  
4 suggesting that it ceases to become independent, but as to  
5 this particular manifestation of independence, which happens  
6 to be the only one that's challenged and the only one that  
7 has constitutional significance, it's basically turned off  
8 during the term of -- or I shouldn't say "term" because it's  
9 not a term, but during the temporary service of an acting  
10 director.

11 THE COURT: Okay. Let's turn to the merits of the  
12 separation-of-powers claim. As you heard me say, I wasn't  
13 really persuaded by *PHH*, and you heard me explain why --  
14 just by the approach of *PHH*, which there just was so much  
15 focus on the quality of decision-making and the  
16 accountability of non-presidents to other non-presidents.

17 I think of this inquiry to be -- to what we're  
18 looking at is the degree of presidential control over the  
19 agency or, put another way, the accountability of the agency  
20 to the President. That's the focus of *Free Enterprise Fund*.  
21 That's what I think the proper focus is. But I don't know  
22 how you measure this.

23 As you heard me say to Mr. Knudson, in some ways a  
24 particular president could have far more control over a  
25 single-headed agency, as my hypothetical about President



1 Trump appointing the head in his first year of office, than  
2 you would have if there is a multiple commission. Another  
3 hypothetical is you could have a president with literally  
4 zero control over the agency if the five-year term started  
5 and ended after the president's four-year term. I don't  
6 know what to do with that. I don't know how you measure a  
7 level of control in *Humphrey's Executor*, say that that's a  
8 floor, which is not necessarily true -- *Humphrey's* didn't  
9 say you couldn't go below this -- and then compare a whole  
10 different agency set-up degree of control. I don't know if  
11 you have any thoughts about how you go about doing that.

12 I mean, I think the most damaging thing to your  
13 case is you do have this set up in a way -- besides the  
14 historical -- you have the problem with the history, which  
15 is something that's pretty new, pretty unusual. We have the  
16 possibility of a president of the United States being  
17 elected, serving a full four-year term, and never having any  
18 influence whatsoever over the agency because he never gets a  
19 chance even to appoint a single member of a multi-member  
20 commission.

21 MR. KATERBERG: So several thoughts on that, Your  
22 Honor. First, as to sort of the mode of analysis, how Your  
23 Honor approaches kind of looking at whether there is an  
24 incremental loss of control and it's kind of the time frame  
25 focus for that. I mean, I know we've moved on to merits, so

1 I don't want to take us back and I won't belabor it, but I  
2 think a logical place to look at it would've been as of the  
3 time of the agency action that is being challenged where, as  
4 I just got through explaining, DeMarco didn't have the  
5 for-cause protection. So you could look at it that way, is  
6 at the time that he made that decision. And that would be  
7 logical because we generally want the constitutional issue  
8 to be anchored in the thing that's actually causing them  
9 their injury.

10 Another way to look at it would be sort of  
11 holistically, big picture, and that's Judge Mariani of the  
12 Middle District of Pennsylvania -- I commend Your Honor to  
13 the *Naviant* decision involving the FCPB earlier this year.  
14 He actually did -- or his law clerk did -- a mathematical  
15 analysis and looked at the comparison of the CFPB to the FTC  
16 and looked at sort of with the staggered terms and the  
17 number of commissioners how does it actually compare. And  
18 what he found, and the assumption was presidential four-year  
19 terms and the CFPB director having a five-year term, which  
20 happens to be the same as a permanent Senate-confirmed FHFA  
21 director, 80 percent of presidential terms will enable a  
22 president to appoint a director. Whereas, based on the way  
23 that the FTC, its number is set and the terms are staggered,  
24 only four-sevenths, which is 57 percent of presidential  
25 terms, will enable a president to appoint a controlling

1 majority of three or more commissioners.

2 So looking at it sort of from that holistic  
3 perspective of how it's going to play out over time,  
4 statistically a president is more likely to have control  
5 over a single-director agency.

6 I also want to talk about the history because I do  
7 think it's very important to bring the Comptroller of the  
8 Currency into this. You know, they claim that this is a  
9 very sort of recent phenomenon. Social Security  
10 Administration, not exactly sort of a little two-bit agency.  
11 It manages a trillion dollars a year in retirement benefits.  
12 The Office of Special Counsel --

13 THE COURT: Didn't *PHH* say the comptroller is not  
14 -- maybe I'm mixing it up with somebody else. I thought *PHH*  
15 said the comptroller did not enjoy for-cause removal  
16 protection.

17 MR. KATERBERG: You're right about that, Your  
18 Honor. There's an issue about that. It's a little bit more  
19 ambiguous because it doesn't contain a provision that's  
20 worded in the traditional way of saying cause or good cause.  
21 Or the other formulation you often see is inefficiency,  
22 neglect of duty or malfeasance.

23 What the comptroller statute says -- and this is  
24 12 U.S.C. 2 -- is that the President can remove the  
25 Comptroller of the Currency only for reasons communicated to

1 the Senate. And I should mention that that's -- the  
2 comptroller has a fixed term of years, so in that way it's  
3 similar to the others. And so there's a dispute about what  
4 "reasons" mean. Evidently, Judge Kavanaugh is of the view  
5 that "reasons" doesn't require much. But, I mean, I've  
6 looked in several dictionaries and thesauruses and, as far  
7 as I can tell, "reason" and "cause" is pretty much  
8 synonymous with each other. I think when courts talk about  
9 employment at will and contrast it with a for-cause standard  
10 for removing an employee in the ordinary context, the  
11 typical thing you hear is that if employment is at will, you  
12 can dismiss for a good reason, a bad reason, or no reason at  
13 all. So I think there might be shades of difference between  
14 those two, but it certainly --

15 THE COURT: It does suggest you have to have a  
16 reason, because if you don't have a reason, you can't  
17 explain your reasons. Yeah, I understand what you're  
18 saying. I take it it's never been adjudicated, though?

19 MR. KATERBERG: It's never been adjudicated.  
20 There is an 1868 opinion from the Eastern District of  
21 Pennsylvania. The opinion is actually dealing with a  
22 totally different question, but I think it's -- it's cited  
23 in our briefs. It's called *Case of the District Attorney*.  
24 I think it's valuable in guidance because it's just so  
25 contemporaneous, and it sort of mentions this example as

1 kind of a marked departure of the past practice up to that  
2 date of the President having at will removal authority over  
3 officials.

4 The government -- the court in the case *Future*  
5 *Income Payments*, which is another recent decision involving  
6 the CFPB -- I believe that was the Central District of  
7 California -- they went with our argument on this. They  
8 included the OCC as an example of an independent agency.

9 There's one other kicker to this, which is the  
10 statute of the OCC -- and this is 12 U.S.C. 1(b)(1) --  
11 specifically forbids the Treasury Department, which is --  
12 organizationally the OCC is housed within the Treasury  
13 Department, and the statute specifically forbids Treasury  
14 from intervening or interfering in any OCC proceeding or  
15 rule or adjudication or anything like that.

16 So, yes, it's not worded exactly the same way, but  
17 I think it's important. Certainly, kind of functionally,  
18 the OCC is more similar to FHFA in terms of being a  
19 financial regulator than these other examples. And it  
20 actually dates back to the Lincoln administration, which  
21 gives it a longer pedigree than the FT C, than the ICC,  
22 which is sometimes thought of as the first independent  
23 multi-member commission. Before any of those were a glimmer  
24 in anybody's eye, we had the OCC, a federal financial  
25 regulator, and Congress adopting this model that they were

1 going to be to some degree independent from the President.

2 THE COURT: Okay. Anything more you wanted to say  
3 on separation of powers?

4 MR. KATERBERG: I don't think so, Your Honor --  
5 actually, one point. I mean, the multi-member structure --  
6 the ironic thing is up until the panel opinion in *PHH*, a  
7 multi-member structure for an agency was deemed to be sort  
8 of an indicium of independence.

9 So the idea that you would have multiple members  
10 was seen as something that would lessen presidential  
11 influence. There's lots about this in the scholarship,  
12 because a president might get an appointment or two -- and I  
13 think this is what Judge Mariani was talking about -- but  
14 the President is going to have to deal with people who are  
15 holdovers from the previous administration that are going to  
16 dissent from everything his chosen appointees want to do.

17 So it's just very ironic because the theory behind  
18 the plaintiffs' claim today and kind of the idea that is  
19 woven into the *PHH* panel opinion is that the multi-member  
20 nature acts as a check on the independence. But in reality,  
21 if you kind of think about how this plays out over time,  
22 it's much more likely to contribute to independence than to  
23 check it.

24 THE COURT: Yeah. It occurred to me if you took a  
25 president who really cared about a particular agency's work,

1 there was some matter the President really had at issue, if  
2 you said to the President, well, we'll either let you  
3 appoint two of the seven members of the Commission during  
4 your four years in office or we'll let you during the last  
5 two years of office have your sole -- you get to appoint the  
6 one person heading the agency, I suspect most presidents  
7 would happily take the one person over the two-sevenths or  
8 the three-sevenths even if it was only for a limited time.  
9 So it's very hard to make apples to apples comparison.  
10 These control issues are going to depend very much on how  
11 many members, how long the terms are, who the chair is, how  
12 the chair is selected, whether there's a bipartisan  
13 requirement, what a quorum is. It's really just very hard  
14 to make apples to apples comparison.

15 MR. KATERBERG: Well, that's exactly right, Your  
16 Honor. I think where this discussion has sort of led is  
17 that their argument as it evolved, it's really not so much  
18 about having a single director. It's about the fact that  
19 the single director in this instance happens to have a term  
20 of five years because that, as I heard the argument on the  
21 other side, is kind of the principle issues that's driving  
22 this, is the hypothetical you could have a president that  
23 gets all the way through their term without being able to  
24 appoint an FHFA director. Of course, you could have the  
25 very same thing with a multi-member body depending how long

1 their terms are. The Federal Reserve Board of Governors has  
2 terms that are much longer. I believe it's 14 years. I  
3 don't know how they're staggered. Essentially, it's kind of  
4 migrated to really a constitutional challenge than the one  
5 in the Complaint. I don't want to suggest ideas to them  
6 because then we'll see that pop up in the next wave of  
7 complaints, but it's not really about single member anymore.  
8 It's about that it's five years as opposed to two years or  
9 three years or four or whatever.

10 THE COURT: Well, another thing that factors in  
11 this is just because a president can appoint somebody  
12 doesn't mean he will be successful, especially these days.  
13 If you did the research, I suspect there's going to be --  
14 there are multi-member commissions where in theory the  
15 President was supposed to be able to appoint one or two or  
16 three people and the Senate never confirmed the appointment,  
17 so the President in effect never got anybody on the --

18 MR. KATERBERG: We could probably go back into  
19 history and find many, many examples of multi-member  
20 commissions that have really been at loggerheads with  
21 presidential administrations and frustrated the President in  
22 their attempt to achieve their policy agenda.

23 THE COURT: Okay. Thanks, Mr. Katerberg.

24 The Treasury lawyer. I'm sorry, I don't have your  
25 name written down here. What was your name again?



1 MR. MERRITT: Mr. Merritt, Your Honor. Robert  
2 Charles Merritt.

3 THE COURT: Merritt?

4 MR. MERRITT: Yes. M-E-R-R-I-T-T.

5 THE COURT: Okay. Mr. Merritt, other than saying  
6 this isn't Treasury, is there anything more that you wanted  
7 to say? You can take the podium if you do.

8 MR. MERRITT: No, Your Honor. We don't have  
9 anything else to add to the arguments that have been  
10 addressed to this point.

11 THE COURT: Mr. Knudson, let me have you back up  
12 to say anything more that you'd like, and then we'll take a  
13 break and turn to the other issues after the break.

14 MR. KNUDSON: Thank you, Your Honor.

15 With respect to the injury, I would turn the  
16 Court's attention to paragraph 3 of our Prayer For Relief  
17 that sets out the alternatives: pay down the liquidation  
18 preference or the return of the dividends. That was the  
19 \$130 billion number I gave you earlier. It's certainly  
20 concrete harm.

21 I'd like to say with respect to the issue of  
22 separation of powers, the President's removal power, we have  
23 a circumstance here where this agency may be in a situation  
24 where the President may never have any opportunity to pick  
25 the director. If there's any chance he has no influence,

1 that should be a clear indication that there's a  
2 separation-of-powers problem, a violation of the  
3 Appointments Clause of Article II.

4 With respect to what I heard about the presumption  
5 of correctness, that doesn't apply to a separation-of-powers  
6 violation.

7 With respect to *Ryder*, the --

8 THE COURT: I'm sorry?

9 MR. KNUDSON: *Ryder*, the case that was the  
10 criminal conviction with the Article IV judge on the panel.

11 THE COURT: Oh, right. Okay.

12 MR. KNUDSON: That, of course, was a decision  
13 involving that particular conviction and reversing it. But  
14 I would submit that the other defendants who might have been  
15 convicted or had their appeals decided by a  
16 similarly-constituted panel would have an opportunity to  
17 seek habeas relief. I think the courts then would be  
18 required to take a look at what the Supreme Court said in  
19 *Ryder* and review the conviction.

20 I think what we're talking about simply here is --  
21 last point I want to make here is with the OCC and the  
22 statutory provision that's cited that the President has to  
23 give a reason. That's such a narrow, minor limitation on  
24 his removal power. He could have any reason he wants. He  
25 just has to state what that reason is. So you would give it

1 a constitutional interpretation to say that's not any  
2 limitation on the President's removal power. So as far as  
3 establishing long-term precedent, that does not stand.

4 Thank you, Your Honor.

5 THE COURT: Thank you.

6 All right. Let's take a 10- or 15-minute break,  
7 and we'll come back and start working our way through the  
8 other issues.

9 THE LAW CLERK: All rise.

10 (A brief recess was taken.)

11 THE LAW CLERK: All rise. This court is now in  
12 session.

13 THE COURT: I want to turn to Count Three, relying  
14 on the Appointments Clause. Mr. Katerberg, if I could have  
15 you first to the podium on this count.

16 MR. KATERBERG: Thank you, Your Honor.

17 THE COURT: So is there any limit on how long an  
18 acting director can serve, any limit do you think under the  
19 Constitution?

20 MR. KATERBERG: I would say not, not a  
21 judicially-enforceable limit and not a numerical limit. We  
22 know that OLC advises administrations to make appointments  
23 within a timely matter, but it's not simply a calculation of  
24 a number of months or a number of years. There's a lot of  
25 factors that go into that.

1 THE COURT: How do you answer Mr. Knudson's  
2 question that if there wasn't any limit on the time --  
3 putting aside whatever the limit would be, but if there's no  
4 limit on the time, then why would presidents ever do recess  
5 appointments? They could just appoint acting directors and  
6 let them serve for four years or six years or eight years.

7 MR. KATERBERG: So it's a fair concern and there's  
8 a good answer to that. I can't really say it better than  
9 OLC did. I think I'm going to get this right. It's the  
10 opinion at 6 OLC 122. It's cited in our briefs. But there  
11 are many political and sort of policy reasons for presidents  
12 to exercise their power to appoint a permanent nominee,  
13 because the fact of the matter is often acting officials are  
14 kind of looked at with second-hand status, you know, when  
15 they deal with Capitol Hill, both houses of Congress.  
16 They're not necessarily held in sort of the same esteem as  
17 the permanent head of the agency would be. An acting  
18 employee stays at their previous position, their subordinate  
19 position. They don't get paid for the salary of the full  
20 appointee to that position.

21 You know, frankly, if Congress perceives that  
22 there's abuses going on, which has happened before -- that's  
23 what led to the Federal Vacancies Reform Act of 1998 -- you  
24 know, it's imminently within Congress's power to adopt  
25 statutes that impose a time limit. I mean, that's exactly

1 what Congress has done in the Vacancies Act, which is an  
2 alternative source of authority for acting officials. Here  
3 they chose not to do that. Our submission would be that  
4 it's sort of up to Congress, and Congress can provide  
5 whatever it wants to; when it doesn't, there's not sort of a  
6 flee-floating, numerical limitation under the Constitution  
7 that's susceptible to judicial enforcement.

8 THE COURT: This count is challenging because I  
9 actually find the challenge itself -- personally I find this  
10 to be a better challenge than the separation-of-powers  
11 challenge. But it's just so hard to know how -- sometimes,  
12 as a judge, you run across things that seem wrong and  
13 there's just nothing a judge can do about them. It happens  
14 a lot in Washington because they deal much more with  
15 political questions and justiciability issues than I do.

16 If you go back to *Eaton* and you see what the  
17 Supreme Court thought they had in mind talking about special  
18 and temporary conditions and limited time and you see what  
19 that's grown into over time where in this case we had  
20 Mr. DeMarco serving almost the five years that he would've  
21 served if he had gotten a regular appointment, it certainly  
22 seems inconsistent with the spirit, if not the letter, of  
23 Supreme Court decisions and with the spirit, if not the  
24 letter, of the Appointments Clause. But it's also a real  
25 struggle to know what a judge can do about this.

1           The multi-factored reasonable circumstances  
2           test -- and I get your point that OLC wasn't articulating  
3           this test for my situation but for the OMB position -- but  
4           the problem with any kind of a reasonable circumstances test  
5           is -- the problem is you'd be dealing with acting directors  
6           and you would have no idea whether you were dealing with  
7           somebody who could do the things he was doing or not. We  
8           can't have a government run where you literally don't know  
9           if the official you're dealing with does or does not have  
10          authority until some judge three years later tells you  
11          whether that extra month was reasonable or not reasonable.  
12          The two-year limit is -- you know, it's the kind of thing  
13          the Supreme Court could do, but it makes a district-court  
14          judge kind of nervous. I don't even know, like, what the  
15          ripples would be.

16                 Let me ask you this. I just don't know how this  
17                 works. If a president appoints somebody to a recess  
18                 appointment, that's to the end of the session, right, the  
19                 session of Congress?

20                 MR. KATERBERG: Into the next session.

21                 THE COURT: The next session.

22                 The next time there's a recess after that can the  
23                 President do another recess appointment for the same  
24                 position to the same person? Can recess appointments be  
25                 consecutive?

1 MR. KATERBERG: I believe that is a possibility.  
2 I haven't studied it. As Your Honor knows, DeMarco is not a  
3 recess appointee, so we don't have issues under the recess  
4 Appointments Clause in this case. I see no reason why that  
5 couldn't take place, but I just couldn't vouch for it for  
6 sure because I haven't studied it.

7 THE COURT: Okay. I completely understand that  
8 they're not arguing DeMarco was subject to the two-year  
9 limit because he's a recess appointee. It was an analogy.  
10 It was a good argument by analogy.

11 I was going to ask whether acting directors, if  
12 they were limited to two years, could they succeed  
13 themselves, but it's not your proposal so you wouldn't know  
14 because you're not the one proposing it.

15 MR. KATERBERG: Well, that's right. I just want  
16 to point out we're talking about numbers of years, and Your  
17 Honor mentioned it was a few years shy of the five-year  
18 term. I think it was a little over four years. But really,  
19 I mean, just to get a couple things down, as of the Third  
20 Amendment, it was three years.

21 THE COURT: Right.

22 MR. KATERBERG: And during that three years a  
23 nomination had been sent to the Senate, was rejected. They  
24 don't dispute that it was an extremely polarized time in  
25 this environment. And then for the last maybe eight months

1 of DeMarco serving as acting Director, which really isn't  
2 that relevant anyway because it postdates the action at  
3 issue here, but there was a nomination pending, the  
4 nomination that ultimately got approved of the current  
5 sitting Director, Mel Watt.

6 But Your Honor's concern about sort of the  
7 unpredictabilities is exactly why I think it makes sense to  
8 let Congress do what it wants to do here, because when you  
9 have something like the provisions in the Vacancies Act,  
10 it's very specific. It establishes the very reticulated  
11 regime that tells you how the timelines are going to work.  
12 The timelines are tolled, for example, during nominations.  
13 The timelines can be stacked on top of each other, so you  
14 can have somebody continue to serve in an acting capacity  
15 for 210 days and then potentially, if there's another  
16 nomination, another 210 days. But there is very detailed  
17 regime for how that works. So that really fosters  
18 predictability. You know, somebody in the White House staff  
19 can calendar it. They can put a tickler to remind them that  
20 the date is coming up. I mean, none of that is possible if  
21 we just have this sort of free-floating, after-the-fact  
22 analysis. In addition to not allowing for predictability  
23 and stability, a lot of the things that Your Honor would  
24 need to look at and we would need to get discovery on are  
25 things that courts don't normally take discovery of, you



1 know: the President's personnel selections and the types of  
2 obstacles and considerations that go into that process.

3 THE COURT: It would be almost impossible. Were  
4 we at war? Were we not at war? Were we at an economic  
5 crisis? Were we not in an economic crisis? There would be  
6 so much to -- it would be very hard to do kind of a  
7 reasonable analysis of this.

8 Your opponents argue, and they're right, that  
9 sometimes you have to make hard decisions, and the NLRB  
10 decision was one of them. Generally, as judges, you try not  
11 to get involved in this stuff if you don't have to.

12 MR. KATERBERG: Well, that's all right, but there  
13 is a threshold reason why the Court doesn't really need to  
14 reach any of this in the de facto officer doctrine.

15 THE COURT: Yeah, I was going to ask you about it.  
16 Were you able to find any cases -- and if you said this in  
17 your brief, I just forgot, I'm sorry -- that the doctrine by  
18 name -- I realize *Buckley* applies something like it, but the  
19 doctrine by name is applied outside of adjudicative context?

20 MR. KATERBERG: Well, it's typically raised in the  
21 adjudicative context, but typically it doesn't work there  
22 because what happens is somebody that's subject to the  
23 adjudicatory authority of an official will raise the  
24 challenge in the context of the adjudication. Let me give  
25 you an example.

1           So there's a case that's cited in our brief called  
2     *Andrade v. Lauer*, the D.C. Circuit. What that involved is  
3     there was a reduction in force, a RIF, in DOJ and the  
4     decision-makers and the people that were implementing that  
5     were acting officials. The court, I think it was J. Skelly  
6     Wright, went through a very detailed analysis of the de  
7     facto officer doctrine. By the way, this was a  
8     constitutional challenge, Appointments Clause challenge to  
9     the ability of these acting officials to decide on the RIF.  
10    Ultimately, the de facto officer doctrine did not bar that  
11    challenge from going forward, but only because they filed  
12    for a PI the day before the RIF was scheduled to occur.

13           So the de facto officer doctrine says, you know,  
14    if people are going to bring these kind of challenges, we  
15    want it to be done kind of in realtime.

16           THE COURT: So the implication of the opinion is  
17    if they had waited two years and then sued about the RIF,  
18    they would have lost?

19           MR. KATERBERG: That's exactly right, Your Honor.  
20    That's also manifested more recently. The *Andrade* decision  
21    is from the '80s, but their more recent decision of the D.C.  
22    Circuit is *Southwest General*. That was a case that  
23    ultimately went up to the Supreme Court, and it has to do  
24    with an acting general counsel of the NLRB, not to be  
25    confused with *Noel Canning*, which is a separation of powers

1 with the NLRB.

2 In the *Southwest General* case, that was another  
3 one where the NLRB was exercising adjudicatory authority  
4 over a company dealing with unfair labor practices. The  
5 issue was whether the proceeding was validly approved,  
6 because you needed a proper general counsel to approve the  
7 proceeding. That was objected to.

8 The D.C. Circuit discussed the de facto officer  
9 doctrine, reaffirmed their earlier decision in *Andrade* and  
10 said we're going to let this go forward, and the reason for  
11 that was because it was raised, you know, in connection with  
12 that proceeding.

13 Now, it doesn't really map neatly onto the  
14 situation here because it's not an adjudication, but I don't  
15 think that's a reason not to apply the de facto officer  
16 doctrine at all. And certainly it's not a reason to let it  
17 be raised almost five years after the action took place.

18 In the context of an action like this, like we  
19 were discussing earlier, that's entry into a contract by two  
20 different parties that is deemed to have an incidental  
21 effect on shareholders.

22 THE COURT: Your opponents argue that the  
23 difficulty there is they're not parties to an adjudication,  
24 so they can't raise it before the person that they think  
25 doesn't have authority. They have to kind of sue from the

1 outside. They point out that they brought their suit within  
2 the statute of limitations. I'm just forgetting this, but  
3 what is the statute of limitations that applies? Is it in  
4 the HERA or is it -- are they borrowing a state statute of  
5 limitations?

6 MR. KATERBERG: Well, I believe it's in 28 U.S.C.,  
7 I want to say, 2401, which is, I think, a general -- it's a  
8 generalized six-year statute of limitations for all actions.

9 THE COURT: Okay. I was just wondering whether  
10 Congress -- do you say HERA or do you call it HERA?

11 MR. KATERBERG: I have heard it both ways. I  
12 personally use HERA.

13 THE COURT: I was wondering whether Congress had  
14 given a specific statute in HERA that applied to this  
15 lawsuit, which would help their argument, if they're just  
16 using the general statute of limitations that applies where  
17 there isn't one otherwise specified and it doesn't help as  
18 much as.

19 MR. KATERBERG: I think that's right, Your Honor.  
20 It's a generalized statute of limitations that applies to  
21 all sorts of different actions against the federal  
22 government and agencies involving all kinds of different  
23 claims.

24 It's probably fair to say that if you took the  
25 mine-run of lawsuits against the United States, that's a

1 very, very small portion of those that are going to raise  
2 the kinds of challenges to an agency's authority on grounds  
3 of the Appointments Clause like we have here. So the  
4 general statute of limitations just isn't really designed to  
5 deal with the unique concerns that animate the de facto  
6 officer doctrine. So that's kind of our point, that it's  
7 not -- I think their position is, well, what do you want  
8 from us? Of course, it's timely. We sued within the  
9 statute of limitations. But that's not really a response,  
10 because the concerns that animate the de facto officer  
11 doctrine are specific to this type of issue and it's not  
12 subsumed within a general statute of limitations.

13 Your Honor, we also -- you know, we cited a few  
14 examples in our brief, but, you know, we could go on. I  
15 mean, there are many situations where acting officials have  
16 served in high-ranking capacities across many different  
17 branches of government. If Your Honor wanted more, I would  
18 refer you to the Congressional Research Service Report  
19 that's cited in our brief. It gives more examples. But  
20 just to give one, so the Social Security Administration,  
21 which, as we discussed earlier, is an independent agency  
22 headed by a single director like FHFA, it has had an acting  
23 administrator for the last four-and-a-half years as of  
24 today. So that exceeds by half the three years that DeMarco  
25 had served as acting Director as of the Third Amendment. So

1 it's not at all unprecedented on the first count. You know,  
2 they want to put a lot of stress on precedent, let's look  
3 for examples where this is done before. *Noel Canning*  
4 teaches us that if there's a lot of examples in history  
5 where the political branches have gone with a particular  
6 type of practice, that's one indicator of its  
7 constitutionality. We see many, many examples of  
8 high-ranking acting officials serving for a number of years.  
9 And I think it's telling, it's instructive that you won't  
10 find a single judicial decision since the history of the  
11 republic.

12 In *Southwest General*, the Supreme Court, Chief  
13 Justice Roberts, talks about how acting officers has been a  
14 wide-spread practice since the George Washington  
15 administration; never been a case where a court has  
16 invalidated the action of an acting officer for staying too  
17 long, and I think that's instructive. They are essentially  
18 asking Your Honor to create a new, sort of implied right of  
19 action under the Appointments Clause.

20 THE COURT: All right. Thank you, Mr. Katerberg.

21 Mr. Knudson. So, as you heard me say, I have some  
22 sympathy for your argument just kind of as an original  
23 matter, but I'm wondering about remedies, and I'm wondering  
24 about the de facto officer doctrine.

25 I'm sympathetic to the idea that the Supreme Court

1 didn't seem to have in mind people serving for five years as  
2 acting officers. I get the argument about recess appointees  
3 and why would you bother making a recess appointee. It's  
4 hard for me to know what to do.

5 The kind of reasonable circumstances test that you  
6 suggest, besides being a very difficult test to apply and  
7 having courts sticking their nose into things that courts  
8 are at least reluctant to stick their nose into in trying to  
9 make that decision, the problem with that is you'd never  
10 know when you're dealing with somebody whether you were  
11 dealing with an officer who had the authority to deal with  
12 you or not. It seems to me it would be very problematic for  
13 any acting official to not know as she was sitting at her  
14 desk whether she had the power of office or a reasonable  
15 time had passed.

16 With respect to the two-year limitations, it's a  
17 good argument and I get why you're using that by analogy,  
18 but it's just unprecedented. I mean, no court has ever  
19 suggested that acting officers can only serve for two years,  
20 and there are a number of historical examples of acting  
21 officers serving more than two years.

22 So even if I was bold enough to agree with you and  
23 even if I was bold enough to adopt the two-year rule, it  
24 would seem grossly unfair to say to the people who has dealt  
25 with the agency and dealt with Mr. DeMarco beginning the two

1 years and one day and the rest of his term that all those  
2 things that you thought you did, I'm wiping those all out  
3 because unbeknownst to you there's a two-year rule that no  
4 one has ever heard of before but I have imposed. And not  
5 only am I imposing it, I'm retroactively applying it and  
6 wiping out lots of decisions. That would be a very extreme  
7 remedy and a very disruptive thing to do to the government.

8 I could see, like, the Supreme Court adopting this  
9 rule and applying it going forward, but it would be --  
10 you're essentially suggesting that if I were to adopt the  
11 two-year rule, that I hold that three years of this  
12 officer's activities were all ultra vires; he didn't have  
13 the authority to do them. So that's my concerns. Let me  
14 invite you to respond.

15 MR. KNUDSON: Well, in terms of remedy, again, I  
16 turn the Court's attention to *Noel Canning*. There the court  
17 said, look, the board wasn't properly constituted, there  
18 wasn't a quorum. So those decisions made by the board were  
19 undone.

20 THE COURT: Well, the Commissioner of Social  
21 Security, who has now served as the acting person for four  
22 years plus, thousands and thousands of Social Security cases  
23 are adjudicated in her name every year, too bad? We wipe  
24 out all the ones that occurred after she passed the second  
25 year or after she passed the reasonable time? I mean, do



1 you really think any court is going to make the Social  
2 Security -- if the court were to adopt your rule, make the  
3 Social Security Administration re-do three years', four  
4 years' worth of tens, hundreds of thousands of Social  
5 Security determinations?

6 MR. KNUDSON: Well, the argument there is what  
7 does a de facto officer doctrine apply. We're arguing that  
8 in the context of this particular agency all we need to  
9 decide is what's significant about this agency. You could  
10 distinguish away the Social Security Administration in terms  
11 of ministerial actions that the agency is taking in  
12 administering claims and so forth, the quasi judicial  
13 function that is performing in terms of determining  
14 disability eligibility would be a different situation where  
15 perhaps the de facto officers doctrine might apply.

16 Here we've got a situation where the Supreme Court  
17 has said in *Nguyen*, in *Ryder*, based on an earlier case  
18 called *Glidden*, that the de facto officer doctrine doesn't  
19 apply when there's an important statutory policy in effect  
20 and, by necessary implication, if there is a constitutional  
21 violation, it doesn't apply. That was certainly the case in  
22 *Nguyen* and *Ryder*. We had criminal convictions, improperly  
23 constituted courts of appeal, so the decisions of those  
24 panels had to be revisited. So we think --

25 THE COURT: But that feels differently. I read

1       Ryder. That feels differently to me than what's going on  
2       here. We all the time have an adjudication that goes up on  
3       appeal. We get reversed. It comes back. We re-adjudicate.  
4       That we're very familiar with.

5                You're suggesting that I hold that, for example,  
6       under one of your alternate arguments, that when Mr. DeMarco  
7       hit his second year anniversary, he no longer could function  
8       as acting officer, and that everything he did after that  
9       date is invalid, and that for the people who depended on the  
10      validity of his credentials, it's just too bad for them.  
11      They're going to have to go and rewind their lives three  
12      years or four years or whatever it is from today. That  
13      seems like exactly what the de facto officer doctrine -- and  
14      I understand it's been pretty much limited to the  
15      adjudicative context, although not exclusively it sounds  
16      like, but that sounds like exactly the kind of concerns the  
17      doctrine is designed to prevent, just the horrible  
18      disruption of trying to unwind two or three or four years of  
19      agency action.

20               MR. KNUDSON: Well, I think the agency overstates  
21      the hardship issue in the context of what decisions would be  
22      undone by determining the acting Director DeMarco served too  
23      long in that capacity.

24               First, I could point out that Director Lockhart  
25      was operating under Senate confirmation. Director Watt was

1 confirmed by the Senate. So we're looking at a period of  
2 time in which acting Director DeMarco in his decisions would  
3 be implicated.

4 THE COURT: Yeah, five years' worth, right?

5 MR. KNUDSON: Four years and four months, I  
6 believe.

7 THE COURT: If I bought the two-year theory, it  
8 would be basically two-and-a-half years or so of decisions.

9 MR. KNUDSON: Well, certainly we're suggesting a  
10 bright line. That's for ease of application. There is  
11 certainly a constitutional basis for that bright-line rule.  
12 And I don't think it's --

13 THE COURT: Suppose the Supreme Court adopted your  
14 bright-line rule or I did it or somebody did it, so it's now  
15 a two-year bright-line rule. Going forward now we have a  
16 vacancy in an agency and they have an acting director and  
17 she hits the two-year mark and there's no replacement. Now  
18 what?

19 MR. KNUDSON: Well, then the President would have  
20 to determine what to do, because I think at that point then  
21 the acting director would lose authority to act.

22 THE COURT: Can the President appoint a new acting  
23 director at that point?

24 MR. KNUDSON: The President would have to nominate  
25 somebody to the Senate because you can't avoid the

1 confirmation process.

2 THE COURT: Okay. So then the agency just shuts  
3 down?

4 MR. KNUDSON: No. There would still be officials  
5 that would have authority to act.

6 THE COURT: A lot of statutes put the authority in  
7 the head of the agency, you know, the Commissioner of Social  
8 Security shall have the power to X. Without a commissioner,  
9 you can't exercise that power.

10 Suppose your rule had been in effect, we got to  
11 the two-year mark of the Commissioner of Social Security.  
12 The agency just has to shut down until the President  
13 nominates and the Senate confirms a new commissioner?

14 MR. KNUDSON: Well, I think that there would be  
15 functions of the Social Security Administration that would  
16 continue to operate that would be ministerial in nature and  
17 would continue.

18 THE COURT: Well, let's take the ones that  
19 wouldn't continue to operate. Those just cease? The agency  
20 just ceases those functions? Or can the President appoint a  
21 new commissioner and give her two years?

22 MR. KNUDSON: I think then the default rule would  
23 be, yes, they'd have to be able to fix the problem, but they  
24 would have to find somebody who would be qualified and put  
25 them up for Senate confirmation subject to the two-year

1 limitation.

2 THE COURT: So the answer is he can't just appoint  
3 another acting director?

4 MR. KNUDSON: He can't renominate the same person.

5 THE COURT: Well, can he appoint a different  
6 person to be acting director for two years?

7 MR. KNUDSON: I think you would have to nominate  
8 somebody, put them to the test of Senate confirmation;  
9 otherwise, you would be voiding the power of the Senate to  
10 give its consent and --

11 THE COURT: I don't know if that's yes or no.  
12 Let's say we have an agency, the Social Security  
13 Administration, and it has an acting director right now who  
14 is about to hit her second year. There is a nominee,  
15 somebody else who has been nominated to be the commissioner,  
16 but the Senate hasn't acted on it. We now get to the  
17 two-year anniversary. Tomorrow is a new day. What happens?  
18 No acting director? Or the President could appoint another  
19 temporary acting director while this nomination pends?

20 MR. KNUDSON: Of course, there are situations  
21 where the government will stop functioning, such as it runs  
22 out of money because there hasn't been an appropriation. So  
23 there are circumstances where the constitutional limits on  
24 the structure of the government or on the President's  
25 appointment power would implicate a situation where there

1 would a possibility that that particular agency would have  
2 to evaluate what functions could be covered by the de facto  
3 officer doctrine and which ones could not.

4 So if they were ministerial, administrative in  
5 nature, I think the agency would continue to operate. But  
6 if it's something where there's a significant statutory  
7 policy or constitutional issue involved, then the de facto  
8 officer doctrine doesn't apply and there has to be -- it  
9 would force the issue to the Senate. Now they have to take  
10 an action and resolve this crisis.

11 THE COURT: Remind me of the timeline. So in our  
12 case -- the facts of our case suppose you lost on your other  
13 challenges and you won on your Appointments Clause  
14 challenge. Let's just say I agreed with the two-year  
15 bright-line rule. So that would mean the Third Amendment  
16 was invalid because DeMarco would've been past his  
17 expiration date. Right? But the PSPAs would -- again, if  
18 you only win on the Appointments Clause, the PSPAs would be  
19 valid, right, because those were signed by Lockhart? Right?

20 MR. KNUDSON: Correct.

21 THE COURT: And the conservatorship would be  
22 valid.

23 I assume if there was a Third Amendment, there was  
24 a First Amendment and a Second Amendment. Were they during  
25 DeMarco's term or Lockhart's? If you don't have that at

1 hand, that's fine. I'm just curious.

2 MR. KNUDSON: The PSPAs were in September of '08.  
3 That was Lockhart's. Then the Second Amendment, I believe,  
4 was within the two-year time frame.

5 THE COURT: It was DeMarco within the first two  
6 years?

7 MR. KNUDSON: I think he was three months into his  
8 term.

9 THE COURT: Okay. So we would have to unwind it  
10 to the situation that existed at the time of the Second  
11 Amendment?

12 MR. KNUDSON: Correct.

13 THE COURT: Okay. Anything more you wanted to say  
14 about the Appointments Clause?

15 MR. KNUDSON: Also, we talk about justiciability,  
16 and I think you can see the *Eaton* court addressed this and  
17 said ten months was okay under the circumstances there. The  
18 OLC opinion talks about what is reasonable. I think if you  
19 look at the Supreme Court's most recent pronouncement on  
20 justiciability political question, it was the question in  
21 *Zivotofsky* as to what you could put on a passport as a place  
22 of birth, and the Supreme Court said that's not a political  
23 question and sent it back to the D.C. Circuit to decide it  
24 in the first instance. And, of course, you're aware the  
25 court has taken the *Jermandy* (ph) case for this term.

1           So the courts are obligated to weigh in on issues  
2           that are complex, where it's not an easy line-drawing  
3           situation. That's why we suggested the two-year bright-line  
4           rule. But certainly if you look at the OLC opinion, an  
5           acting director can serve only as long as what's reasonable  
6           in the circumstances. DeMarco served without presidential  
7           supervision from August '09 to January of '14. The Obama  
8           Administration sat on that position for over two years  
9           before nominating somebody that the Senate did not confirm.  
10          By the time the Net Worth Sweep Rule was imposed, the crisis  
11          that ostensibly generated the aging in the first place had  
12          passed by. The President had plenty of time to find a new  
13          appointee. So we're saying the 2008 crisis did not suspend  
14          the Constitution. The President had an obligation to put  
15          somebody up. At some point, the Senate had an obligation to  
16          confirm the President. The Executive Branch, the  
17          Legislative Branch had to find a solution. This court can  
18          tell them that's the case. Thank you.

19                 THE COURT: Okay. Let me just ask you a couple  
20                 follow-up questions that I forgot. One is can you confirm  
21                 the -- the statute of limitations that applies to this  
22                 action before me, it's the general federal statute of  
23                 limitations?

24                 MR. KNUDSON: Yes, 28 U.S.C. --

25                 THE COURT: Secondly -- I forgot to ask



1 Mr. Katerberg about this -- you make this argument based on  
2 4512(f) that it talks about in the event of the death,  
3 resignation, sickness or absence of the director, the  
4 President can designate an acting director, and you make the  
5 argument that Lockhart was not the director. I just want to  
6 clarify -- I didn't have a chance to look up these cases,  
7 but are there courts that have actually considered this  
8 argument and either accepted it or rejected it? The case  
9 you rely on is a '98 case, *Doolin Security Savings Bank*. So  
10 I assume that's a case you're using by analogy since --

11 MR. KNUDSON: By analogy, Your Honor, yes.

12 THE COURT: Right. Have there been cases that  
13 specifically address this argument?

14 MR. KNUDSON: I'm not aware of any, Your Honor.

15 THE COURT: Thank you, Mr. Knudson.

16 Mr. Katerberg. Are you aware of any cases  
17 addressing this 4512(f)?

18 MR. KATERBERG: Yes, Your Honor. I've got two.  
19 They're cited in our brief.

20 THE COURT: There's this *UBS America*?

21 MR. KATERBERG: *UBS America*. I think we probably  
22 cited the Second Circuit decision. I think there's a  
23 Southern District decision that was affirmed that also  
24 contained some reasoning. Then there's a Northern District  
25 of Illinois decision called *City of Chicago*.

1 I just want to emphasize, so *Doolin* is about a  
2 statute, the Vacancies Act, and it's really two steps  
3 removed. One, it's not about HERA, the unique acting  
4 director provision in HERA. It's about the Vacancies Act.  
5 On top of that, it's about a prior version of the Vacancies  
6 Act that is no longer even in existence.

7 But even if you assume *arguendo* that *Doolin*  
8 applies, what *Doolin* essentially says is in order for the  
9 acting director power to be triggered under this  
10 pre-existing version of the Vacancies Act, the prior person  
11 needs to have been presidentially appointed and Senate  
12 confirmed. We have that here because DeMarco's predecessor  
13 was a guy named James Lockhart, and he was presidentially  
14 appointed and confirmed by the Senate as the Director of  
15 OFHEO, O-F-H-E-O (FHFA's predecessor) and then was sort of  
16 carried over by HERA.

17 So really I can't even understand what their  
18 challenge is getting at, because even if this case that is  
19 inapplicable for several reasons applies, our facts line up  
20 with what the Court said would be permissible in that case.

21 If I could address a few other things that came up  
22 during counsel's presentation? Your Honor, their position  
23 would invite chaos across the government. I mean, I shudder  
24 to think what it would look like the day after the ruling in  
25 the General Counsel's Offices of agencies across the

1 government because this practice of acting officers is  
2 extremely common.

3 I think while we're talking about *Doolin*, I can  
4 refer to Judge Randolph's opinion in *Doolin* where he traces  
5 through the history of acting officials in the government,  
6 and the way he describes it is it gives a little play in the  
7 joints that's needed for government to work, because I  
8 think, as citizens, we don't want the government agency to  
9 completely shut down and stop doing the important things it  
10 does during the sort of transitory periods. Sometimes those  
11 transitory periods last longer than others, and there can be  
12 a variety of reasons for that.

13 I think the way that the Court should approach it  
14 in this case is essentially you're being asked to invalidate  
15 an act of Congress. And the reason I say that is because in  
16 HERA, in 4512(f), Congress did not do what it normally does  
17 in the Vacancies Act and in other acting official  
18 provisions. It did not put a temporal limit on the service  
19 of the acting director. I think Your Honor has to assume  
20 that that was deliberate on Congress' part. They knew how  
21 to put that in if they wanted to; they didn't. So, I mean,  
22 I guess it would be an as-applied challenge, not a facial  
23 challenge, but that's essentially the relief they're seeking  
24 here, is declaring an act of Congress unconstitutional.

25 I want to talk a little about the de facto officer

1 doctrine because I think some confusion has been introduced.  
2 I think the issue I've heard is whether the de facto officer  
3 doctrine is limited to the adjudicatory situation. If I can  
4 sort of reframe that. I think the way we would put it is  
5 the de facto officer doctrine applies across the board. But  
6 there have been a recent line of cases where courts have  
7 been less willing to apply it in the adjudicatory context,  
8 and those cases have involved judges -- challenges to  
9 judges, as we talked about earlier this morning, hearing  
10 criminal cases when they were not proper Article III judges  
11 or where their appointment was otherwise defective.

12 So I think it's instructive to look at what *Ryder*  
13 says. This is 515 U.S. at 182: We think that one who makes  
14 a timely challenge to the constitutional validity of the  
15 appointment of an officer who adjudicates his case is  
16 entitled to a decision on the merits of the question. So  
17 there are several things built into that: timely. You  
18 know, it's got to be timely. So that's perfectly consistent  
19 with the position we've been urging all along.

20 Now, some of these cases what they'll say is even  
21 though it wasn't raised below, we're not going to deem it  
22 forfeited. You know, that's logical because in some sense  
23 it goes to jurisdiction. If the lower court didn't have  
24 jurisdiction because the judge wasn't an Article III judge,  
25 then maybe, even though they didn't raise that below, will

1 let them make that challenge to their conviction on appeal,  
2 but it's still timely in the sense that I'm talking about  
3 and in the sense that the de facto officer doctrine is  
4 concerned with, because normally you have to appeal, I  
5 think, within 30 days or 60 days, and similar for a petition  
6 for cert in a case like *Nguyen* and *Ryder* that ends up in the  
7 Supreme Court. So we're talking about sort of orders of  
8 magnitude different than the four some years, almost five  
9 years in our case here.

10 OLC, Your Honor, has opined specifically about the  
11 de facto officer doctrine being what they call a "common  
12 cure" for any issues posed by acting officers potentially  
13 staying too long. Again, there's no judicial decision that  
14 has ever said that this is a problem, but the opinion,  
15 acting officers, which is 6 OLC 119, at the end they say, In  
16 many instances, potential infirmities in the authority of  
17 acting officers will be cured by the de facto officer  
18 doctrine. They give some examples.

19 You know, there's no case I can point Your Honor  
20 to that's exactly like this because, like I said, it's never  
21 been done before. But what OLC points to, which I think  
22 provides a coherent analogy, is a typical case of a de facto  
23 officer is one who has been properly appointed but who  
24 continues to serve after his term of office is expired. And  
25 they cite a couple of cases: *Waite v. Santa Cruz*, Supreme

1 Court case and the district court from Maine. So it's been  
2 held to apply in that context, and so I see no reason why it  
3 wouldn't equally apply where the nature of the challenge is  
4 that you have an acting officer that stayed too long, as  
5 opposed to somebody who was properly in office at one point  
6 but their term is expired. They're essentially serving too  
7 long as well.

8 Finally, I want to address the suggestion that it  
9 doesn't apply to constitutional issues. There is some  
10 language like that in some of the cases, but, again, that's  
11 confined to the judicial context. So the constitutional  
12 challenge is to judges sitting on a particular case based on  
13 not having life tenure as related to Article III. The  
14 Supreme Court has said, you know, we're not going to allow  
15 the de facto officer doctrine to bar somebody from bringing  
16 that kind of challenge to their conviction. But there is  
17 not any sort of across-the-board exemption for  
18 constitutional claims from the de facto officer doctrine.

19 I'd go back to *Buckley v. Valeo*. I think they  
20 used the words "de facto." I don't think they added  
21 "officer" appended to that, so we could debate whether it's  
22 exactly the concern. But the cases that *Buckley* refers to  
23 in that paragraph of the opinion, they relate to something  
24 that's kind of analogous too, which is when legislative  
25 apportionments have been held unconstitutional in the past,

1 there's many cases that say we're not going to go back and  
2 say that the acts that the Legislature passed, you know,  
3 under the illegal, unconstitutional apportionment are going  
4 to be retroactively invalidated, and that's the principle  
5 that the court used to inform how it's going to handle the  
6 situation of the past acts of the Federal Election  
7 Commission. All this sounds in constitutional issues and so  
8 there is no reason to think it would be limited to statutory  
9 challenges.

10 That's all I have, unless Your Honor has  
11 questions.

12 THE COURT: Okay. While you're there, why don't  
13 we move to the next issue, which is the non-delegation  
14 doctrine.

15 I've really struggled with the arguments about  
16 whether the FHFA, when it was acting as conservator, was  
17 exercising governmental authority such that the traditional  
18 non-delegation doctrine would apply. It also would apply to  
19 the separation-of-powers issue and so on. Here's what I'm  
20 sincerely struggling with, is at what level are we focusing  
21 here?

22 So there is, on the one hand, the character of the  
23 agency. The FHFA is a government agency. On another level,  
24 there's the role it's playing. It's playing the role of  
25 conservator, which typically a conservator steps in the

1 shoes of the entity for which it is acting as conservator,  
2 and if it's private entity, it's essentially acting as a  
3 private entity. And then there's the individual task that's  
4 being done. So there's arguments in the briefs about, well,  
5 the powers that the FHFA had as the conservator under the  
6 statute, focusing on its role as conservator, and there's  
7 other arguments about the specific challenged act, signing  
8 the Third Amendment, and whether that's government -- so  
9 what am I -- this is kind of like I have a lens on my  
10 camera. I'm trying to figure out where I'm supposed to be  
11 focusing it. What is it that matters here, that signing the  
12 Third Amendment -- is my question whether signing the Third  
13 Amendment was a governmental act or is the question whether  
14 acting as a conservator for the GSEs was a governmental act?  
15 What's the right question to ask here?

16 MR. KATERBERG: So I think it derives from  
17 underlying principles of Article III standing. We have not  
18 raised an Article III standing to the non-delegation counts  
19 in this case, but the only thing that they have standing to  
20 raise a non-delegation challenge to is the specific thing  
21 that causes them injury. Here that is entry into the Third  
22 Amendment.

23 So could FHFA as regulator, for example, have the  
24 power to promulgate rules and regulations? You know, that's  
25 probably legislative in nature, but they haven't alleged any



1 rule or regulation of FHFA that has caused them injury.

2 THE COURT: Well, they do allege some. I'm not  
3 sure the argument works, but they argue that even if the --  
4 the problem is that all their arguments depend on the Third  
5 Amendment being illegal. If the Third Amendment is legal,  
6 then they aren't harmed by the current director abiding by  
7 the Third Amendment.

8 They say that the FHFA would have regulatory  
9 authority to stop the FHFA as conservator from making the  
10 dividend payment. But if you can't challenge the Third  
11 Amendment, then it seems to me the premise for those  
12 arguments falls apart. If the Third Amendment is legal,  
13 then there there's nothing illegal about any of its actions.

14 MR. KATERBERG: That's absolutely right.

15 There is another important point that's sort of  
16 baked into this, which is that argument actually doesn't  
17 work because if Your Honor looks at the certificates of  
18 designation for the preferred stock, the consequence -- if a  
19 dividend is not paid that's due -- well, let me back up for  
20 a step. The amount of the dividend and the dividend  
21 obligation is set by the Third Amendment, which is the  
22 contract entered into in August 2012, and so it spells out  
23 what's due each quarter.

24 If the director in a regulatory capacity opted not  
25 to approve a dividend for a given quarter under the terms of

1 the Treasury agreement and the certificates of designation,  
2 what happens is the amount simply gets added to the  
3 liquidation preference. So it essentially becomes are you  
4 going to pay Treasury now or are you going to pay Treasury  
5 later.

6 THE COURT: Now or later.

7 MR. KATERBERG: But I don't see them arguing that  
8 paying Treasury later and just adding it to the liquidation  
9 preference would in any way assuage the injury that they  
10 claim to have suffered from the Third Amendment. As Your  
11 Honor noted, it's all rooted in the Third Amendment. I  
12 mean, that's the underlying transaction that's being  
13 challenged here.

14 Now, I think for the non-delegation claim Your  
15 Honor needs to look at the Third Amendment, and what the  
16 Third Amendment is is it's a financial transaction. In  
17 character it's no different than transactions that all kinds  
18 of businesses that are failing or near failure engage in  
19 bankruptcy or any number of contexts with entities that are  
20 willing to provide credit. Now, the scale is, of course,  
21 extremely different. It's orders of magnitude different in  
22 scale. And it's also different in the sense that Congress  
23 has seen to fit to attach certain consequences and certain  
24 protections to the nature of the transaction. But the  
25 transaction itself, it's not an exercise of sovereign

1 governmental power, and that's really what we look at for  
2 non-delegation. I mean, for the traditional Article I  
3 non-delegation where we talk about intelligible principles,  
4 really that's talking specifically about legislative power  
5 of Congress. So Congress, you know, subject to certain  
6 limits, can't totally abdicate its legislative powers and  
7 just say to an agency, you know, you figure it out. I think  
8 it's pretty clear this is not an exercise of legislative  
9 power, this transaction. It's not prescribing rules of  
10 conduct that are going to govern private individuals.

11 THE COURT: So their argument is that the FHFA is  
12 acting as a governmental entity when it signs the Third  
13 Amendment and they argue the private non-delegation doctrine  
14 only in the alternative. So your position is essentially  
15 that FHFA was not acting as a government entity when it  
16 signed the Third Amendment. So you would say that the  
17 legislative non-delegation doctrine is just irrelevant  
18 because they weren't exercising government power?

19 MR. KATERBERG: That's one way of putting it. I  
20 guess I would say it doesn't matter to me much whether it's  
21 relevant because I think we prevail under either way of  
22 looking at. The intelligible principles test is not --

23 THE COURT: We'll get into that. I'm still having  
24 trouble. I don't know whether the question for me is  
25 whether in signing the Third Amendment the FHFA was

1 exercising governmental authority or the question is in  
2 acting as a conservator, the FHFA was acting as a  
3 governmental -- was exercising governmental authority.  
4 What's the right question?

5 MR. KATERBERG: I don't think Your Honor needs to  
6 address the broader question. There may be some things that  
7 the FHFA could do as conservator that are governmental in  
8 character. They are not -- whatever those things may be,  
9 they are not challenged in this case.

10 What's challenged in this case is entry into the  
11 Third Amendment. That is a business transaction. It's not  
12 sovereign in character. It's not regulating anybody. It's  
13 not imposing sanctions on anybody. It's not coining money,  
14 none of these things that are sort of deemed to be unique to  
15 the government.

16 So it's kind of like the *Pittston* case, the Fourth  
17 Circuit case we cited in our briefs, where a statute creates  
18 a coal industry retirement board to take retirement savings  
19 and invest it and do certain things, and that's no different  
20 than any other number of private pension funds do in  
21 character. Again, it could be a different scale, but you've  
22 got to look at the character of the activity. The character  
23 of the activity entering into a deal like the Third  
24 Amendment is fundamentally sort of --

25 THE COURT: The problem with that is, though,

1 government agencies do things all the time for which there  
2 are equivalents in their private counterparts and we don't  
3 say that that's not government action. The agency for which  
4 I work -- not an agency, but we have payroll people who pay  
5 payroll. We have HR people who give advice about HR things.  
6 They're all government actors who are acting as public  
7 employees when they do that, even though down the street  
8 there's a hundred other people paying payrolls for private  
9 companies and giving HR advice to private employees. So the  
10 fact that the private people do X doesn't mean that when the  
11 government does it it's not exercising government authority  
12 or it's not acting as a public actor.

13 MR. KATERBERG: So, Your Honor, I'm with you on  
14 that, but I would take it a step further and say, you know,  
15 you're not going to see the non-delegation doctrine applied  
16 to those kinds of activities because, again, the  
17 non-delegation doctrine is about Congress delegating its  
18 legislative power.

19 I doubt very much if you had a statute that gave  
20 an agency the broadest possible authority in the world with  
21 no intelligible principles whatsoever -- let's imagine  
22 that's the case -- and it has to do with buying an  
23 automobile fleet or hiring and firing employees or buying  
24 office supplies, I don't think that's the kind of thing that  
25 would be susceptible to a challenge on the ground that

1 Congress, by authorizing the agency to do that, vested the  
2 agency with legislative power because the nature of the  
3 activity is not legislative in nature.

4 THE COURT: I think that's your best argument here  
5 -- that is -- whether they were exercising governmental  
6 authority, it's hard for me. I'm just not sure what the  
7 answer to that is. But if they are exercising governmental  
8 authority in signing the Third Amendment, it doesn't look  
9 anything like legislative authority. Legislative authority  
10 is about prescribing standards of conduct. It's a contract.  
11 Executives sign contracts, not legislatures. I think that's  
12 your best argument.

13 On the intelligible principle what do you do with  
14 the *Perry Capital* case? I mean, I read half of *Perry*  
15 *Capital* before I ran out of time this morning, but it  
16 sounded like the panel there thought essentially there's  
17 almost no restrictions whatsoever on the actions of the FHFA  
18 as conservator. It was hard for me to find -- if you take  
19 *Perry Capital* at its word, it's hard for me to find any  
20 intelligible principles in that. I realize this is a really  
21 low threshold.

22 Courts in the past have found -- I have a friend  
23 who teaches Constitutional Law in a law school and I just  
24 mentioned to him I had, among other things, a non-delegation  
25 issue coming up and he said, Well, the plaintiff will lose

1 then because no plaintiff has won in 100 years. I said,  
2 Well, you know, this might be the case because I've got this  
3 D.C. Circuit opinion that essentially says they can do  
4 whatever they want.

5 MR. KATERBERG: Right. Well, so the first thing  
6 is I'm gratified that Your Honor looked at the *Perry Capital*  
7 opinion because I think --

8 THE COURT: Half of it.

9 MR. KATERBERG: -- if you rested on their  
10 characterization of it, you would find it to be sort of  
11 distorted and exaggerated. I think it's important to look  
12 at what *Perry Capital* says.

13 *Perry Capital* does supply limiting principles,  
14 which is the action of the agency has to be within its  
15 conservatorship authority. Now, yes, that authority is  
16 broad, but it is constrained.

17 THE COURT: If I asked you to show me the most  
18 intelligible of intelligible principles that guided the FHFA  
19 in its actions as conservator, what would you say is the  
20 most intelligible of those principles?

21 MR. KATERBERG: I'd say, well, the charters of  
22 Fannie Mae and Freddie Mac, which FHFA is conservator, is  
23 charged with taking steps to allow the agencies to continue  
24 to -- excuse me, the enterprises to continue to promote  
25 those public purposes and their charters. I think that

1 would be among them.

2 I think the powers of FHFA that are laid out in  
3 4617(b) of the statute.

4 THE COURT: I'm sorry, I'm just thinking aloud  
5 here. Those principles, you mention that in the brief, but  
6 the principles in Fannie Mae's charter provide intelligible  
7 principles about how Fannie Mae should conduct Fannie Mae  
8 business. But is there an intelligible principle governing  
9 FHFA in how it conducts its conservator business insofar as  
10 they're -- I realize part of what a conservator does is to  
11 run the business that it's conserving, but it makes  
12 decisions as conservator, too.

13 Is there anything in HERA or anything other than  
14 in the charters of Fannie Mae and Freddie Mac that you think  
15 provides intelligible principles to FHFA in its exercise as  
16 conservatorship?

17 MR. KATERBERG: Well, and I don't think it can be  
18 divorced from the charters because, I mean, the charters are  
19 statute. So Congress enacted these statutes that created  
20 Fannie Mae and Freddie Mac. And part of a very essential  
21 function of being a conservator is to ensure they can  
22 continue to accomplish those purposes. So I don't think it  
23 can be read in a vacuum without looking at the charter.

24 But the provisions of HERA in 4617(b) that talk  
25 about preserving and conserving assets, carrying on the



1 business of the regulated entity, the D.C. Circuit looked at  
2 that and they said this gives sufficient guidance because  
3 FHFA has to engage in activities within the scope of the  
4 conservator authority, which is essentially running the  
5 business to allow these enterprises to continue to perform  
6 the important public mission that they performing.

7 If FHFA were hypothetically to do something that  
8 was outside the conservatorship power, you know, there could  
9 be issues with that. This is well within the heartland of  
10 conservator power to run the business.

11 THE COURT: Is there anything they could do that  
12 would be outside of their conservatorship powers given how  
13 broad they are?

14 MR. KATERBERG: I mean, there could be -- you  
15 know, if an FHFA employee embezzled the funds and gave it to  
16 his brother-in-law. I mean, I guess we could imagine a wide  
17 variety of hypotheticals I think everybody would agree is  
18 not what conservators are supposed to be doing.

19 Every court that has looked at this -- this has  
20 come up in the APA challenges to date. And there's a  
21 footnote in our brief that collects all the citations -- and  
22 Your Honor will find that every judge that has looked at  
23 this, save for the one dissenting judge in *Perry Capital* in  
24 the D.C. Circuit, has said that this is well within the  
25 range of powers that conservators do when they're charged

1 with rescuing financial institutions that have systemic  
2 importance beyond that particular company and its  
3 shareholders.

4 THE COURT: Let me ask you about a couple of the  
5 arguments they make. One of them -- or one or two of these  
6 I'm not quite sure I understand what the argument is, so  
7 maybe you can clarify it and then respond to it, because --

8 So one of the phrases that they keep saying in  
9 their briefs is that they keep pointing out that when the  
10 FHFA acts as a conservator, unlike conservators in any other  
11 context, they are allowed to consider their own interests  
12 and, hence, because they're a government agency the  
13 government's interest and, therefore, they are exercising  
14 government authority, not private authority. How do you  
15 respond to that?

16 MR. KATERBERG: I don't think that makes a  
17 difference to whether the character of the activity is  
18 private or governmental. It's saying that you're allowed to  
19 take into account, for example, the important public mission  
20 of Fannie Mae and Freddie Mac and trying to sort of keep  
21 them afloat, to keep the housing markets functional, and  
22 kind of what's going to be best for that perspective.

23 I mean, one way of looking at --

24 THE COURT: Just to be clear, I'm not asking this  
25 on the intelligible principle issue. I'm asking this on

1 whether they are exercising private or government authority.  
2 I guess the argument is they could have entered the Third  
3 Amendment consistent with their statutory guidance. They  
4 could have entered the Third Amendment even if they thought  
5 it was going to be really bad for the GSEs because they're  
6 explicitly allowed to do things for their own benefit or for  
7 the benefit of the government. They could have decided,  
8 well, this is going to be tough on the GSEs, but it's great  
9 for us, great for the government, so we're going to do it.  
10 That's something a traditional conservator would never be  
11 allowed to do and wouldn't even occur to them.

12 MR. KATERBERG: Well, and Congress is free to do  
13 that. It's Congress' policy choice.

14 THE COURT: Yeah, they could do that.

15 MR. KATERBERG: It doesn't change the character of  
16 the activity, though. They're still engaging in a  
17 fundamentally private transaction when they do the Third  
18 Amendment and the fact that the statute directs them that  
19 they can take into account certain considerations when they  
20 do that.

21 THE COURT: So if the agency acting as conservator  
22 takes an act to further the government's interests, even  
23 potentially at the cost of the private entities into whose  
24 shoes they've stepped, you would still say that's an  
25 exercise of private authority, not public authority?

1 MR. KATERBERG: That's right, Your Honor. The  
2 nature of the transaction is still not something that's  
3 inherently sovereign and governmental in character.

4 THE COURT: Okay. Another argument they make is  
5 they refer -- and you did respond to this, and I didn't  
6 understand either the argument or the response, and I didn't  
7 have time to look into it -- they keep talking about the  
8 FHFA having the power to suspend the applicable provisions  
9 of the APA in HERA. What are they talking about, and what  
10 is your response?

11 MR. KATERBERG: It's a gross embellishment that  
12 doesn't really have any connection to reality, Your Honor.  
13 I think what they're talking about is there's a statutory  
14 provision in 4617 called 4617(f) and it says that no court  
15 may take action to restrain or affect the conservator.

16 THE COURT: That is all they're referring to, is  
17 the anti-injunction provision?

18 MR. KATERBERG: I think Your Honor would have to  
19 ask them.

20 THE COURT: I'll ask them.

21 MR. KATERBERG: My answer to that is it's not  
22 dealing remotely with what they describe because that  
23 provision says that a court can't enter an injunction  
24 against FHFA or against -- potentially an injunction against  
25 somebody else that is going to disrupt FHFA in carrying out

1 its conservatorship responsibilities. But it doesn't say  
2 anything about suspending the application of --

3 THE COURT: There's a difference between -- as a  
4 practical matter, it might not make much of a difference,  
5 but legally there's a big difference between saying you are  
6 exempt from the APA and the APA applies to you, but a judge  
7 can't enter an injunction to enforce it.

8 MR. KATERBERG: Your Honor, we don't purport to  
9 claim the authority to make illegal things legal or anything  
10 like that. I mean, there's nothing in the statute that  
11 provides for that.

12 Congress made a policy decision that it wanted to  
13 give FHFA's conservator wide latitude in running the  
14 businesses as conservator and so it didn't want courts  
15 interfering with kind of the day-to-day management, the  
16 business judgments, and those sorts of things. But nothing  
17 about that renders what is illegal legal, which is how  
18 they've characterized it.

19 THE COURT: Okay. And then, last, they repeatedly  
20 refer to the fact that the FHFA exercised authority under a  
21 statute to alter legal rights and obligations of third  
22 parties. I think they're referring to the Third Amendment  
23 entering a contract, which do you -- I probably should have  
24 this in the opposite -- I should have had Mr. Knudson up  
25 first. I understand the response that entering a contract

1 is not a governmental activity, private people do it all the  
2 time, and contracts affect third parties all the time.  
3 Other than that, do you understand them to be referring to  
4 anything other than entering the contract?

5 MR. KATERBERG: No. I think Your Honor is right,  
6 I think they are referring to entry into the contract. You  
7 know, contracts can have incidental effects on other people.  
8 You know, if a regular company outside the context of  
9 conservatorship enters into a major financing contract, it  
10 may have an effect on other stakeholders with relation to  
11 that company. And, you know, what the rights are can be  
12 sorted out under state law and under contract law and that  
13 sort of thing, but it's not anything that gives it a  
14 uniquely governmental attribute.

15 I mean, really what the non-delegation doctrine is  
16 concerned with -- and I would focus on the private  
17 non-delegation doctrine here -- is the few cases that have  
18 applied that branch of the nondelegation doctrine, what it's  
19 about is private companies having the ability to enact  
20 basically laws that are going to be binding on their  
21 competitors, you know, to get an unfair advantage in the  
22 marketplace by prescribing rules of conduct, you know. So  
23 this was in the cases from the 1930s. The D.C. Circuit did  
24 it more recently in the *Amtrak* case; although, ultimately  
25 that was reversed by the Supreme Court on other grounds.

1 But the idea is we don't want Congress to be able to pick  
2 out one winner in a competitive area in an industry and  
3 allow that company to basically write the rules for its  
4 competitors on paying of penalty. This couldn't be more far  
5 afield from that.

6 So, again, what we have here is entry into a  
7 contract that they claim incidentally affects their rights,  
8 but we didn't prescribe rules of conducts for shareholders,  
9 we're not sanctioning shareholders, we're not investigating  
10 shareholders. Those latter kinds of things would be the  
11 kind of governmental powers that the non-delegation  
12 doctrine, as related to the private side, is concerned with,  
13 but it simply doesn't apply here.

14 THE COURT: Anything more you want to say on the  
15 delegation issues?

16 MR. KATERBERG: No, Your Honor. I think that  
17 covers it.

18 THE COURT: Okay. Thank you.

19 MR. KATERBERG: Thank you.

20 THE COURT: Mr. Knudson.

21 MR. KNUDSON: Thank you, Your Honor.

22 Just a prefatory comment about *Nguyen* that was  
23 mentioned earlier. In that case, they held that the party  
24 hadn't raised a de facto officer issue in the Ninth Circuit.  
25 The court accepted that argument before it in the Supreme

1 Court, so it's not untimely for us to be bringing this  
2 lawsuit now.

3 THE COURT: Okay.

4 MR. KNUDSON: I also want to point out that the  
5 Treasury Department has taken the position in *PHH*, and it's  
6 filed this in the *Collins* case that's mentioned in the  
7 briefs, that the government now takes the position that the  
8 single officer for clause situation is unconstitutional. I  
9 haven't heard anything from the Treasury here today  
10 addressing that particular issue.

11 With respect to the non-delegation --

12 THE COURT: Well, wait a minute. The Treasury in  
13 *PHH* argued that the -- why was Treasury involved in *PHH*?

14 MR. KNUDSON: Filed an amicus brief --

15 THE COURT: Oh, it was an amicus brief.

16 MR. KNUDSON: -- setting forth the position of the  
17 United States. They agreed with the conclusion of the panel  
18 that the for-cause removal provision applicable to the  
19 director of the CFPB violates the constitutional separation  
20 in powers. This is a filing called an advisory as filed in  
21 *Collins v. FHFA* in the Southern District of Texas - - --

22 THE COURT: All right. With the non-delegation  
23 doctrine let me start just by asking -- just assume that I  
24 agree with you that whether I'm supposed to be looking at  
25 the task or the role or whatever that it was governmental,



1 and that the agency was exercising governmental authority  
2 when it entered into the Third Amendment. Why is that  
3 legislative authority? It doesn't look to me anything like  
4 legislative authority to enter into a contract. That's not  
5 what Congress does. That's not what the Minnesota State  
6 Legislature does.

7 MR. KNUDSON: -- but the director, acting Director  
8 DeMarco, was acting as a public official.

9 THE COURT: I'm saying assume I'm agreeing. But  
10 the non-delegation doctrine is -- I'm not talking about the  
11 private one. I'm talking about the traditional  
12 non-delegation doctrine. It's the non-delegation of  
13 legislative authority. Entering the Third Amendment wasn't  
14 an exercise of -- even if it was exercising government  
15 authority, it wasn't legislative authority is my suggestion.

16 MR. KNUDSON: Well, the conservator was acting  
17 under authority granted by Congress in HERA, and it was  
18 given unfettered authority to do what it chose to do as a  
19 conservator. It could prescribe rules affecting the  
20 entities. In one of those terms, it was a contractual term,  
21 but it was still implicating the structure of these  
22 entities. In essence, what the director did was adopt a  
23 term that was completely inconsistent with what a  
24 conservator would be doing. It adopted a term that  
25 essentially gutted financial viability of Fannie Mae and

1 Freddie Mac. This is an unbelievable delegation of  
2 unfettered authority.

3 The *Perry Capital* decision says that the  
4 conservator is bound by no federal statute except HERA or  
5 the Constitution. So it has nothing -- and no court can  
6 tell it what to do unless it can find a violation of HERA.  
7 Interpretation of the conservator powers in *Perry Capital*  
8 basically removed any practical limitation on the powers of  
9 the conservator.

10 So we're saying that creating an agency with  
11 unfettered discretion, delegating to that agency something  
12 that's in violation of the non-delegation doctrine. So by  
13 being able to prescribe conduct, which is what a legislative  
14 function would be --

15 THE COURT: It is, but you're not suing them for a  
16 regulation prescribing conduct. You're suing them -- the  
17 heart of your lawsuit is for entering into a contract, and  
18 entering into a contract -- that's why I'm having trouble  
19 understanding what the non-delegation of legislative  
20 authority has to do. If you were suing them for --  
21 typically when you see a non-delegation challenge, and you  
22 don't see many of them because they are hard to win, but  
23 when you see them, it's typically the agency has promulgated  
24 a rule, a regulation, and the argument is that's a  
25 legislative act and they were delegated legislative

1 authority without a guiding principle.

2 Here I just don't -- and if you know such a case,  
3 tell me -- I'm just not ever aware of a government agency's  
4 decision to enter into a contract being challenged on  
5 non-delegation grounds. Have you seen such a challenge  
6 before or a case involving such a challenge?

7 MR. KNUDSON: The argument we're making here is  
8 that there is no intelligible principle to guide the conduct  
9 of FHFA.

10 THE COURT: Yeah, and I understand your argument,  
11 and I follow that completely. But it doesn't matter unless  
12 the action you're complaining of is a legislative act, is an  
13 exercise of legislative power. That's what I keep getting  
14 stuck on.

15 MR. KNUDSON: It isn't necessarily limited to  
16 legislative acts. It can apply to this contracting  
17 situation, as well. So that Congress has to give the agency  
18 some intelligible principle as to how to conduct itself, how  
19 to --

20 THE COURT: In the exercise of legislative  
21 authority.

22 MR. KNUDSON: Well, the authority granted in the  
23 statute, yes. So we believe the non-delegation doctrine  
24 would apply to limit what Congress could authorize the  
25 agency to do given the limitations on judicial review in

1 4712(f), which basically says the court can't enjoin  
2 anything the agency tries to do unless you can find a  
3 violation of the statute itself. And the statute is devoid  
4 of any principles to guide the conduct of the agency when  
5 acting as a conservator.

6 THE COURT: Okay. Let me ask about the government  
7 action. So we start with the baseline that, generally  
8 speaking, when someone is a conservator, that person is  
9 stepping into the shoes of the entity for which he's acting  
10 as conservator. If that entity is private, then the  
11 conservator is acting in a private capacity when he acts on  
12 behalf of the agency. If it's public, I assume it would be  
13 public. So given that that's the general rule and given  
14 there's no dispute that Fannie Mae and Freddie Mac are  
15 private entities, just -- I recognize you read this and you  
16 have this in your brief, but I just want you to crystallize  
17 for me what you think the best argument or two are -- why is  
18 it that when this agency stepped into the shoes of private  
19 agencies as conservator their actions were governmental  
20 rather than private?

21 MR. KNUDSON: Let's talk through a timeline on  
22 this one then.

23 THE COURT: Okay.

24 MR. KNUDSON: First we have Director Lockhart  
25 bringing the companies into conservatorship acting as

1 regulator. Then on the back-end in the timeline we have  
2 Director Watt authorizing the payment of dividends as  
3 regulator because there is a regulatory provision, 12 CFR  
4 1231.12, which says no dividends can be paid out without  
5 approval of the agency. So the entities go into  
6 conservatorship under a regulatory process. They continue  
7 to pay dividends to the Treasury being approved by the  
8 Director as regulator. So on the front-end and the back-end  
9 we clearly have the government controlling the conduct of  
10 these entities.

11 Then with respect to the Net Worth Sweep Rule,  
12 what the agency has argued in *Perry Capital* was it was  
13 acting in the governmental interest, in the public interest.  
14 It can't be heard here to argue otherwise. The money that  
15 they take that would go to the entities goes to the  
16 government. So, again, it's a public function.

17 So conduct of the conservator here should be  
18 deemed to be a public action because of the context in which  
19 power to direct the dividends arose out of a regulatory  
20 action. Payment of those dividends is done under a  
21 regulatory approval.

22 The choice the director made in 2012 to adopt or  
23 impose the Net Worth Sweep Rule was under a policy decision  
24 to essentially put these entities out of the housing market  
25 business. As of that time, they thought there should be a

1 different model for the housing market. Now, they didn't  
2 get rid of them, but they made it very difficult for them to  
3 operate going forward.

4 THE COURT: I don't know that this is relevant to  
5 anything, but they dumped tens of billions of dollars of  
6 taxpayer money into the entities. That seems like a silly  
7 way to try to put them out of business.

8 MR. KNUDSON: That was before the Net Worth Sweep  
9 Rule was adopted, Your Honor. Now the companies have turned  
10 around. They are making large profits, and the profits are  
11 all going to the Treasury.

12 So it was a situation where at the time it was  
13 adopted the market was turning around. These companies  
14 could be restored to financial stability. They had to  
15 continue this rule that essentially prevents that from  
16 happening.

17 THE COURT: Okay. But you want to argue the *Perry*  
18 *Capital* case here and we don't have the *Perry Capital* case  
19 here. We have this constitutional case.

20 So there's a couple of arguments -- I went through  
21 these with Mr. Katerberg, and I just want to clarify that I  
22 understand your arguments. These are arguments as to why  
23 when the agency entered into the Third Amendment they were,  
24 in your view, exercising governmental authority.

25 You talk about they exercised authority to alter

1 legal rights and obligations of third parties. Other than  
2 through entering into the Third Amendment, is there anything  
3 else you're referring to when you make that argument in your  
4 briefs?

5 MR. KNUDSON: That's our point, Your Honor.

6 THE COURT: Okay. And then when you say they were  
7 acting in the public interest, and you've just repeated that  
8 point, I understand that; I think that's a good argument for  
9 you.

10 When you talk about them suspending the  
11 application of the APA in HERA, are you referring to  
12 something other than the anti-injunction provision?

13 MR. KNUDSON: No, we're referring to that.

14 THE COURT: Okay. I just wanted to make sure I  
15 understand that.

16 Is there anything more you want to say about the  
17 non-delegation issues?

18 MR. KNUDSON: No, Your Honor. That should sum it  
19 up.

20 THE COURT: Okay. Thank you, Mr. Knudson.

21 Mr. Katerberg, is there anything more you wanted  
22 to say on the non-delegation issues?

23 MR. KATERBERG: Nothing more, unless Your Honor  
24 has questions.

25 THE COURT: Okay. Why don't we just take another

1 short break here. My court reporter has been going about 90  
2 minutes. We'll come back and talk about the last two  
3 issues, which are the succession-clause issue and the  
4 res judicata. So we'll see you in about ten minutes.

5 THE LAW CLERK: All rise.

6 (A brief recess was taken.)

7 THE LAW CLERK: All rise. This court is now in  
8 session.

9 THE COURT: Please be seated.

10 I want to turn to the issue of res judicata. This  
11 was raised by Treasury. Are you going to argue it,  
12 Mr. Merritt?

13 MR. MERRITT: Yes, Your Honor.

14 THE COURT: Okay. Can I have you at the podium  
15 then, please.

16 Now, this issue dovetails with the  
17 succession-clause issue. Are you prepared to address that  
18 as well?

19 MR. MERRITT: Yes, Your Honor.

20 THE COURT: Okay. So I used it be a law professor  
21 before I became a judge, and I taught Civil Procedure, and  
22 this would have made a fantastic exam question on res  
23 judicata because there's, like, three really, I think, hard  
24 issues on this.

25 The first issue is whether the *Perry Capital* and



1        *Saxton* cases ended in final judgments on the merits. You  
2        say they did. Your opponents say they didn't. I think this  
3        is just a hard question. I'm wondering whether there is --  
4        here's my first reaction to this, and it really -- like  
5        everything I'm saying today, it's just a first reaction  
6        subject to further thinking. If a lawsuit was dismissed on  
7        the basis of the succession clause, that does not feel to me  
8        like a judgment on the merits. That is essentially saying  
9        if I were to dismiss a lawsuit on the basis of the  
10       succession clause, I would be saying to the plaintiffs you  
11       don't have the right to adjudicate this lawsuit on the  
12       merits, somebody else has a claim on the merits, somebody  
13       else might, but you don't. That feels like it's akin to a  
14       standing ruling or a failure to certify a class ruling.  
15       That doesn't feel like a judgment on the merits to me. I'm  
16       saying you're not entitled to a judgment on the merits from  
17       me. That's why I'm dismissing the lawsuit.

18                The anti-injunction provision is interesting.  
19        That feels to me more like the merits. That's basically  
20        saying under the law, Congress has said you don't get a  
21        remedy for this even if you do find a wrong and, therefore,  
22        you lose. You don't get the remedy. There's lots of  
23        lawsuits where you lose because you're not entitled to  
24        remedy. Those feel like merits-based decisions.

25                So I guess my questions are, number one, what do

1 you think of my first reaction? And, number two, just  
2 assuming for the sake of argument that I'm right, what do I  
3 do with a case like *Perry Capital* which has both in it? It  
4 has some anti-injunction ruling in it, and it has some  
5 succession clause ruling in it.

6 MR. MERRITT: So regarding your initial thoughts  
7 on this issue, Your Honor, I think, as you admit, it can be  
8 a close issue. I think it's useful to contrast what a  
9 ruling on the shareholder succession provision does versus  
10 some other kind of precondition to suit or something like  
11 that, how it would operate.

12 What a ruling that says a claim is barred pursuant  
13 to the shareholders' succession provision says that if that  
14 plaintiff -- actually, the claim does not belong to him  
15 because it is a derivative cause of action, which is what  
16 was a necessary precondition of the findings in both *Perry*  
17 *Capital* and *Saxton*. So that is just saying that so long as  
18 a shareholder in the GSEs is attempting to bring any claim  
19 that is derivative in nature during the conservatorship that  
20 they don't have the ability to do that.

21 So I think that can be distinguished from  
22 something that they could easily fix, something like -- some  
23 of the examples cited in the Wright Miller in their briefs  
24 were failure to plead demand or like a failure to exhaust  
25 administrative remedies or something that you just kind of

1 send back and they can fix and they can come back.

2 I think on the shareholder succession provision at  
3 least so long as the conservator remains in effect and  
4 plaintiffs attempt to pursue claims that are derivative in  
5 nature, that they are precluded by doing so by the prior  
6 judgments adjudicating that issue.

7 THE COURT: But standing is not easily fixed. If  
8 you have somebody who sues and you can tell that person  
9 doesn't have standing to pursue that claim, that's not  
10 considered a judgment on the merits. It doesn't have  
11 preclusive effect later on.

12 Wouldn't a ruling that you don't have the right to  
13 bring a derivative action because only the conservator has  
14 the right to bring that action, wouldn't that be pretty  
15 close to a standing issue?

16 MR. MERRITT: It certainly does dovetail with the  
17 issue of standing because in many ways, as pointed out in  
18 our briefs and other places, the shareholder succession  
19 provision kind of operates in a similar way to the  
20 shareholder standing rule that has been long recognized  
21 essentially saying that shareholders of corporations cannot  
22 bring claims based on harms to the corporation, you know, in  
23 their own name.

24 I think, I mean, the main difference here is that  
25 this was -- the thing that deprived them of standing was the

1 statute itself, a statutory bar, which is in some ways  
2 different from kind of a finding based on standing.

3 THE COURT: Well, it's different than Article III  
4 standing, but then there's this doctrine that I find  
5 impenetrable called statutory standing or -- what's the word  
6 for the other -- prudential standing -- prudential standing,  
7 which it's just unintelligible, but that's not here nor  
8 there today.

9 So what about my second question? What happens if  
10 you have a -- you've given me two opinions that have both in  
11 them. They have both these doctrines cited in them. If, in  
12 fact, one is a judgment on the merits and one is not a  
13 judgment on the merits, what do I do about that?

14 MR. MERRITT: So in that situation you would be  
15 saying that -- I guess it probably doesn't matter if it's a  
16 hypothetical, but assuming the 4617(f) bar was not a  
17 judgment on the merits --

18 THE COURT: Right.

19 MR. MERRITT: I think our position is so long as  
20 there was a judgment on the merits -- on a basis that you  
21 could characterize it as a judgment on the merits that it  
22 would bar a later suit.

23 THE COURT: Okay. Let me skip to a later element.  
24 Three of the four elements of res judicata are kind of in  
25 play today. The last is whether it's the -- I forget the

1 exact way that it's put -- whether both suits are based on  
2 the same claims or causes of action.

3 So here there's a bitter dispute between my law  
4 clerk and me as to whether these are or are not on the  
5 basis -- to me they feel like they are based on the same  
6 claims. To me it feels like *Perry* attacked the legality of  
7 the Third Amendment on certain grounds and then *Saxton*  
8 attacked the legality of the Third Amendment on certain  
9 grounds, and this is just yet another case attacking the  
10 validity of the Third Amendment on just different grounds.  
11 And that's exactly the kind of claim splitting that *res*  
12 *judicata* is supposed to prevent. If you don't like the  
13 Third Amendment, you're not supposed to be able to bring a  
14 first lawsuit and make certain arguments and then bring a  
15 second lawsuit and bring other arguments and a third lawsuit  
16 and make other arguments. You're supposed to make all your  
17 arguments in your first lawsuit. But to my law clerk -- I  
18 hate to put words in her mouth, but she would put her  
19 argument better than me -- to her it feels differently. The  
20 earlier lawsuits were attacks on the Third Amendment. This  
21 lawsuit, although we all know it's an attack on the Third  
22 Amendment, isn't structured as such. It's an attack on the  
23 agency, the constitution of the agency.

24 Now, if the lawsuit is successful, the Third  
25 Amendment would fall because, as I said earlier today, you'd

1 be killing the host and the organisms would fall. But it  
2 isn't a lawsuit -- even though it mentions the Third  
3 Amendment a thousand times in the Complaint, it's  
4 technically a lawsuit attacking the structure of the agency  
5 and, therefore, this is a lawsuit that could've been brought  
6 before the Third Amendment was even signed. So she would  
7 ask how can it be about the Third Amendment when the exact  
8 same lawsuit could've been brought before there even was a  
9 Third Amendment? So, in her view, it's not part of the same  
10 claims. So why is she wrong and I'm right?

11 MR. MERRITT: Your Honor, I would humbly agree  
12 with your position on that. I think what the claim  
13 preclusion test looks at is whether the actions essentially  
14 challenge the same transaction or a series of transactions.

15 It also looks at what type of harm the action is  
16 getting at, like what is the basis for the harm that the  
17 plaintiff has suffered that they bring the action in. At  
18 that point, I would go to back to something Mr. Katerberg  
19 said regarding what the plaintiffs have actually alleged  
20 here that would give them standing and what would give them  
21 an injury in this case and that is the Third Amendment. I  
22 mean, without the Third Amendment it is true -- and this is  
23 one the reasons why Treasury has argued that there should be  
24 no claims against it, that the claims against it should be  
25 dismissed -- that this case is not a direct challenge to the

1 Third Amendment, but is instead structured as a challenge to  
2 FHFA's constitutionality. But at bottom what they're  
3 alleging their harm is is the Third Amendment, which is the  
4 same harm -- or harm inflicted upon them through what the  
5 Third Amendment did to the GSEs, which is the same harm that  
6 was at issue in all the prior cases, including *Perry Capital*  
7 and *Saxton*. So not only does this arise out of the same  
8 transaction, but it also is getting at seeking to remedy the  
9 same harm.

10 THE COURT: Okay. The third issue is the privity  
11 issue, whether these plaintiffs are in privity with the  
12 plaintiffs in the previous actions. That seems to turn on  
13 whether, at least in part, this is a derivative action.  
14 This goes to the succession clause issue, as well.

15 Just, again, on a 30,000-foot level, I'm  
16 sympathetic to your position. I agree with you that the way  
17 that we normally decide whether something is a derivative  
18 action is you look at who suffered the harm and who would be  
19 benefited by the remedy. It seems to me that, on first  
20 glance, there's nothing here that the FHFA did to the  
21 shareholders as shareholders. They did something to the  
22 companies, and the thing they did to the companies hurt the  
23 value of the shareholders' shares. But that's a derivative  
24 action.

25 Likewise, it doesn't feel to me like any remedy

1 would have anything to do with the shareholders, except  
2 indirectly. I'm not going to order anybody to pay any money  
3 to a shareholder. I'm not going to enjoin anybody from  
4 doing anything with respect to a shareholder. It feels like  
5 a derivative action.

6 There's two things that give me pause, though.  
7 One is they asked the question, and it's a legitimate  
8 question, is if they can't challenge the constitutionality  
9 of the agency in this way, who can?

10 Just assume that FHFA is unconstitutionally  
11 structured. Assume that the Third Amendment, along with  
12 everything else it did, is invalid because of it's  
13 unconstitutional structure. If they can't bring that claim,  
14 who can? Who can?

15 MR. MERRITT: Well, Your Honor, I think the answer  
16 to that -- I mean, even if it is that no one can bring that  
17 claim, I don't think there should be concern about getting  
18 to that point for the reasons stated in our brief. I mean,  
19 I think it's important to remember that, you know, the  
20 actual legal theories asserted here are, as you say,  
21 challenges to FHFA's constitutionality. So the notion that  
22 that constitutional violation cannot be challenged by anyone  
23 is not at issue here.

24 Assuming there was some party out there, such as a  
25 party affected hypothetically, of course, by FHFA in its



1 regulatory capacity or some party that was able to show  
2 direct personal injury as a result of the constitutional  
3 allegations that are at issue here, that party would not be  
4 barred by these provisions and would be able to bring a  
5 claim. And separately the plaintiffs have the ability to  
6 challenge the Third Amendment.

7 THE COURT: Well, what if the person is somebody  
8 harmed by the Third Amendment, though? How could anybody on  
9 earth who believed themselves to be harmed by the Third  
10 Amendment and believed that the Third Amendment was unlawful  
11 because of the constitutional structure of the agency, how  
12 could anybody get that claim heard? Or maybe the answer is  
13 nobody can.

14 MR. MERRITT: Yeah, in response to that I would  
15 submit that a party, a shareholder in the FHFA or in the  
16 GSEs that were unable to show direct personal injury as a  
17 result would -- unless -- sorry. I will back up on that.  
18 Unless a party was able to show direct personal injury -- if  
19 the only party was a shareholder in the GSEs that showed a  
20 derivative injury through the corporation to themselves,  
21 then that party would not be able to bring suit.

22 THE COURT: So essentially nobody, except the GSEs  
23 themselves, could sue if in fact the Third Amendment was  
24 unlawful because the FHFA was unconstitutionally structured?

25 MR. MERRITT: I think that's -- I mean -- for the

1 reasons we've stated, we don't think it would get to that  
2 point, but, yeah, I think that's right. I don't think there  
3 is any harm in that.

4 Again, one of the points made in the briefs is  
5 that the shareholder standing rule, which is kind of a  
6 similar proposition of law to have the shareholder  
7 succession provision operate, which basically says  
8 plaintiffs cannot bring claims based on injury to the  
9 corporation, that has been applied in other contexts too for  
10 findings based on the Constitution. So there would be no  
11 special --

12 THE COURT: The problem here is that by statute  
13 the claim can only be brought by the conservator, and the  
14 claim is against the conservator. Normally we don't give  
15 effect to statutory provisions that would literally bar --  
16 would allow government agents to act unconstitutionally  
17 without anybody being able to bring them to account or to  
18 get a remedy for that, which seems -- unless -- this isn't  
19 mentioned in your brief, but I wondered, is it theoretically  
20 -- I assume it's theoretically possible for FHFA as  
21 conservator to sue FHFA as agent. I shouldn't say I assume.  
22 I mean, it seems like it's a possibility to me because the  
23 FHFA, as conservator, is stepping in the shoes of the GSEs.  
24 GSEs can sue FHFA. You didn't seem to contest this. Your  
25 opponent said, well, FHFA couldn't sue itself. There would

1 be an Article III problem. But it wouldn't -- at least it  
2 seems to me there's an argument that FHFA, as conservator,  
3 it's not suing as FHFA. It's suing as Fannie Mae. Fannie  
4 Mae can sue the FHFA, as unlikely as it would be that such a  
5 lawsuit would be brought.

6 MR. MERRITT: Yes, Your Honor. We didn't get into  
7 that in the briefs partly because we don't think that there  
8 is any basis for these constitutional claims asserted,  
9 especially insofar as they challenge the Third Amendment.  
10 But I think -- I mean, I haven't again scoured -- done full  
11 research on that, but I think the point you make is possible  
12 in theory and isn't that different from the situation in  
13 which derivative suits are often brought in which a -- you  
14 know, we're talking about situations in which the  
15 corporation is injured by something, a corporate board or  
16 something like that does, and should the corporation agree  
17 to -- like such as if demand is made and agree to pursue the  
18 action on its own would be a potentially similar situation.

19 THE COURT: The other argument they made that I'd  
20 like to ask you about -- as I told you, my first reaction is  
21 that this looks like a derivative lawsuit to me. But they  
22 characterize their claim -- and I don't know enough about  
23 the facts and the operative documents to know if this is  
24 true, but they say if hypothetically you have a case where a  
25 corporation takes an action that deprives one set of

1 shareholders of a legal right they have to benefit another  
2 set of shareholders, then the harmed shareholders could sue  
3 and it wouldn't be a derivative action. It's suing the  
4 corporation for favoring one group of shareholders over  
5 another. I mean, that's a shareholder claim, not a  
6 corporate claim. Okay? And they say, well, that's what  
7 happened here. We had a legal right to certain dividends.  
8 And I don't know if they are also arguing rights of  
9 corporate governance or whatever, but we had certain legal  
10 rights, and FHFA took those from us to give them to another  
11 shareholder, Treasury. So this isn't a claim we're making  
12 on behalf of the corporation to remedy a wrong to the  
13 corporation. We got screwed as shareholders to favor other  
14 shareholders, and that's the kind of lawsuit we're bringing  
15 here. If that's right, it doesn't sound derivative. What  
16 is your response to that argument?

17 MR. MERRITT: I would say, first of all, what they  
18 are -- again, what they are challenging here is the Third  
19 Amendment, which is not due to a lot of things you are  
20 describing. All it really does is renegotiate the dividend  
21 that was payable from a fixed rate to a variable dividend.

22 THE COURT: Did the shareholders of Fannie Mae  
23 preconservatorship, just as it was operating, did they have  
24 a legal right to dividends or only such dividends as Fannie  
25 Mae decided to declare?

1 MR. MERRITT: Preconservatorship?

2 THE COURT: Yeah.

3 MR. MERRITT: I can't speak on -- I know that  
4 there is -- the right to dividends were extinguished by the  
5 conservatorship, and that's kind of the era we're operating  
6 in here. I can't say with confidence.

7 THE COURT: Okay. I'm sorry, I cut you off. What  
8 is your response then to that argument?

9 MR. MERRITT: Okay. So one response is that, you  
10 know, if what the plaintiffs are arguing is essentially that  
11 -- I guess you could call it some sort of expropriation  
12 theory, that the value of their shares were taken -- you  
13 know, clearly what we would consider -- how we measure the  
14 value of the shares but was taken from them and given to  
15 Treasury. That is essentially an argument that economic  
16 value of their shares is what's being appropriated, and that  
17 is the kind of claim that has been classically considered  
18 derivative as the --

19 THE COURT: Well, if I understand it right, it's  
20 derivative -- if somebody outside the corporation does  
21 something to hurt the corporation and as a result of what  
22 they do to hurt the corporation the value of the shares is  
23 diminished, that's certainly a derivative claim. That's a  
24 classic derivative claim.

25 Now, are you talking about -- but they're talking

1 about something different, which is -- let's just talk about  
2 it hypothetically. Hypothetically the corporation's value  
3 is exactly the same. The corporation hasn't been harmed at  
4 all. But what has happened is the corporation has somehow  
5 acted to harm one group of shareholders to benefit another  
6 group of shareholders. The corporation hasn't been harmed.  
7 It's not seeking any remedy. That's how they're trying to  
8 portray what they're doing here. Why isn't that an accurate  
9 portrayal of what's happening here?

10 MR. MERRITT: If what their injury is is reduced  
11 value in the shares, that is an injury to the corporation.

12 There is another species of what is called  
13 economic dilution claims, when one shareholder gets more  
14 value in their shares as related to another shareholder, and  
15 that is also, in general, considered to be a derivative  
16 injury again, because regardless of --

17 THE COURT: When does that come up, like when an  
18 corporation issues additional shares and thus dilutes the  
19 existing shares?

20 MR. MERRITT: That's one way. So I think it can  
21 be useful to look at the cases finding an exception to the  
22 rule that that kind of behavior would be a derivative  
23 injury.

24 We specifically cited a case, the *Gentile* case --  
25 which I thought was pronounced *gentile*, but I think it's

1     *gen-tilly* -- that essentially recognized that when you have  
2     a controlling shareholder and they take some sort of action  
3     -- transact with the corporation in a way that, you know, as  
4     set forth in the briefs, but causes the issuance of some  
5     sort of excessive amount of shares and for less  
6     consideration than that would be worth, that causes them to  
7     have an excessive amount of shares in a corporation  
8     vis-a-vis the minority shareholders and that also creates  
9     some injury to the minority shareholders' voting power, in  
10    that narrow circumstance this type of kind of economic  
11    dilution of the shares -- expropriation of economic  
12    valuation of the shares could be considered what they called  
13    "dual natured." As the recent Delaware Supreme Court  
14    decision in the *El Paso Pipeline* case made clear, the  
15    *Gentile* exception should be limited to its facts.

16           So in this case, plaintiffs did not even attempt  
17    to fit their claims into that or allege that Treasury is the  
18    controlling shareholder or it has voting rights or they were  
19    benefited and, most importantly, that plaintiffs' voting  
20    rights were in some way diminished based on the Third  
21    Amendment specifically. As the *El Paso Pipeline* court  
22    determined, extraction of solely economic value from the  
23    minority by a controlling shareholder does not constitute  
24    direct injury.

25           So I would point Your Honor as well to a couple of

1 other recent district-court cases that were dealing with  
2 similar allegations by GSE shareholders that the value of  
3 their shares had been expropriated in some way from them to  
4 Treasury and found that absent allegations of kind of a harm  
5 to voting power, something beyond extraction of economic  
6 value, that those were derivative in nature, and those would  
7 be the *Saxton* case in the Northern District of Iowa and the  
8 *Edwards* case in the Southern District of Florida.

9 THE COURT: Okay. Is there anything more you  
10 wanted to say on these issues?

11 MR. MERRITT: Not on these issues, Your Honor.

12 I don't know if this is the appropriate time, if  
13 you want to talk about it later, which is --

14 THE COURT: About Treasury?

15 MR. MERRITT: -- Treasury's main argument.

16 THE COURT: I figure at some point you want to  
17 talk about Treasury.

18 This is a puzzler. This is just such a hard case.  
19 There are so many hard issues. There aren't any claims  
20 against you per se. Nowhere in their 59-page brief do they  
21 anywhere suggest that Treasury violated the law in any way,  
22 so I get that. At the same time, they are seeking to  
23 invalidate the contract to which Treasury is a party. It's  
24 a weird lawsuit because somebody who is not a party to a  
25 contract is suing to invalidate a contract on the grounds



1 that one of the parties to the contract didn't have the  
2 ability, capacity, whatever to enter the contract. So I  
3 completely understand why they want both parties to the  
4 contract in the lawsuit, because they want the eventual  
5 judgment to bind both parties. They don't want to win and  
6 then have Treasury come in and say, wait a minute, we're not  
7 bound by that judgment and we're parties. But they also  
8 don't really have any claims against Treasury, maybe a  
9 declaratory judgment claim, maybe.

10 So I agree with you, there aren't any claims here.  
11 Treasury doesn't have to write a check here. That's  
12 completely true. But at the same time I understand why they  
13 want you in the lawsuit. I just don't know what to do with  
14 that.

15 MR. MERRITT: So Treasury can only respond to the  
16 Complaint as it's currently pled. And, you know, as you  
17 mentioned, the basis for Treasury being in this was kind of  
18 stated in our reply brief, which is this is what the  
19 plaintiffs characterize as an action to invalidate a  
20 contract to which Treasury is a party. But as I think has  
21 been made clear in today's discussions and in the briefs,  
22 this is not really what this action or at least -- it's an  
23 action to invalidate an agency.

24 THE COURT: We keep going back between what it  
25 really is and what it's being portrayed as. I understand,

1 and it's a little tricky.

2 MR. MERRITT: So I think given that kind of  
3 disconnect, you know -- the case as pled asserts five counts  
4 and asserts that Treasury has violated the President's  
5 removal power and Treasury has done all this, and having  
6 pled it that way, plaintiffs were certainly capable of, and  
7 have done many times, challenged this contract directly,  
8 challenged that it is invalid in its terms and that Treasury  
9 --

10 THE COURT: That's the blind alley they have put  
11 themselves in because they can't -- they're trying to not  
12 make this a claim to invalidate the Third Amendment based  
13 upon *Perry Capital* type of grounds. But if you are just  
14 genuinely bringing a lawsuit because you genuinely want to  
15 have an agency declared unconstitutional, then Treasury has  
16 no -- you've got no dog in that fight. So it's a --

17 MR. MERRITT: Right. I mean, that is the subject  
18 matter as it's presented. We're not a necessary or proper  
19 party to the adjudication of FHFA's status.

20 THE COURT: Right, not to that claim you're not.  
21 Right. Correct. Yeah. Okay. But other than that, I  
22 completely understand. No one here is pretending that there  
23 is any direct claim against you in the lawsuit.

24 MR. MERRITT: And, Your Honor, if I might make one  
25 more point in response to opposing counsel's argument about

1 what the government had filed in the *PHH* panel rehearing. I  
2 would just like to --

3 THE COURT: Oh, right, where they said you agreed  
4 with their position.

5 MR. MERRITT: That was an amicus brief in a  
6 different case involving CFPB, and the government has not  
7 taken any position with respect to FHFA and does --

8 THE COURT: Well, did Treasury in fact argue that  
9 the CFPB was unconstitutional because it had a single  
10 director instead of multiple directors?

11 MR. MERRITT: That was the thrust of the amicus  
12 brief in that case, Your Honor. I think -- just I would  
13 point out that has no relation to this case.

14 THE COURT: Well, except it's addressing the same  
15 issue, just different names.

16 MR. MERRITT: Well, one of the issues in the  
17 lawsuit that we don't think there is any reason to get to in  
18 this case for the reasons stated in the brief.

19 THE COURT: Okay. Well, it's possible on that  
20 issue I will end up ruling against both you and the  
21 plaintiffs and in favor of FHFA, but these are tricky times  
22 that we live in.

23 Okay. Thank you, Mr. Merritt.

24 MR. MERRITT: Thank you, Your Honor.

25 THE COURT: Yeah, Mr. Katerberg -- now, I've been

1 calling you kat-er-berg. Is it kate-er-berg?

2 MR. KATERBERG: I answer to both, Your Honor.

3 THE COURT: So when your parents told you how to  
4 pronounce your name, which one did they tell you?

5 MR. KATERBERG: Kate-er-berg would be the default.

6 THE COURT: Kate-er-berg, okay.

7 MR. KATERBERG: I have no objection whatsoever.

8 Your Honor, I'd just like to make some quick,  
9 discrete points mostly on the succession clause and the  
10 claim preclusion issues. We do join -- FHFA does join in  
11 those arguments.

12 First, Your Honor had a question about the  
13 entitlement of shareholders to dividends preconservatorship.  
14 I am completely confident, at least for common stock, it was  
15 discretionary. I believe it was discretionary for preferred  
16 stock as well. I can't say that categorically. I think in  
17 the Complaint they don't specify what series of preferred  
18 stock the three plaintiffs in this case owned. I believe  
19 it's discretionary for all of them. I'm sure we could get  
20 to the bottom of that. If I'm wrong about that, they will  
21 tell you so.

22 On the claim preclusion issue, the element that  
23 the same claims are causes of action, there is a very useful  
24 data point that I think it's worthwhile to throw into the  
25 mix, because some of the discussion, I think framed by

1 plaintiffs, has proceeded as if the prior cases, the APA  
2 claims, and the constitutional claims are sort of two paths  
3 that never shall meet. In fact, earlier this year, the case  
4 in the Southern District of Texas, *Collins v. FHFA*, was a  
5 case that blended the two elements.

6 So the *Collins* decision, which is 254 F. Supp. 3d  
7 841, rejected all these challenges. Counts One to Three of  
8 the complaints sought relief under the Administrative  
9 Procedure Act, like the *Perry Capital* case and the *Saxton*  
10 case that we're relying on for claim preclusion.

11 Count Four, and this is going to sound familiar,  
12 challenges the provision in here that requires cause for  
13 removal of the FHFA director arguing that it's not  
14 constitutional violation of the separation of powers.

15 So I really think you have an Exhibit A that shows  
16 that it's only natural to join these claims in the same  
17 action.

18 I want to address a concern that Your Honor had  
19 about -- and I'll call it the concern if they can't  
20 challenge it, who can, referring to the constitutionality of  
21 FHFA, and I want to address that on two levels:

22 First, I don't think that that should actually be  
23 a proper area of concern, and we know that from, for  
24 example, Chief Justice Rehnquist's decision in the *Valley*  
25 *Forge v. Americans United for Separation of Church and State*

1 case where it essentially makes the point, and there are  
2 other cases that say the same thing, the fact that there may  
3 be a constitutional violation out there is not a reason to  
4 stretch standing requirements or to find some -- to assume  
5 that someone must have standing to bring the challenge; I  
6 mean, standing operates independently. We don't need to  
7 sort of lean toward finding that someone necessarily must  
8 have standing just because there is a constitutional issue  
9 adjudicated.

10 THE COURT: We can't avoid requiring standing  
11 because it's part of Article III, which is part of the  
12 Constitution. At the same time, the Supreme Court generally  
13 doesn't allow Congress to insulate people from their  
14 unconstitutional acts. At least we try hard not to construe  
15 statutes to make unconstitutional acts unremediable in  
16 court.

17 MR. KATERBERG: Sure. So that gets to my second  
18 point, which is FHFA does a lot of things other than the  
19 Third Amendment and other than the conservatorship issues  
20 that are in this case. There's plenty of times -- and I  
21 know because my firm represents FHFA in many of these  
22 cases -- there are plenty of times where they get sued for  
23 various regulatory actions that affect people in various  
24 capacities. So it's not as if the Third Amendment lawsuits  
25 are the exclusive avenue for any constitutional issues to be

1 brought to the attention of an Article III court. If those  
2 arguments have merits, they're going to --

3 THE COURT: Well, the question, to be more  
4 precise, how does someone who has been harmed by the Third  
5 Amendment -- there might be people harmed by other things,  
6 but how does someone harmed by the Third Amendment who  
7 believes that the Third Amendment was invalid because of the  
8 constitutional infirmities in the agency, how do they bring  
9 that claim if they can't bring it as a derivative claim, if  
10 they can't bring it as an individual claim?

11 MR. KATERBERG: I think the answer is if their  
12 harm -- I mean, their harm -- and we think it is derivative  
13 of the harm to the corporation -- then they don't own that  
14 claim. I mean, the idea behind derivative lawsuits is that  
15 in certain circumstances we're going to allow shareholders  
16 to assert the rights of the corporation. But, essentially,  
17 if the injury is to corporation -- and, again, we think it  
18 is -- then HERA has said we're altering the normal rule that  
19 will apply outside conservatorship where Delaware law and  
20 Virginia law allow derivative claims. In certain  
21 circumstances, it's the corporation's to bring.

22 Now, I know the next question is going to be,  
23 well, you control the corporation. The corporation is not  
24 going to do that. I guess I just don't think that's a  
25 problem. I mean, one way to look at it is in any sort of

1 market situation if two companies are suing each other for  
2 patent infringement or an antitrust claim or whatever and  
3 one of those companies buys the other, there's not going to  
4 be anybody anymore to bring the patent-infringement claim as  
5 to that action or to bring the antitrust claim, but that's  
6 not a problem because --

7 THE COURT: There you have both the wrongdoer and  
8 the person injured by the wrongdoing that become one. Here  
9 allegedly you have the people being harmed who aren't part  
10 of the -- they wouldn't be part of the one. Here you have  
11 plaintiffs who say we were harmed because party A hurt our  
12 corporation, party B. And if the only person who can sue  
13 party A for harming corporation B is the wrongdoer, is A,  
14 the claim won't get brought. I mean, it would be an  
15 argument in favor, recognizing the exception -- whether it  
16 be a conflict of interest exception or a reading statute so  
17 they don't foreclose constitutional claims unless it's  
18 clear -- but that's the argument.

19 I think you're acknowledging that if I agree with  
20 your argument, that this is a derivative suit and doesn't  
21 create an exception, then they're basically out of luck,  
22 plaintiffs.

23 MR. KATERBERG: Well, again, to sort of map it  
24 onto my hypo, you could have shareholders of a corporation  
25 that is the victim of an antitrust violation that believe



1 it's just the most terrible antitrust violation ever and  
2 you've got to go after all these guys, but if the defendant  
3 buys the plaintiff, they're not going to be able to assert  
4 that claim because the claim belongs to the corporation.

5 So if the claim is truly derivative -- and, again,  
6 we think here it is because the injury derives from the  
7 diminution in the value of the common stock -- then it's the  
8 corporation's choice to make. And if the corporation gets  
9 bought by the alleged wrongdoer, that lawsuit is not going  
10 to go on anymore. But I don't think that's anything that  
11 really we need to worry about as a policy matter.

12 Your Honor also asked about sort of harm to their  
13 interests as shareholders and whether that would make it  
14 other than a derivative case. I want to address -- I may  
15 not have taken these down exactly right, but I think Your  
16 Honor mentioned sort of dividends -- we talked about that --  
17 voting rights, interest as shareholders. But I think if we  
18 pierce through -- I mean, fundamentally what they are  
19 complaining about, again, is the injury to the value of the  
20 stock. The dividends weren't there before. I mean, we can  
21 sort of divide it into three periods. There's the  
22 preconservatorship; dividends discretionary. But the moment  
23 of the conservatorship and the entry into the original PSPAs  
24 they weren't getting any dividends more at that point  
25 anyway. They weren't having voting rights at that point

1        anyway. So there maybe is a mismatch. I mean, to the  
2        extent they're complaining about those things, maybe they  
3        should be attacking the original entry into the  
4        conservatorship.

5                THE COURT: Oh, I see what you're saying. The  
6        before and after has to be not preconservatorship and Third  
7        Amendment. It has to be Third Amendment and  
8        conservatorship.

9                MR. KATERBERG: That's exactly right, Your Honor,  
10       because, I mean, really the Third Amendment altered the  
11       terms of how Treasury was going to get paid dividends.

12                THE COURT: Yeah, that's a good point. I hadn't  
13       thought of that. That's a good point.

14                MR. KATERBERG: They were already far under water;  
15       I mean, we're talking at the bottom of the ocean.

16                THE COURT: Apparently, they don't think so.  
17       Apparently, their briefs say they would have been just fine.

18                MR. KATERBERG: And I understand that, but --

19                THE COURT: They didn't need your hundreds of  
20       billions of dollars.

21                MR. KATERBERG: But I think for the purposes of  
22       the derivative claim -- I mean, this is the claim  
23       challenging the Third Amendment, and the proper mode of  
24       analysis is to look at how the Third Amendment specifically  
25       altered the legal regime, as opposed to --

1 THE COURT: I think you're right on that. I think  
2 that's a good point, and I had not focused on that.

3 MR. KATERBERG: So I want to briefly address the  
4 Department of Justice brief that they referred to. So this  
5 is -- I believe this is in the record, because I think it's  
6 Exhibit 1 to Plaintiffs' motion for summary judgment, ECF  
7 No. 46-1. First of all, just to clarify, it's not Treasury.  
8 It's the Department of Justice filing on behalf of the  
9 United States' amicus in the D.C. Circuit en banc proceeding  
10 in *PHH*. But the brief specifically distinguishes FHFA from  
11 the CFPB. It says that in contrast to the CFPB, the FHFA is  
12 a safety and soundness regulator for specified  
13 government-sponsored enterprises, namely Fannie Mae and  
14 Freddie Mac, for which the agency has acted as conservator  
15 since its conception. This is page 18 of Exhibit 1 to  
16 plaintiffs' motion for summary judgment. So it carves out  
17 FHFA. There's no way this can be favorably read as  
18 expressing a position.

19 THE COURT: Well, I heard what you read, but it  
20 didn't make any sense to me. Why would that have any  
21 implications for separation of powers?

22 MR. KATERBERG: Well, because Your Honor has read  
23 the panel opinion and you've seen that it is replete with  
24 references -- I think it's in the second sentence in the  
25 opinion -- to the exercise of executive law enforcement

1 power against citizens. That's what this is all about.

2 *PHH* Corporation had a \$109 million fine against  
3 it. That is a thread that's woven throughout *PHH*. So what  
4 this is saying is that --

5 THE COURT: Oh, I see. So they are distinguishing  
6 between exercising that kind of enforcement authority and  
7 not?

8 MR. KATERBERG: That's exactly right. So they're  
9 saying that FHFA is a different category than CFPB, and it  
10 would be a separate analysis.

11 Secondly, page 19 of the same brief, the DOJ  
12 endorses the panel's conclusion that the proper remedy for a  
13 constitutional violation is to sever the provision limiting  
14 the President's authority to remove the CFPB's director, not  
15 to declare the entire agency and its operations  
16 unconstitutional.

17 This gets back to one of the points we were  
18 discussing at the very beginning this morning, which is when  
19 you do have in the rare case an instance where removal  
20 restrictions are found to be unconstitutional, as the *PHH*  
21 panel found, the *PHH* panel agreed with us that the remedy  
22 wouldn't be to go back and declare everything  
23 unconstitutional; as I put it, burn down the house. So DOJ  
24 in this amicus brief has registered that they agree with  
25 that as well, and that's another reason why Counts One and

1 Two in this case should be dismissed.

2 THE COURT: All right. Thank you, Mr. Katerberg.

3 Mr. Knudson. So since you have lots of sticky  
4 notes and since it's getting late, I'll just let you go and  
5 I'll stop you if I have any questions.

6 MR. KNUDSON: All right. First, let me respond to  
7 what Mr. Katerberg just said about what the government was  
8 saying with respect to the constitutionality of the CFPB and  
9 also what Treasury was saying about that, as well.

10 The advisory was filed in *Collins v. FHFA*. So it  
11 took the position, with respect to this agency, that the  
12 structure with the for-cause removal power was  
13 unconstitutional.

14 THE COURT: Is that in the record?

15 MR. KNUDSON: It is in the record. I have a copy  
16 of this, Your Honor.

17 THE COURT: Or you can just tell me where it is in  
18 the record. Does it have the ECF --

19 MR. KNUDSON: It's Document 46 in case 16-3113.

20 THE COURT: Okay. We can find it then.

21 MR. KNUDSON: Then with respect to why the issues  
22 here are more critical in terms of the constitutional  
23 violations as between the CFPB and the FHFA: One, both  
24 agencies are exempt or have exemption from executive  
25 oversight by the for-cause removal provision. Both agencies

1 are self-funding, so they are not subject to legislative  
2 oversight.

3 What makes this agency different is 4712(f), the  
4 insulation of that agency from judicial review. When we  
5 were talking about --

6 THE COURT: Forgive me if I'm wrong, but (f) just  
7 applies to its conservator function, right?

8 MR. KNUDSON: That's right, but that's what we  
9 have here.

10 THE COURT: Of course. It says a lot of other  
11 things other than to act as conservator for Freddie Mac and  
12 Fannie Mae, I assume, right?

13 MR. KNUDSON: Yes.

14 THE COURT: Okay.

15 MR. KNUDSON: So with respect to the argument that  
16 the agency was making regarding the fact there is no harm if  
17 only the agency can bring this constitutional challenge to  
18 its structure and, therefore, it's a derivative claim and  
19 barred for private enforcement action under 4712(f), nobody  
20 can bring that claim because, as you pointed out, there is  
21 an Article III problem here. And the *U.S. v. ICC* Supreme  
22 Court decision essentially says you can't expect the agency  
23 to sue itself for something that it has done improperly.

24 THE COURT: Is it conceivable that an agency, as  
25 conservator, could sue itself as agency?

1 MR. KNUDSON: No.

2 THE COURT: You don't think so?

3 MR. KNUDSON: Posited hypothetically, yes, you  
4 could put on both sides --

5 THE COURT: I know practically it's unlikely.

6 MR. KNUDSON: -- you don't have a real lawsuit  
7 then. So it would be an improper use of judicial power to  
8 resolve a case where there is no adversity. That's  
9 basically where the problem would be.

10 Then with respect to the question of whether or  
11 not there's been an adjudication on the merits yet of these  
12 constitutional claims, I would submit that your law clerk  
13 has analyzed it correctly, that this is in fact a different  
14 kind of claim.

15 The claims that have been adjudicated in *Perry* or  
16 *Saxton* were decisions that were decided on jurisdictional  
17 grounds, so lack of capacity to sue is not a determination  
18 on the merits. In fact, we cite to the restatement first of  
19 judgments as to how far that principle has been. Lack of  
20 capacity is not a determination on the merits. So we --

21 THE COURT: This isn't the issue we disagreed on,  
22 but that's okay. I'm sympathetic to your argument insofar  
23 as a dismissal is based upon the succession clause because  
24 that feels like lack of capacity. If you brought one of  
25 these lawsuits and I dismissed it because of the succession

1 clause, I would basically say the claim isn't yours, it's  
2 somebody else's. That's like saying you don't have the  
3 capacity to bring this claim. But if the dismissal is based  
4 on the anti-injunction provision, that's not capacity.  
5 That's saying you lose. You're not entitled to the remedy  
6 you are seeking. That feels to me more like it's on the  
7 merits.

8 MR. KNUDSON: Well, I would suggest then -- the  
9 *Saxton* court dismissed the case bringing claims against the  
10 agency under 4617(f).

11 THE COURT: That's the anti-injunction provision.

12 MR. KNUDSON: Yes, but that's a jurisdictional  
13 determination. The Court doesn't have the authority to rule  
14 on the merits of your claim. Congress has taken away that  
15 power, unless you can prove up a HERA violation.

16 THE COURT: Well, I have to look at it again, but  
17 I thought it was not that you have no authority to  
18 adjudicate violations, but a particular remedy you can't --  
19 there's no sense in me talking about it, I can't remember  
20 what --

21 MR. KNUDSON: We've both been at it a long time  
22 this morning.

23 So with respect to -- you were concerned about,  
24 well, courts look for ways to prevent the constitutional  
25 violation from going without a remedy.



1 THE COURT: Correct.

2 MR. KNUDSON: HERA is modeled after the FIRREA  
3 statute. The Ninth Circuit and the federal circuit have  
4 addressed this concern because they had the same  
5 anti-injunction provision in them and said that if there is  
6 a manifest conflict of interest, even if it's a derivative  
7 claim, the shareholder can bring that claim. So we would  
8 urge the Court to follow form because the logic of that  
9 decision is consistent with the principle that if there is a  
10 constitutional violation, there should be a forum in which  
11 that issue can be addressed in the wrong remedy then, we  
12 believe, under state law or under federal principles of what  
13 would govern here. The *Kamen* case we say that federal law  
14 should determine whether or not these claims can be brought  
15 as direct claims, and as a constitutional issue we should be  
16 able to bring these claims.

17 THE COURT: Putting aside the -- let's just forget  
18 that you're bringing a constitutional issue and forget any  
19 kind of conflict or of interest or constitutional exception.  
20 As you heard me say, these kind of look to me like  
21 derivative claims. The FHFA didn't do anything to  
22 shareholders directly. They did something to Fannie Mae,  
23 and as a result of what they did to Fannie Mae, your  
24 clients' shares are worth less. But that's an indirect  
25 injury. That's not a direct injury.

1           The remedies you're seeking -- I haven't gone  
2 through them and checked them all against this, but  
3 overwhelmingly my memory is it's asking for money to be  
4 restored to the company, to declare a contract that the  
5 company is a party to to be invalid. That's all relief to  
6 the company. Your clients might indirectly benefit from  
7 that, but no one is cutting a check to them. I'm not  
8 ordering anybody to pay any money to them. This looks like  
9 a derivative. Why isn't this a derivative claim?

10           MR. KNUDSON: We cite to some of the Delaware  
11 precedent that suggests when you've got a reallocation of  
12 economic interests among shareholders or between  
13 shareholders that that's a direct claim.

14           THE COURT: How is the reallocation of the -- any  
15 time a company, like, issues new stock, there is necessarily  
16 going to be a reallocation, and yet I don't think -- I think  
17 those are derivative claims if somebody sues -- maybe I'm  
18 wrong about that.

19           Are you claiming that prior to the Third Amendment  
20 your clients had a right to dividends, a legally enforceable  
21 right to dividends?

22           MR. KNUDSON: Let's go before conservatorship  
23 then, because once conservatorship steps in, then payment of  
24 dividends is --

25           THE COURT: But the Third Amendment didn't change

1 your -- I mean, the Third Amendment, if that's the focus of  
2 your challenge -- as Mr. Katerberg correctly points out to  
3 me, if the Third Amendment is struck down, you don't go back  
4 to preconservatorship. You go back to Amendment II, the  
5 Amendment II world. In the Amendment II world you didn't  
6 have any right to dividends.

7 MR. KNUDSON: What has happened here is sort of  
8 reallocation of rights relative to shareholders. So, all of  
9 a sudden, what money is being paid out is going to Treasury  
10 as a shareholder, and it's not available to be paid to the  
11 individual, private shareholders. So the money is going to  
12 the wrong place as a result of the Net Worth Sweep Rule.

13 THE COURT: But did the individual shareholders  
14 have any legal right to that money as dividends?

15 MR. KNUDSON: Well, if we go preconservatorship,  
16 profits of the companies then get paid to the shareholders.

17 THE COURT: Do they have a right to the dividends  
18 or is it within this -- preconservatorship was it within the  
19 discretion of Fannie Mae to declare a dividend and how much  
20 the dividend would be?

21 MR. KNUDSON: There's a limit on what the board  
22 could decide to do. There is two points. One is they have  
23 a fiduciary duty to their shareholders, and if they're  
24 sitting on the money and not paying it out in dividends,  
25 they have to have a sound business reason for doing so.

1           Two, there are tax implications for not paying out  
2 money in dividends, so there is an incentive to do so.  
3 There is a justifiable expectation that you get paid some  
4 dividends as virtue of being a shareholder in what was at  
5 one time a profitable business.

6           THE COURT: If we go ahead now to the day before  
7 the Third Amendment was signed, did your clients have any  
8 rights to dividends then?

9           MR. KNUDSON: If there were profits coming in  
10 subject to the conservator allowing them to be paid, yes,  
11 they had a right to dividends.

12           THE COURT: Well, I mean, they were borrowing  
13 money to -- they weren't even able to fulfill their  
14 obligations to Treasury. I mean, there was no excess --

15           MR. KNUDSON: Prior to the Third Amendment, yes,  
16 the companies were losing money, but that situation changed  
17 significantly soon afterwards, and they've been making  
18 substantial profits in the recent years.

19           THE COURT: Okay. I'm sorry, I cut you off.

20           MR. KNUDSON: So my point there being is that  
21 under Delaware law this would be deemed to be a direct  
22 claim. Because we're asserting a situation where there is  
23 no other remedy available to us, you should adopt the  
24 manifest conflict-of-interest exception that would allow  
25 these claims to be asserted against the agency along the

1 lines to consider them against the FDIC.

2 At the end of the day, there is certain residual  
3 value of these companies the shareholders have that has been  
4 impacted by the agency's actions and so there, again, is a  
5 direct claim.

6 THE COURT: Well, that's not -- I mean, if  
7 somebody goes and burns down 3M's headquarters and all its  
8 contents, that has a huge value on the shareholders' stock,  
9 but it wouldn't be a direct claim. It would be 3M's claim.

10 MR. KNUDSON: Well, in that instance that's true.

11 THE COURT: So in terms of if the Third Amendment  
12 has some impact on the residual value of the companies, that  
13 strikes me as a derivative claim, not a direct claim.

14 MR. KNUDSON: But it's as between shareholders.  
15 Relative rights between shareholders becomes a direct claim  
16 by -- the shareholders have been harmed by this particular  
17 action. So if the company decides that they are going to  
18 give a preference to one set of shareholders over another,  
19 that's a direct claim and direct injury to the harmed  
20 shareholders.

21 THE COURT: Okay. Anything more you wanted to  
22 say?

23 MR. KNUDSON: I think that should sum it up, sir.

24 THE COURT: All right. Thank you, Mr. Knudson. I  
25 know it has been a long morning. Oh, I'm sorry, let me make

1 it one minute longer. Talk to me about your claims against  
2 Treasury. You heard what I said with Mr. Merritt.

3 MR. KNUDSON: Oh, yes. Sorry, Your Honor.

4 THE COURT: You don't have any claims against  
5 Treasury. At least your Complaint doesn't say Treasury did  
6 anything unlawful. There's five counts in your Complaint  
7 and none of them allege that Treasury violated any law.

8 MR. KNUDSON: Well, a very simple answer to that  
9 is that we believe we would have to make Treasury a party to  
10 this litigation in order to have relief that could be  
11 effective against it. It's a point you noted earlier. We  
12 think at least it's a permissive party defendant, if not a  
13 necessary party to this lawsuit.

14 We do cite the case out of South Dakota where some  
15 tribal members brought actions against a vendor and the  
16 issue was, well, doesn't the tribe have to be a party to  
17 this lawsuit, and the answer was yes, and sovereign immunity  
18 prevented them from being made a party to that lawsuit.  
19 Without the tribe being a part of the lawsuit, the claims  
20 were dismissed.

21 So we think we're in a situation somewhat similar  
22 where we need to have Treasury before this Court so it can  
23 be bound by the equitable relief we're seeking.

24 THE COURT: I think the problem is you need a  
25 claim against Treasury. It might be that if you amended

1 your Complaint to bring a declaratory judgment action or  
2 something, but as the Complaint is drafted, there just isn't  
3 a viable claim against Treasury is the problem.

4 I completely sympathize with why you want them in  
5 here. You want to make sure that if you do win and the  
6 Third Amendment is declared unconstitutional or invalid that  
7 it binds Treasury. You don't want to have to then defend a  
8 lawsuit by Treasury to re-argue the issues. There just  
9 isn't a claim against Treasury. So it may be that what you  
10 would have to do is amend your Complaint to bring a dec  
11 action or something against Treasury; I don't know.

12 MR. KNUDSON: We certainly could do that.

13 THE COURT: It's a tricky situation. It doesn't  
14 come up a lot.

15 MR. KNUDSON: Very tricky. We could amend that if  
16 that's the remedy you seek.

17 THE COURT: Thank you, Mr. Knudson.

18 Let's see. Mr. Katerberg, you had a --

19 MR. KATERBERG: Your Honor, may I be heard? I  
20 know we've been here for a long time. I just want to clear  
21 up something, a very discrete thing, because I think the  
22 question has been muddied a little bit about whether the  
23 shareholders could get dividends during conservatorship. It  
24 shouldn't be muddy because there is a very clear answer and  
25 it's in the record.

1           The original preferred stock purchase agreements,  
2           and I'm referring to Document 37-1 in the record, has a  
3           covenant. This was in September 7, 2008, four years before  
4           the Third Amendment. It says, Seller -- and the "Seller" is  
5           Fannie and Freddie -- shall not, and shall not permit any of  
6           its subsidiaries, to in each case without the prior written  
7           consent of Treasury declare or pay any dividend with respect  
8           to any of Seller's equity interest, which would cover all  
9           the common stock, preferred stock, everything. So that we  
10          should be very clear on that, there's no dividends for the  
11          private shareholders during conservatorship. That's with or  
12          without the Third Amendment.

13                   Thank you.

14                   THE COURT: Okay. Thank you.

15                   Let's see. Mr. Merritt, did you have something  
16          more you wanted to say?

17                   MR. MERRITT: Very briefly, Your Honor. Again, I  
18          don't want to belabor these points; we've been here awhile  
19          and you understand the issues.

20                   With respect to something opposing counsel just  
21          said about that they believe Treasury is a necessary -- or  
22          would be properly joined, I would just submit that that's  
23          not how they've pled this case. As you pointed out, they  
24          submitted substantive claims against it and without factual  
25          allegations to back that up, they should be dismissed. If



1 they were to amend their Complaint to bring actions against  
2 Treasury, they would have to back those claims up with some  
3 sort of allegations that Treasury wronged them in some way  
4 out of this transaction. So I just wanted to make that  
5 clear.

6 Just briefly to address the point about the  
7 conflict of interest, because I know this isn't in our  
8 briefs, but we would urge Your Honor to follow the logic of  
9 the *Perry Capital* -- the D.C. Circuit in *Perry Capital* on  
10 that point which basically finds that the shareholder  
11 succession provision does not speak of any exceptions by its  
12 plain text.

13 The cases plaintiffs cite, *Delta Savings Bank* and  
14 *First Hartford*, are based on logic that wouldn't be  
15 applicable here when dealing with a bar. They analogized it  
16 to shareholder derivative actions, but if we were to  
17 recognize an exception to a statutory provision that bars  
18 such derivative actions every time there was a conflict of  
19 interest, the exception would potentially swallow the rule  
20 because presumably derivative actions are brought because  
21 there is such a conflict of interest. That's all I have.

22 THE COURT: Mr. Knudson, you want one more bite at  
23 the apple? Sure, come on up.

24 MR. KNUDSON: I want to clarify toward the end of  
25 my remarks if you think there is a defect in our Complaint

1 vis-a-vis Treasury, we would seek leave to amend and cure  
2 that defect.

3 THE COURT: All right. Thank you.

4 Thank you all. As I said, I know this has been a  
5 very long day. It's also a very, very difficult case. I  
6 appreciate your help with it.

7 I'll take the motions under advisement. We'll get  
8 an order out when we can. I don't think it will be anytime  
9 soon. There is a ton of stuff for us to research and think  
10 about here. I imagine it will be a while before I can get  
11 an order out, but we'll do the best we can.

12 Happy holidays to all of you, and safe travels for  
13 those of you who are traveling.

14 THE LAW CLERK: All rise.

15 (Court adjourned at 1:15 p.m.)

16 \* \* \*

17 I, Debra Beauvais, certify that the foregoing is a  
18 correct transcript from the record of proceedings in the  
19 above-entitled matter.

20 Certified by: s/Debra Beauvais  
21 Debra Beauvais, RPR-CRR

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