UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF MINNESOTA

NICHOLE WILLIAMS, et al., Plaintiffs, vs. TIMOTHY GEITHNER, et al., Defendants.	Case No.: 09-CV-01959 ADM JJG

DEFENDANT FEDERAL HOUSING FINANCE AGENCY'S MEMORANDUM OF LAW IN SUPPORT OF MOTION TO DISMISS THE PLAINTIFFS' FIRST AMENDED CLASS ACTION COMPLAINT

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Plaintiffs' due process claims against FHFA as a federal agency and as Conservator of Fannie Mae and Freddie Mac fail as a matter of law. First, Plaintiffs utterly fail to demonstrate that loan modifications under HAMP are constitutionally protected property rights. In fact, no statute or directive provides Plaintiffs with anything more than an opportunity to apply for modifications that are subject to complex and individualized determinations made by private servicers. Plaintiffs similarly fail to demonstrate that those private servicers are state actors or that the government actors made any determinations denying HAMP modifications. Finally, Plaintiffs fail to allege that the process already afforded is constitutionally deficient. Accordingly, Plaintiffs' First Amended Complaint should be dismissed in its entirety.

BACKGROUND

A. Procedural History

On July 28, 2009, Plaintiffs instituted this action by filing a Complaint and Motion for Preliminary Injunction ("Pl. Br."), requesting declaratory and injunctive relief against the Federal Housing Finance Agency ("FHFA" or "Conservator"), Secretary of the Treasury, Federal National Mortgage Association ("Fannie Mae"), Federal National Home Loan Mortgage Corporation ("Freddie Mac") (together with Fannie Mae, the "Enterprises" or "GSEs") and three loan servicers. Three weeks later, on August 17, 2009, Plaintiffs filed a First Amended Class Action Complaint ("FAC"). In the FAC, Plaintiffs allege to have a constitutionally protected property interest in receiving a loan modification pursuant to the Home Affordable Modification Program ("HAMP").

See, e.g., FAC ¶ 6. Furthermore, Plaintiffs claim to be entitled to notice and a hearing in the event that their request for a modification is denied by the loan servicer.

On September 16, 2009, FHFA ("FHFA Opp."), Treasury ("Treas. Opp."), Fannie Mae and Freddie Mac jointly ("GSE Opp."), and each loan servicer filed memoranda in opposition to Plaintiffs' motion for preliminary injunction. All Defendants argued that Plaintiffs could not satisfy the four-factor test articulated by the Eighth Circuit in *Dataphase Systems, Inc. v. CL Systems, Inc.*, 640 F.2d 109, 114 (8th Cir. 1981) (en banc) necessary for the issuance of a preliminary injunction. Subsequently, on September 25, 2009, Plaintiffs filed their Reply in support of a preliminary injunction. This court heard oral argument on the motions for preliminary injunction on October 15, 2009.

B. The Role Of FHFA As Conservator Of Fannie Mae And Freddie Mac

On July 30, 2008, Congress passed the Housing and Economic Recovery Act of 2008 ("HERA"), Pub. L. No. 110-289, 122 Stat. 2654, thereby creating FHFA as an independent federal agency. Pursuant to HERA, FHFA succeeded to the authorities previously granted to both the Office of Federal Housing Enterprise Oversight ("OFHEO") and the Federal Housing Finance Board ("FHFB"), and the Agency now serves as the sole regulatory and oversight authority for Fannie Mae, Freddie Mac, and the Federal Home Loan Bank System. *Id*. Among its "principal duties," FHFA is charged with examining the financial safety and soundness and overall risk management practices of Fannie Mae and Freddie Mac in order "to ensure that [] each [Enterprise] operates in a safe and sound manner, including maintenance of adequate capital and internal controls." 12 U.S.C. § 4513(a)(1)(B)(i). Furthermore, Congress granted the

Director of FHFA the authority to place the Enterprises into conservatorship or receivership "for the purpose of reorganizing, rehabilitating, or winding up the affairs of [the Enterprises]." *Id*. § 4617(a)(2). On September 7, 2008, pursuant to the authority granted under HERA, and after determining that the Enterprises could not "continue to operate safely and soundly and fulfill their critical public mission,"[1] the Director placed Fannie Mae and Freddie Mac under the conservatorship of FHFA.[2]

In its capacity as Conservator, FHFA is vested with broad statutory powers to act on behalf of and through the Enterprises. Pursuant to 12 U.S.C. § 4617(b)(2)(A)(i), upon its appointment as Conservator, FHFA "immediately succeed[ed]" to "all rights, titles, powers, and privileges of [the Enterprises], and of any stockholder, officer, or director of [the Enterprises] . . . ." In addition, pursuant to 12 U.S.C. § 4617(b)(2)(B)(i), FHFA is empowered as Conservator to:

> take over the assets of and operate [the Enterprises] with all the powers of the shareholders, the directors, and the officers of [the Enterprises] and conduct all business of [the Enterprises].

[1] Statement of FHFA Dir. James B. Lockhart, 5 (Sept. 7, 2008), *available at* http://www.fhfa.gov/webfiles/23/FHFAStatement9708final.pdf.

[2] *Id.* at 5-6. The Director's actions were widely supported by other senior U.S. officials, including the Treasury Secretary and the Chairman of the Federal Reserve Board, both of whom stated publicly that placing Fannie Mae and Freddie Mac into FHFA Conservatorships was an action necessary to promote stability in the U.S. housing and financial markets. *See* Statement by Sec'y Henry M. Paulson, Jr. on Treasury and Federal Housing Finance Agency Action to Protect Financial Markets and Taxpayers (Sept. 7, 2008), *available at* http://www.treas.gov/press/releases/hp1129.htm; Statement by Fed. Reserve Bd. Chairman Ben S. Bernanke (Sept. 7, 2008), *available at* http://www.federalreserve.gov/newsevents/press/other/20080907a.htm.

FHFA is entitled to exercise these powers to "preserve and conserve the assets and property of [the Enterprises]." *Id.* § 4617(b)(2)(B)(iv). Furthermore, FHFA is statutorily empowered to:

- "collect all obligations and money due the [Enterprises]," *id.* § 4617(b)(2)(B)(ii);
- "perform all functions of the [Enterprises]," *id.* § 4617(b)(2)(B)(iii);
- "take any such action as may be [] necessary to put the regulated entity in a sound and solvent condition; and [] appropriate to carry on the business of the [Enterprises] and preserve and conserve the assets and property of the [Enterprises]," *id.* § 4617(b)(2)(D)(i)-(ii);
- "transfer or sell any asset or liability of the [Enterprises] in default, and []do so without any approval, assignment, or consent with respect to such transfer or sale," *id.* § 4617(b)(2)(G);
- "exercise all powers and authorities specifically granted to conservators . . . and such incidental powers as shall be necessary to carry out such powers," *id.* § 4617(b)(2)(J)(i); and
- "take any action authorized by this section, which the Agency determines is in the best interests of the [Enterprises] or the Agency," *id.* § 4617(b)(2)(J)(ii).

To provide the Conservator with the broadest possible latitude to exercise its statutory duties and to preserve and conserve the assets of the Enterprises without interference, Congress expressly prohibited judicial review of the Conservator's statutorily authorized powers: "*[N]o court may take any action to restrain or affect the exercise of powers or functions of [FHFA] as a conservator*." *Id.* § 4617(f) (emphasis added).

C. HAMP

The Emergency Economic Stabilization Act of 2008 ("EESA"), Pub. L. No. 110-343, 122 Stat. 3765, provides for FHFA, in its role as Conservator for the Enterprises, to seek to assist homeowners to avoid foreclosure. The relevant section reads, in pertinent part:

> To the extent that [FHFA, as Conservator for the Enterprises,] holds, owns, or controls mortgages, mortgage backed securities, and other assets secured by residential real estate, including multifamily housing, [FHFA] shall implement a plan *that seeks to* maximize assistance for homeowners and use its authority to encourage the servicers of the underlying mortgages, and considering net present value to the taxpayer, to take advantage of the HOPE for Homeowners Program under section 257 of the National Housing Act or other available programs to minimize foreclosures.

12 U.S.C. § 5220(b)(1) (emphasis added). EESA states that "[i]n developing the plan required by this subsection, the Federal property managers [including FHFA] shall consult with one another and, *to the extent possible*, utilize consistent approaches to implement the requirements of this subsection." 12 U.S.C. § 5220(b)(6) (emphasis added).

With respect to loans not owned by the Enterprises, EESA's directive requires FHFA to "encourage" modifications by the servicers but does not require them. EESA states:

> In any case in which a Federal property manager is not the owner of a residential mortgage loan, but holds an interest in obligations or pools of obligations secured by residential mortgage loans, the Federal property manager shall – (1) encourage implementation by the loan servicers of loan modifications developed under subsection (b); and (2) assist in facilitating any such modifications, to the extent possible.

12 U.S.C. § 5220(c).

Further, in the subsection entitled "Limitation," Congress explicitly limited the effect of EESA on any of FHFA's existing duties and responsibilities, stating: "[t]he requirements of this section shall not supersede any other duty or requirement imposed on [FHFA] under otherwise applicable law." 12 U.S.C. § 5220(d). Accordingly, EESA does not supersede any of the duties imposed on FHFA by HERA, including the duty to "to preserve and conserve the assets and property of [the Enterprises]" and the other duties enumerated above. Nor does EESA vitiate HERA's bar on judicial interference with the Conservator's activities.

On February 18, 2009, President Obama announced the creation of the Homeowner Affordability and Stability Plan, which is designed to help between 7 million and 9 million homeowners avoid foreclosure. *See* Treasury Department, Supplemental Directive 09-01 (Apr. 6, 2009) (FAC Exhibit E (Docket No. 28)) ("Supplemental Directive 09-01"). As part of that plan, and pursuant to EESA, Treasury, in conjunction with FHFA and other federal agencies, developed HAMP. HAMP guidelines for loans owned by Fannie Mae and Freddie Mac ("GSE loans") were incorporated into Fannie Mae's and Freddie Mac's agreements with the servicers of their loans. For loans not owned by the GSEs, servicers of non-GSE loans entered into contracts with Fannie Mae as Treasury's financial agent in order to be eligible for incentive payments under the program.

The Conservator incorporates herein the description of HAMP contained in the Memorandum of Law of Defendants Federal National Mortgage Association (d/b/a

Fannie Mae) and Federal Home Loan Mortgage Corporation (d/b/a Freddie Mac) in Support of Motion to Dismiss the First Amended Complaint ("Enterprises Br."). As described therein and in the Plaintiffs' FAC, borrowers apply for HAMP modifications directly with the servicers of their loans and the private servicers make determinations regarding eligibility for HAMP. *See, e.g.*, FAC ¶¶ 126-31. Borrowers must meet certain initial eligibility criteria for HAMP. *See* Supplemental Directive 09-01 at 2-3. Those criteria include the requirement that the loan is "delinquent or default is reasonably foreseeable." *Id.* at 2. The servicer makes the determination of whether default is "reasonably foreseeable" (i.e. "imminent") based on the "servicer's standards for imminent default consistent with applicable contractual agreements and accounting standards." *Id.* at 4. If a borrower meets the initial eligibility requirements, the servicer must provide a Trial Period Plan unless certain other factors are present, including (1) a prohibition contained in an applicable investor servicing agreement or pooling and servicing agreement for which reasonable efforts to remove the prohibitions were unsuccessful, *see id.* at 1; (2) a determination by the servicer that the net present value (NPV) of the loan as modified would be less than the NPV of the loan without a modification, *see id.* at 4-5; (3) the modification waterfall steps do not yield a monthly mortgage payment of 31% the borrowers' gross income, *see id.* at 8-10. If the Trial Period Plan is offered, the borrower stays current and the servicer verifies the borrower's eligibility, the servicer must make the permanent modification. *Id.* at 14-15, 17-18.

The Enterprises employ the same initial eligibility criteria as the Treasury guidelines. *See* Enterprises Br. at 9-10. Under the GSE guidelines, even if a borrower

meets the initial eligibility criteria, a modification will not be provided if application of the modification waterfall does not achieve the 31% target monthly mortgage payment. *See* Fannie Mae Announcement 09-05R (Apr. 21, 2009) (FAC Exhibit C) at 10-11; Freddie Mac Single Family Seller/Servicer Guide (FAC Exhibit D) at Ch. C65.6(b). Furthermore, modifications are not allowed where forbearance of principal pursuant to the modification waterfall would yield a lower principal amount than the value of the home securing the mortgage. *See* Fannie Mae Announcement 09-05R (Apr. 21, 2009) (FAC Exhibit C) at 11; Freddie Mac Single Family Seller/Servicer Guide (FAC Exhibit D) at Ch. C65.6(a).

If a borrower meets the initial eligibility requirements and is offered a Trial Period Plan and is determined ineligible for a modification based on verified income levels, servicers are required to provide notice to the borrower. *See* Supplemental Directive 09-01 at 18 (if, based on verified income, the borrower is not eligible for a modification, "the servicer must notify the borrower of that determination"). Servicers are also required to investigate complaints made by borrowers and to ensure that "complaints are provided fair consideration, and timely and appropriate responses and resolution." *Id.* at 13. Applicants may seek free housing counseling from certified housing counselors or elevate their concerns to the HAMP Support Center (for non-GSE loans) or to Fannie Mae or Freddie Mac directly (for GSE loans). *See* Treas. Opp. at 11-13; GSE Opp. at 11-12, 29. Furthermore, Treasury has "established denial codes that require servicers to

report the reason for modification denials in writing to Treasury"[3] and will "require servicers to use those denial codes as a uniform basis for sending letters to borrowers who were evaluated for HAMP but denied a modification."[4]

HAMP is projected to prevent foreclosure of 3 million to 4 million homes by reducing monthly mortgage payments. According to recent testimony before the Congressional Oversight Panel, as of September 30, 2009, "more than 757,955 trial modifications have been offered under HAMP, and as of October 8th, more than 500,000 trial modifications are underway."[5]

ARGUMENT

Plaintiffs entirely fail to assert viable constitutional due process claims. The loan modifications determined by private servicers under HAMP are not an entitlement; the parties that make determinations regarding eligibility for loan modifications are private parties, and thus alleged deprivations cannot meet the element of state action required by law; and the existing procedural protections afforded are constitutionally sufficient. Accordingly, Plaintiffs fail to plead claims upon which relief can be granted and this Court should dismiss this action pursuant to Rule 12(b)(6) of the Federal Rules of Civil Procedure.

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[3] *See* Herbert M. Allison, Jr., Assistant Sec'y of the Treasury for Fin. Stability of the United States, Written Testimony to the Congressional Oversight Panel (Oct. 22, 2009), *available at* http://www.treasury.gov/press/releases/tg325.htm.

[4] *Id.*

[5] *Id.*

In order to survive a motion to dismiss, "a plaintiff 'must assert facts that affirmatively and plausibly suggest that the pleader has the right he claims . . . rather than facts that are merely consistent with such a right.' " *Gregory v. Dillard's, Inc.*, 565 F.3d 464, 473 (8th Cir. 2009) (quoting *Stalley v. Catholic Health Initiatives*, 509 F.3d 517, 521 (8th Cir. 2007)). The complaint must include sufficient factual allegations to provide the grounds on which the claim rests. *Id.* Thus, a district court "need not 'conjure up unpled allegations' to save a complaint." *Id.* (quoting *Rios v. City of Del Rio*, 444 F.3d 417, 421 (5th Cir. 2006)). As set forth below, the FAC fails to sufficiently allege claims against FHFA that would entitle Plaintiffs to the relief they seek. Therefore, as a matter of law, the FAC must be dismissed pursuant to Rule 12(b)(6) of the Federal Rules of Civil Procedure.

I. Plaintiffs Do Not Possess A Constitutionally Protected Property Interest In Loan Modifications

Plaintiffs must "demonstrate that [they have] a protected liberty or property interest at stake" and that they were "deprived of such an interest without due process of law." *Marler v. Mo. State Bd. of Optometry*, 102 F.3d 1453, 1456 (8th Cir. 1996). A loan modification under HAMP does not constitute a constitutionally protected property interest because Plaintiffs are not entitled to modifications. A property interest requires " 'more than an abstract need or desire' and 'more than a unilateral expectation of [a benefit]. [A person] must, instead, have a legitimate claim of entitlement to it.' " *Town of Castle Rock, Colo. v. Gonzales*, 545 U.S. 748, 756 (2005) (quoting *Bd. of Regents v. Roth*, 408 U.S. 564, 577 (1972)). Further, "a benefit is not a protected entitlement if

government officials may grant or deny it in their discretion." *Id*. at 756 (citing *Ky. Dep't of Corr. v. Thompson*, 490 U.S. 454, 462-63 (1989)).

A. EESA Does Not Provide An Entitlement

EESA does not create an entitlement to a loan modification. Plaintiffs allege only that FHFA was required to create and implement a plan to prevent foreclosures. *See, e.g.*, FAC ¶ 105 (citing a provision of EESA for the proposition that the law requires FHFA to "implement a plan to prevent foreclosures"). A full reading of the cited provision reveals that EESA does *not* establish an entitlement to a federal benefit. That section, in full, states:

> To the extent that [FHFA, as Conservator for the Enterprises], holds, owns, or controls mortgages, mortgage backed securities, and other assets secured by residential real estate, including multifamily housing, [FHFA] shall implement a plan that seeks to maximize assistance for homeowners and use its authority *to encourage* the servicers of the underlying mortgages, and *considering net present value to the taxpayer*, to take advantage of the HOPE for Homeowners Program under section 257 of the National Housing Act or other available programs to minimize foreclosures.

12 U.S.C. § 5220(b)(1) (emphasis added); s*ee also* 12 U.S.C. § 5220(c) (encouraging modifications by servicers where loans not owned by Fannie Mae or Freddie Mac). The statute directs FHFA to "encourage the servicers" and consider "net present value to the taxpayer," leaving the government with ample discretion regarding the contours of the program and the criteria for loan modifications. The law requires the federal government to establish a program but does not require it to make any determinations or to guarantee benefits to any class of persons. Accordingly, an entitlement to benefits cannot possibly be read into EESA.

The text and legislative history of EESA further demonstrate that Congress did not intend to require the federal government to provide modifications. Legislative history reveals that Congress understood that EESA did not require any particular loan modification, but, in fact, rejected that approach. Congresswoman Jackson-Lee stated:

> [I]n Section 109, which addresses "foreclosure mitigation efforts," the language should be changed from "shall encourage" to "shall require" to provide stronger relief for Americans. Specifically, current section 109(a) states in pertinent part that "the Secretary shall implement a plan that seeks to maximize assistance for homeowners and use the authority of the Secretary to encourage the servicers of the underlying mortgages . . . to minimize foreclosures." I believe if the true intent is to bailout "Main Street," the Secretary should be required to minimize foreclosures.

154 Cong. Rec. H10702-06 (2008), 2008 WL 4449105 at *H10708; s*ee also id.* at H10712-02, 2008 WL 4449108, at *H10791 (statement of Rep. Udall) ("I believe we *could* have added provisions that . . . *required* the government to help responsible homeowners refinance their mortgages . . . .")(emphasis added).

Furthermore, the limitation provision contained in EESA's text shows that Congress did not intend to create a new set of property rights that would vitiate the broad grant of discretion afforded to the Conservator. In Section 5220(d) of the statute, entitled "Limitation," Congress purposefully limited the effect of EESA on any of FHFA's existing duties, stating: "[t]he requirements of this section shall not supersede any other duty or requirement imposed on the [FHFA] under otherwise applicable law." *Id.* EESA was signed into law on October 3, 2008, just two months after enactment of the HERA, on July 30, 2008. HERA affords the Conservator with broad powers to preserve and conserve the assets of the Enterprises under Conservatorship, including a provision

significantly limiting the role that courts may play in issuing relief that would affect the Conservator. HERA provides: "[N]o court may take any action to restrain or affect the exercise of powers or functions of [FHFA] as a conservator . . . ." 12 U.S.C. § 4617(f); s*ee also In re Fed. Nat'l Mortgage Ass'n Sec., Derivative, and "ERISA" Litig.*, 629 F. Supp. 2d 1, 4 n.4 (D.D.C. June 25, 2009) ("HERA explicitly prohibits" courts from "tak[ing] action that would 'restrain or affect' FHFA's discretion") (citing 12 U.S.C. § 4617(f)); *Esther Sadowsky Testamentary Trust v. Syron*, No. 08-cv-5221(BSJ), 2009 WL 1309776, at *1 (S.D.N.Y. May 6, 2009) (same); *In re Fed. Home Loan Mortgage Corp. Derivative Litig.*, No. 1:08cv773(LMB/TCB), 2009 WL 2421447, at *6 (E.D. Va. July 27, 2009) (same).[6]

This broad grant of power and discretion expresses Congress' manifest intent to afford FHFA with as much flexibility as possible in restoring the Enterprises to sound financial condition. *See In re Fed. Nat'l Mortgage Ass'n Sec., Derivative, and "ERISA"*

[6] In addition, many courts have interpreted the identical anti-injunction provision of the Financial Institutions Reform, Recovery and Enforcement Act of 1989 ("FIRREA"), , Pub. L. 101-73, 103 Stat. 498, which grants the Federal Deposit Insurance Corp. ("FDIC") broad powers as conservator and receiver of failed institutions, to bar judicial action that would interfere with an FDIC conservatorship or receivership. HERA mirrors the language of FIRREA in almost all respects, and the three courts that have analyzed FHFA's powers under HERA have relied on cases invoking similar or identical provisions of FIRREA. *See In re Fed. Home Loan Mortgage Corp. Derivative Litig.*, 2009 WL 2421447, at *3 ("[T]he Court is persuaded by decisions that have reached the same conclusion when interpreting [FIRREA], whose provisions regarding the powers of federal bank receivers and conservators are substantially identical to those of HERA."); *In re Fed. Nat'l Mortgage Ass'n Sec., Derivative, and "ERISA" Litig.*, 2009 WL 1837757, at *2 (relying on analysis from *Pareto v. FDIC*, 139 F.3d 696 (9th Cir. 1998), which "confronted a similar provision in [FIRREA], which, for the first time, vested in the FDIC 'all rights, titles, powers, and privileges' of shareholders when a bank entered FDIC receivership"). Congress surely was aware of how the nearly identical anti-injunction language of FIRREA had been interpreted by courts when drafting Section 4617(f) of HERA.

Litig., 629 F. Supp. 2d at 4 n.4 ("Congress has determined that responsibility for deciding how to best preserve and conserve Fannie Mae's assets lies solely with FHFA for the conservatorship period."); *see also* FHFA Opp. at 15-16 (discussing cases holding the language of 12 U.S.C. § 4617(f) generally bars courts from enjoining foreclosures of assets in default).

Congress passed EESA on the heels of granting FHFA this broad grant of discretion to act without court interference. It strains logic to believe that the same Congress would so severely restrict that very power by creating a constitutionally protected property right that would override the broad grant of discretion afforded to the Conservator to preserve and conserve the assets of the Enterprises after they were placed in conservatorship. Accordingly, because no entitlement can be found in the text or legislative history of EESA — and because EESA expressly does not rescind the broad powers that HERA conferred on the Conservator — Plaintiffs' allegations that the statute creates an entitlement must be rejected.

B. Treasury Directives And Enterprise Guidelines Do Not Provide An Entitlement To Benefits

Plaintiffs' allegations that the guidelines for HAMP modifications create an entitlement fail. Under the Supplemental Directives issued by Treasury and the guidelines issued by Fannie Mae and Freddie Mac, there are numerous complex factors that could cause a borrower to be ineligible for a HAMP modification. For example, under the Enterprise guidelines and the Treasury Directives, servicers with large servicing books are permitted to customize their determination of whether the "net

present value" of the modified loan would be positive for the taxpayer. *See* Fannie Mae Announcement 09-05R (Apr. 21, 2009) (FAC Exhibit C) at 6-7; Supplemental Directive 09-01 at 4. Furthermore, the Supplemental Directives acknowledge that servicer modifications will "likely vary even when borrowers' circumstances appear to be similar." *See* Home Affordable Modification Program Net Present Value (NPV) Model Specifications (June 11, 2009) at 3, (Treas. Opp. Ex. 4). Because modification determinations are complex, individualized, and vary from servicer to servicer, HAMP cannot be said to be an entitlement. *Town of Castle Rock, Colo.*, 545 U.S. at 756 ("[A] benefit is not a protected entitlement if government officials may grant or deny it in their discretion."). Such uncertain determinations are inconsistent with the type of programs found to give rise to a property interest protected by the Due Process Clause. *See, e.g.*, *Reed v. Vill. of Shorewood*, 704 F.2d 943, 948 (7th Cir. 1983) (defining property as "what is securely and durably yours under state (or . . . federal) law, as distinct from what you hold subject to so many conditions as to make your interest meager, transitory, or uncertain"). Because Plaintiffs cannot provide any statutory, regulatory, or contractual provision that supports their claim of entitlement in language of an "unmistakably mandatory character," their claims fail. *See Hill v. Group Three Hous. Dev. Corp.*, 799 F.2d 385, 392 (8th Cir. 1986) (holding no entitlement where "[t]he Section 8 statute, regulations, and HUD guidelines do not use '*language of an unmistakably mandatory character*,' similar in substance or form to those statutes found sufficient to create a protected interest") (internal citation omitted) (emphasis added).

II. Plaintiffs Fail To Allege That FHFA, Or Any Government Actor, Deprived Them Of Property

The Fifth Amendment applies to and restricts "only the Federal Government and not private persons." *Pub. Utils. Comm'n v. Pollak*, 343 U.S. 451, 461 (1952). Accordingly, in situations of purely private conduct, the Constitution provides no due process protection, "no matter how unfair that conduct may be." *Nat'l Collegiate Athletic Ass'n v. Tarkanian*, 488 U.S. 179, 191 (1988) (applying due process clause of the Fourteenth Amendment). Not conceding any unfairness here, nonetheless, in order to state a claim upon which relief can be granted, Plaintiffs must show " 'a sufficiently close nexus between the [government] and the challenged action of the regulated entity so that the action of the latter may be fairly treated as that of the [government] itself.' " *Blum v. Yaretsky*, 457 U.S. 991, 1004 (1982) (quoting *Jackson v. Metro. Edison Co.*, 419 U.S. 345, 351 (1974)). Plaintiffs fail to allege that any government actor deprived them of their alleged property interest in a HAMP modification.

Plaintiffs admit that private servicers make the determinations regarding Plaintiffs' applications for HAMP modifications, s*ee, e.g.*, FAC ¶¶ 126-31, and that private mortgage servicers denied Plaintiffs' applications for modifications, *see* FAC ¶¶ 43, 68, 80, 96. Because private actors, and not any state actor, make the determinations that allegedly deprive Plaintiffs of their purported property interest in a HAMP modification, constitutional due process is not required. *See Lugar v. Edmondson Oil Co.*, 457 U.S. 922, 937 (1982) ("[T]he party charged with the deprivation must be a person who may fairly said to be a state actor"); *Am. Mfrs. Mut. Ins. Co. v. Sullivan*, 526 U.S. 40, 51

(1999) (focusing analysis of state action on "the specific conduct of which the plaintiff complains"). Rather, the Supreme Court has held that the government is "responsible for a private decision only when it has exercised coercive power or has provided such significant encouragement, either overt or covert, that the choice must in law be deemed to be that of the State." *Blum*, 457 U.S. at 1004. Plaintiffs make no allegation whatsoever that FHFA or Treasury exercise coercive power over the servicers in individual HAMP modification determinations, or otherwise acted in such a way as to provide encouragement that dictated a choice in favor or against any individual HAMP modification.

Nor does the funding of HAMP by the federal government equate the determinations made by private servicers regarding modifications with state action. *See Blum*, 457 U.S. at 1010-1011; *Rendell-Baker v. Kohn*, 457 U.S. 830, 840-41 (1982). In *Nichols v. Metro. Center for Independent Living, Inc.*, 50 F.3d 514, 518 (8th Cir. 1995), plaintiff was dismissed from her job and argued that the defendant-employer was "a state actor because it depends upon government for nearly all its funding; because it performs uniquely public functions; and because it is subject to extensive governmental regulation and licensing." The Eighth Circuit squarely rejected plaintiff's argument:

> What was missing here and in *Rendell-Baker*, and what was present in *McVarish v. Mid-Nebraska Community Mental Health Ctr*., 696 F.2d 69 (8th Cir.1982), upon which [the plaintiff] relies, is direct government control, *either of the organization*, like the multi-county health center in *McVarish, or of the conduct that caused the alleged deprivation of plaintiff's rights*. Here, as in *Rendell-Baker*, the government does not control or dictate [the defendant's] personnel decisions, as confirmed by the State agency's response to [the plaintiff's] post-termination complaint.

Id. (emphasis added). In the present case, Plaintiffs fail to allege that the government either controlled the private servicers or caused the lenders to deny the loan modifications under HAMP.

Furthermore, the fact of conservatorship does not convert Fannie Mae or Freddie Mac into a state actor. As Plaintiffs point out, federal courts have continually held that Fannie Mae and Freddie Mac are not government actors. *See* Pl. Br. at 32-33; *see also* GSE Opp. at 26. Because the federal government has not taken "permanent authority" over the Enterprises but, rather, has exercised "temporary control" for the purpose of "reorganizing, rehabilitating, or winding up the affairs" of the Enterprises under conservatorship, *see* 12 U.S.C. § 4617(a)(2), Fannie Mae and Freddie Mac are not state actors. *See Lebron v. Nat'l R.R. Passenger Corp.*, 513 U.S. 374, 398, 400 (1995).

Accordingly, because Plaintiffs fail to allege that any government actor had any role in determinations denying HAMP modifications, the "state actor" requirement for an actionable constitutional due process claim is not satisfied.

III. The Procedures Already In Place Satisfy Due Process Under *Mathews*

Assuming *arguendo* that Plaintiffs are entitled to some degree of notice, the procedures already established by Defendants are more than constitutionally sufficient. The legal framework established to test the sufficiency of the process due in a given situation requires consideration of three distinct factors:

> First, the private interest that will be affected by the official action; second, the risk of an erroneous deprivation of such interest through the procedures used, and the probable value, if any, of additional or substitute procedural safeguards; and finally, the Government's interest, including the function involved and the fiscal and

> administrative burdens that the additional or substitute procedural requirement would entail.

Mathews v. Eldridge, 424 U.S. 319, 335 (1976). Notably, the requirements of due process are "flexible and call[] for such procedural protections as the particular situation demands." *Morrissey v. Brewer*, 408 U.S. 471, 481 (1972).

Plaintiffs' FAC fails to demonstrate that the process Plaintiffs demand is required under *Mathews.* Plaintiffs assert that they are entitled to notice of the basis for a decision and an opportunity to appeal. *See, e.g.*, FAC ¶¶ 176, 177, 183. But the procedures *already in place* under HAMP to protect against an erroneous deprivation of property are sufficient as a matter of law. Directives already instruct private servicers to provide borrowers with written notice if borrowers who qualify for a Trial Period Plan are determined to be ineligible due to income verification. *See* Supplemental Directive 09-01 at 18. Furthermore, Treasury is in the process of requiring servicers to notify borrowers of the reasons for a HAMP denial, rendering the relief sought by Plaintiffs moot. *See* Written Testimony of Herbert M. Allison, Jr., *supra* note 3 (Treasury will "require servicers to use those denial codes as a uniform basis for sending letters to borrowers who were evaluated for HAMP but denied a modification."). In addition, borrowers may seek free housing counseling from certified housing counselors or elevate their concerns to the HAMP Support Center (for non-GSE loans) or to Fannie Mae or Freddie Mac directly (for GSE-owned loans). *See* Treas. Opp. at 37-40; GSE Opp. at 11-12, 29.

The Plaintiffs are not entitled to any more notice than HAMP already provides. Courts have rejected such burdensome notice requirements in similar situations. For

example, in *Woodsmall v. Lyng*, 816 F.2d 1241, 1246 (8th Cir. 1987), plaintiffs, after being rejected for a loan by Farmers Home Administration, argued that the Secretary of Agriculture's failure to promulgate more detailed standards to evaluate creditworthiness violated their Due Process rights. The court squarely rejected plaintiffs' argument with respect to the burden that the proposed notice would place upon the government:

> Finally, the government interest in maintaining flexibility and discretion in evaluating creditworthiness is significant. The rural housing loan program is, after all, a loan program. Each loan application *presents a different set of financial circumstances*, which the Secretary contends must be evaluated *on an individual basis*. The Secretary argues that "an attempt to articulate fully all of the matters considered by a good loan officer would likely produce a mind-boggling regulatory quagmire." We agree that the administrative burdens of requiring standards for evaluating creditworthiness would be undue in the context of this program.

Id. at 1247 (emphasis added) (citations omitted). Likewise, providing every applicant for a HAMP loan modification the detailed notice that Plaintiffs seek would result in a "mind-boggling" array of administrative burdens. Such burdens are particularly costly here given the critical importance of proceeding with loan modifications as quickly as possible.[7] Plaintiffs' demand for a right to appeal also fails because "[t]here is, of course, no constitutional right to an appeal." *Jones v. Barnes*, 463 U.S. 745, 751 (1983).

The Supreme Court has acknowledged that "the marginal gains from affording an additional procedural safeguard often may be outweighed by the societal cost of

[7] *See* H.R. Rep. No. 111-19, at 8 (2009) ("In the 18 months since the Judiciary Committee first began exploring the foreclosure crisis, solutions offered by the industry and the Federal Government have failed to address the problem . . . We are behind the curve . . . . 'We are falling behind. . . . [W]e need to act and we need to act quickly and we need to act dramatically.' ") (internal citation omitted).

providing such a safeguard." *Walters v. Nat'l Ass'n of Radiation Survivors*, 473 U.S. 305, 320-21. Plaintiffs' limited allegations demonstrate no significant risk of erroneous denials under HAMP. However, as mentioned above, it is nearly certain that the additional procedures that Plaintiffs seek will entail an enormous cost to society. HAMP is working to address the foreclosure crisis by modifying the mortgages of *3 million to 4 million* borrowers by December 31, 2012. There is a significant possibility that the burdensome and unnecessary procedures demanded by Plaintiffs will ultimately cause *more* foreclosures by drastically impeding the application process.

CONCLUSION

For the reasons stated herein, FHFA as Conservator for Fannie Mae and Freddie Mac, respectfully requests that the Court dismiss Plaintiffs' First Amended Complaint.

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