Receipt number 9998-4837220

IN THE UNITED STATES COURT OF FEDERAL CLAIMS

HIGHFIELDS CAPITAL I LP, HIGHFIELDS CAPITAL II LP, and HIGHFIELDS CAPITAL III L.P.,

Plaintiffs,

v.

THE UNITED STATES OF AMERICA,

Defendant.

Case No. 18-1150 C

COMPLAINT

Plaintiffs Highfields Capital I LP, Highfields Capital II LP, and Highfields Capital III L.P. (collectively, "Plaintiffs") hereby bring this action against the United States of America seeking compensation for the taking or, alternatively, the illegal exaction of Plaintiffs' property and damages for breach of fiduciary duty and implied-in-fact contracts with the Government. By and through their undersigned attorneys, Plaintiffs allege on personal knowledge as to themselves and their own conduct and on information and belief as to all other matters as follows:

NATURE AND SUMMARY OF THE ACTION

1. This action seeks compensation for the United States' taking of all profits of the Federal National Mortgage Association ("Fannie Mae") and the Federal Home Loan Mortgage Corporation ("Freddie Mac" and, with Fannie Mae, the "Enterprises") forever.

2. Plaintiffs hold stock in the Enterprises. For decades, the Enterprises had generated consistent profits as privately owned entities.

3. In 2008, pursuant to the Housing and Economic Recovery Act ("HERA"), Pub. L. No. 110-289, 122 Stat. 2654, an agency of the Government, the Federal Housing Finance

Agency ("FHFA"), appointed itself as conservator of the Enterprises. Having done so, FHFA entered into agreements with the U.S. Department of the Treasury ("Treasury") whereby the Enterprises would issue stock to Treasury. Under the terms of these agreements and the resulting stock, Treasury invested in the Enterprises. In exchange, the Enterprises agreed to pay Treasury a certain dividend every quarter.

4. By 2012, despite actions by FHFA that diminished the financial health of the Enterprises on paper, the Enterprises were generating robust profits and expected to continue doing so for years to come.

5. But the Government saw fit to appropriate those profits for itself. On August 17, 2012, Treasury and FHFA amended their prior agreements. The central feature of this amendment is known as the "Net Worth Sweep." The Net Worth Sweep replaced the Enterprises' previous dividend obligations with an obligation to pay the Enterprises' entire net worth (minus a small capital buffer) to Treasury, forever.

6. As expected, the Net Worth Sweep has been immensely profitable for the United States. By the end of 2017, it had sucked more than $129 billion (above and beyond what was required pre-Sweep) out of the Enterprises and into the Government's coffers. But for the Net Worth Sweep, that money would have enabled proper capitalization of the Enterprises and generated significant value for the Enterprises' stockholders.

7. The Net Worth Sweep is a taking of the property rights held by the Enterprises' stockholders as a result of their stock. Alternatively, it constitutes an illegal exaction of those property rights. In addition, the Net Worth Sweep breaches the fiduciary duties owed by the United States (through FHFA and Treasury) to the Enterprises' private stockholders and breaches the implied-in-fact contract between FHFA and the Enterprises.

JURISDICTION AND VENUE

8. This Court has jurisdiction over this action, and venue is proper in this Court, pursuant to 28 U.S.C. § 1491(a)(1).

THE PARTIES

9. Plaintiff Highfields Capital I LP is a limited partnership organized under the laws of Delaware.

10. Plaintiff Highfields Capital II LP is a limited partnership organized under the laws of Delaware.

11. Plaintiff Highfields Capital III L.P. is an exempted limited partnership organized under the laws of the Cayman Islands.

12. Plaintiffs collectively hold shares of junior preferred stock issued by Fannie Mae, shares of junior preferred stock issued by Freddie Mac, shares of common stock issued by Fannie Mae, and shares of common stock issued by Freddie Mac

13. Defendant United States of America includes Treasury, FHFA, and agents acting at their direction.

CONSTITUTIONAL AND STATUTORY PROVISIONS

14. Plaintiffs' claims are founded on the Fifth Amendment to the United States Constitution, which provides, in relevant part, that no person shall "be deprived of life, liberty, or property, without due process of law; nor shall private property be taken for public use, without just compensation," and on HERA, 12 U.S.C. §§ 1455(*l*), 1719(g), 4617.

FACTUAL ALLEGATIONS

Fannie Mae and Freddie Mac

15. Fannie Mae is a corporation established by Congress in 1938 with its principal executive offices located at 3900 Wisconsin Avenue, N.W., Washington, D.C. 20016. Freddie

Mac is a corporation established by Congress in 1970 with its principal executive offices located at 8200 Jones Branch Drive, McLean, VA 22102.

16. The businesses of both Fannie Mae and Freddie Mac include purchasing and guaranteeing mortgages originated by private banks and bundling the mortgages into mortgage-related securities that can be sold to investors. These activities increase liquidity in the mortgage market, which enables private banks to make additional loans to individuals for home purchases.

17. Prior to September 6, 2008, Fannie Mae and Freddie Mac each issued preferred stock (now known as junior preferred stock) and common stock.

18. Each Enterprise issued numerous series of junior preferred stock. Under their respective certificates of designation, each series of junior preferred stock has a contractually specified dividend rate and liquidation value. Each Enterprise's series of junior preferred stock ranks pari passu with all other outstanding series of the Enterprise's junior preferred stock as to payment of dividends and distribution of assets upon dissolution or liquidation.

19. Each Enterprise's common stock is entitled to the residual economic value of the Enterprise as well as to any dividend declared and paid by the Enterprise.

20. Prior to September 6, 2008, both Enterprises actively marketed their stock to private investors. For example, in May 2008, Fannie Mae produced a "Capital Raise Roadshow" presentation touting Fannie Mae's "[l]ong-term growth and profitability prospects" and "[c]ompelling investment opportunities in [the] current environment."

21. Likewise, the Enterprises' former regulator, the Office of Federal Housing Enterprise Oversight ("<u>OFHEO</u>"), sought to assure private investors. For example, that Office issued a press release on March 19, 2008, quoting its Director as stating that both Enterprises "have prudent cushions above the OFHEO-directed capital requirements" and that "[w]e believe

they can play an even more positive role in providing the stability and liquidity the markets need right now."

22. Prior to September 6, 2008, the Enterprises had operated successfully as private corporations for decades. Before 2007, Fannie Mae had not reported a full-year loss since 1985, and Freddie Mac had not reported a full-year loss since 1989. In addition, during these times, both Enterprises regularly declared and paid dividends on their junior preferred stock and common stock.

2008: HERA Creates FHFA, And FHFA Puts The Enterprises Into Conservatorship

23. In the summer of 2008, the Enterprises remained financially sound. On July 10 of that year, then-Secretary of the Treasury Henry Paulson testified to Congress that the Enterprises' "regulator has made clear that [the Enterprises] are adequately capitalized." In August 2008, the Enterprises issued their financial statements, which reflected that, as of the end of June 2008, Fannie Mae's assets exceeded its liabilities by over $41 billion and Freddie Mac's assets exceeded its liabilities by approximately $13 billion.

24. In July 2008, Congress passed HERA, and President George W. Bush signed it into law.

25. HERA created a new federal agency, FHFA. FHFA replaced OFHEO as the Enterprises' federal regulator.

26. Unlike OFHEO, FHFA is an "independent" agency. 12 U.S.C. § 4511(a). It is headed by a Director whom HERA made removable only "for cause by the President." *Id.* § 4512(b)(2). It is insulated from oversight or supervision from other agencies. *Id.* § 4617(a)(7). And, unlike virtually all other "independent" agencies established by Congress, FHFA is subject to the control of only a single individual.

27. HERA authorized the Director of FHFA in certain circumstances to appoint FHFA as the conservator or receiver of the Enterprises. Those circumstances included that the Enterprises had obligations exceeding their assets, that the Enterprises were in an "unsafe or unsound condition," and that the Enterprises were undercapitalized. 12 U.S.C. § 4617(a)(3).

28. HERA set forth duties for FHFA as conservator that differed from its duties as receiver. For example, as conservator, FHFA may "take such action as may be (i) necessary to put the [Enterprises] in a sound and solvent condition; and (ii) appropriate to carry on the business of the [Enterprises] and preserve and conserve the assets and property of the [Enterprises]." 12 U.S.C. § 4617(b)(2)(D). By contrast, as receiver, FHFA "shall place the [Enterprises] in liquidation." *Id.* § 4617(b)(2)(E). As FHFA's notice promulgating regulations implementing the statute explains, "[t]he ultimate responsibility of FHFA as receiver is to resolve and liquidate the" Enterprises, whereas "[a] conservator's goal is to continue the operations of a[n Enterprise], rehabilitate it and return it to a safe, sound and solvent condition." Conservatorship and Receivership, 76 Fed. Reg. 35,724, 35,730 (June 20, 2011). In other words, "activities of a conservator may not be aligned with the ultimate duty of a receiver." *Id.*

29. HERA also provided that FHFA, in all of its activities, "shall not be subject to the direction or supervision of any other agency of the United States . . . in the exercise of [its] rights, powers, and privileges." 12 U.S.C. § 4617(a)(7).

30. On August 22, 2008, the Enterprises' new regulator, FHFA, confirmed in letters to each Enterprise that each was adequately capitalized, including under additional capital requirements imposed by FHFA.

31. Even so, on September 6, 2008, FHFA's Director appointed FHFA as conservator of both Enterprises.

32. Treasury was the driving force behind the appointment of FHFA as conservator. Then-Secretary Paulson has written that "FHFA had been balky all along. That was a big problem because only FHFA had the statutory power to put Fannie and Freddie into conservatorship. We had to convince its people that this was the right thing to do, while making sure to let them feel they were still in charge." Henry M. Paulson, Jr., *On the Brink: Inside the Race to Stop the Collapse of the Global Financial System* 6 (2010).

2008: Treasury Buys Senior Preferred Stock In The Enterprises

33. In addition to authorizing certain acts by FHFA, HERA authorized certain acts by Treasury. As relevant here, HERA authorized Treasury to "purchase any obligations and other securities" of the Enterprises and to "determine" the "terms and conditions" and "amounts" of those purchases. 12 U.S.C. § 1455(*l*)(1)(A) (Freddie Mac); *id.* § 1719(g)(1)(A) (Fannie Mae). Before exercising this authority, the Secretary of the Treasury was required to consider factors including "[t]he need for preferences or priorities regarding payments to the Government," the Enterprises' "plan[s] for the orderly resumption of private market funding," and "[t]he need to maintain the [Enterprises'] status as . . . private shareholder-owned compan[ies]." *Id.* §§ 1455(*l*)(1)(C), 1719(g)(1)(C).

34. Treasury's authority to make such purchases expired on December 31, 2009. 12 U.S.C. §§ 1455(*l*)(4), 1719(g)(4). After that date, HERA authorized Treasury only "to hold, exercise any rights received in connection with, or sell, any obligations or securities purchased" before then. *Id.* §§ 1455(*l*)(2)(D), 1719(g)(2)(D).

35. On September 7, 2008—the day after FHFA was appointed conservator of the Enterprises—Treasury entered into a Senior Preferred Stock Purchase Agreement ("PSPA") with each Enterprise, signed by FHFA as the Enterprise's conservator. The two Enterprises' PSPAs are identical in all material respects.

36. Under each PSPA, Treasury agreed to provide each Enterprise with a commitment of up to $100 billion, to be drawn on as and when necessary for the Enterprises to maintain a positive net worth. In exchange, Treasury received one million newly issued shares of senior preferred stock. Treasury also received (i) an initial liquidation preference of $1,000 per share (equal to $1 billion), plus any outstanding amount drawn from the commitment; (ii) warrants to buy up to 79.9% of each Enterprise's common stock for $0.00001 per share; and (iii) the right to receive payment of a periodic commitment fee (the "Periodic Commitment Fee"), in an undetermined amount, to be paid by the Enterprises quarterly beginning in 2010. Treasury's new senior preferred stock was senior to all junior preferred stock, such that no dividends or liquidation distributions on any junior preferred stock could be paid until after Treasury had received its full dividend or liquidation distributions.

37. The senior preferred stock issued to Treasury under the PSPAs earned an annual dividend, payable quarterly, which Treasury could receive, at the Enterprises' election, either (i) as a cash dividend, payable at a rate equal to 10% of the outstanding liquidation preference per year; or (ii) by payment "in kind" in the form of an increase in the amount of Treasury's liquidation preference, equivalent to a rate equal to 12% of the outstanding liquidation preference per year. If the Enterprises elected to make a payment in kind, then the dividend rate for all dividends would increase to 12% per year, until the Enterprise paid all cumulative dividends in cash, at which point, the rate would return to 10%. The payment in kind option meant that the Enterprises were never required to pay a cash dividend. *See* N. Eric Weiss, *Fannie Mae's and Freddie Mac's Financial Problems* i (Cong. Research Serv. Report No. RL34661, Aug. 10, 2012) ("The [E]nterprises could . . . pay a 12% annual senior preferred stock dividend indefinitely.").

38. In addition, covenants in the PSPAs granted Treasury substantial ability to control the Enterprises and FHFA's conduct of the conservatorship, by restricting their ability to take certain actions without Treasury's prior written consent. This included restricting their ability to (i) declare dividends on any outstanding common or preferred stock other than the senior preferred stock; (ii) sell or issue equity interests; (iii) terminate the conservatorship; (iv) transfer assets; (v) incur indebtedness; (vi) enter into a merger, reorganization, or recapitalization, or make acquisitions; or (vii) enter into transactions with affiliates.

2008: FHFA Assures Investors That It Will Act As A True Conservator

39. After FHFA became conservator of the Enterprises and caused the Enterprises to issue senior preferred stock to Treasury, FHFA stated to investors that these actions were intended to restore the Enterprises to their pre-conservatorship condition. For example:

a. On September 7, 2008, FHFA issued a document titled "Questions and Answers on Conservatorship." The document stated that FHFA had been appointed conservator "to keep the [Enterprises] in a safe and solvent financial condition"; that "[u]pon the Director's determination that the Conservator's plan to restore the Company to a safe and solvent condition has been completed successfully, the Director will issue an order terminating the conservatorship"; that "[t]here are no plans to liquidate" the Enterprises; and that "[s]tockholders will continue to retain all rights in the stock's financial worth; as such worth is determined by the market."

b. On September 7, 2008, FHFA's Director issued a statement, which stated: "FHFA has placed Fannie Mae and Freddie Mac into conservatorship. That is a statutory process designed to stabilize a troubled institution with the objective of returning the entities to normal business operations.

FHFA will act as the conservator to operate the Enterprises until they are stabilized."

c. On September 23, 2008, in public testimony to the Senate Committee on Banking, Housing, and Urban Affairs, FHFA's Director stated that FHFA's conservatorship "is a statutory process designed to stabilize a troubled institution with the objective of maintaining normal business operations and restoring its safety and soundness."

d. On September 25, 2008, in public testimony to the House Committee on Financial Services, FHFA's Director stated that "[t]he shareholders are still in place; both the preferred and common shareholders have an economic interest in the companies."

e. An internal FHFA presentation dated October 20, 2008, acknowledged that the "[c]onservatorship statutes provide broad authority for a conservator to operate the institution until it is stabilized and then returned to the shareholders."

40. In subsequent years, FHFA repeated this message. For example:

a. On June 3, 2009, in public testimony to the House Subcommittee on Capital Markets, Insurance, and Government Sponsored Enterprises, FHFA's Director stated that, "[a]s the conservator, FHFA's most important goal is to preserve the assets of Fannie Mae and Freddie Mac. That is our statutory responsibility."

b. On February 2, 2010, in a letter to the leaders of relevant congressional committees, FHFA's Acting Director wrote that "[t]here are a variety of

options available for post-conservatorship outcomes, but the only one that FHFA may implement today under existing law is to reconstitute the two [Enterprises] under their current charters."

c. On September 15, 2010, in public testimony to the House Subcommittee on Capital Markets, Insurance, and Government-Sponsored Enterprises, FHFA's Acting Director stated that "[t]he statutory purpose of conservatorship is to preserve and conserve each [Enterprise's] assets and put them in a sound and solvent condition."

d. On November 10, 2011, in a public letter to the Senate, FHFA's Acting Director stated that, "[b]y law, the conservatorships are intended to rehabilitate the Enterprises as private firms."

2009: The First And Second Amendments

41. In 2009, FHFA and Treasury made two amendments to the PSPAs they had entered into on September 7, 2008.

42. On May 6, 2009, Treasury and FHFA agreed to increase Treasury's funding commitment for each Enterprise from $100 billion to $200 billion.

43. On December 24, 2009, Treasury and FHFA agreed to replace the $200 billion fixed cap with a formula to allow Treasury's total commitment to each Enterprise to exceed (but not fall below) $200 billion, depending on the Enterprise's financial condition until December 31, 2012.

2008–2012: The Government Artificially Reduces The Enterprises' Financial Performance And Contemplates Winding Them Down

44. After being appointed conservator, FHFA projected that the Enterprises would likely incur large losses in the coming years. These projections were based on unrealistic

assumptions regarding the Enterprises' financial prospects. FHFA relied on these unrealistic projections to direct the Enterprises to book substantial loss reserves (i.e., anticipated mortgage loan losses before they were actually incurred). FHFA further required the Enterprises to eliminate from their balance sheets the value of deferred tax assets that would be of use only if the Enterprises became profitable, based on the implausible assumption that the Enterprises would never again be profitable. The combined effect of these accounting assumptions was to decrease the Enterprises' reported net worth substantially.

45. This decrease in reported net worth, among other factors, required the Enterprises to draw funds from Treasury pursuant to the PSPAs. As the Enterprises drew additional funds from Treasury, Treasury's liquidation preference increased. This, in turn, increased the size of the quarterly dividend owed to Treasury.

46. By August 2012, the Enterprises had drawn over $187 billion from Treasury's funding commitment.

47. Meanwhile, despite FHFA's public recognition of its duty as conservator to restore the Enterprises, Treasury was contemplating steps to wind them down. An internal memorandum for the Secretary of the Treasury, dated December 20, 2010, stated that the Administration had a "commitment to ensure existing common equity holders will not have access to any positive earnings from the [Enterprises] in the future." On February 11, 2011, Treasury issued a press release announcing a "plan [to] wind down Fannie Mae and Freddie Mac."

48. Given the extent of Treasury's control over FHFA and the Enterprises, FHFA was constrained to go along. On January 4, 2012, Treasury sent FHFA's Acting Director a meeting agenda stating that "FHFA and Treasury share . . . a clear plan to wind down the [Enterprises]."

On February 21, 2012, FHFA issued a report to Congress stating that "the unanticipated length of the conservatorships poses additional risks for taxpayers and markets not contemplated by HERA. FHFA views those risks as best managed by contracting the Enterprises' footprint in the marketplace."

2012: The Government Knows The Enterprises Are Financially Healthy And Expects Them To Remain So

49. Notwithstanding the unjustified loss reserves and write-downs of deferred tax assets, the Enterprises were in sound financial health by mid-2012.

50. In early August 2012, the Enterprises reported a combined net income of more than $11 billion in the first two quarters of 2012.

51. In addition to increased earnings, the Enterprises' balance sheets also benefitted from reversal of the excessive loan loss reserves that they had been forced to take early in the conservatorships, because the Enterprises' loans suffered far fewer losses than FHFA had caused the Enterprises to estimate. On August 8, 2012, Fannie Mae reported second quarter income of $5.4 billion, up from a $2.9 billion loss in the second quarter of 2011—largely attributable to a decrease in loan loss reserves. Freddie Mac reported in filings with the SEC that its "provision for credit losses declined to $0.2 billion in the second quarter of 2012, compared to $2.5 billion in the second quarter of 2011, and was $2.0 billion in the first half of 2012 compared to $4.5 billion in the first half of 2011."

52. This increased profitability allowed the Enterprises to begin paying Treasury's dividends from available cash. In the second quarter of 2012, the Enterprises paid Treasury's $4.7 billion quarterly dividend using their combined quarterly profit of $8.3 billion.

53. FHFA and Treasury reasonably should have expected, and did in fact expect, this trend of positive financial results to continue.

54. As early as November 8, 2011, the accounting and consulting firm Grant Thornton LLP prepared a report for Treasury acknowledging that "[f]rom December 31, 2012 through September 30, 2018, Freddie Mac is not projected to draw on the liquidity commitment to make its dividend payments because of increased earnings driven by significantly reduced credit losses in 2012 and 2014."

55. In June 2012, FHFA informed Treasury that "the [Enterprises] will be generating large revenues over the coming years, thereby enabling them to pay the 10% annual dividend well into the future even with the caps" on Treasury's commitment.

56. According to July 13, 2012, documents circulated among FHFA officials regarding a Fannie Mae Executive Management Meeting held on July 9, 2012, the following eight years were likely to be "the golden years of [Enterprise] earnings." In the same documents, Fannie Mae official Ann Gehrig noted that "[c]umulative 2012-2016 income is now forecast at $56.6 billion, $12.3 billion higher than the last projection." The same documents included a report from Fannie Mae Treasurer Dave Benson acknowledging that "[c]urrent projections show that cumulative [Enterprises] dividends paid will surpass cumulative [Enterprises] Treasury draws by 2020." A forecast presented to the Fannie Mae Board of Directors on July 19, 2012, projected positive annual Total Comprehensive Income for both Enterprises from 2012 through 2022.

57. In addition, as FHFA and Treasury were aware, the Enterprises had certain deferred tax credits that would further enhance their profitability in the near term. In a May 29, 2012, meeting between Treasury and various financial advisors, there was a discussion of "[r]eturning the deferred tax asset to the [Enterprises'] balance sheets." A series of August 14, 2012, emails between FHFA officials acknowledged that "re-recording certain deferred tax

assets" had been discussed "on the view that" the Enterprises "were going to be profitable going forward."

2012: The Third Amendment And The Net Worth Sweep

58. On August 17, 2012, FHFA and Treasury entered into a third written amendment to the PSPAs (the "Third Amendment").

59. The central feature of the Third Amendment is known as the Net Worth Sweep. Under the Net Worth Sweep, the dividend on the Enterprises' senior preferred stock (owned by Treasury) was changed from 10% of Treasury's liquidation preference (or a 12% payment "in kind") to 100% of each Entity's net worth (minus a small capital reserve that would decline to zero by 2018). The Net Worth Sweep has no termination date.

60. The Net Worth Sweep ensures that the Enterprises will never pay off their debt to Treasury. That is because, under its terms, quarterly dividend payments do not offset prior Treasury draws. Thus, no matter how profitable the Enterprises become, or how much money they pay to Treasury as dividends, all of the $189.5 billion owed to Treasury as of August 2012 on the senior preferred stock will remain outstanding.

61. Moreover, Treasury's liquidation preference includes the amount of all unpaid dividends. The Net Worth Sweep therefore guarantees that if and when the Enterprises are liquidated, Treasury will receive any remaining net worth they have.

62. Neither the Enterprises nor their stockholders received meaningful consideration for the Net Worth Sweep. Because the Enterprises always had the option to pay dividends "in kind" at a 12% interest rate, the Net Worth Sweep did not provide the Enterprises with any additional flexibility or benefit. Even setting aside this "in kind" option, under the Net Worth Sweep, (i) if the Enterprises' profits exceed the 10% dividend owed under the original PSPAs, they always pay more to Treasury than 10%, but can never build capital to repay Treasury's

liquidation preference, and (ii) if the Enterprises' profits do not exceed the 10% dividend owed under the original PSPAs, they still pay their entire net worth to Treasury and still cannot build capital or repay Treasury's liquidation preference. By contrast, under the original PSPAs, (i) if the Enterprises' profits exceed the 10% dividend, they pay only 10% to Treasury, and can retain the balance to build capital to repay Treasury's liquidation preference, and (ii) if the Enterprises' profits do not exceed 10%, HERA does not permit the Enterprises to pay Treasury more than their net worth in cash to Treasury.

63. The stated goal of the Net Worth Sweep was to transfer the Enterprises' profits from their stockholders to Treasury and to ensure that the Enterprises never exit conservatorship:

a. On August 17, 2012, Treasury stated in a press release that the Net Worth Sweep "make[s] sure that every dollar of earnings each firm generates is used to benefit taxpayers" and "[a]cting upon the commitment made in the Administration's 2011 White Paper that the [Enterprises] will be wound down and will not be allowed to retain profits, rebuild capital return to the market in their prior form."

b. On August 17, 2012, the Acting Director of FHFA issued a statement recognizing that one of the Net Worth Sweep's goals was "gradually contracting [the Enterprises'] operations."

c. On April 18, 2013, in a statement to the Senate Committee on Banking, Housing and Urban Affairs, FHFA's Acting Director stated that "[t]he Administration has made clear that its preferred course of action is to wind down the Enterprises" and that "recent changes to the Preferred Stock Purchase Agreements (PSPAs), replacing the 10 percent dividend with a

net worth sweep, reinforce the notion that the Enterprises will not be building capital as a potential step to regaining their former corporate status."

d. On June 13, 2013, FHFA issued a report to Congress which explained that the Net Worth Sweep "ensures all the Enterprises' earnings are used to benefit taxpayers" and "reinforces the fact that the Enterprises will not be building capital."

e. On March 12, 2014, the Secretary of the Treasury publicly stated to Congress that "we have had a very clear policy on Fannie and Freddie, which is that we are winding them down."

f. In a May 2014 interview, FHFA's Director stated that "I don't lay awake at night worrying about what's fair to the shareholders" and that "I just don't have time to think about what might happen in the future with the shareholders."

64. Internal communications reinforce the fact that the aim of the Net Worth Sweep was to transfer the Enterprises' profits from their stockholders to Treasury and to ensure that the Enterprises never exit conservatorship:

a. On July 20, 2012, a draft internal Treasury document entitled "PSPA Modification: Key Points To Make" stated that the Net Worth Sweep would put taxpayers in a "better position." "Under the current arrangement Treasury's upside was capped at the 10% dividend, now the taxpayer will be the beneficiary of any future earnings produced by the [Enterprises]."

b. On August 13, 2012, a White House official wrote in an email that "[w]e are making sure that each of these entities pays the taxpayer back *every dollar of profit they make*, not just a 10% dividend" and that "[t]he taxpayer will . . . ultimately collect more money with the changes."

c. On August 14, 2012, a FHFA official wrote in an email that the Net Worth Sweep was "designed to demonstrate wind down," notwithstanding that the Enterprises' boards believed that the Enterprises "were going to be profitable going forward."

d. On August 15, 2012, a Treasury official wrote in an email to White House officials that, "[b]y taking all of their profits going forward, we are making clear that the [Enterprises] will *not* ever be allowed to return to profitable entities at the center of our housing finance system," and he confirmed that "taxpayers will receive every dollar of profit the [Enterprises] make."

e. On August 16, 2012, a draft document captioned "PSPA Amendment Q&As" was produced within Treasury. It stated, among other things:

- "We are announcing steps to wind-down the enterprises more quickly and responsibly and make sure they are not allowed to recapitalize and return to the market in their prior form";
- "That full income sweep will mean that Fannie Mae and Freddie Mac *will . . . not be allowed* to retain their profits, rebuild capital, and return to the market in their prior form";

- "100 percent of the funds in the reserve account, and 100 percent of the profit of these entities generate, will be returned to Treasury and ultimately to taxpayers";
- "By taking all of their profits going forward, we are making clear that the [Enterprises] will *not* ever be allowed to return to profitable entities at the center of our housing finance system";
- "Taxpayers will receive every dollar of profit the [Enterprises] make";
- "Over time, [the Net Worth Sweep] will result in all comprehensive income generated by the [Enterprises] being paid to the government and thus the taxpayer";
- "We made these changes to make sure that these entities pay the taxpayer every dollar of profit that they make"; and
- "Given the [Enterprises'] improving operating performance and our goal to wind down the enterprises, we believe this change is appropriate today."

f. On August 17, 2012, a White House senior advisor wrote in an email that the Net Worth Sweep would "ensur[e] that [the Enterprises] can't recapitalize." Later that day, in an email to a senior Treasury official, the same White House advisor stated that "we've closed off [the] possibility that [the Enterprises] ever[] go (pretend) private again and sped up the clock on the wind-down of their portfolio." Late that night, the same advisor wrote that the "[d]ividend is variable, set at whatever profit for

quarter is, eliminating ability to pay down principal (so they can[']t repay their debt and escape as it were)."

g. On August 17, 2012, a FHFA official wrote to others at FHFA, including its Acting Director, that the Net Worth Sweep "does not allow the Enterprises to build up retained surplus, which may give the impression that they are healthy institutions."

h. On August 18, 2012, a White House senior advisor sent an email to Treasury officials stating: "Team T[reasur]y, [y]ou guys did a remarkable job on the PSPAs this week. You delivered on a policy change of enormous importance that's actually being recognized as such by the outside world . . . , and as a credit to the Secretary and the President."

65. As a result of the Net Worth Sweep, the Enterprises are unable to retain or build capital and instead have been forced to operate on the brink of insolvency with an ever-dwindling capital buffer. That result is inconsistent with FHFA's mandate under HERA, as conservator, to put the Enterprises "in a sound and solvent condition" and "preserve and conserve the[ir] assets and property." 12 U.S.C. § 4617(b)(2)(D).

66. This result also makes the Enterprises unique in financial regulation. Other financial institutions are required to retain minimum levels of capital to ensure that they can withstand the vicissitudes of the economic cycle and are prohibited from paying dividends when they are not adequately capitalized. The Enterprises, by contrast, are compelled by the Net Worth Sweep to operate subject to a capital maximum, as any amount of retained capital that they hold in excess of a small capital buffer is swept to Treasury on a quarterly basis.

67. As with the decision to put the Enterprises into conservatorship, Treasury was the driving force behind the Net Worth Sweep. As early as February 2012, Treasury had prepared a 14-page proposal for housing finance reform. A key component of "Step 1" was to "[r]estructure PSPAs to allow for variable dividend payment based on positive net worth." On June 13, 2012, Treasury prepared a "[s]ensitive" and "[p]re-[d]ecisional" presentation, which stated that "Treasury would like to modify the PSPAs given the challenges and circularity embedded in the current structure." Treasury's proposed modification was to "[r]eplace the fixed 10 percent quarterly cash dividend paid by each [Enterprise] to Treasury with a variable quarterly dividend equal to a net worth sweep based upon financial results." Jim Parrott, a senior White House advisor at the time of the Net Worth Sweep, has testified that the Sweep was a "Treasury-driven process."

68. In addition to imposing the Net Worth Sweep, the Third Amendment suspended the Periodic Commitment Fee. But Treasury had consistently waived the Periodic Commitment Fee before the Net Worth Sweep, and it could set the amount of the fee only with the agreement of the Enterprises and at a market rate. Furthermore, the purpose of the Periodic Commitment Fee was to compensate Treasury for its ongoing support in the form of the commitment to invest in the Enterprises' senior preferred stock. By the time of the Net Worth Sweep, the 10% cash dividends on the senior preferred stock and the warrants to purchase 79.9% of the common stock for a nominal price provided a more than adequate return on the Government's commitment, so that any additional fee would have been inappropriate.

The Government's Post Hoc Rationalizations For The Third Amendment

69. In litigation, the Government has advanced two rationalizations for the Third Amendment. Neither comports with the facts.

70. First, the Government has argued that the Net Worth Sweep was necessary to prevent a "downward spiral" whereby the Enterprises drew from Treasury's commitment to pay their 10% dividends, thus increasing Treasury's liquidation preference and, consequently, the Enterprises' future dividend obligations. This is false. In August 2012, Treasury and FHFA knew that the Enterprises had returned to profitability and were projected to be able to pay the dividends owed to Treasury without drawing on additional funds long into the future. Indeed, the Net Worth Sweep was imposed after the Enterprises had disclosed that they had returned to stable profitability and had earned several billion dollars more than was necessary to pay Treasury the dividend in cash. Moreover, the Enterprises' dividends could be paid "in kind" at a 12% rate, which would not require a further draw. In testimony, a Treasury official was unable to identify any "problems of the circularity [in dividend payments that] would have remained had the [payment in kind] option been adopted."

71. Second, the Government has argued that the suspension of the Periodic Commitment Fee benefitted the Enterprises. This argument is litigation pretext. Before the Third Amendment, Treasury had always waived the Periodic Commitment Fee. Under the Third Amendment, the Periodic Commitment Fee is suspended only so long as the Net Worth Sweep is in place. Given the Enterprises' return to profitability by August 2012, there was no need for the ongoing commitment, nor to further compensate Treasury: Treasury was earning a 10% return on the money the Enterprises had drawn from it and was entitled to 79.9% of the Enterprises' common stock, enabling it to fully participate in and benefit from the Enterprises' return to profitability.

2013–2017: The Net Worth Sweep Transfers Tons Of Cash To Treasury

72. The Net Worth Sweep took effect in the first quarter of 2013. From that time through the end of 2017, the Enterprises have been very profitable, as anticipated in August 2012.

73. From the first quarter of 2013 through the last quarter of 2017, the Enterprises together paid more than $223 billion in "dividends" to Treasury pursuant to the Net Worth Sweep.

74. Over the same time period, had the Net Worth Sweep never been imposed and the Enterprises elected to pay 10% cash dividends under the PSPAs, the Enterprises would have paid no more than $94 billion in dividends to Treasury. Thus, through the end of 2017, the Net Worth Sweep added at least $129 billion beyond the pre-Third Amendment baseline to Treasury's coffers.

75. The Enterprises' net worths from 2013 through 2017 have included items that predated the Third Amendment. For example, in 2013, the Enterprises released their previously imposed valuation allowances against their deferred tax assets, which added more than $45 billion (for Fannie Mae) and $20 billion (for Freddie Mac) to the Enterprises' earnings that year. Also in 2013, the Enterprises reached large settlements concerning conduct that predated the Third Amendment. For example, in October 2013, three large banks agreed to pay Freddie Mac a total of $1.3 billion concerning Freddie Mac's claims relating to representations and warranties on pre-2013 loans. The same month, FHFA reached settlements with J.P. Morgan totaling $5.1 billion, which went to the Enterprises.

76. The Net Worth Sweep thus has more than adequately compensated Treasury for its investment in the Enterprises. As of August 2012, the Enterprises had drawn $189.5 billion from Treasury. That amount is dwarfed by the $223 billion-plus paid pursuant to the Net Worth

Sweep. And the $223 billion includes only dividends paid in 2013 through 2017; the Enterprises had paid tens of billions of dollars in cash dividends in the years before 2013.

77. The dividends paid pursuant to the Net Worth Sweep have, under the terms of the Third Amendment, not reduced Treasury's liquidation preference. Thus, in addition to the billions of dollars in cash dividends, Treasury retains a right to the first $189.5 billion to be distributed if the Enterprises are liquidated.

2017: The Fourth Amendment

78. Under the PSPAs (as amended through the Third Amendment), the Net Worth Sweep required the entire net worth of each Enterprise to be paid to Treasury, minus a small reserve that would shrink to zero by January 1, 2018.

79. On December 21, 2017, Treasury and FHFA executed letter agreements amending each Enterprise's PSPA for a fourth time. Under the letter agreements, Treasury and FHFA agreed to permit each Enterprise to retain a $3 billion capital reserve while it is in operation, so that the quarterly dividend is equal to each Enterprise's net worth minus the $3 billion reserve.

80. However, Treasury and FHFA also made sure that this capital reserve did not create any possible risk of any amount ever being available for distribution to private stockholders. They agreed that Treasury's liquidation preference in each Enterprise would increase by $3 billion. Thus, even the capital reserve must be paid out to Treasury upon liquidation.

CAUSES OF ACTION

COUNT I

Just Compensation Under The Fifth Amendment For The Taking Of Private Property For Public Use

81. Plaintiffs incorporate by reference and re-allege each allegation set forth above, as though fully set forth herein.

82. The Fifth Amendment to the United States Constitution provides, in relevant part, that no person shall "be deprived of life, liberty, or property, without due process of law; nor shall private property be taken for public use, without just compensation."

83. Plaintiffs had cognizable property interests in their stock in the Enterprises, including a contractual right to dividends, a contractual right to liquidation preferences, and an economic interest in each Enterprise's future earnings and the equity and value of their stock.

84. Plaintiffs had investment-backed expectations to participate in the Enterprises' future earnings and to receive a share of any residual value of the Enterprises in the event of liquidation, and those expectations were reasonable.

85. By way of the Third Amendment, executed under the purported authority of HERA and by two arms of the federal government, the United States directly appropriated for itself Plaintiffs' property interests in their stock. The Third Amendment, although unlawful, was an authorized act of the Government, done within the general scope of the duties of the agencies and officers who executed it.

86. The Third Amendment diminished the value of Plaintiffs' stock, repudiated Plaintiffs' contractual property rights, and directly and proximately caused a severe, present, continuing, and actual economic injury to Plaintiffs' property interests. Indeed, Plaintiffs have been deprived of all economically beneficial uses of its stock in the Enterprises, while the United

States has received payments from the Enterprises of more than $200 billion since the Third Amendment, without any corresponding reduction in the liquidation preference payable to the United States.

87. The Government has provided no compensation, let alone just compensation, to Plaintiffs for the expropriation of their property rights.

88. Plaintiffs have suffered, and are continuing to suffer, a taking and are entitled to just compensation.

COUNT II

Illegal Exaction In Violation Of The Fifth Amendment

89. Plaintiffs incorporate by reference and re-allege each allegation set forth above, as though fully set forth herein.

90. Alternatively, the Third Amendment was imposed by the United States without authority. Under HERA, FHFA "as conservator" was to act to put the Enterprises "in a sound and solvent condition," to "preserve and conserve [their] assets," and to "carry on" their business. Contrary to these requirements, the Third Amendment ensures that the Enterprises will perpetually be on the verge of insolvency, wastes their assets, and destroys their ability to carry on their mandate as private, shareholder-owned companies. It does the opposite of conserving the Enterprises, and accomplishes a wind-down. Moreover, the Third Amendment was ultra vires on the part of Treasury, because it was executed contrary to the provisions of HERA (and the Enterprises' charters) granting Treasury only temporary emergency authority to purchase and determine the terms, conditions, and amounts of securities of the Enterprises.

91. The Third Amendment was imposed without authority for the additional and separate reason that, at the time of the Third Amendment, FHFA was structured in a way that violated Article II of the United States Constitution. The Constitution provides that all

"executive Power shall be vested in a President." U.S. Const. art. II, § 1. By making FHFA's head a single Director rather than a multi-member board and eliminating the President's power to remove the Director at will, HERA violated the Constitution's separation of powers. An independent agency headed by a single Director is virtually unprecedented in our Nation's history, and this structure impermissibly concentrated power in a single individual who was not the President.

92. Through the Third Amendment, the United States, in obtaining for itself a quarterly payment in perpetuity equal to the Enterprises' net worth, has appropriated to itself the property of Plaintiffs, which own stock in the Enterprises. This appropriation was, in effect, a forced payment of money by Plaintiffs to the Government.

93. To the extent that the United States' violation of a "money mandating" statute is a necessary predicate for this Count, HERA is such a statute, particularly in the circumstances here, where the United States, in and as the result of assuming control of the Enterprises, assumed a fiduciary duty the breach of which is appropriately remedied by damages.

94. The Third Amendment is therefore an illegal exaction imposed in violation of the Due Process Clause of the Fifth Amendment.

95. Plaintiffs are entitled to just compensation for their illegally exacted property.

COUNT III

Breach Of Fiduciary Duty

96. Plaintiffs incorporate by reference and re-allege each allegation set forth above, as though fully set forth herein.

97. The conservatorship provisions of HERA create a fiduciary relationship between an agency of the Government (FHFA), on the one hand, and the Enterprises' stockholders, on the other. The Government therefore has a fiduciary responsibility to manage the conservatorships

of the Enterprises for the benefit of their stockholders—or, at least, in a manner that is not expressly understood and intended to be directly adverse to the interests of the stockholders, and intended to benefit the Government and harm the stockholders.

98. Given the existence of a fiduciary relationship between FHFA and the Enterprises' stockholders, it follows that the Government should be liable in damages for the breach of its fiduciary duties.

99. The Net Worth Sweep is a self-dealing transaction between two sister agencies of the Government, and improperly (and in bad faith) expropriates the economic interest in the Enterprises held by their private stockholders for the benefit of the Government.

100. The Net Worth Sweep was neither entirely fair nor intrinsically fair. It was manifestly unfair.

101. The Net Worth Sweep constituted waste, gross and palpable overreaching, and a gross abuse of discretion.

102. The Net Worth Sweep did not further any valid business purpose or reasonable business objective of the Enterprises, did not reflect FHFA's good-faith business judgment of what was in the best interests of the Enterprises or their stockholders, and was unfair to the Enterprises and their stockholders.

103. Thus, by entering into the Net Worth Sweep, FHFA violated its fiduciary duty to Plaintiffs.

104. Plaintiffs suffered damages as a direct and proximate result of the foregoing breach of fiduciary duties.

COUNT IV

Breach Of Implied-In-Fact Contract Between The United States And The Enterprises

105. Plaintiffs incorporate by reference and re-allege each allegation set forth above, as though fully set forth herein.

106. Prior to appointing itself conservator on September 6, 2008, FHFA unambiguously offered to place the Enterprises by consent, under 12 U.S.C. § 4617(a)(3)(I), with certain conditions described below, and the boards of directors of the Enterprises accepted this offer. FHFA made no finding of insolvency, undercapitalization, or any other ground to impose conservatorship under 12 U.S.C. § 4617(a)(3)(A)-(H) or (J)-(L).

107. FHFA offered, and the boards of the Enterprises accepted, a conservatorship that would aim to "preserve and conserve the [Enterprises'] assets and property" and restore the Enterprises to a "sound and solvent condition." *See* 12 U.S.C. § 4617(b)(2)(D). The offer was also of a conservatorship that would end when that goal was achieved. Neither of these conditions was ambiguous, and both would benefit the known and distinct class of stockholders of the Enterprises, on whose behalf the boards of directors of the Enterprises had a fiduciary duty to act. In fact, FHFA obtained the boards' consent on the ground, in part, that conservatorship would serve the interests of the Enterprises' stockholders.

108. Underlying FHFA's offer was its promise that FHFA would not, as conservator, wind down or liquidate the Enterprises. FHFA stated contemporaneously with its offer that it could not, as conservator, place the Enterprises into liquidation. FHFA stated at the time, and for several years into the conservatorship, that its goal was instead to restore the Enterprises' assets and property to a sound and solvent condition, which continued course of performance constitutes evidence of the offer's original terms.

109. When consenting to the conservatorship, the boards of the Enterprises furnished good and valuable consideration to FHFA by agreeing to forbear from a judicial or legislative challenge that the United States feared. *See* 12 U.S.C. § 4617(a)(5). This forbearance was unambiguously furnished in exchange for FHFA's promises to act to restore the Enterprises to a safe and solvent condition.

110. The United States and the Enterprises, through the acts described above, entered into an implied-in-fact contract. The terms of that contract were, as relevant here, that FHFA, if made conservator, would preserve and conserve the Enterprises' assets and property, that its conservatorship would continue only until the Enterprises were placed in a safe and solvent condition, and that, in exchange, the boards of the Enterprises would consent to, and not challenge or litigate, such a course of action. Both FHFA and the Enterprises intended that an implied contract would exist. That contract required FHFA to preserve the Enterprises' assets and property, and forbade it from diminishing or expropriating the Enterprises' assets and property. This intent was demonstrated through the offer and acceptance detailed above. FHFA's offer was not ambiguous in its terms, and the boards' acceptance was manifested in FHFA's subsequent imposition of conservatorship based on the boards' consent.

111. Under these terms of the implied-in-fact contract, and given the known fiduciary duty of the boards of directors of the Enterprises, the stockholders of the Enterprises were intended beneficiaries of the contract.

112. FHFA had actual authority, as an agency of the Government, to bind the United States.

113. The Third Amendment breached the contract by rendering it impossible for the Enterprises to build and retain the capital necessary to exit conservatorship and return to normal business operations.

114. Each subsequent Net Worth Sweep payment independently breaches that contract by depleting the Enterprises of capital (rather than preserving and conserving it), in a manner that FHFA has expressly recognized undermines the goals of conservatorship.

115. Had the United States adhered to the contract, it would have protected the rights of holders of stock (other than itself) in the Enterprises. Through the Third Amendment, however, the United States instead engaged in self-dealing, benefitting itself while harming the stockholders other than itself.

116. The Third Amendment, therefore, directly harmed Plaintiffs, by preventing the termination of the conservatorship; stripping the Enterprises of their ability to generate and retain funds to ever distribute as dividends to holders of the Enterprises' stock; and nullifying Plaintiffs' contractual right, as holders of the Enterprises' stock, to ever receive a liquidation preference upon the dissolution, liquidation, or winding up of the Enterprises. Plaintiffs are accordingly entitled to damages.

PRAYER FOR RELIEF

WHEREFORE, Plaintiffs seek a judgment as follows:

A. Finding that the United States has taken or illegally exacted Plaintiffs' private property in violation of the Takings or Due Process Clauses of the Constitution;

B. Awarding Plaintiffs just compensation under the Fifth Amendment for the United States' taking of its property;

C. Determining and awarding to Plaintiffs the damages sustained by them as a result of the violations set forth above;

D. Awarding rescissory damages, based upon the breach of fiduciary duty that occurred;

E. Awarding Plaintiffs pre-judgment and post-judgment interest;

F. Awarding to Plaintiffs the costs and disbursements of this action, including reasonable attorneys' and experts' fees, costs and expenses; and

G. Granting such other and further relief as the Court deems just and proper.

Dated: August 7, 2018

Respectfully submitted.

By: s/ Mark T. Stancil

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