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FAIRHOLME PROVIDES UPDATE ON FANNIE MAE AND FREDDIE MAC

MIAMI, FL – Last week, Fannie Mae and Freddie Mac reported annual net income of $12.3 billion and $7.8 billion, respectively. This remarkable performance – their fifth straight year of positive earnings, with growing books of business – is further proof that these indispensable mortgage insurers have been successfully rehabilitated. Fannie Mae and Freddie Mac are fulfilling their historic role of ensuring adequate levels of liquidity to lenders of all sizes. In 2016, Fannie Mae and Freddie Mac provided almost $1.1 *trillion* in mortgage financing to America's housing market, enabling millions of American families to buy, refinance, or rent homes. Today, after eight long years in federal conservatorship, Fannie Mae and Freddie Mac stand irreversibly transformed: both companies are back to basics, squarely focused on executing their core mission of providing liquidity, access to credit, and affordability to qualified borrowers in all U.S. housing markets at all times. No one does it better.

Despite their robust profitability and significant operational improvements, the Federal Housing Finance Agency ("FHFA"), in its capacity as conservator, "sabotage[d] the Companies' recovery by confiscating their assets quarterly to ensure they cannot pay off their crippling indebtedness."[1] By imposing the so-called "Net Worth Sweep" on Fannie Mae and Freddie Mac in August 2012, FHFA enabled the United States Treasury "to loot the Companies to the guaranteed exclusion of all other investors."[2] These statements, attributable to Judge Janice Rogers Brown in a split decision issued yesterday by the United States Court of Appeals for the District of Columbia Circuit (the "Court"), accurately reflect the basis for our legal actions against the government.

In that February 21st Opinion, the Court was divided 2-1 on a case in which we sought to protect our rights as Fannie Mae and Freddie Mac preferred shareholders. We have long maintained that the Net Worth Sweep impermissibly eliminates the rights of preferred shareholders to any return *of* their principal (i.e., the liquidation preference) or any return *on* their principal (i.e., dividends). In fact, since 2013 we have emphasized that this litigation seeks nothing more than the enforcement of existing rights associated with ownership of Fannie Mae and Freddie Mac preferred stock – rights that transfer with the sale of the securities. In its ruling, the Court revived and remanded for further review certain common law claims advanced by a class of plaintiffs defined as "all persons and entities who held shares . . . and who were damaged thereby"[3] – specifically that the "Net Worth Sweep" (i) violated the Companies' contractual duties to its preferred shareholders, and (ii) breached the implied covenant of good faith and fair dealing. Notably, the Court held that these claims were properly characterized as claims of repudiation (i.e., anticipatory breach) and are therefore ripe.

With respect to the separate claims brought under the Administrative Procedure Act ("APA"), we were disappointed that Judges Patricia Millett and Douglas Ginsburg refused to enjoin the Net Worth Sweep – especially since the significant amount of discovery "information recently obtained in this litigation creates, to put it mildly, a dispute of fact regarding the motivations behind FHFA and Treasury's decision to execute the Third Amendment."[4] Dissenting from the majority's decision to dismiss those APA claims, Judge Janice Rogers Brown noted that FHFA "pole vaulted over" the boundaries of its statutory authority when it agreed to the Net Worth Sweep, "disregarding the plain text of its authorizing statute and engaging in *ultra vires* conduct."[5] Judge Brown concluded that: "[T]he Net Worth Sweep fundamentally transformed the relationship between the Companies and Treasury: a 10 percent dividend became a sweep of the Companies' near-entire net worth; an in-kind dividend option disappeared in favor of cash payments; the

[1] *Perry Capital LLC v. Steven Mnuchin*, No. 14-5243, at 9, n. 1 (D.C. Cir. Feb. 21, 2017) (Brown, J., dissenting).
[2] *Id.* at 21.
[3] *Id*. at 69 (majority opinion).
[4] *Id*. at 24, n. 7 (Brown, J. dissenting).
[5] *Id*. at 4.

ability to retain capital above and beyond the required dividend payment evaporated; and, most importantly, the Companies lost any hope of repaying Treasury's liquidation preference and freeing themselves from its debt. Indeed, the capital depletion accomplished in the Third Amendment, regardless of motive, is patently incompatible with any definition of the conservator role … rendering Fannie and Freddie mere pass-through entities for huge amounts of money destined for Treasury does exactly that which FHFA has deemed impermissible."[6]

Judge Brown's well-reasoned dissenting opinion could prove persuasive in cases in which similar APA challenges to the Net Worth Sweep are pending before the United States Court of Appeals for the Sixth Circuit and federal district courts in Illinois, Iowa, and Texas.

Bruce R. Berkowitz, Chief Investment Officer of Fairholme Capital Management, stated: "The Net Worth Sweep cannot be defended on its merits, and no Court has done so. Make no mistake – this is far from over. We firmly believe that the rights of preferred shareholders in these two enormously profitable, publicly traded companies will be upheld one way or another."

Charles J. Cooper, Founding Member and Chairman of Cooper & Kirk, which represented The Fairholme Fund in the D.C. Circuit, stated: "Since the Net Worth Sweep was imposed, we have strenuously resisted the government's attempted confiscation of our client's property rights and economic interests. No conservator, state or federal, has ever acted in a manner even remotely similar to how FHFA has conducted itself here. We are continuing to evaluate the implications of yesterday's decision, but at a minimum, it certainly strengthens our conviction that the Net Worth Sweep amounted to a taking of property in violation of the Fifth Amendment."

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[6] *Id*. at 24.