

Summary of the Supreme Court's Decision in *Collins v. Yellen* June 23, 2021

Key Takeaways:

- The Supreme Court found that the Federal Housing Finance Agency's (FHFA) structure, with a single director removable only for cause, violates the Constitution's separation of powers scheme. A President can thus remove the FHFA Director before the end of his or her statutory five year term.
- The Court also held that because the Agency did not exceed its authority under the Housing and Economic Recovery Act of 2008 ("Recovery Act") as conservator of Fannie Mae and Freddie Mac, the anti-injunction provisions of the Act bar the statutory claim brought by shareholders of those entities. The Court therefore denied relief on the shareholders' statutory claim.
- The Court remanded the case back to the lower court to determine whether the unconstitutional removal provision inflicted compensable harm.

Case History: Shortly after the FHFA was created, it placed Fannie Mae and Freddie Mac into conservatorship and negotiated agreements to take control of the companies with the Department of Treasury. Later, the FHFA and Treasury amended the agreements and replaced the prior fixed-rate dividend formula with a variable one that required the companies to make quarterly payments to Treasury consisting of their entire net worth minus a small, specified capital reserve. This deal is referred to as the "third amendment" or "net worth sweep." A group of Fannie Mae and Freddie Mac's shareholders challenged the third amendment on statutory and constitutional grounds. The District Court dismissed the statutory claim and granted summary judgment in favor of the FHFA on the constitutional claim. A three-judge panel of the Fifth Circuit Court of Appeals affirmed in part and reversed in part. The Fifth Circuit then heard the case en banc and reversed the District Court's dismissal of the statutory claim. It further held that the FHFA's structure violated the separation of powers. Both parties sought review and the Supreme Court agreed to hear the appeal.

Issues: The opinion considers two issues.

- (1) Constitutional Claim: Does the FHFA's leadership by a single Director removable only for-cause violate the Constitution's required separation of powers?
- (2) Statutory Claim: Did the FHFA exceed its authority as a conservator under the Recovery Act by agreeing to the new variable dividend formula (the third amendment)?

Majority Opinion: The majority opinion was authored by Justice Alito, and joined by Roberts, Thomas, Kavanaugh, and Barrett in full, Kagan, Breyer, Gorsuch and Sotomayor joined in part. Thomas and Kagan filed a concurring opinion, and Sotomayor filed an opinion concurring in part and dissenting in part, which Breyer joined. On the constitutional claim, Alito was joined by Roberts, Thomas, Kavanaugh, Barrett in full, and Kagan and Gorsuch concurring in the judgment.

Constitutional Claim:

Justice Alito first concluded that the shareholders had standing to sue, and then further held that the constitutional challenge could proceed even though the FHFA was led by an Acting Director, as opposed to Senate-confirmed Director, at the time the third amendment was adopted. As Alito explains, the harm allegedly caused by the third amendment did not end during the tenure of the Acting Director who was in office when the amendment was adopted, but rather the harm was alleged to have continued after the Acting Director was replaced by a succession of confirmed directors. Because confirmed Directors chose to continue implementing the third amendment while insulated from Presidential control, the survival of the shareholders' constitutional claim does not depend on whether the Recovery Act restricted the removal of an Acting Director. The answer to that question could, however, have a bearing on the scope of relief that may be awarded to the shareholders, as explained later in the summary.

The majority opinion then concluded that the Recovery Act's for-cause restriction on the President's removal authority violates the Constitution's separation of powers scheme, relying on last year's decision in *Seila Law v. CFPB*. The Court explained that like the Consumer Financial Protection Bureau (CFPB), the FHFA is an agency led by a single director, and the Housing and Economic Recovery Act of 2008 (the "Recovery Act," also commonly referred to as "HERA"), like Dodd-Frank, restricts the President's removal power. In *Seila*, the Court held that Congress could not limit the President's power to remove the Director of the CFPB to instances of "inefficiency, neglect, or malfeasance," and Justice Alito therefore determined that the *Seila* decision dictates a similar result here.

Justice Alito then addressed and ultimately rejected distinctions between the FHFA and CFPB drawn by Court-appointed amicus attempting to justify a different result. The first distinction was that the FHFA has more limited authority than the CFPB as FHFA administers one statute compared to the nineteen under the CFPB, FHFA regulates government-sponsored enterprises while the CFPB regulates millions of individuals and businesses, and the FHFA receives a smaller budget. Justice Alito dismissed this, explaining that the nature and breadth of an agency's authority is not dispositive in determining whether Congress may limit the President's power to remove its head. Moreover, practical problems would arise without a clear standard to distinguish which agency leaders must be removable at will.

Another distinction made was that Congress may restrict the removal of the FHFA Director because when an agency steps into the shoes of a regulated entity as its conservator, it takes on the status of a private party and thus does not exercise executive power. Justice Alito rejected this theory as well, explaining that not only does the Agency not always act in such capacity, but its authority stems from a special statute, not the laws that generally govern conservators and receivers and it must interpret the Recovery Act enacted by Congress, which is the very essence of the “execution of the law” that the Executive Branch is entrusted with by the Constitution. Moreover, FHFA’s powers differ critically from those of most conservators, including the ability to subordinate the best interests of the company to its own best interests and those of the public, and its business decisions are protected from judicial review.

Third, amici attempted to distinguish between *Seila* and this case since the FHFA regulates government-sponsored enterprises which have federal charters and serve public objectives, which in they argued would eliminate the individual liberty concerns. In rejecting this argument, Alito stated that the President’s removal power serves important purposes regardless of whether the agency’s actions affect ordinary Americans directly or indirectly.

Finally, Justice Alito dismissed the argument that there was no constitutional problem because the Recovery Act offers only “modest tenure protections.” He stated that the Constitution prohibits even “modest restrictions” on the President’s power to remove the head of an agency with a single top officer. Therefore, the FHFA’s leadership structure is unconstitutional because the Court had previously determined that a single-director, for-cause removal provision violates the separation of powers, and no distinctions were sufficient to justify a different result.

Statutory Claim: In addressing the shareholders’ statutory claim, Justice Alito started by explaining that in the Recovery Act Congress sharply circumscribed judicial review of any action that the FHFA takes as a conservator or receiver. As the Act states, unless review is specifically authorized by one of its provisions or is requested by the Director, “no court may take any action to restrain or affect the exercise of powers or functions of the Agency as a conservator or a receiver.” Alito then went on to demonstrate that every Court of Appeals confronted with this language has held that it prohibits relief where the FHFA action at issue fell within the scope the agency’s authority as a conservator, and relief is allowed only if FHFA exceeded that authority. The anti-injunction clause applies only where the FHFA exercised its powers or functions as a conservator or receiver. Therefore, Alito explains, the court must decide whether the FHFA was exercising its powers as a conservator when it agreed to the third amendment. If it was, then the anti-injunction clause bars the shareholders’ statutory claim.

In addressing this question, Justice Alito rests his decision on the notion that an FHFA conservatorship differs from a typical conservatorship in a key respect. Instead of

mandating that the FHFA always act in the best interests of the regulated entity, the Recovery Act authorizes the Agency to act in what it determines is “in the best interests of the regulated entity or the Agency.” Therefore, when the FHFA acts as a conservator, it may aim to rehabilitate the regulated entity in a way that, while not in the best interests of the regulated entity, is beneficial to the agency, and by extension, the public it serves. Whether or not the third amendment was in the best interests of the companies or their shareholders, the FHFA could have reasonably concluded that it was in the best interests of the members of the public who rely on a stable secondary mortgage market. The Recovery Act therefore authorized the agency to choose this option.

Alito further explained that it is not necessary for the Court to decide whether the FHFA made the best business decision when it adopted the third amendment. Rather, the Court’s sole inquiry was to conclude whether FHFA exceeded its authority as a conservator under the terms of the Recovery Act. By determining that it did not, the anti-injunction clause bars the shareholders’ statutory claim.

Remedy: In determining the appropriate remedy, the Court rejected the shareholders’ argument that the third amendment must be considered void. The Court rejected this argument because the Acting Director, who entered into the agreement, was removable at will. Therefore, the only contention about remedy is with respect to the actions that the confirmed Directors have taken to implement the third amendment during their tenures. Because all officers during the time in question were properly appointed, there is no reason to regard any actions taken by the FHFA in relation to the third amendment as void. The Court then explains that the only determination it must make was whether the unconstitutional *removal* restriction caused any compensable harm. The Court concluded that there is a possibility that the unconstitutional restriction might have inflicted harm, citing the possibility that the President may have replaced one of the confirmed directors who supervised the implementation of the third amendment. The Court therefore remanded the case to the lower court to resolve this remaining issue.

If you have any questions, please contact:

Justin Wiseman
Associate Vice President,
Managing Regulatory Counsel
(202) 557-2854
jwiseman@mba.org

Blake Chavis
Assistant Regulatory Counsel
(202) 557-2930
bchavis@mba.org

Lucia Jacangelo
Regulatory Specialist
(202) 557-2941
ljacangelo@mba.org