Collins v. Yellen, Secretary of Treasury

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COLLINS V. YELLEN, SECRETARY OF TREASURY

Collins v. Yellen, Secretary of Treasury , decided by a 7–2 vote, June 23, 2021; Alito wrote the opinion; Sotomayor and Breyer dissented in part.

Congress may not restrict the president's power to remove the head of the Federal Housing Finance Agency (FHFA), but lower courts had to determine whether shareholders of two mortgage finance companies regulated by the agency could reverse actions taken by the agency's past directors to divert the companies' profits to the U.S. Treasury.

The bifurcated ruling was a setback for public shareholders of the private government-chartered corporations known respectively as Fannie Mae and Freddie Mac (the Federal National Mortgage Association and the Federal Home Loan Mortgage Corporation) who were seeking to reverse the agency's previous decisions as conservator to divert the companies' profits to the U.S. Treasury.

The Court divided 6–3 on the presidential power issue, but the justices agreed unanimously that the agency had not exceeded its statutory authority in diverting the companies' profits to the U.S. Treasury as dividends for a four-year period starting in 2013.

The ruling sent the plaintiffs back to the lower courts to try to prove that they had suffered losses from implementation of the dividend requirements by the agency's past directors. The decision was a significant setback to shareholders of the companies in their long-running challenge to actions that they alleged significantly impaired the value of their holdings.

The litigation, initiated by shareholders in fall 2016, arose under the Housing and Economic Recovery Act of 2008 as adopted by Congress in the wake of the 2008 financial crisis. Together, Fannie Mae and Freddie Mac served as two of the nation's main sources of home mortgage financing. By 2007, the two companies together owned almost $5 trillion of residential mortgage-backed securities; they suffered historic losses on their securities portfolios when the residential housing bubble burst in 2008 ($108 billion in 2008 alone).

Fearing the possible collapse of these companies and unknowable disruption to the housing market, Congress created the FHFA as "an independent agency" to regulate the two companies and ensure their financial stability. The agency was to be headed by a single director appointed by the president subject to Senate confirmation and removable only "for cause" and was authorized, if necessary, to act as conservator to restore them to financial health or to supervise their liquidation.

The Recovery Act also initially authorized the U.S. Treasury to invest up to $100 billion in each of the two companies. Importantly for the ensuing litigation, the Recovery Act also contained an anti-injunction clause, codified at 12 U.S.C. §4617(f), providing that "no court may take any action to restrain or affect the exercise of powers or functions of the Agency [i.e., FHFA] as a conservator."

FHFA placed both companies into conservatorship on September 6, 2008, and the next day entered into financing agreements with the Treasury under which the Treasury committed to invest up to $100 billion in each company in exchange for preferred stock, warrants for 79.9 percent of their common stock and periodic commitment fees. The preferred stock initially entitled the Treasury to dividends in the amount of 10 percent of its investment from time to time.

When Treasury's initial commitments proved inadequate, the FHFA and Treasury amended their agreements in May 2009 and again in December 2009 to increase the amounts Treasury was able to invest. After the companies were repeatedly unable to pay their required dividends from earnings, the FHFA and Treasury amended their agreements for a third time in August 2012, replacing the fixed dividend requirements with a variable dividend equal to the entire net worth of each company in excess of a specified capital reserve. The agreement also provided that the companies need not pay dividends to the Treasury if they did not generate a surplus in a given year.

The companies' financial performance improved after the third amendment went into effect. They were required, under the so-called "net worth sweep," to transfer approximately $200 billion to the Treasury in the years 2013 through 2016. That amount greatly exceeded the dividends the companies would have been required to pay under the previous fixed rate terms.

The adoption of the third amendment gave rise to what the Supreme Court called in its eventual decision "a slew of lawsuits" by holders of the companies' outstanding securities, which remained in private hands. The case that reached the Supreme Court stemmed from a suit filed on October 20, 2016, in U.S. District Court for the Southern District of Texas by three individual shareholders—Patrick J. Collins, Marcus J. Liotta, and William M. Hitchcock—against the then secretary of the Treasury, Steven Mnuchin, and the FHFA and its then director, Melvin Watt. The shareholders claimed among other things that the agency had exceeded its statutory authority by adopting the third amendment and that the director-removal provision of the statute was an unconstitutional limit on the president's powers.

These shareholders asked for various forms of declaratory and injunctive relief, including orders vacating and setting aside the third amendment and directing the Treasury to return to Fannie and Freddie all the dividend payments that had been made under the third amendment or to treat them as payments in redemption of the government's preferred stock.

Senior Judge Nancy F. Atlas, sitting in Houston, dismissed the Texas plaintiffs' statutory claim and granted summary judgment in favor of the FHFA on the constitutional claim on May 22, 2017. After an appeal to a three-judge panel of the U.S. Court of Appeals for the Fifth Circuit, the case was reheard en banc by the Fifth Circuit, which reversed the district court's dismissal of the statutory claim in an opinion issued on September 6, 2019. A different majority of the appeals court also held that the FHFA's structure violated the separation of powers and ordered the removal restriction severed from the balance of the statute, but declined to vacate and set aside the third amendment.

The individual plaintiffs and the federal parties asked the Supreme Court to review the decision in petitions for certiorari filed respectively on September 25, 2019, and October 25, 2019. The Court granted both petitions on July 9, 2020. The Court consolidated the two cases for purposes of argument and, after the Trump administration declined to defend the constitutionality of the director-removal provision, appointed Utah attorney Aaron Nielson to do so. The Court heard oral argument on December 9, 2020.

In a slightly fractured decision with two justices dissenting in part, the Supreme Court held that the for-cause restriction on the president's power to remove the director of the FHFA was unconstitutional and that plaintiffs challenging actions by the FHFA's director might be entitled to retrospective relief if any of the director's actions inflicted compensable harm. On a less divisive issue, Alito concluded on behalf of all nine justices that the FHFA had acted within its statutory authority as conservator in diverting the companies' profits to the U.S. Treasury.

Writing for five justices and for four others in most of his thirty-six-page opinion, Alito began by recounting the history of the 2008 financial crisis, the adoption of the Recovery Act, and the FHFA's powers. He then addressed the shareholders' claims based on violation of the statute and asked whether they should be barred by the statute's anti-injunction clause. He noted that the act's anti-injunction clause applied only when the FHFA was exercising its powers or functions "as a conservator or receiver." On that basis, he concluded that the first question to be decided was "whether the FHFA was exercising its powers or functions as a conservator when it agreed to the third amendment."

The FHFA's mission in acting as a conservator, Alito explained, was rehabilitation—"to put the regulated entity in a sound and solvent condition." He added, however, that an FHFA conservatorship "differs from a typical conservatorship in a key respect." He then elaborated on the difference. "Instead of mandating that the FHFA always act in the best interests of the regulated entity," Alito wrote, "the Recovery Act authorizes the Agency to act in what it determines is 'in the best interest of the regulated entity or the Agency.'"

Alito acknowledged that the third amendment prevented the companies from accumulating any profits, but also meant that the companies had no further need for capital from the Treasury's investment commitment to satisfy their preferred stock dividend obligations. "And that," he explained, "ensured that all of Treasury's capital was available to backstop the companies' operations during difficult quarters" and thus support the nation's housing market.

"Whether or not this new arrangement was in the best interests of the companies or their shareholders," Alito continued, "the FHFA could have reasonably concluded that it was in the best interests of members of the public who rely on a stable secondary mortgage market." On that basis, he concluded that the FHFA was acting within its statutory authority when it entered into the third amendment and the anti-injunction clause barred the shareholders' statutory claims.

On the constitutional issue, Alito concluded that the for-cause restriction on the president's authority to remove the FHFA director "violates the separation of powers" based on what he called "a straightforward application" of the Court's decision in the previous term invalidating a similar provision regarding the head of what he called another "independent agency led by a single Director." The Court's decision in that case, *Seila Law LLC v. Consumer Financial Protection Bureau* (2020), was on a 5–4 vote divided along conservative–liberal lines.

Unlimited removal authority, Alito explained, helps the president maintain a degree of control over subordinates and thus "is essential to subject Executive Branch actions to a degree of electoral accountability," a principle that applies "whenever an agency does important work."

On the question of remedies for the shareholders, Alito voiced doubts but left open the possibility that they were entitled to some relief. "[T]he shareholders nevertheless claim that the unconstitutional removal provision inflicted harm," he explained. "Were it not for that provision, they suggest, the President might have replaced one of the confirmed Directors who supervised the implementation of the third amendment, or a confirmed Director might have altered his behavior in a way that would have benefited the shareholders."

Four justices joined Alito's opinion in full: Roberts, Thomas, Kavanaugh, and Barrett. In separate opinions, Thomas wrote a concurring opinion; Gorsuch wrote an opinion concurring in part. Kagan wrote an opinion for the three liberal justices concurring in part and concurring in the judgment. Sotomayor wrote a separate opinion concurring in part and dissenting in part.

In his opinion, Thomas voiced doubts that the plaintiffs were entitled to any relief. By contrast, Gorsuch concluded that the plaintiffs were entitled to relief; he did not join the part of Alito's opinion finding the plaintiffs only possibly entitled to relief.

In her partial concurrence for the three liberal justices, Kagan concurred in finding that the FHFA had acted within its statutory authority but concurred on the director-removal issue only on the basis of precedent—specifically, the ruling in Seila Law. Kagan led four liberal justices in dissenting from that decision.

In her opinion, Sotomayor, joined by Breyer, disagreed with the decision on the director-removal provision. She noted what she called "a long tradition of independence enjoyed by financial regulators," including, among others, the Comptroller of the Currency. "All considerations," she wrote, "weigh in favor of recognizing Congress' power to make the FHFA Director removable only for cause."

The decision affirmed the Fifth Circuit's judgment in part, reversed the judgment in part, vacated the judgment in part, and remanded the case for "further proceedings consistent with this opinion."

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