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Altering the Deal: The Importance of GSE Shareholder Litigation

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Altering the Deal: The Importance of GSE Shareholder Litigation

I. INTRODUCTION

"I am altering the deal. Pray I don't alter it any further."[1] Ever the classical villain, the Star Wars saga's Darth Vader informs Lando Calrissian that the princess and the Chewbacca are now his.[2] The lesson gleaned from the short exchange is simple: Deals struck with despots are not deals at all. Darth Vader's words likely resonate in the ears of private investors in the Federal National Mortgage Association ("Fannie Mae") and the Federal Home Loan Mortgage Corporation ("Freddie Mac"), (collectively, the "GSEs").[3] Perry Capital LLC ("Perry") and other private investors in the GSEs are currently embroiled in a legal battle against the federal government in connection with the conservatorship of the GSEs.[4] Their claims, in essence, are that agencies of the federal government have impermissibly decided to "alter the deal," and that the deal should be undone.[5]

Now on appeal after being dismissed in the United States District Court for the District of Columbia,[6] Perry's lawsuit against the

1. THE EMPIRE STRIKES BACK (Lucasfilm 1982).

2. *Id.*

3. The term "Government Sponsored Enterprises," or "GSEs," may refer to other companies "born from statutory charters issued by Congress," such as the Federal Home Loan Bank. Perry Capital LLC v. Lew, No. 13-1025, 2014 WL 4829559, at *1 n.1 (D.D.C. Sept. 30, 2014). For the purposes of this Note, the term "GSEs" will refer to Fannie Mae and Freddie Mac exclusively.

4. *See* Margaret Cronin Fisk et al., *Fannie Mae, Freddie Mac Investors Lose Suits Over Lost Dividends*, BLOOMBERG (Oct. 1, 2014, 12:01 AM), http://www.bloomberg.com/news/2014-09-30/Fannie Mae-Freddie Mac-investor-suits-over-treasury-dividend-thrown-out.html (noting Perry's suit is "among . . . almost 20 related cases . . . filed by investors").

5. See Nathan Vardi, *Why Hedge Funds Suing the Government over Fannie Mae and Freddie Mac Have a Bad Case*, FORBES (July 15, 2013, 9:50 AM), http://www.forbes.com/sites/nathanvardi/2013/07/15/why-hedge-funds-suing-the-government-over-Fannie Mae-and-Freddie Mac-have-a-bad-case; Complaint and Prayer for Declaratory and Injunctive Relief ¶ 16, Perry Capital LLC v. Lew, No. 13-1025 (D.D.C. July 7, 2013) [hereinafter Complaint] (noting that the plaintiff "seeks to prevent Defendants from giving effect to or enforcing the so-called Third Amendment").

6. Notice of Appeal, Perry Capital LLC v. Lew, No. 13-1025 (D.D.C. Oct. 2, 2014).

United States Treasury (the "Treasury") and the Federal Housing Finance Agency (the "FHFA"), (collectively, the "Government") is but one example of current litigation brought by private investors in connection with the GSEs.[7] These cases, sometimes referred to collectively as "dividend sweep litigation,"[8] stem from a 2012 amendment (the "Third Amendment") to the Senior Preferred Stock Purchase Agreements ("PSPAs").[9] The plaintiffs in these cases challenge the validity of the Third Amendment because, they claim, the changes it wrought to the PSPAs negatively impact the value of private stock in the GSEs.[10]

Perry's suit in district court against the FHFA and the Treasury specifically focused on administrative law arguments against the enforcement of the Third Amendment to the PSPAs.[11] Perry relied almost entirely on alleged violations of the Administrative Procedure Act ("APA")[12] to seek the nullification of the Third Amendment.[13] As presaged in dicta of the district court's opinion,[14] the climate in which the Housing and Economic Recovery Act of 2008 ("HERA")[15] was passed and the broad discretion it affords the FHFA when acting as conservator renders these claims difficult to make.

It is the overarching goal of this Note to provide a broad framework for understanding the issues at stake in current dividend

7. *See* Fisk et al., *supra* note 4 (noting that "Bruce Berkowitz, the head of Fairholme Capital Management LLC," and "[h]edge-fund manager Bill Ackman's Pershing Square Capital Management LP" are among those involved in various suits challenging the Third Amendment).

8. The phrase "dividend sweep litigation," as it appears in this Note, refers collectively to the various lawsuits against the federal government in connection with the Third Amendment.

9. Complaint, *supra* note 5, ¶ 16.

10. *Id.*

11. *See id.* ¶¶ 59–94 (enumerating four administrative law grounds on which the court should grant relief).

12. Administrative Procedure Act (APA), Pub. L. 404-79, 60 Stat. 237 (1946), as codified by An Act to enact Title 5, United States Code, Pub. L. No. 89-554, 80 Stat. 378 (1996), as amended through Pub. L. No. 107-245, 116 Stat. 1504 (2002) (codified as amended at 5 U.S.C. §§ 551–559, 701–706 (2012)).

13. Complaint, *supra* note 5, ¶ 95.

14. *See* Perry Capital LLC v. Lew, No. 13-1025, 2014 WL 4829559, at *2–3 (D.D.C. Sept. 30, 2014) (quoting HERA's broad empowering language and the emergency nature of the sub-prime mortgage crisis).

15. Housing and Economic Recovery Act of 2008 (HERA), Pub. L. No. 110-289, 122 Stat. 2654 (2008) (codified as amended at 12 U.S.C. §§ 1455, 1719, 4511, 4513 & 4617 (2012)); Vardi, *supra* note 5.

sweep litigation against the Government. Specifically, this Note asserts that although Perry and similarly situated plaintiffs bringing APA-based actions rightfully question the Government's reasoning in entering the Third Amendment, HERA's anti-injunction provision[16] presents what is likely an insurmountable jurisdiction problem for dividend sweep litigation plaintiffs. This Note proceeds in four parts. Part II provides a general background of the GSEs' history, role in the secondary mortgage market, and path to conservatorship.[17] Part III summarizes the arguments Perry and other plaintiffs made in district court,[18] while Part IV discusses why these claims failed in district court and why HERA's anti-injunction provision successfully insulates the Government from virtually all judicial review from APA-based claims.[19] Part V concludes by discussing the negative implications of insulating the Third Amendment from review by using HERA's anti-injunction provision.[20]

II. THE GSES' ROAD TO CONSERVATORSHIP

A. Fannie Mae and Freddie: A Brief History

The mission of the GSEs is to provide liquidity and stability to the mortgage industry by purchasing, guaranteeing, and securitizing mortgage loans from loan originators to sell on the secondary market.[21] Fannie Mae was formed in 1938 under U.S. Government charter and privatized in 1968.[22] Freddie Mac was formed in 1970 under the umbrella of the Federal Home Loan Banks and became fully privatized in 1989.[23] When banks sell long-term mortgages in the secondary market for securitization, the asset (a thirty year fixed rate mortgage, for

16. 12 U.S.C. § 4617(f).
17. *See infra* Part II.
18. *See infra* Part III.
19. *See infra* Part IV.
20. *See infra* Part V.
21. Avni P. Patel, *The Bailout of Fannie Mae and Freddie Mac*, 28 REV. BANKING & FIN. L. 21, 22 (2009).
22. *Id.*
23. Julie Andersen Hill, *Shifting Losses: The Impact of Fannie Mae's and Freddie Mac's Conservatorships on Commercial Banks*, 35 HAMLINE L. REV. 343, 350 (2012).

example) is converted into cash.[24] This sale reduces the bank's exposure to interest rate and default risks.[25] By providing a ready-made market for long-term streams of payment, the secondary mortgage market increases loan originators' liquidity and removes the long-term interest rate and default risks associated with holding a typical mortgage loan to maturity—all of which increase the availability of home mortgage loans.[26] The GSEs' role in the U.S. housing market is paramount. When the GSEs were put into conservatorship in September 2008, they collectively "owned or guaranteed more than $5 trillion in residential mortgages."[27]

Because of pressure by the Department of Housing and Urban Development ("HUD") to increase mortgage loan availability for lower-income borrowers, the GSEs purchased increasing levels of subprime loans made by originators in the years leading up to 2007.[28] Once subprime mortgage defaults reached a feverish pace in late 2007, private investors lost confidence in the GSEs and began to sell GSE stock en masse.[29] In 2008, Congress passed HERA as a response to the subprime mortgage crisis.[30] HERA provides the statutory basis for the FHFA to place Fannie Mae and Freddie Mac into either conservatorship or receivership.[31] According to Perry, "[b]efore the FHFA placed the Companies into conservatorship, [the] Treasury . . . encouraged private investors to purchase Private Sector Preferred Stock."[32]

24. Patel, *supra* note 21, at 22–23.

25. *See* LISSA L. BROOME & JERRY W. MARKHAM, REGULATION OF BANK FINANCIAL SERVICE ACTIVITIES 329–33 (4th ed. 2010) (discussing how the sale of mortgage loans by loan originators to securitizers like Fannie Mae and Freddie Mac allows banks and other loan originators to reduce the risk that market rates paid to depositors might exceed fixed rates earned on long-term mortgages).

26. *See* Patel, *supra* note 21, at 22 (noting that "[a]fter banks and other loan originators sell mortgages to [the GSEs], they use profits to make new loans," and that "[these] loans increase liquidity and flexibility in the housing market").

27. Hill, *supra* note 23, at 344.

28. Patel, *supra* note 21, at 23 (noting that "HUD required [the GSEs] to purchase 'affordable' loans made available to . . . low and middle-income buyers").

29. *Id.* at 24–25.

30. *Id.* at 24; Steven M. Davidoff & David Zaring, *Regulation by Deal: The Government's Response to the Financial Crisis*, 61 ADMIN. L. REV. 463, 484–85 (2009).

31. *See* Housing and Economic Recovery Act of 2008 (HERA), Pub. L. No. 110-289, 122 Stat. 2654 (codified as amended at 12 U.S.C. §§ 1455, 1719, 4511, 4513 & 4617 (2012)).

32. Complaint, *supra* note 5, ¶ 39.

B. The GSEs Enter into the Original PSPA

On September 7, 2008, the Treasury exercised its new grant of authority to place the GSEs into conservatorship and execute the original PSPAs as a means of ensuring their solvency when it deemed their recapitalization efforts woefully inadequate.[33] As a result, the GSEs have been wards of the state ever since.

The conservatorships of the GSEs are structured so that the FHFA runs the firms in place of their previous executive leadership, and negotiates with the Treasury on behalf of the GSEs for the terms of the PSPAs.[34] The GSEs were given an extension of an initial $100 billion (later extended to $200 billion)[35] line of credit immediately after they were placed into conservatorship under the FHFA.[36] This "bailout" of sorts was effected through an initial agreement that the Treasury would buy all of the newly-created senior preferred stock for a nominal price of $1 billion.[37] If at any time the FHFA determined that Fannie Mae or Freddie Mac's liabilities exceed its assets, "[the] Treasury [would] contribute cash capital to the GSE in an amount equal to the difference between liabilities and assets" and that amount "[would] be added to the senior preferred stock."[38] In return for access to this liquidity, the senior preferred stock would earn a 10% annual dividend, and the Treasury would receive warrants for the purchase of 79.9% of Fannie Mae or Freddie Mac's common stock at a nominal price.[39] In the event Fannie Mae or Freddie Mac was unable to pay the 10% dividend on the value of the senior preferred stock, the dividend rate would rise to 12% annually which would accrue until the GSE could resume payment of the dividend.[40] This draw and dividend structure was meant to quickly infuse the GSEs with cash and assuage "widespread concern that the

33. Davidoff & Zaring, *supra* note 30, at 486.

34. Patel, *supra* note 21, at 25–26.

35. *See* Perry Capital LLC v. Lew, No. 13-1025, 2014 WL 4829559, at *3 (D.D.C. Sept. 30, 2014) ("On May 6, 2009, Treasury and the GSEs, through [the] FHFA . . . doubled its funding cap to $200 billion for each GSE.").

36. Press Release, U.S. Treasury Dep't Office of Pub. Affairs, Fact Sheet: Treasury Senior Preferred Stock Purchase Agreement (Sept. 7, 2008), *available at* http://www.treasury.gov/press-center/press-releases/Documents/pspa_factsheet_090708%20hp1128.pdf.

37. *Id.*

38. *Id.*

39. *Id.*

40. *Id.*

[GSEs] were insolvent."[41]

Conservators are meant "to conduct an institution as an ongoing business."[42] As such, Perry argued that the FHFA was required to run the GSEs in a manner consistent with securing their future as private firms.[43] Indeed, Perry argued that the FHFA is "strictly limited by HERA" in its role as conservator.[44]

C. The FHFA and the Treasury Enter into the Third Amendment

Entered into by the FHFA as conservator for the GSEs, and the Treasury as holder of the senior preferred stock on August 17, 2012,[45] the Third Amendment was the genesis of the dividend sweep litigation. The Third Amendment drastically changed the nature of the relationships between the GSEs, the Treasury, and the FHFA by erasing the prior 10% dividend of the government preferred stock and instead "sweeps" all profits over a certain threshold to the Treasury.[46] These new dividend payments made to the Treasury are calculated by subtracting the "Applicable Capital Reserve Amount"[47] from any positive net worth generated by the GSEs in each quarter.[48] Every net worth dollar the GSEs generate above that reserve amount is paid to the

41. DAVID H. CARPENTER & M. MAUREEN MURPHY, CONG. RESEARCH SERV., RL34657, FINANCIAL INSTITUTION INSOLVENCY: FEDERAL AUTHORITY OVER FANNIE MAE, FREDDIE MAC, AND DEPOSITORY INSTITUTIONS 2 (2008).

42. Resolution Trust Corp. v. CedarMinn Bldg. Ltd. P'ship, 956 F.2d 1446, 1454 (8th Cir. 1992) (drawing the distinction between the roles of conservators and receivers).

43. *See* Complaint, *supra* note 5, ¶ 81 ("HERA requires the FHFA to take steps to put [the GSEs] in a sound and solvent condition and to work to conserve [their] assets and property." (citation omitted) (internal quotations omitted)).

44. *Id.*

45. Third Amendment to Amended and Restated Senior Preferred Stock Purchase Agreement between U.S. Dep't of Treasury and Fed. Home Loan Mortg. Corp. 1, 8 (Aug. 17, 2012), *available at* http://www.sec.gov/Archives/edgar/data/1026214/000119312512359938/d398152dex101.htm.

46. *See id.* at 4 (replacing the "Dividend Rate" of 10.0% after December 31, 2012 with the "Dividend Amount," defined as "the amount, if any, by which the Net Worth Amount . . . less the Applicable Capital Reserve Amount exceeds zero").

47. The "Applicable Capital Reserve Amount" is the amount of capital per quarter that Fannie Mae and Freddie Mac are permitted to retain. This capital reserve amount is decreased from $3 billion per quarter in 2013 to $0 by January 1, 2018, such that Fannie Mae and Freddie Mac are permitted to retain a maximum of $12 billion in 2013, $9.6 billion in 2014, $7.2 billion in 2015, $4.8 billion in 2016, $2.4 billion in 2017, and $0 beginning in 2018. *Id.*

48. *Id.*

Treasury as a dividend on the existing senior preferred stock.[49] Thus, the GSEs are barred from building any capital, save the nominal reserve amounts,[50] and operate as indentured servants to the Treasury.

The Government's cited reason for entering into the Third Amendment was the growing concern over the "circularity of payments"[51] death spiral that might ensue when an unprofitable GSE would be forced to draw funds from the Treasury to meet the 10% interest payments on existing Treasury-held senior preferred stock.[52] This would have the effect of increasing the GSEs' dividend obligations because the draw amount would be added to the liquidation preference amount that would accrue interest at 10%.[53] According to the Treasury and the FHFA, this cycle of paying 10% dividends to the Treasury with additional draws from the Treasury had the potential to exhaust the Treasury's lending limit of $200 billion.[54] Creating this negative feedback loop of borrowing funds from the Treasury to pay the interest charges on other Treasury draws could potentially spiral the GSEs into insolvency.[55]

The Government claimed that the Third Amendment was a reasonable way to ensure that neither Fannie Mae nor Freddie Mac could exhaust their access to capital, given that the purpose of the PSPAs was to instill market confidence in the GSEs.[56] If the FHFA were to permit Fannie Mae or Freddie Mac to exhaust their funding commitments, it would send strong market signals that that GSE was in a precarious position—unable to turn to the government for any additional cash.[57] Although that stated concern may seem reasonable,

49. *Id.*

50. The reserve amount of capital that the GSEs are permitted to retain, assuming a positive net worth is generated, is decreased annually until it reaches $0 in 2018, at which point neither Fannie Mae nor Freddie Mac are permitted to retain any positive earnings. *Id.*

51. Treasury Defendant's Reply in Support of Their Dispositive Motions and Opposition to Plaintiff's Summary Judgment Motions at 43, Perry Capital LLC v. Lew, No. 13-1025, (D.D.C. May 2, 2014) [hereinafter Treasury Reply].

52. Treasury Reply, *supra* note 51, at 43–47.

53. *Id.* at 43.

54. *Id.*

55. *See id.* at 44–45 (claiming the Third Amendment was necessary because of "the need to maintain investor confidence in the GSEs by minimizing those entities' draws on the finite Treasury funds available to them").

56. *Id.*

57. *See id.* (arguing that the Government had a duty to calm and reassure the mortgage-backed securities market that Fannie Mae and Freddie Mac were healthy and that, with this chief concern in mind, the Third Amendment was abundantly reasonable).

plaintiffs in all dividend sweep litigation cases fundamentally disagree about the necessity and legitimacy of the Third Amendment.

The concerns that the GSEs' lack of profitability might precipitate a negative feedback loop became moot when the two mortgage giants returned to consistent profitability in the quarters following the Third Amendment's enactment.[58] After drawing a final $20 million in the first quarter of 2012, Freddie Mac has paid the Treasury approximately $91 billion of the Treasury's $71 billion investment—a return of 128%.[59] Fannie Mae has paid the Treasury approximately $134.5 billion of the Treasury's $116.1 billion investment—a return of 115%.[60] Combined, the GSEs have returned approximately $225 billion to the Treasury for the Treasury's $188 billion commitment—a return of approximately 119% to the U.S. taxpayers.[61] Fannie Mae's news release succinctly sums up the issue: "Fannie Mae will have paid a total of $134.5 billion in dividends to [the] Treasury in comparison to $116.1 billion in draw requests since 2008. Dividend payments do not reduce prior Treasury draws."[62]

Perhaps unsurprisingly, investors in private preferred stock and common stock of the GSEs filed a slew of civil actions containing various claims against the Government in 2013.[63] Perry's suit focused

58. *See* FREDDIE MAC, UPDATE: INVESTOR PRESENTATION 12–13 (Dec. 2014) [hereinafter FREDDIE MAC UPDATE], *available at* http://www.Freddie Macmac.com/investors/pdffiles/investor-presentation.pdf (showing profitable quarters since 3Q12 with zero Treasury draw requests since 1Q12 for approximately $20 million); Press Release, Fannie Mae, Fannie Mae Reports Largest Net Income in Company History; $17.2 Billion for 2012 and $7.6 Billion for Fourth Quarter 2012 10 (Apr. 2, 2013) [hereinafter Fannie Mae Report 4Q12], *available at* http://www.Fanniemae.com/resources/file/ir/pdf/quarterly-annual-results/2012/q42012_release.pdf (showing profitable quarters in 3Q and 4Q12, immediately following the Third Amendment).

59. *See* FREDDIE MAC UPDATE, *supra* note 58, at 13.

60. *See* Press Release, Fannie Mae, Fannie Mae Reports Net Income of $3.9 billion and Comprehensive Income $4.0 billion for Third Quarter 2014 1 (Nov. 6, 2014) [hereinafter Fannie Mae Report 3Q14], *available at* http://www.Fanniemae.com/resources/file/ir/pdf/quarterly-annual-results/2014/q32014_release.pdf.

61. Freddie Mac's $91 billion and Fannie Mae's $134 billion combine to $225 billion. Dividing that figure by the government's total funding commitment of $188 billion yields 119%.

62. Fannie Mae Report 3Q14, *supra* note 60, at 1.

63. *See* Fisk et al., *supra* note 4 (noting that Perry's suit is "among the first of almost 20 related cases to be decided"); Press Release, Gibson, Dunn & Crutcher LLP, Fannie Mae, Freddie Mac Investors File Suit Challenging U.S. Treasury's 2012 "Sweep Amendment" (July 7, 2013) (on file with author) (announcing the filing of a suit against the federal government to nullify the Third Amendment as illegal).

on the administrative law aspects of the actions of the FHFA and the Treasury, arguing that the Third Amendment should be vacated.[64] According to Perry, the administrative agencies essentially abused their statutory powers and strayed from HERA's mandate by extracting billions from the mortgage giants before winding them down and creating a world without the GSEs.[65]

D. Parallel Litigation Underway

Although the approximately twenty lawsuits all spring from the same set of facts—the enactment of the Third Amendment—groups holding stock in the GSEs have taken a number of different approaches to attacking the validity of the Third Amendment.[66] All combined, the lawsuits take five general approaches in respect to their substantive claims: (1) administrative law arguments that the Government exceeded its statutory authority, (2) administrative law arguments that the Government acted arbitrarily and capriciously when entering into the Third Amendment, (3) constitutional arguments that the United States effected a taking of property from the private preferred and common stockholders, (4) breach of contractual agreement, and (5) breach of fiduciary duty owed to the private preferred stock and common stockholders.[67]

64. *See* Complaint, *supra* note 5, ¶ 95.

65. *See* Plaintiffs Perry Capital LLC, Fairholme Funds, Inc., Fairholme Fund, Berkley Ins. Co., Acadia Ins. Co., Admiral Indem. Co., Admiral Ins. Co., Berkley Reg'l Ins. Co., Carolina Cas. Ins. Co., Midwest Emp's Cas. Ins. Co., Nautilus Ins. Co., Preferred Emp's Ins. Co., Arrowood Indem. Co., Arrowood Surplus Lines Ins. Co., and Fin. Structures Ltd. Reply in Support of their Cross-Motion for Summary Judgment on Administrative Procedure Act Claims at 1–2, Perry Capital LLC v. Lew, No. 13-1025 (D.D.C. June 2, 2014) [hereinafter Plaintiffs Reply].

66. *See* Todd Sullivan, *Fannie Mae, Freddie Mac: The WSJ Misinterprets Sweeney Decision*, VALUEPLAYS (Sept. 24, 2014, 6:01 PM), http://www.valueplays.net/2014/09/24/wsj-misinterprets-sweeney-decision (noting that "[t]here is a reason many of these are separate actions, the cases and arguments being made are not the same"). Mr. Sullivan correctly notes the dangers in drawing parallels from results in other cases against the government because the nature of the arguments differ based on the plaintiff and the particular arguments each makes. *Id.*

67. *See* Consolidated Class Action and Derivative Plaintiffs' Omnibus Memorandum of Law in Opposition to Defendants' Motions to Dismiss the Consolidated Amended Class Action and Derivative Complaint, or, in the Alternative, for Summary Judgment at 20–37, In Re Fannie Mae/Freddie Mac Senior Preferred Stock Purchase Agreement Class Action Litigations, No. 13-1288 (D.D.C. Mar. 21, 2014) (making arguments based on the common-law of contracts, fiduciary duties, and takings claims); Complaint, *supra* note 5.

III. PERRY'S CASE

At the pleading stage of the case in district court, Perry made administrative law arguments against the Treasury[68] and against the FHFA[69] in an attempt to invalidate the Third Amendment and revive the value of the private preferred stock.[70] On September 30, 2014, however, the district court ruled in favor of the Government on motions to dismiss Perry's case[71] along with lawsuits brought by Fairholme Funds,[72] Arrowood Indemnity Company,[73] and a class of litigants represented by Boies, Schiller & Flexner LLP[74] (collectively, the "Plaintiffs"). The four suits made many similar and overlapping arguments.[75] The dismissal surprised many interested in the litigation, because the case was dismissed while the Government was still compiling their administrative records, before either party had presented oral arguments on motions, before discovery, and before trial.[76]

Although the Plaintiffs' claims in these four cases failed before they were advanced at trial, the basic substance of their arguments warrants examination as several plaintiffs filed notices of appeal immediately following the dismissal.[77] These arguments are useful as a

68. *See* Complaint, *supra* note 5, ¶¶ 68, 73 (claiming that the Treasury exceeded its statutory authority under HERA and acted arbitrarily and capriciously in violation of the APA).

69. *See id.* ¶¶ 87, 94 (claiming that the FHFA violated its statutory mandate to preserve and conserve the GSEs and acted arbitrarily and capriciously in violation of the APA).

70. *See id.* ¶ 1; Vardi, *supra* note 15.

71. Order at 2–3, Perry Capital LLC v. Lew, No. 13-1025 (D.D.C. Sept. 30, 2014).

72. Consolidated Amended Class Action and Derivative Complaint, Fairholme Funds, Inc. v. Fed. Hous. Fin. Agency, No. 13-1053 (D.D.C. July 10, 2013).

73. Complaint, Arrowood Indem. Co. v. Fed. Nat'l Mortg. Ass'n, No. 13-1439 (D.D.C. Sept. 20, 2013).

74. Consolidated Amended Class Action and Derivative Compliant, In Re Fannie Mae/Freddie Mac Senior Preferred Stock Purchase Agreement Class Action Litigations, No. 13-1288 (D.D.C. Nov. 18, 2013).

75. Order, *supra* note 71, at 2. Several of the motions and accompanying memoranda were written and filed jointly. *See* Plaintiffs Reply, *supra* note 65, (filing three separate actions and case numbers together for the fifty-one page memorandum of law).

76. *See* Richard Epstein, *The WSJ's Improbable Defense of Judge Lamberth's Indefensible Decision in Perry Capital*, FORBES (Oct. 2, 2014, 1:49 PM), http://www.forbes.com/sites/richardepstein/2014/10/02/godzilla-versus-the-thing-the-wall-street-journals-improbable-defense-of-judge-lamberths-indefensible-decision-in-perry-capital.

77. Joe Light, *Fairholme Funds to Appeal Dismissal of Fannie, Freddie Suit*, WALL ST. J. (Oct. 10, 2014, 10:23 AM), http://www.wsj.com/articles/fairholme-funds-to-appeal-dismissal-of-fannie-freddie-suit-1412950991 (noting that Fairholme Funds, Inc. and Perry Capital, LLC had filed notices of appeal from the District Court's decision).

representative sample of the APA-based dividend sweep litigation arguments.

Perry used a two-pronged approach to attack the Treasury's actions.[78] Perry claimed that the Treasury violated the APA by exceeding its statutory authority under HERA and that the Treasury acted "arbitrarily and capriciously" when it entered into the Third Amendment.[79]

A. The Government Lacked Statutory Authority

Under the APA, a court can "hold unlawful and set aside agency action, findings, and conclusions" if they are "in excess of statutory jurisdiction, authority, or limitations."[80] Perry relied on this administrative law statute to provide the legal mechanism for invalidating the Treasury's actions, because the Treasury is an agency subject to the APA.[81] HERA empowers the Treasury to purchase securities in the GSEs to make them solvent.[82] It also limits the time in which the Treasury may purchase those securities or advance them additional funds.[83] HERA explicitly limits the Treasury's power to "hold, exercise any rights received in connection with, or sell, any obligations or securities purchased" after December 31, 2009.[84] Perry's argument was simply that by amending the stock certificates through the Third Amendment in 2012, the Treasury materially altered the securities in such a way that it amounts to a "purchase" of securities long after its authority to do so had expired.[85]

According to Perry, the Treasury "did not exercise any right" to

78. *See* Complaint, *supra* note 5, ¶¶ 68, 73, 87, 94 (making two APA-based arguments against each defendant—that they exceeded their statutory authority, and that they acted arbitrarily and capriciously).

79. *See id.* ¶¶ 64, 68, 73, 78.

80. Administrative Procedure Act, 5 U.S.C. § 706(2)(C) (2012).

81. Complaint, *supra* note 5, ¶ 68.

82. *See* Housing and Economic Recovery Act of 2008 (HERA), 12 U.S.C. § 4617(b) (2012) (granting the FHFA the authority to "[o]perate the [GSE]" and "provide by contract for assistance in fulfilling any function, activity, action, or duty of the [FHFA] as conservator or receiver." *Id.* This provision, when coupled with the FHFA's mandate to conserve the GSE's assets is the basis on which the FHFA finds authority to contract with the Treasury to ensure the GSEs are solvent.

83. §§ 1455(*l*)(4), 1719(g)(4).

84. § 1719(g)(2)(D).

85. *See* Plaintiffs Reply, *supra* note 65, at 18–26.

which it was entitled under the terms of the PSPAs.[86] Perry argued that the power to amend the PSPAs was not a "right [the] Treasury received that could be exercised after December 31, 2009."[87] In response, the Treasury, in essence, argued that the right to amend the PSPAs was a contractual right contained in the original PSPAs.[88] The Treasury claimed that the right to *amend* the PSPAs survived the expiration of the right to *purchase* securities in the GSEs at the end of 2009.[89] In that case, the Third Amendment would simply be the exercise of that right "received in connection with"[90] the original PSPAs.[91] Perry responded by asserting that the Treasury's right to amend the PSPAs vanished at the stroke of midnight on December 31, 2009, at which point the Treasury was left only with whatever stock it had purchased up to that date.[92]

Perry then asserted that the Treasury changed the nature of the stock it owned in the GSEs by executing the total net worth sweep and that the "fundamental change" securities law doctrine should render the amendment an illegal purchase of securities.[93] This doctrine represents an exception to the default rule for bringing a securities fraud action under § 10(b).[94] Under that provision, "a plaintiff [must] be an actual 'purchaser' or 'seller' of securities who has been injured by deception or fraud 'in connection with' the purchase or sale."[95]

The fundamental change doctrine provides a cause of action for plaintiffs to bring a securities fraud claim when the default rule's technical requirement of a purchase or sale is not met.[96] When a plaintiff experiences a drastic and unintentional change in the nature of a security, courts will deem the holder of that security to have effectively purchased or sold it.[97] Perry used this narrow exception to

86. *Id.* at 18.
87. *Id.* at 18–20.
88. Treasury Reply, *supra* note 51, at 28.
89. *Id.* at 27–28.
90. Housing and Economic Recovery Act of 2008 (HERA), 12 U.S.C. § 1719(g)(2)(D) (2012).
91. *See* Treasury Reply, *supra* note 51, at 26–29 (arguing that amending the PSPAs was a permissible exercise of rights not subject to the Sunset Provision).
92. *See* Plaintiffs Reply, *supra* note 65, at 19.
93. *Id.* at 20–22.
94. 7547 Corp. v. Parker & Parsley Dev. Partners, L.P., 38 F.3d 211, 226 (1994).
95. *Id.* (citing Birnbaum v. Newport Steel Corp., 193 F.2d 461, 464 (2d Cir. 1952)).
96. *Id.*
97. *Id.* at 226–27.

define the term "purchase" to establish that the change in the GSEs' stock resulting from the Third Amendment was a "purchase" made after the Treasury's express authority to do so had expired.[98] This securities law doctrine and a common sense understanding of the word "purchase," Perry argued, means that the Treasury bought rights after its authority to do so had expired.[99]

Perry also argued that the FHFA, because of its special role as the GSEs' conservator, had a "statutory responsibility to ensure each [GSE] 'operates in a safe and sound manner.' "[100] The FHFA owed a special duty as the GSEs' conservator to protect and conserve them as private, ongoing businesses.[101] According to Perry, agreeing to surrender all company net worth was antithetical to the FHFA's role in protecting the GSEs and their shareholders.[102] Perry alleged that Congress "requires [the] FHFA . . . to preserve and conserve the [GSEs'] assets and place [them] in a sound and solvent condition."[103] In other words, preventing the companies from retaining or building capital could not logically further the goal of reestablishing the GSEs as private firms—a goal that necessarily required the GSEs to buy back the government preferred shares.[104]

B. The Government Acted Arbitrarily and Capriciously

Perry's second line of argument comes from the "arbitrary and capricious" provision of the APA.[105] Pursuant to the APA, a court may

98. Plaintiff's Reply, *supra* note 65, at 22.

99. *Id.* at 20.

100. *Id.* at 29 (quoting News Release, Fed. Hous. Fin. Agency, A Strategic Plan for Enterprise Conservatorships: The Next Chapter in a Story that Needs an Ending 7 (Feb. 21, 2012)).

101. *See id.*

102. *See id.* at 2–3 (claiming that "FHFA's contentions that the [Third Amendment] is consistent with its conservatorship authority . . . fall flat," and that the Third Amendment "renders those goals [of preserving the GSEs assets for normal resumption of business] impossible").

103. *Id.* (citing Housing and Economic Recovery Act of 2008 (HERA), 12 U.S.C. § 4617(b)(2)(D) (2012)) (internal quotation omitted).

104. As part of the original agreement with Fannie Mae and Freddie Mac, new "Treasury Senior Preferred Stock" was created to provide the mechanism for funding Fannie Mae and Freddie Mac. *See* Press Release, U.S. Treasury Dep't Office of Pub. Affairs, *supra* note 36. Those shares have an outstanding value of $189.5 billion—an amount that would need to be satisfied in order for Fannie Mae and Freddie Mac to repurchase those shares and resume normal operations.

105. Plaintiffs Reply, *supra* note 65, at 39.

invalidate "agency action, findings, and conclusions" found to be "arbitrary, capricious, an abuse of discretion, or otherwise not in accordance with law."[106] As articulated in *Motor Vehicle Manufacturers Ass'n v. State Farm Mutual Automobile Insurance Co.*,[107] the test for challenging an agency action as "arbitrary and capricious" turns on whether the action is the product of "reasoned decisionmaking."[108] Although judicial review under this standard is deferential to the agency, courts still require that the agency "examine the relevant data and articulate a satisfactory explanation for its action including a 'rational connection between the facts found and the choice made.' "[109] Based on this standard, Perry argued that the Treasury and the FHFA "failed to consider factors required by Congress, [] failed to take into account the agencies' prior explanations of their statutory authority," "failed to engage in reasoned decisionmaking," and "clearly breached their fiduciary duties" in entering into the Third Amendment.[110]

Perry asserted that the administrative record provided by the Treasury does not provide the congressionally required explanation for why the Third Amendment was consistent with the plan for the GSEs to resume operations as a private entity.[111] According to Perry, this lack of a record demonstrates that neither the Treasury nor the FHFA can justify the Third Amendment in light of its mandate to revive and release the GSEs.[112]

Perry further argued that although "[a]n agency's predictive judgments *may* be entitled to some deference . . . no deference is owed to predictions that are *contradicted by the record*."[113] Perry's claim was, again, simple: The data available at the time of the Third Amendment clearly showed a healthier future for both of the GSEs, rendering the Third Amendment unnecessary for the mortgage giants.[114]

106. Administrative Procedure Act (APA), 5 U.S.C. § 706(2)(A) (2012).

107. 463 U.S. 29 (1983).

108. *Id.* at 52.

109. *Id.* at 43 (quoting Burlington Truck Lines v. United States, 371 U.S. 156, 168 (1962)).

110. Plaintiffs Reply, *supra* note 65, at 39.

111. *Id.* at 39–40.

112. *See id.*

113. *Id.* (emphasis added) (citing BellSouth Telecomms., Inc. v. FCC, 469 F.3d 1052, 1060 (D.C. Cir. 2006)).

114. *Id.* at 41.

The final avenue of argument on the arbitrary and capricious theory is that the Treasury, as the majority shareholder in the GSEs, breached its fiduciary duty to the private preferred and common stockholders by entering into the Third Amendment.[115] Independent of any contractual-based theory, the Treasury and the FHFA owed fiduciary duties to the private shareholders in the companies the FHFA was supposed to be rehabilitating—duties they breached.[116]

IV. WHY PERRY LOST AND THE IMPLICATIONS OF HERA'S ANTI-INJUNCTION PROVISION

Perry's claims failed in district court for one reason: HERA's anti-injunction provision, contained in 12 U.S.C. § 4617(f), bars judicial review of any action that "restrain[s] or affect[s]"[117] the FHFA in conserving the assets of the GSEs, as long as it acts within its statutory authority.[118] To escape that provision's reach and expose the Government to judicial review requires evidence that the Government exceeded its statutory authority.[119]

The district court found that HERA clearly grants broad powers to the FHFA to act in furtherance of its conservator objectives,[120] and that HERA's anti-injunction provision prevents judicial review of all equitable claims against the FHFA when acting pursuant to its statutory

115. *See id.* at 46–48.

116. Memorandum of Law of Plaintiffs Perry Capital LLC, Fairholme Funds, Inc., Fairholme Fund, Berkley Ins. Co., Acadia Ins. Co., Admiral Indem. Co., Admiral Ins. Co., Berkley Reg'l Ins. Co., Carolina Cas. Ins. Co., Midwest Emp's Cas. Ins. Co., Nautilus Ins. Co., Preferred Emp's Ins. Co., Arrowood Indem. Co., Arrowood Surplus Lines Ins. Co., and Fin. Structures Ltd. in Opposition to Defendants' Motions to Dismiss and Motions for Summary Judgment and in Support of Plaintiff's Cross-Motion for Summary Judgment on Administrative Procedure Act Claims at 85–88, Perry Capital LLC v. Lew, No. 13-1025 (D.D.C. Mar. 21, 2014).

117. Housing and Economic Recovery Act of 2008 (HERA), 12 U.S.C. § 4617(f) (2012).

118. *See* Perry Capital LLC v. Lew, No. 13-1025, 2014 WL 4829559, at *6 (D.D.C. Sept. 30, 2014) (explaining that twenty-four of the thirty-seven claims brought by the five groups of litigants seek a type of relief that is effectively barred).

119. *See id.* at *6, 8 (explaining that dismissal is proper if the plaintiffs fail to "sufficiently plead that the FHFA acted beyond the scope of its statutory [authority]" as conservator which would require a purchase of securities).

120. *See* 12 U.S.C. § 4617(b)(1)(D) (stating that "[the FHFA] may, as conservator, take action as may be—(i) necessary to put the [GSE] in a sound and solvent condition; and (ii) appropriate to carry on the business of the [GSE] and preserve the assets and property of the [GSE]").

authority.[121] In addition to the broad protections for the FHFA from judicial review of "the exercise of [its] powers or functions . . . as a conservator,"[122] the Treasury's authority is afforded the protections of the anti-injunction provision because "granting relief against the counterparty to a contract with [the] FHFA would directly restrain [the] FHFA's ability as a conservator vis-à-vis that contract."[123] In short, the court's principal inquiry is whether the Government was acting within its statutory authority.[124] If so, then HERA's anti-injunction provision bars all claims seeking non-monetary relief.[125]

A. The District Court's Dismissal

In the court's memorandum opinion supporting the dismissal of Plaintiffs' cases, Judge Lamberth details the pertinent background information for the cases, the applicable legal standard on a motion to dismiss, and the analysis for why the various plaintiffs' claims failed.[126] In a few short pages,[127] Judge Lamberth found that HERA's anti-injunction provision: "bars claims of arbitrary and capricious conduct,"[128] and "applies to Treasury's authority."[129] He further found that the "Treasury . . . did not violate [its] authority" under HERA,[130] and that the "FHFA acted within its statutory authority."[131]

HERA's anti-injunction provision states in pertinent part, "no court may take any action to restrain or affect the exercise of powers or

121. *Perry*, 2014 WL 4829559, at *6.

122. 12 U.S.C. § 4617(f).

123. *Perry*, 2014 WL 4829559, at *7 (citing Treasury Reply, *supra* note 51, at 12–13).

124. *Id.* at *6 (citing previous D.C. Circuit decisions on agency review and noting that "the question for this Court is whether the plaintiffs sufficiently plead that [the Government] acted beyond the scope of its 'statutory powers or functions' "); Natural Res. Def. Council, Inc. v. FHFA, 815 F. Supp. 2d 630, 641 (S.D.N.Y. 2011) (noting that "the critical question" in determining if § 4617(f) "precludes this Court from exercising jurisdiction" is "whether the FHFA's [action] constitutes an exercise of a conservatorship power or function").

125. *Perry*, 2014 WL 4829559, at *6 (noting that a failure to plead that the Government exceeded its powers, "the Court must dismiss all of the [plaintiffs'] claims for declaratory, injunctive, or other equitable relief").

126. *Id.* at *1–25.

127. *Id.* at *7–12.

128. *Id.* at *7.

129. *Id.*

130. *Id.* at *9.

131. *Id.*

functions of [the FHFA] as a conservator or a receiver."[132] Because case law on HERA's anti-injunction provision is admittedly "sparse,"[133] courts have looked to a "nearly identical jurisdictional bar"[134] contained in the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 ("FIRREA")[135] for guidance.[136] FIRREA's anti-injunction provision, contained in 12 U.S.C. § 1821(j), applies to the Federal Deposit Insurance Corporation ("FDIC") and prevents judicial review of the FDIC's action as a conservator.[137] This usage of FIRREA's anti-injunction provision to inform HERA's anti-injunction provision spells disaster for Perry and other plaintiffs who seek equitable relief from the Third Amendment.[138]

In the midst of the savings and loan crisis, Congress passed FIRREA, amending the Federal Deposit Insurance Act of 1950 ("FDIA")[139] to strengthen the FDIC's authority to put troubled financial institutions into conservatorship or receivership and to repudiate contracts entered into by those depository institutions.[140] In *Freeman v. FDIC*,[141] the D.C. Circuit found that the language of FIRREA's injunction bar "does indeed effect a sweeping ouster of courts' power to grant equitable remedies."[142] FIRREA's anti-injunction provision bars judicial review as long as the FDIC acts within its statutorily permitted role as conservator or receiver.[143] The D.C. Circuit read FIRREA's anti-injunction provision as barring any court from granting non-

132. Housing and Economic Recovery Act of 2008 (HERA), 12 U.S.C. § 4617(f) (2012).

133. *Perry*, 2014 WL 4829559, at *6.

134. Natural Res. Def. Council, Inc. v. FHFA, 815 F. Supp. 2d 630, 641 (S.D.N.Y. 2011) (referencing 12 U.S.C. § 1821(j) (2012)).

135. Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA), Pub. L. No. 101-73, 103 Stat. 183 (codified as amended in scattered sections of 12 U.S.C.); *Perry*, 2014 WL 4829559, at *6.

136. *Natural Res. Def. Council*, 815 F. Supp. 2d at 641.

137. *Id.* at 641–42.

138. *See Perry*, 2014 WL 4829559, at *7 ("Counts in each of the *Perry*, *Fairholme*, and *Arrowood* Complaints, and related prayers for relief, that claim APA violations for arbitrary and capricious conduct . . . are hereby dismissed.").

139. Federal Deposit Insurance Act of 1950 (FDIA), Pub. L. No. 81-797, 64 Stat. 873 (codified as amended at 12 U.S.C. §§ 1811–1835a (2012)).

140. *Perry*, 2014 WL 4829559, at *6 n.12 (discussing FIRREA's enactment and the "congressional intent to grant the FDIC enormous discretion to act as conservator or receiver during the savings and loan crisis").

141. 56 F.3d 1394 (D.C. Cir. 1995).

142. *Id.* at 1399.

143. *Id.*

monetary remedies that would impede the FDIC in fulfilling its mandate to wind up (as receiver) hundreds of insolvent savings associations.[144]

Referencing the *Freeman* opinion, Judge Lamberth notes that the congressional intent behind FIRREA's anti-injunction provision was to allow the speedy resolution or "wind up" of hundreds of failed thrifts with minimal interruption.[145] Using FIRREA's anti-injunction provision from *Freeman* as the controlling standard, Judge Lamberth determined that "the plaintiffs [did not] sufficiently plead that [the] FHFA acted beyond the scope of its statutory powers or functions . . . as conservator."[146] In the court's view, the Third Amendment was merely another conservator action that falls within the "extraordinary breadth of HERA's statutory grant to [the] FHFA."[147]

The court found that because the FHFA acted within its statutory authority to solve the circularity of payments problem, discussed earlier,[148] the manner in which the FHFA addressed that problem is barred from judicial review.[149] That conclusion left only one question for the court to resolve: Whether the Third Amendment Treasury was statutorily impermissible purchase of securities, and not the permissible exercise of an existing contractual right.[150]

1. The FHFA Did Not Exceed its Statutory Authority

To evade HERA's anti-injunction provision's bar on inquiry into the reasonableness of the Third Amendment, plaintiffs must demonstrate that the Government acted in some way outside of its statutory authority.[151] Otherwise, the APA-based claims praying for declaratory and equitable relief that plaintiffs rely on are barred because they would "restrain or affect" the FHFA's statutory powers to run the

144. *Id.*

145. *Perry*, 2014 WL 4829559, at *6 n.12.

146. *Id.* at *6.

147. *Id.* at *9.

148. *See supra* Part II.C.

149. *See Perry*, 2014 WL 4829559, at *9 (noting that HERA's broad grant of power to the FHFA, "coupled with the anti-injunction provision, narrows the Court's jurisdictional analysis to *what* the Third Amendment entails, rather than *why* [the] FHFA executed [it]") (emphasis in original).

150. *Id.* at *7–8.

151. *Id.* at *6, 8.

GSEs.[152] The reason HERA's anti-injunction provision is such a problem for plaintiffs is that the crux of the argument against the FHFA is that the decision to enter into the Third Amendment was based on concerns other than legitimate conservator duties.[153] The real reason for the Third Amendment, Perry claimed, was to begin the GSEs' own death spiral and prevent them from reentering the private sector.[154] To reach that argument, however, plaintiffs have to show that the FHFA *did not have the authority to make that decision* under HERA.[155] The argument that the FHFA acted *outside* the power it was given as a conservator is exceedingly difficult, given the broad terms in which HERA grants power to the FHFA.[156]

Some agency decisions may be reached arbitrarily and capriciously while remaining within the bounds of what the agency was permitted to pass judgment on pursuant to its statutory authority.[157] This is because, as the district court noted, the limit of an agency's statutory authority is not necessarily congruent to the standard of finding an agency decision arbitrary and capricious.[158] As long as the FHFA can demonstrate that changing the dividend structure for the GSEs' payments to the Treasury was within its power to do, it matters not how they went about doing it.[159] This means that the FHFA is permitted to escape review of what may well be arbitrary and capricious decisions about the future of the GSEs—simply because it had the power to make that decision.[160] This creates an unreasonably thick

152. *See* Housing and Economic Recovery Act of 2008 (HERA), 12 U.S.C. § 4617(f) (2012). Any non-monetary relief sought—such as the nullification of a contract amendment and an unwinding of the dividend structure—is action that would affect the conservator. Opinion, *supra* note 3, at 12 (citing Freeman v. FDIC, 56 F.3d 1394, 1399 (1995)). The District Court read FIRREA's anti-injunction provision to be essentially identical to the intent behind preventing non-monetary claims from interfering with the FHFA as conservator. *Id.*

153. *See* Plaintiff Reply, *supra* note 65, at 1 (claiming that statements made in 2012 "reveal a very different rationale for the [Third Amendment]").

154. *See id.* (quoting Government press releases on the plan to "wind up" the GSEs).

155. *Perry*, 2014 WL 4829559, at *9–10.

156. *See id.* (drawing the distinction between questioning the *reasoning* underlying the Third Amendment and questioning whether the FHFA had the *authority* to enact it).

157. *Id.* at *7. The District Court opinion maintained that the D.C. Circuit, "implicitly draws a distinction between acting beyond the scope of the constitution or a statute . . . and acting within the scope of a statute, but doing so arbitrarily and capriciously." *Id.*

158. *Id.*

159. *Id.* at *9–10.

160. *Id.*

layer of insulation for the FHFA from judicial review.

The FHFA will escape judicial review of its questionable reasoning for the Third Amendment because in order to review that reasoning, the plaintiffs are required to plead that the FHFA was not permitted to consider any such action.[161] To be sure, there are colorable arguments that the FHFA knew the GSEs had a positive financial outlook when the Third Amendment was enacted, and that they were not at risk, immediate or otherwise, of exhausting their funding commitments.[162] To raise those issues, however, plaintiffs have to demonstrate far more evidence than would be required for proving that this action was arbitrary and capricious.

2. The Treasury Did Not Exceed its Statutory Authority

In order to evade HERA's anti-injunction provision, the Plaintiffs had to assert, as with their claims against the FHFA, that the Treasury acted outside "the scope of its authority"[163] by agreeing to the Third Amendment. As was detailed earlier[164] and discussed below, this required Perry to advance two highly technical arguments in district court that the Treasury exceeded its statutory authority.[165] First, that the Third Amendment was not the exercise of a contract right to which it was entitled after December 31, 2009, and second, that the Third Amendment was a purchase of securities in direct violation of 12 U.S.C. § 1455(*l*)(4), 1719(g) (HERA's "Sunset Provisions").[166] Judge Lamberth found neither argument persuasive.[167]

Lamberth first addressed the argument that the Third Amendment was not a permissible "exercise of rights" in connection

161. *Id.* at *6.

162. At the time the Third Amendment was entered into, Fannie Mae was regularly meeting the 10% dividend obligation and had over $117 billion of remaining credit it was able to draw from the Treasury. Fannie Mae Report 4Q12, *supra* note 58, at 2 (listing the amount of remaining funding available at $117.6 billion). Likewise, Freddie Mac had drawn a mere $71 billion at the time of the Third Amendment—a far cry from the "death spiral" the FHFA was supposedly so concerned about. Freddie Mac Update, *supra* note 58, at 13.

163. *Perry*, 2014 WL 4829559, at *7–9.

164. *See supra* Part III.

165. *See infra* Part III.A.1.

166. Housing and Economic Recovery Act of 2008 (HERA), 12 U.S.C. §§ 1455(*l*)(4), 1719(g) (2012).

167. *Perry*, 2014 WL 4829559, at *8–9.

with the existing preferred stock.[168] A central premise in the argument that the Third Amendment was a purchase of new securities is that the Third Amendment *was not* an exercise of permissible contractual rights inherent in the senior preferred stock that could be exercised after December 31, 2009.[169] HERA allows for the exercise of any right in connection with the securities after December 31, 2009, as long as it is not a purchase of additional senior preferred stock securities.[170] The two points are discrete, but interrelated. According to Lamberth, however, the plaintiffs read the Sunset Provisions too narrowly.[171] That provision specifically exempts the holding or selling of the senior preferred stock, and would also prevent the FHFA from exercising "any provision within [the] Treasury's contracts with the GSEs that requires mutual assent," according to Lamberth.[172] In other words, the argument went too far in asserting that the Sunset Provision would prevent any and all activity requiring mutual assent.[173]

Predictably, Judge Lamberth was also unconvinced that the Third Amendment can constitute a "purchase" of new securities.[174] Using a plain language approach to the word "purchase," Lamberth found it determinative that the Treasury did not "grant[] the GSEs additional funding commitments *nor* [did the Treasury] receive[] an increased liquidation preference."[175] The telltale signs of a purchase were absent, the determinative sign being consideration evidencing an exchange.[176] While the opinion makes passing reference to Perry's fundamental change doctrine arguments, the issue "strikes the Court as straightforward" that there was no "purchase" of securities.[177]

168. *Id.* at *8.

169. *See* Plaintiff's Reply, *supra* note 65, at 18 (arguing that the Third Amendment was not an exercise of a contractual right to which the Treasury was entitled after December 31, 2009). This argument is important for the plaintiffs because if the amendment was simply the exercise of a right stemming from the stock purchase agreements, which are contracts, HERA would not bar the exercise of those rights since that would be permissible.

170. 12 U.S.C. § 1719(g)(2)(D).

171. *Perry*, 2014 WL 4829559, at *8.

172. *Id.* (internal quotation marks omitted).

173. *Id.* at *8–9.

174. *Id.*

175. *Id.* at *9.

176. *See id.* (noting that, aside from the complex arguments over the term "purchase," the fact that the Treasury did not "provide[] an additional funding commitment or receiv[e] new securities from the GSEs as consideration" is further reason to disfavor finding a purchase).

177. *Id.*

Because the preliminary question of whether the Treasury acted within its statutory authority to "exercise any right received in connection with the PSPAs"[178] is answered in the affirmative, the manner in which it exercised that authority becomes irrelevant and barred from review by the protections of HERA's anti-injunction provision.[179] Thus, although the Treasury is not the conservator of the GSEs, any judicial review of the substantive claims on how it acted in connection with the GSEs' conservatorship is barred.[180]

B. Implications of HERA's Anti-Injunction Provision

The FHFA and the Treasury have found too thick a layer of insulation from judicial review in HERA's anti-injunction provision. That provision effectively insulates the Government from any review of its actions when the FHFA invokes its conservator authority, and when the review of the Treasury actions affect the FHFA as conservator in any way.[181] This is unfortunate for the Plaintiffs because many of the strongest factual arguments that the FHFA and the Treasury acted improperly, arbitrarily and capriciously, and to the detriment of private shareholders[182] may never be aired. A jurisdictional bar enacted to "enable the FDIC and [RTC] to expeditiously wind up the affairs of literally hundreds of failed financial institutions,"[183] should not have the same application and effect in the context of a previously private, but now de facto state-run financial institution that shows no signs of being wound up, "expeditiously" or otherwise.[184] It is, however, ultimately Congress who failed to incorporate more vigorous judicial review of the FHFA's actions—possibly because they never envisioned a never-ending conservatorship of the GSEs and expected the conservatorship to accomplish the fundamental goal of a " 'resumption of normal business

178. Housing and Economic Recovery Act of 2008 (HERA), 12 U.S.C. § 1719(g)(2)(D) (2012).

179. *Perry*, 2014 WL 4829559, at *7–9.

180. *Id.* at *7.

181. *Id.* at *7–8.

182. *See* Complaint, *supra* note 5, ¶¶ 58–94 (making various factual allegations that the FHFA was motivated by concerns other than its duties as the GSEs' conservator).

183. *Perry*, 2014 WL 4829559, at *6 (alteration in original).

184. The GSEs have been in conservatorship since September 2008 and will likely remain wards of the state until GSE reform measures at the Congressional level dictate their future.

operations.' "[185]

The immediate effect of this result for the Plaintiffs is measurable. Many investors in GSE stock, especially common stockholders, were smaller community banks and pension funds.[186] Market reactions to Judge Lamberth's ruling are powerful indicators of what shareholders stand to lose if their bid to nullify the Third Amendment is ultimately unsuccessful. The day after the cases were dismissed, preferred shares in the GSEs with an approximately $33 billion face-value lost over 50% of their value, while common shares of Fannie Mae and Freddie Mac dropped 37% and 38%, respectively.[187] The favorable regulatory treatment (and categorization as Tier 1 capital) of investments in GSE securities induced many investors seeking stable and safe stocks to choose GSE common and preferred shares.[188] Consequently, although sophisticated financiers like Perry may be assuming the mantle for investors in GSE stock, a negative result could have a drastic effect on smaller regional and community institutions.

As is often the case with litigation involving federal agencies and great recession bailouts, opinions are mixed on whether the dismissal is the proper and just outcome.[189] Although some maintain that "[t]he investors may have no better luck on appeal,"[190] others believe that the dismissal was a "misguided blockbuster,"[191] and that

185. Plaintiff Reply, *supra* note 65, at 2 (citation omitted).

186. *See Investor Rights*, INVESTORS UNITE, http://investorsunite.org/the-issues/investor-rights.

187. Margaret Cronin Fisk, *Perry Capital Appeals Fannie Mae, Freddie Mac Bailout Ruling*, BLOOMBERG (Oct. 2, 2014, 9:01 PM), http://www.bloomberg.com/news/2014-10-02/perry-capital-appeals-Fannie Mae-Freddie Mac-bailout-ruling.html.

188. *See id.* (citing Press Release, U.S. Treasury Dep't Office of Pub. Affairs, *supra* note 36).

189. *See* Richard Epstein, *The WSJ's Improbable Defense of Judge Lamberth's Indefensible Decision in Perry Capital*, FORBES (Oct. 2, 2014, 1:49 PM), http://www.forbes.com/sites/richardepstein/2014/10/02/godzilla-versus-the-thing-the-wall-street-journals-improbable-defense-of-judge-lamberths-indefensible-decision-in-perry-capital (arguing that the decision was wrong and that the Wall Street Journal misinterpreted the ruling and its precedential value). *But see Godzilla Defeats the Thing*, WALL ST. J. (Oct. 2, 2014, 6:51 PM), http://online.wsj.com/articles/godzilla-defeats-the-thing-1412204855 (recounting the decision and arguing that it represents a blow to other plaintiffs and is a victory for U.S. taxpayers).

190. Fisk, *supra* note 187 (quoting Professor Peter Henning, Wayne State University).

191. Richard Epstein, *Will Fannie and Freddie Shareholders Be Able to Set Aside the Third Amendment? Judge Royce Lamberth's Indefensible Decision Is Only One Battle in a Long War*, FORBES (Sept. 30, 2014, 4:59 PM),

"[p]ortions of Lamberth's decision may be vulnerable on appeal."[192] Appealing the district court's ruling will be "a lengthy process,"[193] but upholding the Third Amendment by way of an unreasonably high jurisdictional bar will have far-reaching negative implications for the rule of law.[194]

V. CONCLUSION

As Perry's dismissal in district court demonstrated, HERA's anti-injunction provision is a crucial threshold in the analysis of claims brought against the Government under the APA.[195] While Judge Lamberth's interpretation of HERA's anti-injunction provision appears infallible, it may not be decisive.[196] Judge Sweeney, presiding over dividend sweep litigation in the Court of Federal Claims has continued to grant discovery requests made by the plaintiffs while the case moves closer to trial.[197] Judge Sweeney, citing the same cases and reasoning as Judge Lamberth, seems more able to envision a scenario in which HERA's anti-injunction provision does not bar those plaintiffs' claims.[198] Although the final outcome of dividend sweep litigation is anyone's call, it is apparent that plaintiffs bringing APA-based HERA challenges of Government action in the future have a virtually insurmountable task of clearing the HERA's anti-injunction provision's bar on judicial review.

As unfair as it may seem, Perry and the myriad other investors who felt assured that buying Fannie Mae and Freddie Mac stock was a

http://www.forbes.com/sites/richardepstein/2014/09/30/will-fannie-and-freddie-shareholders-be-able-to-set-aside-the-third-amendment-the-recent-sweeney-decision-will-not-alter-the-basic-dynamics.

192. Margaret Cronin Fisk et al., *Fannie-Freddie Investors Fight on in Court of Claims*, BLOOMBERG (Oct. 3, 2014, 3:00 AM), http://www.bloomberg.com/news/articles/2014-10-03/fannie-freddie-investors-fight-on-in-court-of-claims (attributing the statement to Professor Steven Davidoff Solomon, University of California at Berkeley School of Law).

193. *Id.* (quoting Bruce Berkowitz of Fairholme Capital Management LLC).

194. Epstein, *supra* note 189.

195. *See* Perry Capital LLC v. Lew, No. 13-1025, 2014 WL 4829559, at *6 (D.D.C. Sept. 30, 2014) (dismissing over half of the plaintiff's claims as barred categorically by the anti-injunction provision).

196. Fairholme Funds, Inc. v. United States, 117 Fed. Cl. 365, 367 (2014).

197. *Id.*

198. *Id.* at 367 ("[B]lanket assertions concerning the court's ability to conduct these proceedings . . . hold no merit.").

safe investment[199] are unlikely to prevail against the government on appeal with APA-based claims. This is not because Perry and other dividend sweep litigation plaintiffs have meritless cases.[200] It is the overly broad anti-injunction provision that will likely prevent judicial review of the best substantive arguments available to dividend sweep litigants bringing claims under the APA.[201]

Dividend sweep litigation may hold additional implications for federal administrative agency powers, especially in the context of conservatorships. If the FHFA, as conservator, can exercise the broadest discretion in running the GSEs—surrendering all positive net worth to the Treasury while purporting to "conserve their assets," then the definitional distinctions between conservators and receivers would vanish.[202] The FHFA, in abdication of its duties as conservator of the GSEs, ensured that they would never retain their earnings, build capital, or leave the clutches of its conservatorship—except by receivership or an act of Congress.[203] By claiming the Third Amendment necessary to avoid insolvency, the FHFA seems to have ensured that the GSEs will never escape conservatorship, and will continue to operate as a cash-cow for the federal government.[204] If allowed to evade real judicial scrutiny, agencies acting as conservators might be allowed free-reign to operate companies in conservatorship—altering deals as it pleases.

199. The government admitted as much in the press release regarding the need for the initial senior preferred stock purchase agreement. "Investors have purchased securities of [Fannie Mae and Freddie Mac] in part because the ambiguities in their Congressional charters created a perception of government backing." Press Release, U.S. Treasury Dep't Office of Pub. Affairs, *supra* note 36.

200. *See supra* Part IV.A.1.

201. *See supra* Part IV.B.

202. *See* Plaintiff Reply, *supra* note 65, at 3 ("[The] FHFA's argument that it may 'wind down' the [GSEs] in preparation for liquidation collapses any distinction between receivers and conservators.").

203. Press Release, U.S. Treasury Dep't Office of Pub. Affairs, Treasury Department Announces Further Steps to Expedite Wind Down of Fannie Mae and Freddie Mac (Aug. 17, 2012), http://www.treasury.gov/press-center/press-releases/Pages/tg1684.aspx (promising that "every dollar of earnings that Fannie Mae and Freddie Mac generate will be used to benefit taxpayers for their investment in those firms . . . and [Fannie Mae and Freddie Mac] will not be allowed to retain profits, rebuild capital, [or] return to the market in their prior form").

204. The Third Amendment ensured that Fannie Mae and Freddie Mac's return to profitability would benefit taxpayers at the expense of the private shareholders in Fannie Mae and Freddie Mac. Conservators are charged with nursing troubled firms back to health and return them to private enterprise, to the extent possible. The FHFA ensured that Fannie Mae and Freddie Mac could never satisfy its obligations to the Treasury and return to the private sector.

This result is unacceptable in the financial world. Predictability and adherence to statutory mandates and intent must be favored if governmental intervention in the private sector is to persist. Investors must be able to reasonably predict the ramifications of governmental intervention in private enterprise. A conservator who is allowed to exercise such boundless power to shape a private company's destiny at whim will begin to look less like the noble savior Anakin Skywalker and more like Darth Vader.

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