NLWJC - Kagan

Counsel - Box 024- Folder 010

Savings and Loan Case

THE WHITE HOUSE

WASHINGTON

September 11, 1995

MEMORANDUM TO BOB LITAN

FROM: ELENA KAGAN

SUBJECT: ATTACHED MEMO ON SAVINGS AND LOAN CASE

Attached, for your information, is the memo from the White House Counsel's Office to the President on the Federal Circuit's decision in Winstar v. United States. Thanks very much for all your help.

Please note the last sentence of the memo, which states that OMB is currently looking into the potential cost of the decision. I took this information from the memo you gave to me. I would very much appreciate your keeping me informed of the outcome of OMB's review. Thanks again.

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MEMORANDUM TO JACK LEW

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THE WHITE HOUSE

WASHINGTON

September 7, 1995

MEMORANDUM TO THE PRESIDENT

FROM: ABNER J. MIKVA
Counsel to the President

ELENA KAGAN EK
Associate Counsel to the President

SUBJECT: SAVINGS AND LOAN CASE

On August 30, the U.S. Court of Appeals for the Federal Circuit, sitting en banc, issued a ruling that could add significantly to the cost of cleaning up the savings and loan crisis. The Court held, by a vote of 9-2, that a provision of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA), which restricted the ability of banks to use "supervisory goodwill" to meet minimum capital requirements, breached contracts between the government and the three thrifts that filed the suit. About 90 other thrifts have similar, but not identical, claims pending in the Federal Circuit. If the Supreme Court does not reverse the Federal Circuit's decision and the pending claims also succeed, the eventual pricetag of the ruling, though still very uncertain, would run in the billions.

The case has its beginnings in the efforts of the Federal Savings and Loan Insurance Corporation (FSLIC), in the early 1980s, to encourage mergers between healthy thrifts and failing ones. As part of this effort, FSLIC allowed merged thrifts to count supervisory goodwill -- the difference between the failing thrift's liabilities and assets -- toward capital requirements. FIRREA expressly repudiated this practice: it greatly restricted the continued use of supervisory goodwill to satisfy capital standards. As a result, many thrifts (including the three that brought this suit) suddenly found themselves in violation of capital requirements and subject to seizure by the government.

The thrifts have argued that FIRREA's restriction on the use of supervisory goodwill breached contracts between the thrifts and the government, entered into at the time of the mergers. The government has defended on the grounds that (1) the government never entered into contracts with the thrifts allowing the use of supervisory goodwill to meet capital standards; and (2) assuming such contracts exist, the government is not liable for any breach of the contracts effected by a general statute such as FIRREA.

Although no official decision has yet been made, the Solicitor General intends to request the Supreme Court to hear the case. The Supreme Court almost certainly will grant this request, both because of the importance of the case to the government and because of an arguable conflict between the decision of the Federal Circuit and decisions of other Courts of Appeals. Under the most likely schedule, the Court would take the case in January, hear argument in April, and issue a decision in late June or early July. It is possible, however, that the argument would be deferred until October 1996, with the decision occurrring some months after that. In the meantime, proceedings in the 90 other pending cases, as well as the determination of damages in this case, almost certainly would be stayed.

Those knowledgeable about the case within the Justice Department have a wide variety of views as to the chances for success in the Supreme Court. The only thing that can safely be said is that this is no easy case for the government: it is very possible that the Court will uphold the Federal Circuit's ruling.

Although newspapers have estimated the potential pricetag of all of these cases (including the 90 pending cases) as up to $20 billion, the actual cost is very uncertain. Some of the pending claims involve sufficiently different facts so that even if the Federal Circuit's decision stands, the claims might be dismissed. Moreover, the determination of damages in the cases will involve many tricky questions. In some cases, the government credibly can argue that there are no damages because the thrifts would have failed anyway. Still, if the Federal Circuit's decision stands, the damages likely will run into the billions and may, in an absolute worst-case scenario, total between $10 and $20 billion. OMB is currently exploring this matter further.

The Washington Times
TUESDAY, SEPTEMBER 12, 1995

FRANK GAFFNEY

Selling the high technology rope

Legend has it that Lenin once ridiculed Western capitalists for being willing to sell the communists the rope with which the latter would hang them. While this story may be apocryphal, it nonetheless accurately describes a time-honored practice by communist and other totalitarian regimes: Exploit the West's willingness to disregard legitimate security concerns in its pursuit of commercial transactions involving the transfer of militarily relevant (or "dual-use") technology. By so doing, even governments lacking enormous resources can acquire advanced equipment and know-how needed to field militaries capable of posing powerful threats to the interests of the selling nations.

It seems unlikely that even the cynical Lenin could have imagined the absurd lengths to which the Clinton administration would be willing to go in the rope-selling business, however. This week in Paris, it is setting the stage for making the Kremlin a formal member of a new international technology transfer control mechanism — the so-called "New Forum." This entity is intended to succeed the now officially defunct Coordinating Committee on Multilateral Export Controls (COCOM). If all goes according to plan, starting in January, Moscow will have an equal say about the length and strength of the high technology "rope" to be sold — and who gets it.

By definition, bringing Russia inside the tent in this fashion ensures that it will be given access to detailed information about sensitive Western technology. As a practical matter, moreover, it will be difficult — if not impossible — to deny the Kremlin access to such technology. And the Russians will, of course, be in a position to block efforts to produce a Western consensus against selling dual-use equipment or know-how to the world's rogue nations. As the case of the Russian-Iranian reactor deal graphically demonstrates, Moscow has proven reluctant to deny its clients whatever hardware they want. At a minimum, Moscow can be expected to serve as the middle-man for transfers of any technology that might yet be denied the likes of Iraq, Iran and North Korea, but that can be sold to the former Soviet Union.

Matters are made worse by two related developments. First, the Clinton administration agreed in March 1994 to dismantle COCOM before any successor institution was in place. As a result, multilateral controls on strategic dual-use technology — for example, those governing exports of advanced multi-axis machine tools, underwater exploration equipment, aviation and naval propulsion systems, telecommunications, supercomputers, etc. — have been largely dismantled.

Of particular concern is the resulting absence of pre-notification of sensitive exports. In the past, such notice has been indispensable to U.S. attempts to dissuade its allies from selling "rope" to the bad guys. At this writing, it is not clear whether the parties to the New Forum will agree even to give notice of technology transfers after the fact. As one concerned official put it, "We'll just have to wait until we learn about these dangerous transactions from intelligence — assuming we find out about them."

The New Forum will also leave to "national discretion" decisions about what to control and how rigorously to enforce such controls. Given the proclivities of the Germans and other Europeans (to say nothing of the Russians), "national discretion" amounts to a license for wholesale national indiscretions with respect to the exports of sensitive technology to rogue nations. This initiative has been made even more problematic, thanks to the administration's second mistake: It has undercut its own leadership position by engaging in some of the most irresponsible technology transfers on record. Washington has, for example, unilaterally and greatly expanded the performance standards of supercomputers available for export. This is an area of genuine U.S. market dominance at the moment, so the oft-cited excuse of foreign availability does not apply. Indeed, that fact — combined with the enormous military potential of powerful supercomputers for such applications as nuclear weapons design, effects simulation and operational planning, dual-use air traffic control, undersea warfare, etc. — may explain why Japan and other allies were willing to maintain significant export controls in this area.

With the Clinton administration's decision to sell advanced supercomputers to China (among a host of other technologies enabling the Peoples' Republic to build, for example, advanced, long-range and highly accurate cruise missiles), it has persuaded the other advanced industrial nations that literally anything goes. The result is certain to be a buyer's market for the componentry and manufacturing systems needed for tomorrow's world-class weaponry.

Naturally, the administration would have us believe that, in the post-Cold War world, we need not be concerned about selling high technology "rope" to former communists in Russia or "reform" communists in China. This is, of course, nonsense — not because of ideology but for two practical reasons. First, both countries are actively hawking everything from ballistic missiles to nuclear hardware to anyone with cash. And second, both are engaged in behavior that makes future conflict with them possible, if not inevitable. Third, the two are actively sharing military technology and data.

Under these circumstances, the administration's technology transfer policies cry out for adult supervision from Capitol Hill. A good first step would be to establish that national security considerations, and not simply trade promotion priorities, must be factored into export control decision-making. If there were no other justification for dismantling the Commerce Department — which has traditionally thwarted efforts to address the former in its monomaniacal pursuit of the latter — the evisceration of its Bureau of Export Administration would be sufficient grounds for doing so.

Responsibility for running a restructured security-minded interagency export licensing process should be placed where it belongs: in the Defense Department. Also in order are urgent hearings into the cumulative, detrimental impact of the administration's technology transfer policies.

If corrective action on export controls is not taken promptly by either the executive or legislative branches, the steps being mapped out this week will probably facilitate a grave new impetus to international proliferation. There will be nothing funny on the Clinton administration's way to the New Forum.

Frank J. Gaffney Jr. is the director of the Center for Security Policy and a columnist for The Washington Times.

The Washington Times
TUESDAY, SEPTEMBER 12, 1995

BRUCE FEIN

Government bait and switch

The United States should be celebrating its court loss last month in Glendale Federal Bank vs. United States (Aug. 30, 1995) condemning its treachery in abrogating contracts reminiscent of Third World debt repudiation. A government victory would have proved pyrrhic and escalated future government expense. That bureaucrats are seriously considering seeking reversal in the U.S. Supreme Court of a decision that will save the government money testifies to the lunacy of entrusting economic matters to self-laureled government experts.

how?

The Glendale case was provoked by bait-and-switch tactics of the United States that would have embarrassed even the most notorious used car salesman. In a desperate effort to curtail mushrooming federal deposit insurance losses in the savings and loan industry caused by its countless regulatory follies, the Federal Home Loan Bank Board and the Federal Savings and Loan Insurance Corp., an agency under the board, solicited healthy financial institutions to acquire failing thrifts by the promise of indulgent accounting treatment of "good will" that would save the white knights from insolvency and government seizure. Although painful to both readers and columnists of ordinary mental fortitude, a brief divagation into the mysteries of regulatory accounting at this crossroads seems imperative, not to put too fine a point on it.

As a regulatory hedge against insolvencies, the board required thrifts to maintain a floor of capital which, if not maintained, justified sanctions, including government seizure and liquidation. In calculating a thrift's regulatory capital, its good will, an intangible asset, is typically frowned on because it cannot be marshalled to pay depositors. During FSLIC's insurance hemorrhaging in the 1980s, however, the board relaxed its accounting rules for good will in the hope that financially solvent institutions could be lured to acquire the insolvent and nurse them back to health. In that event, FSLIC would be saved millions in liability to depositors triggered whenever an insolvent institution was liquidated.

The board thus permitted in a variety of circumstances a solvent thrift to treat as good will the difference between the price of acquiring a failing thrift and the fair market value of its assets. That good will, moreover, could be amortized over periods of up to 40 years and could count toward meeting the board's regulatory capital floor.

different than the definition I used?

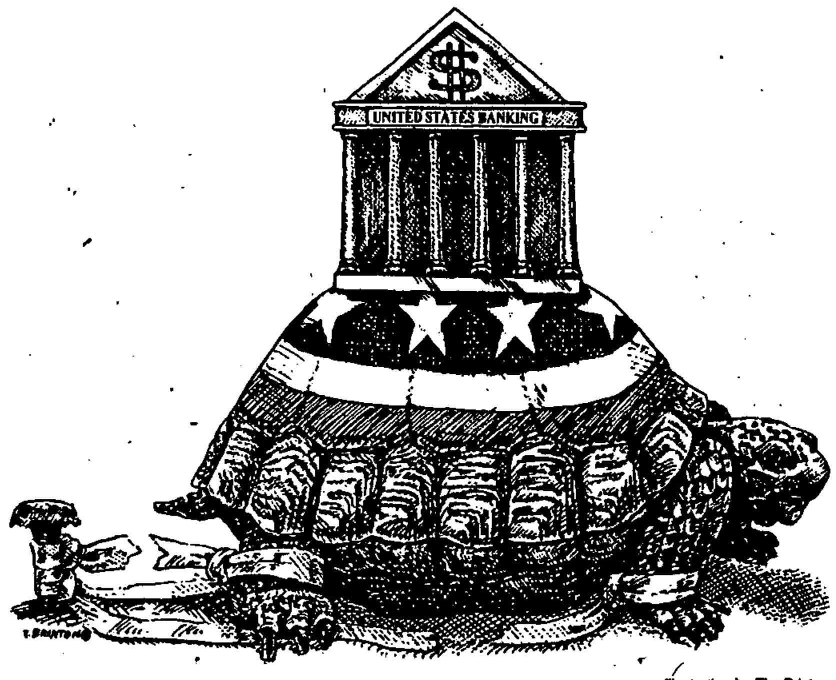

Illustration by Tim Brinton

In 1981, the board approved a proposed merger of Glendale Federal Bank and First Savings and Loan Association of Broward County, Fla., and the use of the resulting intangible good will toward satisfying Glendale's capital floor. At the time of the merger, Broward seemed destined for liquidation because its liabilities exceeded its assets by approximately $734 million. The Board saved FSLIC that handsome sum by its accounting lure to Glendale.

The board approved many other acquisitions of failing thrifts in the 1980s that pivoted on chicanery in the accounting treatment of good will, and saved FSLIC millions through its regulatory attraction of white knights. Congress, however, scuttled the board's regulatory gambits by the enactment of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989. With all the ingratitude Brutus showed Caesar as a plotter and participant in his assassination, FIRREA stilettoed the board's accounting promises to Glendale and other white knights and demanded satisfaction of much stricter minimum capital rules to escape sanctions or government seizure.

They sued the United States to recover their losses caused by the bait and switch swindle, and prevailed in the U.S. Court of Appeals for the Federal Circuit. Writing for a 9-2 majority, Chief Judge Glen Archer concluded that the board's regulatory pledges to the acquiring thrifts were tantamount to contracts that were violated by FIRREA's superseding and retroactive accounting ukases. The chief judge underscored that the Glendale decision placed no handcuffs on the sovereign power of Congress to override government contracts with private parties, but simply required the United States to pay for the losses generated by such imperiousness.

What is stunning about the Glendale litigation is not the defeat of the United States, but the effrontery and obtuseness of the government in maintaining it could renege on its contracts with impunity. After hundreds of millions in savings from white knights, that bravely rescued tottering thrifts, the effort by the United States to steal back what had been promised the saviors offends even a primitive sense of decency. The government should turn square corners when it deals with its citizens.

A government win in Glendale, in any event, would have been an economic disaster. Private parties would either have boycotted government contracts or raised charges to cover the risk of government breach caused by retroactive legislation. Government costs would soar to the levels encountered by Third World nations that routinely treat contracts as no more than scraps of paper.

The frugally minded 104th Congress should shout at the Clinton administration to leave the Glendale ruling undisturbed. Self-inflicted wounds are not the earmark of enlightened government.

Bruce Fein is a lawyer and free-lance writer specializing in legal issues.

Letters to the Editor

Struggles Within the Church

Your Aug. 17 page-one article, "Paranoia Becomes an Article of Faith in a Kansas Town," has a basic flaw running throughout, namely the repeated description of the community in St. Marys, Kan., as "traditionalists," at one point even calling them members of the "traditionalist movement." These people and their associates should be more correctly called "Lefebvrists."

Their defunct founder, suspended and excommunicated French Archbishop Marcel Lefebvre, never spoke truer words than when, first at a press conference in the '70s and on several occasions later on, he unequivocally stated: "I am not a traditionalist."

As to his troubles with Rome, Archbishop Lefebvre was "suspended *a divinis*" (forbidden to offer Mass and administer sacraments) in 1976, not for offering Mass in Latin, but for performing ordinations to the priesthood that were in open violation of traditional church law. Regarding his excommunication in 1988, again, the Latin Mass had nothing to do with it. This second censure was the result of Lefebvre's flagrant violation of the church's traditional law by consecrating bishops without the pope's consent.

Before any critics start accusing us, the traditionalists, of engaging in a hair-splitting exercise by stressing the difference between "traditionalists" and "Lefebvrists," I refer them to Pope John Paul II's own Apostolic Letter, "Ecclesia Dei," of July 2, 1988, in which the pope makes the same distinction: Those "linked in various ways to Monsignor Lefebvre" are directed to "cease their support in any way," and reminded that to do otherwise is "a grave offense against God and carries the penalty of excommunication." Traditionalists, however, whom the pope calls "faithful Catholics who are attached to the Latin liturgical tradition," are given his personal assurance—"my will," he calls it—that, at last, "the necessary measures will be taken to guarantee respect of their rightful aspirations."

FATHER GOMMAR A. DE PAUW, J.C.D.
Founder-President
Catholic Traditionalist Movement Inc.
Westbury, N.Y.

* * *

Your article on religious and political life in St. Marys is contra-factual in one major point, and entirely misses the real religious debate within the U.S. Roman Catholic Church.

First, the real outcome of Vatican Council II was a reaffirmation in modern language of the historic Catholic faith. The council and popes during and after the council cannot in any respect be called "modernist." The modernist heresy was condemned by Pope Pius X, and that condemnation still stands. Modernism holds to radical deconstructionism in scripture studies, to a kind of ethics of the situation, and to a liberal approach to most religious issues that are in no way Catholic, or authentically Christian.

The Lefebvrite movement is, and always has been, a marginal group on the fringe of the church. True, they reject the council and have no respect for the post-conciliar popes and bishops. But such splinter groups spring up in every age. They surfaced after Vatican Council I, and some "Old Catholic" churches from that period still exist, mostly in Europe. But the Lefebvre followers are practically insignificant in the U.S. today.

The real controversy within the church is between liberals and conservatives who remain practicing Catholics within the "authentic" Catholic church. Liberals have adopted some but not all of the tenets of modernism, particularly a suspicion of the words of the Bible, and who have appended a radical social agenda for the church, particularly a rejection of traditional sexual morality, acceptance of divorce and contraception, and the ordination of women as priests. They read America, Commonweal and the National Catholic Reporter.

Conservatives hold to papal teaching on these matters ferociously, have created "defense" organizations such as the St. Joseph Foundation, and read the Wanderer, Our Sunday Visitor and Catholic Family News. The big, and largely unreported, battle between liberals and conservatives right now is over the language of worship. Liberals, who control the official translation authority, ICEL, want to move toward inclusive language and eliminate, for instance, the traditional phrasing of the Lord's Prayer. Conservatives point out that the original translations into English are sloppy, are often ugly, and usually don't represent the Latin original very well. The organization of priests, with lay associates, called Credo has provided a scholarly backup for a handful of bishops who have, with some success, tried to delay the hasty imposition of new liberal, inclusivist translations on the whole American church.

By focusing on St. Marys and its rather unusual juxtaposition of churches, you gave the impression that this kind of conflict is representative of the U.S. church, when it most certainly is not.

W. PATRICK CUNNINGHAM
Division of Economics and Finance
University of Texas at San Antonio
San Antonio

Duped by Dilbert

In response to your Aug. 8 "Managing Your Career" column on the "Dilbert" cartoon strip: Creator Scott Adams regularly dupes dazed fans into thinking he possesses keen insight regarding how a workplace should be managed.

In reality, Mr. Adams is a common office malcontent. Secure in the knowledge that he'll never earn the responsibility of workplace leadership, he lurks in the rear, lobbing cartoon scuds toward the doers on the frontline.

A brief stint in a leadership position might give Mr. Adams a better appreciation of the difficulties of managing in today's workplace. Doubtless he'd grow weary of trying to solve real problems while having to pacify whiners and non-performers like Scott Adams and Dilbert.

PAUL WEIDMAN
Fountain Inn, S.C.

Dr. Frances Kelsey

Richard Hanson, in his Aug. 31 Letter about the FDA, refers to Dr. Francis Kelsey, who kept thalidomide off the U.S. market. The woman who accomplished this was Dr. Frances Kelsey.

JUDITH L. MACK
Wilton, Conn.

Brubeck Overlooked

Terry Teachout's article on the "missing" white faces in the cable-TV program "The Story of Jazz" (Leisure & Arts, Sept. 1) was notable in its omission of one of the art form's most notable innovators and popular figures: Dave Brubeck.

S. RIDGWAY KENNEDY
Somerset, N.J.

In Japan, Kodak Faced Real Barriers

In his Aug. 14 Manager's Journal, "Kodak's Self-Inflicted Wound," Scott Latham acknowledges Eastman Kodak Co.'s contention that it faces anticompetitive trade practices and an exclusionary distribution structure in Japan, but he fails to examine those very real barriers to any extent. Instead, he describes Kodak's relative lack of success in Japan as a function of its own doing and selectively used some of my comments to bolster his case.

As president of Kodak Japan from 1984 until 1991, I can attest to the fact that many of the barriers we faced were real and powerfully effective. They denied Kodak access to the bulk of the market for consumer photographic products. I believe that these same barriers are still effectively in place today.

Mr. Latham states that Kodak didn't get really aggressive in Japan until 1984. While it is true that that was the time we escalated our efforts, it is misleading to imply that we were asleep until then. Japanese law prevented full investment there by foreign capital firms until 1976. Because of our long-term relationship with our main import agent, Nagase & Co., our first efforts were to work with them in every way possible. Any immediate change would have been countercultural and upsetting. Instead, we studied options, and after careful discussion, decided to increase our commitment in Japan by building on our existing relationships.

It was at this point that Mr. Latham cites the business consultants James Abegglen and George Stalk Jr. and their work, published in 1985. These authors concluded that Kodak was an example of an American company that had been following the wrong strategy in Japan. Not cited, however, are conclusions reached by Mr. Abegglen as published in the October 1986 issue of Tokyo Business Today. This in substance stated that in the space of less than two years Kodak, "a company that was under severe threat from Japan's industry, is now in a position to respond to that threat where it matters most, in the Japanese market itself."

Mr. Latham concludes with the idea that American companies can either use "good products, with sound strategy and firm commitment" to enter Asian markets or turn to Washington for help. In the real world, government help on occasion is needed to help open closed markets so that good products and sound strategies have a fair chance at success.

ALBERT L. SIEG
Retired president
Kodak Japan
Rochester, N.Y.

The Court Gets It Half Right on Firrea

Rule of Law

By Jonathan R. Macey

The delicate regulatory structure erected to contain the financial toxic waste created by the collapse of the thrift industry in the 1980s cracked badly last month. The blow was dealt by the U.S. Court of Appeals for the Federal Circuit, which ruled that the U.S. breached a series of contractual promises with various thrift institutions in 1989, when Congress passed the Financial Institutions Reform, Recovery and Enforcement Act (Firrea).

Preliminary estimates of the cost to the government for breaching these contracts are more than $5 billion. On the day the decision was announced, the S&P Savings and Loan Index rallied strongly, gaining more than 6% on a day when the general market declined.

The broken contracts were forged between regulators at the Federal Home Loan Bank Board and individual thrift institutions such as Glendale Federal Bank, Statesman Savings Holding Co. and Winstar Corp. These firms acquired insolvent thrifts during the 1980s that regulators did not want to close. The contracts, which induced a number of thrift mergers in the 1980s, made a lot of well-connected thrift operators millions by enabling them to take over insolvent thrifts without having to put up any money. The operators could make lucrative compensation arrangements with the thrifts they had acquired and then run them until they were closed or merged with healthy thrifts. A handful even turned themselves around and made a profit.

The deals were pretty simple. In order to avoid closing certain insolvent thrifts, the bureaucrats at the Federal Home Loan Bank Board authorized acquirers of these thrifts to use a number of accounting gimmicks that enabled the balance sheets of the insolvent financial institutions to look like they were in compliance with regulatory capital requirements. "Supervisory goodwill" and "capital credits" were added to the asset side of insolvent thrifts' balance sheets in order to make them appear to have assets in excess of liabilities.

Such gimmicks allowed some insolvent thrifts to limp along for a few more years before they were closed and others to be merged into healthier thrifts, which benefited from the new, lower capital requirements and from being able to take over the deposit base of the failed thrifts. The deals also allowed some thrifts to operate with negative capital levels, safe in the knowledge that the regulators would not shut them down. Most important, all of the thrifts that did such deals in the 1980s were able to avoid the capital requirements that applied to their competitors.

In passing Firrea in 1989 Congress put an end to these practices. It decreed what should have been obvious from the beginning; namely that all thrifts should maintain "uniformly applicable capital standards." Firrea also required all thrifts to meet tougher capital standards. And Firrea restricted the use of "supervisory goodwill."

The appeals court correctly held that these provisions of Firrea breached the express agreements made by thrift operators with their regulators back in the 1980s. These agreements had specifically authorized the use of these accounting gimmicks. Once the court recognized that the thrift regulators had the authority to make contracts, assist acquirers of insolvent thrifts and set minimum capital requirements on a case-by-case basis, its conclusion that Firrea has abrogated the contracts was virtually unavoidable.

At another level, however, the court's reasoning was deeply flawed. It accepted at face value the argument that the government saved money as a result of the strange deals struck by the thrift regulators in the 1980s. These savings are supposed to have resulted because the regulators avoided paying off the failing thrifts' insured depositors out of the Federal Savings and Loan Insurance Fund.

But the government doesn't save any money if it has to pay $5 out of the insurance fund tomorrow in order to avoid a $1 payout today. And the fact is that these deals were always highly suspect. They were made by highly politicized bureaucrats in concert with well-connected bankers. The bankers were searching for bargains and for regulatory relief. They got both. The bureaucrats were trying to avoid having the true size of the thrift debacle recognized on their watch, by delaying and denying the true size of the losses. The accounting gimmicks served the interests of both parties all too well.

> *The enormous financial repercussions of the court decision will cast doubt on the wisdom of giving so much power to bureaucrats.*

In passing Firrea, Congress recognized that these accounting gimmicks only postponed the recognition of losses that should have been recognized long ago. Congress was reacting to the public outcry against all the slick deals and special arrangements that had been made by the thrift regulators.

The court was too quick to conclude that the deals served a valid purpose. At best, they gave thrift operators the economic equivalent of an option contract with the government. If all went well, the thrift would return to financial health and the operator would reap the benefits. But if things went badly, the thrift operator had the implicit option to turn the whole operation back over to the government.

This is what always happens to federally insured depository institutions when they fail. But investors in federally insured depository institutions usually have to put up a lot of capital, which they lose if the institution goes belly up. In this case, the investors often did not put up any money of their own. But the reason we have capital requirements for banks is to protect the government from losses.

And the reason we shut down banks that do not meet minimum capital requirements is to cap those losses before they become too great. Once a bank loses its capital, its investors have no more incentive to avoid risks to minimize loss. They have every incentive to pursue a risky, heads we win, tails the government loses strategy. When the thrift deals were done, didn't anybody wonder why, if ignoring capital requirements was a good idea for the weakest thrifts, the same treatment should not have been given to all thrifts?

The enormous financial repercussions of this decision will cast further doubt on the wisdom of giving so much power to administrative agencies. These deals were not in the public interest when they were made.

Even the most ardent supporters of granting plaintiffs expanded legal rights to recover from government "takings" should not applaud the protection of the property interests at issue here. These "rights" were created by government sleight-of-hand rather than legitimate market forces. Congress was right to negate these deals in 1989. But Congress should have gone much further and relieved all federal bureaucrats of the power to cut special deals with particular favored constituents.

Mr. Macey is a professor at Cornell Law School.

REPLACEMENT REPLY BRIEF OF DEFENDANT-APPELLANT UNITED STATES

IN THE UNITED STATES COURT OF APPEALS
FOR THE FEDERAL CIRCUIT

No. 92-5164

WINSTAR CORPORATION, UNITED FEDERAL SAVINGS BANK,
STATESMAN SAVINGS HOLDING CORP., THE STATESMAN GROUP INC.,
and AMERICAN LIFE AND CASUALTY INSURANCE COMPANY.

and

GLENDALE FEDERAL BANK, FSB,

Plaintiffs-Appellees,

v.

THE UNITED STATES,

Defendant-Appellant.

ON A PETITION FOR PERMISSION TO APPEAL FROM AN
ORDER OF THE UNITED STATES CLAIMS COURT IN
90-8 C, 90-772 C AND 90-773 C ENTERED
July 24, 1992, FROM CHIEF JUDGE LOREN A. SMITH

FRANK W. HUNGER
Assistant Attorney General

DOUGLAS LETTER
Appellate Litigation Counsel
Appellate Staff, Civil Division
Room 3617, Department of Justice
Washington, D.C. 20530
Telephone: (202) 514-3602

Attorneys for Appellant United States

December 10, 1993

INTRODUCTION

This reply brief has two primary themes. Although we address specific arguments made in the briefs filed by the plaintiffs/appellees, we ask the Court to keep in mind these two overriding points.

First, plaintiffs assert that they have express contracts with the Federal Government guaranteeing them a particular form of regulatory treatment for periods ranging up to 40 years, regardless of whether Congress enacts legislation prohibiting that treatment. **However, at no point has any of the plaintiffs pointed to a specific contract provision actually stating this alleged guarantee**.

The fact that so much of the key contract language in each of these cases is missing is quite revealing. Its absence means that the terms that now assertedly were so significant to the plaintiffs were never stated clearly so that there would be no doubt about their meaning. Under these circumstances, it is hardly reasonable to conclude that federal regulators agreed to abdicate the duty of the United States to protect the public by tying the hands of federal officials for up to 40 years with particular regulatory practices that no longer work. The thrifts offer no explanation as to why the contract clauses, terms, and provisions that were allegedly so crucial to them show up nowhere clearly, but instead have to be inferred and gleaned by combining snippets from numerous documents that do not resemble contracts.

Thus, for the asserted contract provision at the very heart of all three of these cases, each of the plaintiffs asks this

Court to pretend that the necessary binding language exists. They suggest that this Court imply such important and unlikely long-term contract provisions despite the fact that plaintiffs operated in a pervasively regulated industry in which the statutory and regulatory schemes were constantly changing. Moreover, these are not small contract claims; Glendale alone claims that it has suffered contract damages of well over one billion dollars.

We urge instead that the Court search the relevant documents for the precise contract terms stating the rights that plaintiffs claim. If the Court cannot find those terms, stated in clear, unmistakable language, plaintiffs' contract claims must be rejected.

Second, although plaintiffs' briefs make it seem otherwise this case is **not** about Congress' constitutional ability to abrogate contracts; we agree with plaintiffs' oft stated rhetoric that Congress must honor its contracts. This appeal, however, is about the proper way -- based on the various relevant documents and the "unmistakability" doctrine -- to interpret the contracts that plaintiffs claim exist. Both the trial court and the plaintiffs lost sight of this central point. They rely heavily upon Supreme Court cases that address constitutional issues, but not the question of how to interpret contracts that assertedly prohibit Congress from legislatively changing the applicable regulatory scheme.

ARGUMENT

A. Contract Term Existence Issues

In our opening brief, we contended that none of the three groups of plaintiffs covering the three thrift institutions involved in these cases had contracts providing that the goodwill created by various regulated thrift transactions would be counted toward minimum capital regulatory requirements for extended periods regardless of changes in the governing statutory scheme. Trying not to repeat points made in our opening brief on this issue, we address below arguments specific to individual cases, as well as matters relevant to all three.

1. Glendale

Based on the documents in the record, Glendale has a particularly weak case for demonstrating the important contract right that the thrift claims. In its brief (at 16), the thrift criticizes us for "individually dissecting" the various documents that allegedly make up the contract between Glendale and the Government. We admit to doing that very thing because it was our understanding that the courts look to the wording of the contract documents themselves as the best indicator of the terms of that contract. The documents here belie Glendale's claims.

At various points in its brief, Glendale states that the Government agreed to a commitment to treat the thrift's goodwill as an asset for 40 years. **There is no such commitment**.

Glendale cannot point, and has not pointed, to a single phrase in any document in which a federal official contracted that the thrift regulatory agencies would count goodwill booked by Glendale as an asset for purposes of meeting federal regulatory capital requirements. All that Glendale can show is that the Government required the thrift to use a particular form of accounting for transactions. Significantly, **nothing** in that requirement of a form of accounting purported in any way to bind the federal thrift regulators to treat any particular asset in a specified way for governmental purposes.[1]

Thus, Glendale is asking the Court to imagine that the key provision upon which it relies actually exists; the thrift needs the Court to create contract language because the most important terms for Glendale's argument simply do not appear anywhere in any of the even possibly relevant documents.

Moreover, as we pointed out in our opening brief (at 22), there actually was an agreement between the Government and Glendale. This document was called a Supervisory Action Agreement, and it contained the FSLIC's approval of the acquisition of Broward by Glendale. See A1295-1311.

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[1] It is worth noting that FIRREA does **not** eliminate goodwill; thrifts are entitled to continue counting goodwill for certain purposes. FIRREA does limit the ability of thrifts to include goodwill in meeting capital requirements. But, it nevertheless permits thrifts to include all of their goodwill in determining the extent to which they can make certain types of loans and investments. See, e.g., 12 U.S.C. 1464(c)(2)(A).

Since that agreement nowhere mentions goodwill or the method of accounting for it, Glendale contends that the agreement integrated into its terms a wide variety of other, non-contractual documents. Aside from the fact that not a single one of these documents contains the contract terms that Glendale now claims, the Supervisory Action Agreement expired in November 1991 when the institution was still in capital compliance and thus before the thrift's inability to count goodwill would have had any material effect. See A1307.

Glendale says (Br. 19) that the agreement's expiration term applied only to the Government's potential payment obligation. This is another instance in which the thrift asks this Court to ignore plain language or create contract language that does not exist. The Agreement states: "This Agreement shall terminate and the obligations of the FSLIC to make any payments hereunder shall cease upon the expiration of 10 years from the Effective Date * * *" (A1307). The clause does <u>not</u> state that only the FSLIC obligations will cease; it says that "[t]his Agreement shall terminate" on the appointed date.

2. Winstar

The Winstar plaintiffs have indicated that they rely upon the appellate brief previously filed before the panel of this Court. We provide our response to Winstar here so that the Court does not have to consult various briefs to understand the Government's position.

The most interesting aspect of the contract argument made by Winstar is that it does not embrace the ruling by Chief Judge Smith below that the thrift had an implied contract guaranteeing a particular form of regulatory treatment. The thrift argues on appeal (Br. 16) that Winstar had an express contract on this point. This is troubling for Winstar because Chief Judge Smith found no such express contract.

Like Glendale, Winstar contends (Br. 7) that federal regulators made a binding promise to treat goodwill as an asset for regulatory capital purposes for an extended period. Once again, there is **no** such promise stated in any of the documents in the record. Rather, Winstar must attempt to patch together such a key promise by inferring it from various documents. But none of those documents says the essential words upon which Winstar relies.

As with Glendale, there was an actual agreement for Winstar, called an Assistance Agreement, entered into in July 1984. A61-91. That agreement clearly set out the Government's obligations with regard to the relevant thrift transaction. Those obligations were fulfilled and the agreement terminated in July 1986. A86.

Winstar asserts (Br. 18), however, that the termination provision in the Assistance Agreement was overridden by another clause in the agreement stating that "[e]xcept as otherwise specifically provided in this Agreement," it terminates (A86). Winstar then contends that a forbearance letter and Bank Board resolution were integrated into this agreement, and were excepted from the termination provision because the forbearance letter gave Winstar the ability to amortize goodwill over 35 years.

Unfortunately for Winstar this forbearance letter does not "specifically" provide that it survives the termination of the agreement. A59-60. Like Glendale, Winstar's case depends upon this Court to add new language to create the contract plaintiffs wish they had gotten federal officials to sign. Moreover, the long term effect of the forbearance letter urged by Winstar makes it highly unlikely that it was integrated into the agreement.

Furthermore, Winstar does not claim that the forbearance letter says anything about whether federal regulators agreed to count goodwill as an asset to meet regulatory capitalization requirements. Yet again, this Court is being called upon to fill in the missing, but essential, contract language.

3. Statesman

The case involving Statesman is different from those concerning Glendale and Winstar, but it still lacks specific contract language to support the contract right that the Statesman plaintiffs now claim. Unlike in Glendale and Winstar where there is no contract document of any kind providing that the Government will count goodwill as capital for regulatory purposes for any length of time, a Bank Board resolution and the Assistance Agreement in Statesman -- through which the FSLIC contributed $60 million in cash for the transaction at issue --

provided for $26 million of that cash contribution to be counted as capital for regulatory purposes. A273-74, 803, 941-942.

Thus, the Statesman plaintiffs at least have a provision they can point to dealing with the contract right now claimed. Nevertheless, the claim in Statesman is ultimately no more convincing because it too requires this Court to fill in crucial contract language to which Government officials never agreed.

The Statesman plaintiffs contend that they specifically negotiated and obtained a contract term guaranteeing them the right permanently to count their capital credit as capital for regulatory purposes, regardless of any changes in the underlying statutory scheme. No language in any document relating to Statesman states this term.

In the absence of contract language actually containing the contract right that the Statesman plaintiffs claim, they point to (Br. 22) a provision in the Assistance Agreement concerning accounting principles. The clause refers to "computations made for purposes of this Agreement," and deals with interpretation and construction of "any provision of this Agreement" (A849). Significantly, it speaks of Bank Board "regulations" and how they are to be applied if in conflict with the Bank Board resolution relating to Statesman.

This accounting principles clause nowhere mentions, much less mandates, supremacy for a Bank Board resolution if it comes in direct conflict with **statutory** provisions that Congress enacts as part of a legislative overhaul of the entire thrift regulatory scheme. It would have been quite an extraordinary action if the Bank Board officials had signed a contract providing that new legislation governing the thrift industry would not apply to Statesman. Thus, the absence of such a provision -- upon which Statesman's case depends -- is not surprising.

Indeed, the best way to see the flaw in the Statesman plaintiffs' argument is to envision the type of contract term the thrift now wants, and to consider the likelihood that a government official would have signed such a contract term if it had been presented. That government official would have to have been willing -- and authorized -- to sign an unambiguous contract provision stating that he was guaranteeing a specified form of regulatory treatment for a single thrift, and that the contract would override any attempt by Congress to legislate differently for the thrift industry. Given the unusual contract right that the Statesman plaintiffs seek, is it any wonder that no such language actually appears in any contract document?

Thus, while the Statesman plaintiffs can point at least to a provision dealing with the contract right now claimed -- counting a capital credit for minimum capitalization mandates -- they cannot point to any language guaranteeing continuation of that treatment if Congress changed the underlying law.

4. Common Contract Language Issues

In our opening brief, we relied upon a provision placed by the federal regulators in all of the agreements at issue here: the proviso that nothing in the agreements "shall require any unlawful action or inaction by either of the parties hereto." See A280.

The thrifts argue that this provision applies only to law existing at the time the agreements were signed. This is one more time that the thrifts ask this Court to add contract language that does not exist; the proviso nowhere says that it is so limited.

Furthermore, the likelihood that this proviso prohibits -- as its wording says -- any unlawful action or inaction by the parties, whether present or future, is supported by the fact that so many of the documents upon which the thrifts rely looked to the future. Recall that the thrifts argue that these various forward looking documents were integrated into the three agreements at issue here. Given these circumstances, it would be strange for the proviso we raise to cover only existing law.

Since the federal regulators and thrift officers could reasonably be expected to take care that their agreements did not violate the law at that time,[2] it would seem strange to include a clause requiring compliance with the law, but limiting that clause to the then-existing law only. Those who entered into the agreements could not predict how the law would change, and thus the proviso we rely upon was included to protect all parties.

The thrifts also contend that the law compliance proviso must be limited -- despite its wording -- so as not to interfere

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[2] See Heckler v. Community Health Services of Crawford County, Inc., 467 U.S. 51, 64 (1984).

with the provision in the agreements prohibiting modifications without the written approval of all parties. A88, A855. But that modifications provision can be reconciled with the one prohibiting unlawful action: neither the federal regulators nor the thrift officials could unilaterally change the particular agreements, but that restriction would not prevent Congress from amending the underlying regulatory regime, such as by enacting new capitalization requirements. Such an amendment would likely be -- as indeed FIRREA was -- not a simple attempt to modify a particular term of a single thrift agreement, but would rather represent a major change in the overall scheme regulating the industry as a whole. It is not a "modification" of a contract when the parties merely adhere to an express term that plainly provides that, notwithstanding any other term, no party to the contract is required to do anything contrary to law.

All of the plaintiffs now complain that they would not have entered into the agreements here and the various relevant transactions if they had not had the guarantees they wish immunizing them from statutory changes.

These statements make all the more telling our point about the strangeness of the fact that so much language now thought to be essential is missing. If it was so important that plaintiffs have contract protection against revisions in the regulatory scheme it is especially puzzling that they did not actually include those terms in any of the agreement documents.

The thrifts also now say that the agreements they entered into were illusory. This claim is mistaken.

Plaintiffs sought approval by federal regulators for thrift transactions into which they voluntarily entered. Simply because such transactions were also desired by the regulators and were helpful to the Government at the time does not change the fact that the actions at stake were regulatory agency grants of applications for thrift transactions that statutorily required approval.

Plaintiffs obtained the needed government approvals and acquired the franchises they wanted, thereby gaining particularly favorable accounting treatment for a number of years, and in some instances large infusions of federal deposit insurance money. Under these circumstances, it is difficult to understand the assertion that the agreements were illusory even if they were subject to being affected at some future date by legislative changes, as is all commercial activity. Like any agreements, these entailed certain risks while affording significant benefits of various kinds. That the agreements, with the benefit of hindsight, did not protect plaintiffs from one of the risks does not mean that they were illusory.

In addition, this claim is strange since plaintiffs do not assert that they negotiated any right to be free from legislative adjustments in minimum capitalization levels, which also might have rendered their transactions unprofitable. Does that mean that the agreements were illusory? Surely not.

Furthermore, entities acquiring thrifts had an interest in the length of the amortization period for the goodwill created in their transactions independent of the period during which goodwill might be included in regulatory capital. Thrifts wanted long-term amortization periods for goodwill because the acquired entity could then appear to be generating greater income in the years immediately following the acquisition. See Accounting for Certain Acquisitions of Banking or Thrift Institutions, Statement of Financial Accounting Standards, No. 72 ¶ 5; Accounting Principles Board Opinion No. 16 ¶ 88 (1970). There was thus a reason for thrifts to obtain the approvals and forbearances they sought beyond having goodwill count as regulatory capital.

* * * * * *

In sum, plaintiffs do not have the contracts they now claim. None of them has a binding contract term guaranteeing a set form of regulatory treatment for up to 40 years regardless of whatever changes Congress makes in the underlying legislative regime.

B. The Unmistakability Doctrine

1. As noted earlier, plaintiffs spend much of their briefs addressing an issue not before this Court. They seem to hope to frighten the Court by portraying the governmental action here as going far beyond what it actually does. Thus, plaintiffs discuss at length the question of whether the United States can constitutionally abrogate contract rights.

This issue is not posed by this interlocutory appeal from a specific trial court order finding contract breaches and liability. The question here is whether plaintiffs have the contract rights they claim; this is a contract interpretation issue and does not involve a constitutional question concerning the limits of the powers of Congress.

2. The unmistakability doctrine upon which we rely is a straightforward rule of contract interpretation: a party who claims that the Federal Government has contracted away its sovereign power to change a statutory scheme must show unmistakable evidence of an intent by the Government to so contract.

Our reliance on this rule is solidly based upon Supreme Court precedent, decisions by the District of Columbia, Fourth, and Eleventh Circuits in cases either identical or similar to this one involving FIRREA, and decisions by the D.C., Eighth, and Ninth Circuits in analogous circumstances involving interpretation of claimed contracts with the Federal Government. See Bowen v. Public Agencies Opposed to Social Security Entrapment, 477 U.S. 41 (1986) (hereafter "POSSE"); Transohio Savings Bank v. Director, OTS, 967 F.2d 598 (D.C. Cir. 1992); Charter Federal Savings Bank v. OTS Director, 976 F.2d 203 (4th Cir. 1992); Guaranty Financial Services, Inc. v. Ryan, 928 F.2d 994 (11th Cir. 1991); Education Assistance Corp. v. Cavazos, 902 F. 2d 617, 629-30 (8th Cir.), cert. denied, 498 U.S. 896 (1990); Western Fuels-Utah, Inc. v. Lujan, 895 F.2d 780 (D.C. Cir.), cert. denied, 498 U.S. 811 (1990); Peterson v. Dept. of the

Interior, 899 F.2d 799 (9th Cir.), cert. denied, 498 U.S. 1003 (1990).

Contrary to plaintiffs' attempt to blow it far out of proportion, this rule of contract interpretation is neither startling nor far-reaching. It serves to protect the democratic system through which our government works by properly balancing the public interest generally against individuals with contract rights. It does so by providing that courts will not even reach the issue of potential tension between constitutional doctrines concerning contract rights and Congress' sovereign power to regulate for the public welfare unless it is absolutely clear from the words used in the alleged contract that it contains promises of immunity from the effect of future changes in the law. See POSSE, 477 U.S. at 52-53 (noting Supreme Court's "often-repeated admonitions that contracts should be construed, if possible, to avoid foreclosing exercise of sovereign authority").

The application of the unmistakability doctrine to these cases is straightforward. If any of the alleged contract terms will allow for two interpretations -- one that binds Congress to a particular regulatory treatment and one that does not -- the latter interpretation must be applied. See POSSE, 477 U.S. at 52-53. In the myriad documents offered by plaintiffs as constituting their sundry contracts none clearly requires particular regulatory treatment by Congress. **At most**, some contract terms could be interpreted as requiring the relevant agencies to continue certain regulatory treatment so long as the agency retained the discretion to permit such treatment.

Plaintiffs nevertheless contend that all that their asserted contracts need do is provide that the relevant thrifts could amortize goodwill over an extended period. In so arguing, plaintiffs are merely saying that they do not like the results reached by the Supreme Court in POSSE, and by this Court's sister circuits in Charter, Transohio, and Guaranty, and wish this Court would ignore those rulings.[3] Furthermore, given the cases cited above, plaintiffs' strategy of making it seem like the D.C. Circuit in Transohio is out of the mainstream on this point is patently wrong.

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[3] Plaintiffs argue at various points that Charter is distinguishable because the Fourth Circuit noted the difference (976 F.2d at 211 n.12) between the documents in that case and the ones at bar here. Nevertheless, the fact remains that the Charter court assumed for purpose of analysis a contract between the thrifts and the Government, but then agreed with the D.C. and Eleventh Circuits in Transohio and Guaranty that the unmistakability doctrine defeats the type of contract right claimed here. Plaintiffs also shunt aside Guaranty because the documents there too differed from those in this case. But, again, the legal analysis employed by the Eleventh Circuit in Guaranty, 928 F.2d at 1000-01, is directly at odds with the arguments made by the thrifts here.

3. Plaintiffs attempt to evade POSSE by contending that it does not apply to them because they are not trying to bind the hands of Congress since they are seeking only damages for breach of contract. This argument is cleverly and carefully worded, and, although it has surface appeal, when this point is closely examined it does not make sense.

Plaintiffs' argument that the unmistakability doctrine applies only to attempts to enjoin Congressional legislative action must be rejected. A reading of the Supreme Court's decision in POSSE establishes that the Supreme Court there was setting out a principle of contract interpretation. If the question is what the terms of a contract are in order to determine if it has been breached, then the nature of the remedy that a plaintiff chooses to seek in any particular case -- whether an injunction against a statutory scheme under substantive due process principles, specific performance, or damages for breach -- is irrelevant. The issue is what does the contract provide. POSSE instructs the federal courts how to go about deciding that question, which is the one posed here. (Indeed, in Charter, the Fourth Circuit applied the unmistakability doctrine to a contract claim where the relief sought was rescission.)

Moreover, given plaintiffs' heavy reliance on the Supreme Court's ruling in Lynch v. United States, 292 U.S. 571 (1934), their claim that they are not attempting to bind Congress' hands violates common sense. In Lynch, the Supreme Court held that, in light of the Due Process Clause, Congress was without power to abrogate legislatively the contract rights at issue.

Here, plaintiffs claim that a fully authorized agency of the Federal Government signed valid contracts with them guaranteeing that a particular regulatory regime would apply to their thrifts regardless of changes in the law governing all other thrifts. In simple English, plaintiffs thus contend that they negotiated contracts exempting them from legislative changes, and that, if such changes were nevertheless applied to them, that new regulation would constitute a breach of valid, enforceable contracts rights.

By asserting that they have valid contract rights to a particular form of regulatory treatment, plaintiffs are arguing against Congress' ability to exercise its sovereign power to change the legislative scheme governing the thrift industry, and to apply that new scheme to them specifically. The remedy that plaintiffs choose to enforce the contract rights they claim does not change the nature of the claimed rights or the fact that they are claiming them.

4. Application of the unmistakability doctrine by the D.C. Circuit in Transohio, the Fourth Circuit in Charter, and the Eleventh Circuit in Guaranty, in no way undermines the validity of contracts with the Federal Government. Plaintiffs' attempt to make it seem that no contracts with the Government are safe is mistaken.

Governing law is an inherent part of all contracts; this rule is no less true of contracts with the Government. See POSSE, 477 U.S. at 52. Further, as we pointed out in our opening brief (at 46-49), the Government is obviously **not** free to breach or repudiate its contractual obligations with impunity. The Supreme Court has instructed in Lynch, 292 U.S. at 576-77, that contracts are enforceable against the United States, and the Court reiterated that point in POSSE, 477 U.S. at 52, 55. Thus, this Court should not be stampeded by Statesman's cry (Br. 32) that the Government can now abrogate all contracts.

What is at issue here is not the Government's breach of an asserted standard commercial contract (e.g., for procurement). Rather, Congress has changed the underlying legislative scheme of a comprehensive regulatory program, and that amendment has an impact on all relevant contracts whether or not they are with the Government itself. What the unmistakability doctrine provides is that contracts with the Government will not, absent unequivocal language, be read to provide that they are immune from changes in the governing legislative regime.

Statesman's contention (Br. 47) that the only interest the Government is protecting here "is its own pocketbook" sounds nice, but is wrong. As described in our opening brief, Congress poured hundreds of billions of public dollars into rescuing the thrift industry and has thoroughly revamped the regulatory scheme governing that industry so that a crisis does not recur. Congress changed existing policies regarding intangible assets such as goodwill in order to force thrifts to a sounder footing so that the massive disruption and costs of their failures could be avoided in the future. The legislation and its history prove that FIRREA is not simply about the Government protecting its wallet; it is an overhaul of an entire program affecting the nation's financial and housing market on a massive scale.

Even in a more limited sense Statesman's argument is wrong. The result of Congress' action in FIRREA is that the inadequate capital of many thrifts became apparent, and such thrifts had to be liquidated by the Government at significant cost to the taxpayers. Statesman and Winstar are examples of this phenomenon. Thus, the Government's action hardly protected its own pocketbook.

Furthermore, the overwhelming number of contracts between the United States and private parties are never affected in any way by changes in underlying legislative regulatory schemes. Again, therefore, plaintiffs' attempts in their briefs to make it seem as if all government contract law is being overthrown by the panel's ruling here are wildly overblown.

Moreover, the Supreme Court's opinion in POSSE makes quite clear that the unmistakability doctrine applies even when the new legislation is passed specifically in part to override an existing agreement. There, the states and their localities had an explicitly stated right to withdraw from the Social Security system. When Congress legislatively deleted that right, despite the fact that it was written in agreements, based on the unmistakability doctrine the Supreme Court upheld the legislation against attack.

The thrifts nonetheless argue that their contracts covering treatment of goodwill are sufficient, and that they need not anticipate and specifically prohibit all potential breaches of their contracts by the Government. While the latter part of this claim is certainly true, it does nothing to make the unmistakability doctrine inapplicable here. Parties contracting with the Government do not have to guard against all possible breaches; if they wish to try to make their contracts immune from legislative changes, however, the Supreme Court has stated unequivocally that they must make such a provision unmistakable.

In sum, the unmistakability doctrine applies here with full force, and must be used to determine the content of the contracts between plaintiffs and the Government. Plaintiffs' various arguments about the limited ability of the Government to abrogate contract rights in light of the Constitution simply have no relevance. And, as we pointed out in our opening brief, if we are right and plaintiffs did not have any contract right that was breached, then the constitutional issues are also resolved because, in the absence of such property rights, no constitutionally protected interests could have been violated by the Government.

C. Other Issues

1. At a number of places in its brief (at 13, 28, 40, 41), the Statesman plaintiffs contend that the result reached by the

panel here is unfair because the regulation of goodwill has changed and the Government has been allowed to keep the $21 million investment made by the Statesman plaintiffs. Once more, this is an impressive rhetorical flourish, but wrong.

It is essential to understand that the Statesman investors did not pay money to the United States. Instead, they invested in thrifts that they acquired in the voluntary acquisition by Statesman. Given the virtual collapse of the industry and the subsequent change in the regulatory scheme, this investment turned out to be unprofitable. Plaintiffs failed to invest the additional capital needed to maintain Statesman's viability, and a receiver was appointed because Statesman was financially unsound.

Moreover, the Government fulfilled any agreement that it had with Statesman. As shown above, there was no contract obligation by the United States not to change the legislative scheme covering the thrift industry and to apply that new system to all thrifts.

The $21 million was thus an investment in a thrift by the Statesman plaintiffs. There is no federal agency or coffer that has this $21 million. Once a receiver was appointed, the Federal Government had to pay off Statesman's insured deposits, and all other creditors of the thrift lost money. It is therefore quite inaccurate to make it seem as if the United States somehow has the investment made by the Statesman owners.

2. Both Statesman and Glendale heavily rely upon this Court's recent ruling in Hughes Communications Galaxy, Inc. v. United States, 998 F.2d 953 (Fed. Cir. 1993). Since the full Court is sitting here in banc, it is not constrained by its ruling in Hughes.

As we stated in our rehearing petition in Hughes, we believe that the decision there is mistaken and is inconsistent with the ruling by the panel in this case. We think that the Hughes panel failed to given adequate force to the unmistakability and sovereign acts doctrines.

There are, however, differences between Hughes and this case. First, the Hughes decision was based upon that panel's analysis of the specific contract language at issue there, which involved the asserted binding nature of a Presidential policy concerning space shuttle payloads. The contract language involved here covers a distinct subject and industry, and is phrased very differently. While the contract in Hughes could be read as incorporating a specified Presidential policy, none of the documents in Glendale or Winstar even deals with the policy of treatment of goodwill for regulatory capital purposes, and the documents in Statesman do not address policy contained in legislation conflicting with prior accounting practices.

Second, the Hughes case does not involve the effect of Congressional overhauling of an entire massive regulatory program substantially affecting the national economy.

Despite these differences, we repeat that we think Hughes is wrongly decided and inconsistent with POSSE.

3. At the end of its brief, Statesman contends that its contract was breached for the additional reason that the new regulatory agency -- OTS -- wrongly treated its capital credit as goodwill that will not be counted toward regulatory capital requirements.

The trial court did not adopt this theory. Moreover, we think it highly questionable that this issue can properly be raised before the Court of Federal Claims or this Court as a colorable breach of contract claim.

There is no document in the Statesman record that could be read in any way to include an agreement that the Government will not treat the capital credit here as RAP goodwill, and thus subject to regulation as goodwill. (See our opening brief at 6 for a discussion of this type of intangible asset.) OTS and its predecessor agencies treated capital credits such as those held by Statesman as the equivalent of goodwill, an intangible asset that FIRREA phases out in meeting capitalization requirements. See Transohio, 967 F.2d at 604-05. Indeed, unfortunately for the Statesman plaintiffs, if the capital credits were not treated as RAP goodwill, they would be intangible assets anyway, and completely excluded from most capital calculations under FIRREA. See 12 U.S.C. 1464(t)(9) and 1463(c).

To the extent that the Statesman plaintiffs are complaining about the general regulatory decision by OTS to treat capital credits as RAP goodwill their claim is not a colorable contract breach claim under the Tucker Act because no relevant contract document even arguably addresses this subject. Rather, the Statesman plaintiffs should have proceeded in a United States district court under the Administrative Procedure Act to challenge OTS' regulatory administrative action, which covers all thrift capital credits.

Since no contract document addresses the issue of treatment of a capital credit as RAP goodwill, and the Statesman plaintiffs do not point to one, their contract claim fails in any event on its merits.

CONCLUSION

For the foregoing reasons, as well as those stated in our opening brief, the decisions of the Claims Court should be reversed, and judgment should be entered for the United States on the contract breach claims in each of the three cases covered by this appeal. If the Court reaches this result, it should also direct judgment for the United States on all of plaintiffs' contract and just compensation claims.

Respectfully submitted,

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December 10, 1993

CERTIFICATE OF SERVICE

I hereby certify that on this 10 day of December 1993, I served the foregoing Replacement Reply Brief of Defendant United States upon counsel by causing copies to be mailed, first class postage prepaid, to:

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REPLACEMENT BRIEF OF DEFENDANT-APPELLANT UNITED STATES

IN THE UNITED STATES COURT OF APPEALS
FOR THE FEDERAL CIRCUIT

No. 92-5164

WINSTAR CORPORATION, UNITED FEDERAL SAVINGS BANK,
STATESMAN SAVINGS HOLDING CORP., THE STATESMAN GROUP INC.,
and AMERICAN LIFE AND CASUALTY INSURANCE COMPANY.

and

GLENDALE FEDERAL BANK, FSB,

Plaintiffs-Appellees,

v.

THE UNITED STATES,

Defendant-Appellant.

ON A PETITION FOR PERMISSION TO APPEAL FROM AN
ORDER OF THE UNITED STATES CLAIMS COURT IN
90-8 C, 90-772 C AND 90-773 C ENTERED
July 24, 1992, FROM CHIEF JUDGE LOREN A. SMITH

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October 15, 1993

STATEMENT OF RELATED CASES

The three consolidated cases covered by this appeal have previously been before a panel of this Court, whose ruling has now been vacated by the full Court. There are a large number of cases pending in the Court of Federal Claims that will be directly affected by this Court's decision here. See A272.

STATEMENT OF JURISDICTION

The statutory basis for jurisdiction over these cases in the United States Claims Court was 28 U.S.C. 1491(a)(1). (After these cases were brought, the trial court's name changed to the United States Court of Federal Claims.) This Court has jurisdiction over this interlocutory appeal under 28 U.S.C. 1292(d)(2). The appeal is timely under that statutory provision because permission to appeal was sought from this Court within ten days of the Claims Court's order certifying issues for interlocutory appeal.

STATEMENT OF THE ISSUES

In response to the severe crisis in the savings and loan industry in the late 1980s, Congress passed the Financial Institutions Reform, Recovery and Enforcement Act of 1989 (103 Stat. 183) ("FIRREA"). That Act strengthened capitalization requirements for thrift institutions, and restricted use of intangible assets such as "goodwill" to meet those requirements.

Plaintiffs/appellees here are the owners of two now-defunct thrift institutions and one currently operating thrift. They assert that they had contracts with the United States Government regarding regulatory treatment of goodwill, and that the Government has breached those contracts by applying to them the current statutorily mandated capitalization requirements of FIRREA.

The issues presented in this appeal are:

1. Whether plaintiffs had contracts with the Government guaranteeing a particular method of regulatory treatment for goodwill.

2. Whether, in the absence of contract language specifically so stating, plaintiffs had protected contract rights entitling them to a certain form of regulatory treatment of goodwill for up to 40 years, even if Congress later overhauled the entire regulatory scheme and restricted the use of goodwill for all thrifts.

STATEMENT OF THE CASE

I. Nature Of The Cases

The plaintiffs here are the owners of two now-defunct thrift institutions (United Federal Savings Bank, which was owned by plaintiff Winstar Corporation; and Statesman Bank for Savings, which was owned by plaintiff Statesman Savings Holding Corp.), and one currently operating thrift, plaintiff Glendale Federal Bank, FSB ("Glendale"). They filed three separate actions against the United States in the Claims Court seeking monetary relief for asserted breach or frustration of contracts caused by FIRREA, or just compensation for taking constitutionally protected property rights.

Plaintiffs base their contract claims primarily on agreements that they signed with the Federal Savings and Loan Insurance Corporation ("FSLIC"), and on regulatory approvals and letters issued by the Federal Home Loan Bank Board ("Bank Board") -- both agencies that FIRREA abolished -- governing transactions where an intangible asset known as "goodwill" was created. At the time these asserted contracts were entered into plaintiffs were allowed to count this goodwill in meeting federal minimum regulatory capital requirements.

In each case, the Claims Court determined that plaintiffs had contracts with the United States governing long-term regulatory treatment of goodwill, and that those contracts had been breached by FIRREA's new restrictions on use of goodwill to meet statutory capital mandates.

The Claims Court consolidated these rulings on contract liability, and certified its ruling for immediate interlocutory appeal, which this Court then granted permission to pursue (see 979 F.2d 216).

A divided panel of this Court ruled in favor of the United States, finding no contract rights that Congress had breached through FIRREA. The full Court has now set the case for in banc consideration.

II. Statement Of The Facts

A. Statutory Background

The development of the thrift industry since the Great Depression and the causes of the current upheaval in the industry help to understand the current statutory scheme and the positions of the parties here.

1. The Extensive Federal Regulation of the Thrift Industry.

Savings and loan institutions have been the subject of pervasive federal support, supervision, and regulation since the 1930s. See California Housing Securities, Inc. v. United States, 959 F.2d 955, 958 (Fed. Cir.), cert. denied, 113 S. Ct. 324 (1992) ("banking is one of the longest regulated and most closely supervised of public callings"). Indeed, so all-encompassing has the federal involvement been since the Great Depression that the modern thrift industry is now "a federally-conceived and assisted system to provide citizens with affordable housing funds." H.R. Rep. No. 101-54(I), 101st Cong., 1st Sess. 292 (1989), reprinted in 1989 U.S. Code Cong. & Admin. News ("USCCAN") 86, 88 ("House Report").

In response to the failure of many thrift institutions during the Great Depression, in 1932 Congress created the Bank Board to channel funds to thrifts in order to prevent foreclosures and allow thrifts to make loans on residences. H.R. Rep. No. 1418, 72d Cong., 1st Sess. 4-6, 8-11 (1932); House Report at 292, 1989 USCCAN at 88.

As the industry's problems continued, Congress added the Home Owners' Loan Act of 1933 (48 Stat. 128), which authorized the Bank Board to charter and regulate federal savings and loan associations. This 1933 legislation also provided substantial federal financial support for the thrift industry. House Report at 293, 1989 USCCAN at 89.

In a further effort to restore public confidence in the nation's thrift industry, and to ensure the continued availability of adequate home mortgage funding, Congress provided in the National Housing Act of 1934 (48 Stat. 1246) essential federal support through federal deposit insurance for thrifts. This statute established the Federal Savings and Loan Insurance Corporation ("FSLIC") under the direction of the Bank Board, and authorized the FSLIC to regulate federally-insured thrifts.

For many years, these statutes and the regulations promulgated thereunder provided a comprehensive regulatory scheme for a federally insured thrift's business affairs. See Fidelity

Federal Savings & Loan Ass'n v. de la Cuesta, 458 U.S. 141, 145 (1982); Fahey v. Mallonee, 332 U.S. 245, 250 (1947).

Capital requirements -- both the amount of capital required and the items properly counted as capital -- have long been part of the regulatory scheme. Since their creation, the Bank Board and the FSLIC set minimum capital requirements for federally insured thrifts. These requirements have been the subject of numerous statutory and regulatory changes over the years.[1] In 1982 alone the regulations governing thrift capital reserve requirements changed three times. See 47 Fed. Reg. 3543; id. at 31859; id. at 52961. See also 45 Fed. Reg. 72681 (1980) (Bank Board proposal to change regulatory treatment of goodwill).

2. The Recent Thrift Industry Crisis and Enactment of the FIRREA.

a. In the late 1970s and early 1980s, high interest rates and record inflation resulted in a sharply higher cost of funds for thrifts. At the same time, many thrifts held long-term, low-yielding fixed rate mortgages. This "negative interest rate mismatch" precipitated a major crisis in the thrift industry, with many thrifts suffering immense operating losses. See House Report at 294-95, 1989 USCCAN at 90-91.

Congress and the federal regulators tried to solve the thrift industry problem by, among other methods, expanding thrift operating powers, reducing minimum capital requirements, and

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[1] See, e.g., Garn-St Germain Depository Institutions Act of 1982 (96 Stat. 1469); Depository Institutions Deregulation and Monetary Control Act of 1980 (94 Stat. 132); Emergency Home Finance Act of 1970 (84 Stat. 450).

permitting use of accounting methods that artificially inflated the value of thrift capital. House Report at 295-98, 1989 USCCAN at 91-94; S. Rep. No. 101-19, 101st Cong., 1st Sess. 9 (1989) ("Senate Report").

Among the regulatory methods employed was the Bank Board's policy of permitting goodwill -- an intangible "asset" created under Generally Accepted Accounting Principles ("GAAP") to balance financial statements -- to be used to meet federal regulatory capital requirements. If a thrift used the "purchase method of accounting" for a merger and paid more for the acquired entity than its liquidation value, the thrift could record that excess as goodwill. See Accounting Principles Board ("APB") Opin. No. 16, ¶¶ 11 and 87 (1970).

If a thrift acquired another one having financial difficulties, the former could record as "supervisory goodwill" any excess in the fair market value of the liabilities of the merged thrift over the fair market value of that institution's assets. Put simply, the surviving thrift could declare as an asset the merged thrift's net worth shortfall.

Another type of intangible asset known as Regulatory Accounting Practices ("RAP") goodwill was created from FSLIC cash contributions to merging thrifts, and the Bank Board often allowed double counting of these contributions toward meeting regulatory capital. See Security Savings and Loan v. Director, OTS, 960 F.2d 1318, 1320 n.5 (5th Cir. 1992); Transohio Savings Bank v. Director, OTS, 967 F.2d 598, 604 (D.C. Cir. 1992).

The measures taken to aid the financial situation of the nation's thrifts proved counterproductive. "With little of their own capital at risk, the predominant feeling among many thrift managements was that the easiest way to regain profitability and generate adequate levels of new capital, was to grow rapidly." House Report at 298-99, 1989 USCCAN at 94-95; Senate Report at 9.

Not surprisingly, "[c]onsumer confidence in the nation's savings and loan system * * * decline[d] rapidly" due to fears about the instability of the system; in the first quarter of 1989 alone, thrift depositors withdrew $28.5 billion from institutions, considerably eclipsing the previous annual record. House Report at 305, 1989 USCCAN at 101.

b. With the thrift industry in such disarray, the President and Congress recognized the "clear" need for remedial legislation; "[t]he Administration and the Congress must restore public confidence in the savings and loan industry in order to ensure a safe, stable, and viable system of affordable housing finance." House Report at 306, 1989 USCCAN at 103. Their efforts resulted in FIRREA, which, among other things, has provided well over $100 billion in taxpayer money to close insolvent institutions and recapitalize the insurance fund protecting thrift deposits.

FIRREA also substantially modified the overall federal thrift regulatory scheme by: (1) abolishing the FSLIC and transferring its functions to other agencies; (2) creating a new thrift deposit insurance fund under the FDIC; (3) eliminating the Bank Board and replacing it with the Office of Thrift Supervision

("OTS") -- an office within the Department of the Treasury -- and making the OTS Director responsible for regulation of all federally insured savings associations and chartering of federal thrifts; and (4) establishing the Resolution Trust Corporation, charged with resolving certain closed thrifts. See 12 U.S.C. 1437 note; 1441a; and 1821.

c. At the "heart" of this legislative reform (135 Cong. Rec. 18863 (1989) (Sen. Riegle)) is the requirement that OTS "prescribe and maintain uniformly applicable capital standards for savings associations." 12 U.S.C. 1464(t) (1)(A). FIRREA establishes three categories of thrift capital and sets strict minimum requirements for them. See 12 U.S.C. 1464(t)(2). OTS Regulations implementing these new capital standards became effective within a short period. 54 Fed. Reg. 46861 (1989).

During consideration of FIRREA, Members of Congress time and again emphasized the importance of strengthened capital requirements. As Senator Chafee stated, "raising the capital standard is the strongest and most critical requirement in the conference report. It is the backbone of the legislation." 135 Cong. Rec. 18860 (1989).

The strengthened capital requirements were considered crucial to prevent a recurrence of the thrift crisis, since, in Congress's view, "[t]o a considerable extent, the size of the thrift crisis resulted from the utilization of capital gimmicks that masked the inadequate capitalization of thrifts." <u>House Report</u> at 310, 1989 USCCAN at 106.

Congress determined that strengthening thrift institution capitalization serves two key functions: (1) it "provide[s] the self-restraint necessary to limit risk-taking by Federally insured savings associations" since "[w]ithout sufficient capital, [thrift] owners have little incentive to limit the risks taken with depositors' funds"; and (2) it "protects the deposit insurance fund by providing a cushion against losses if the institution's condition deteriorates." H.R. Conf. Rep. No. 101-222, 101st Cong., 1st Sess. 404 (1989), reprinted in 1989 USCCAN 432, 443.

Accordingly, FIRREA instructs OTS to "require all savings associations to achieve and maintain adequate capital" by meeting or exceeding the new minimum capital standards. 12 U.S.C. 1464(s).

d. As an essential element of requiring greater thrift capitalization, Congress severely restricted the use of goodwill as a component of capital. In Congress' view, goodwill was "one of the remaining poisons of the savings and loan industry" (135 Cong. Rec. 12068 (1989) (Rep. Price)), and its use as capital was considered entirely antithetical to the goal of requiring greater thrift capital.

As Congress recognized, "[g]oodwill is not cash. It is a concept, and a shadowy one at that. When the Federal Government liquidates a failed thrift, goodwill is simply no good. It is valueless. That means, quite simply, that the taxpayer picks up the tab for the shortfall." Id. at 11795.

Numerous Members of Congress explained how allowing use of goodwill to meet capital requirements would be at odds with the regulatory goal of discouraging imprudent practices. The limitation on goodwill as capital was deemed necessary because, as Representative Wylie stated, when a thrift is operating on the basis of goodwill, the thrift's owners and management

> are not really gambling with their own money because they do not have any money up front. [Instead,] [t]hey are gambling with the public's money. If the business succeeds, management gets the profits. If the business goes down the drain, the [federal insurance fund] pick[s] up the losses * * *.

135 Cong. Rec. 12064 (1989).

Thus, a legislative demand for hard money capital was an essential quid pro quo for the expenditure of the billions of dollars to be provided by the United States Treasury to restore the deposit insurance fund to health and to bring back public confidence in the thrift industry. Congressman Frenzel explained: "How can we face those taxpayers who we have to stick with costs of the bailout, if we can't guarantee to them they won't have to bail out the industry again?" 135 Cong. Rec. 12075 (1989).

Consequently, in FIRREA, Congress strictly limited the use of goodwill to meet capital requirements. The new regulatory scheme provides three minimum capital requirements for thrifts to meet, prohibits the use of goodwill and other intangible assets to meet the tangible capital requirement, limits the amortization of goodwill to twenty years or less, and permits only some supervisory goodwill to be used to meet the core and risk based capital requirements during a phase-out period. 12 U.S.C. 1464(t)(1)(A), 1464(t)(2) and (3); 1464(t)(9); and 12 C.F.R. 567.2, and 567.5.

Although it places limits on its use, FIRREA does not eliminate goodwill; it allows some supervisory goodwill to be used to meet two of the capital standards, and also permits goodwill to be counted for the purpose of determining the extent to which thrifts may make certain types of loans and investments. See, e.g., 12 U.S.C. 1464(c)(2)(A), 1464(t)(3).

B. The Individual Thrift Transactions at Issue

1. Glendale

In November 1981, Glendale negotiated a merger with a failing thrift institution -- First Federal Savings and Loan Association of Broward County -- and the two thrifts entered into a Merger Agreement, which required FSLIC regulatory approval. A275.

Glendale applied for FSLIC permission for the merger, and also requested substantial financial assistance from the Government. Later that month, Glendale and the FSLIC entered into a Supervisory Action Agreement, which contained the terms of potential Government assistance for the proposed merger. This agreement said nothing about treatment of goodwill. See generally A1295-1311. It expired in November 1991. A1307.

On the same day, the Bank Board issued a "forbearance letter" whereby the agency stated that it would forbear from bringing enforcement proceedings against Glendale for failing to satisfy regulatory capital requirements following the merger. A276. This forbearance letter did not address goodwill either. A1312-13.

The Bank Board also issued a resolution at that time approving the proposed merger. A276. That resolution required Glendale to provide a justification under GAAP for use of the purchase method of accounting for this merger. A276. Glendale provided that justification, indicating that it would amortize over $716 million in goodwill over 40 years. A277.

Glendale's accounting of goodwill is now inconsistent with the requirements of FIRREA.

2. Winstar

In 1983, the Bank Board solicited bids for Windom Federal Savings & Loan, which had shown considerable losses. Winstar Corporation was formed in 1984 for the purpose of acquiring Windom, and the Bank Board and the FSLIC negotiated terms under which Winstar and United Federal Savings Bank would acquire Windom in 1984. A36.

As part of the regulatory approval of the acquisition, the Government signed an Assistance Agreement under which it would contribute over $5.5 million to United, while Winstar contributed $2 million to United. A41. That agreement expired in July 1986. A86.

The Bank Board issued a forbearance letter in July 1984, which permitted United to account for goodwill from the acquisition (approximately $9.1 million) by the purchase method of accounting, allowing amortization over 35 years. A59-60.

The Bank Board, in Resolution No. 84-363, conditioned approval of the acquisition and Winstar agreed to a Net Worth Maintenance Stipulation, requiring compliance with capitalization regulations "as now or, hereafter in effect * * *." A158. Under this stipulation, Winstar agreed to contribute cash to the thrift in order to maintain compliance with capital standards.

Winstar's treatment of goodwill was inconsistent with FIRREA's terms, enacted five years later, and the thrift failed to meet the new statutory capital requirements. (Even if Winstar had been able to count all goodwill fully, the thrift would most likely have fallen below FIRREA capital standards. See A291-92.) Consequently, the OTS Director appointed a receiver for the thrift, and it no longer exists.

3. <u>Statesman</u>

Statesman approached the Bank Board in 1987 concerning acquisition of a subsidiary of an insolvent thrift in Florida. The FSLIC informed Statesman that the Government could monetarily assist in the acquisition only if Statesman also took over the insolvent thrift, and that, under then-existing regulations, the acquired thrift had to have a certain level of assets. In order to reach that level, FSLIC offered Statesman three other thrifts located in Iowa. Statesman accepted the offer. A273.

As part of the transaction, FSLIC and Statesman entered into an Assistance Agreement under which the Government made a cash contribution of $60 million. Under that agreement and a Bank Board resolution, $26 million of that amount was in the nature of a "capital credit," which the Bank Board would allow the thrift to count as RAP goodwill towards its regulatory capital. A273-74. The Bank Board resolution also permitted use of the purchase method of accounting for the acquisitions. Thus, Statesman was allowed to amortize $25.8 million more in supervisory goodwill for 25 years. A273.

Statesman's accounting of both types of goodwill is now contrary to FIRREA.[2] As a result, Statesman Bank failed to meet the capital requirements, and the OTS Director appointed the RTC as a receiver for the thrift in July 1990. A275.

C. The Claims Court's Rulings

In each of these three cases, the Claims Court held that the thrift had a contract with the Government guaranteeing a particularly favorable long-term regulatory treatment of goodwill, and that FIRREA breached this contract right by restricting use of existing goodwill to meet regulatory capital requirements.

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[2] FIRREA did not impair Statesman's ability to count the FSLIC cash assistance as a capital asset. See 12 U.S.C. 1463(b)(2)(A). However, RAP goodwill is now treated as "other qualifying goodwill" for purposes of computing a thrift's capital compliance under the current regulatory scheme. See 12 C.F.R. 567.5(a)(2)(iii)(B). This limits the double counting of cash assistance -- described above -- that had previously been permitted.

In Winstar, in July 1990, the Claims Court issued a decision (21 Cl. Ct. 112) holding that the thrift had an implied-in-fact contract with the Government concerning treatment of goodwill. A35. However, at that time, the court refrained from granting summary judgment on plaintiffs' breach of contract claims.

In April 1992, the Claims Court issued a new opinion (25 Cl. Ct. 541). A43. The court reiterated its prior holding that Winstar had an implied-in-fact contract with the Government regarding long-term regulatory treatment of goodwill. It rejected our argument that no such contract provisions existed because Congress had not unmistakably waived its sovereign authority to amend regulatory schemes even if contract rights are thereby upset. A46-52. The court then concluded that FIRREA had breached this implied contract by restricting use of goodwill for regulatory capitalization purposes. A52-53.

Finally, the Claims Court rejected our argument that there could be no contract liability in any event because of the "sovereign acts" doctrine. The court found that doctrine inapplicable when legislation abrogates contracts of a particular class of individuals or entities. A53-56. Here, the court concluded that the goodwill restrictions were designed to take away plaintiffs' contract rights regarding goodwill. A55.

Having decided liability in Winstar, the Claims Court announced that it would in subsequent proceedings determine plaintiffs' injury, if any, and the appropriate measure of damages or rescission in that case. A56.

The Claims Court followed its Winstar rulings in Statesman and Glendale, two other pending cases before it. In April 1992, the court held that the plaintiffs in these cases had express contracts with the Government concerning regulatory treatment of goodwill. A271. In so holding, the court rejected our argument that the contracts themselves contained clauses making clear that they were not meant to require any unlawful action or inaction by either party.

The Claims Court then analyzed the D.C. Circuit's ruling in Transohio Savings Bank v. Director, OTS, 967 F.2d 598 (D.C. Cir. 1992), and found the D.C. Circuit mistaken. Contrary to the D.C. Circuit, the Claims Court held that the FSLIC had possessed power to enter into binding contracts, and that, for the contract rights it had found to be valid, the plaintiffs did not need to show an unmistakable intent by the agency to bind Congress to a particular regulatory policy. A284-90.

Under these circumstances, the Claims Court concluded that contracts covering both Statesman and Glendale had been breached by FIRREA. A278-83. It then consolidated these two cases, combined them with Winstar, and certified its order for immediate interlocutory appeal. A291-92.

In May 1993, a divided panel of this Court reversed the Claims Court ruling. Rejecting the arguments made by the plaintiffs, the panel majority held that the plaintiffs had failed to meet the high standard for showing that they had contracts guaranteeing them a specified form of favorable regulatory treatment for lengthy periods stretching well into the next century.

SUMMARY OF ARGUMENT

We recognize that since the panel majority opinion has been vacated by the full Court we cannot rely upon it here. Nevertheless, we note that much of our position follows the analysis of that opinion (slip op. at 25-36). Plaintiffs want this full Court to reject that approach, and thereby ask this Court to place itself in conflict with the three other circuits that have previously ruled on the arguments made here.

Plaintiffs claim that the FSLIC agreements and Bank Board letters and resolutions authorizing their various thrift transactions established binding contracts allowing them to count goodwill in meeting thrift capital regulatory requirements and to amortize this goodwill over an extended period. Further, plaintiffs claim that their contract rights went so far as to protect them against changes that Congress would enact in the underlying regulatory scheme in response to a disastrous crisis affecting the entire thrift industry.

Plaintiffs' claims are wrong for two independent reasons.

First, there were no contracts here purporting to bind the Government to any particular treatment of goodwill for regulatory purposes. In finding such contracts, the Claims Court wrongly relied upon a series of expired agreements between the thrifts and the Government, which in any event did not contain any provisions guaranteeing a set regulatory scheme for the lengthy periods that plaintiffs claim.

Moreover, the Claims Court incorrectly found that administrative actions by the then-existing regulatory agencies assigned to police the industry constituted contractual agreements by those agencies binding the Government. These statements of then-current prosecutorial and regulatory power represented policy decisions by the agencies, and were never intended to form contracts. Therefore, the Claims Court was wrong to rely upon them as constituting either express or implied contracts binding the Government to a set form of regulatory treatment.

Second, as the District of Columbia Circuit in Transohio Savings Bank, supra and the Fourth Circuit in Charter Federal Savings Bank v. OTS, Director, 976 F.2d 203 (4th Cir. 1992), cert. denied, 113 S. Ct. 1643 (1993), held in rejecting arguments nearly identical to those made here, the "unmistakability" doctrine establishes that no contracts existed in the cases at bar whereby the Government agreed that it would permit particular regulatory treatment of goodwill in the event that the statutory program governing thrifts was changed by Congress to prohibit such treatment. Yet, plaintiffs' cases depend upon the claim that they had contracts with the United States guaranteeing that regulatory treatment of goodwill for these individual thrifts would not change for up to 40 years, regardless of changes in the regulatory scheme.

Precedent from the Supreme Court instructs that all contracts entered into by the United States in the context of implementing a regulatory scheme are inherently subject to legislative changes made by the Congress. Thus, such contracts are **not** to be interpreted as interfering with Congress' power to legislate freely unless they say so in unmistakable terms. Without such clear contract language participants in pervasively regulated schemes such as the thrift industry cannot claim that they properly relied upon the regulatory program to remain unchanged. This principle is one of the foundations of our democratic system, which allows the voters to force change by electing new representatives not contractually bound by the rejected policies of their predecessors.

The ability of Congress to change an underlying regulatory scheme is an aspect of every contract in this context, and can be overcome, if at all, only by an unmistakable waiver. There is not even a hint of such a waiver by the Government in any document pointed to by the thrifts in these cases. Therefore, plaintiffs cannot establish that they had contract rights guaranteeing them a specified type of regulatory treatment regardless of legislative changes in the underlying scheme.

Further, interpreting any agreements here to include such a provision should be avoided since neither the Bank Board nor the FSLIC could bind Congress not to change the regulatory scheme as applied to all thrifts. Congress had never delegated authority to them to waive its sovereign power to legislate for the public welfare.

The analysis that we urge here is further compelled by the "sovereign acts" doctrine. That principle provides that, when Congress acts in its sovereign capacity in a public and general way, the effect of that action cannot be deemed a breach of contracts by the Government.

The sovereign acts doctrine is driven by the same reasoning described above that allows our democracy to work. It permits Congress to exercise its powers to act for the general welfare without being liable for contract damages. At the same time, the doctrine protects those holding contracts with the Government because it does not apply if the action taken by Congress is directed at avoiding contractual obligations, as opposed to exercising sovereign power for the general public welfare.

ARGUMENT

I. PLAINTIFFS HAD NO CONTRACTS WITH THE GOVERNMENT GUARANTEEING ANY PARTICULAR TREATMENT OF GOODWILL FOR THRIFT REGULATORY PURPOSES.

Plaintiffs' claims depend entirely upon their demonstrating the existence of contracts with the Government guaranteeing a particular form of regulatory treatment for goodwill stemming from their transactions, regardless of statutory changes. There are no such contract provisions here. To demonstrate this fact, we examine each of the thrift transactions in turn.

A. <u>Glendale</u>

The Claims Court concluded (A279-80) that there was an express contract between Glendale and the Government providing for amortization of goodwill for up to 40 years, and that this goodwill could be used to meet regulatory capitalization requirements during that entire period. There are a number of flaws in the Claims Court's conclusion.

It is not clear where the Claims Court believes this express contract is set out. The court itself could not decide, and listed seven (A275-83) different documents that apparently constituted the contract on this point. These documents include the regulatory agency approvals of Glendale's acquisition of First Federal, a Bank Board general memorandum regarding accounting practices, and even opinion letters from private independent accountants provided by Glendale to the Government. The former documents were never signed or agreed to by Glendale, and the latter were never signed by any representative of the Government. It is therefore somewhat baffling how this agglomeration could together form a single express contract on the issue of the regulatory treatment of goodwill by the Government over an extended period.

Surprisingly, the Claims Court mentions also the existence of a Merger Agreement, and its terms. A275. However, this was an agreement between Glendale and the thrift it was acquiring. See A275. This document was never converted into an express contract between Glendale and the United States, nor did the

Claims Court explain such a how conversion could have happened. The Fourth Circuit in Charter, 976 F.2d at 211, found that this type of agreement to which the United States was not a party did not constitute a contract with the Government.

There was a Supervisory Action Agreement, which contained the FSLIC's approval of the acquisition of Broward by Glendale. But this document nowhere mentions goodwill or the method of accounting for it. See generally A1295-1311. Moreover, that agreement expired in November 1991 (A1307), at which time Glendale was still in capital compliance with FIRREA. It was only in March 1992, after the expiration of the agreement, that Glendale's inability to count goodwill would have had a material effect on the institution.

The Bank Board also issued to Glendale a forbearance letter in November 1981 after the Broward acquisition, but the Claims Court specifically found that this letter "does not mention the use of supervisory goodwill" (A280), and it "did not specifically address the use of the purchase method of accounting for the merger" (A276). Thus, this forbearance letter could hardly serve as an express contract governing the regulatory treatment to be afforded goodwill for 40 years, or even be evidence of such an agreement.

The Claims Court seems to have hinged its holding on Bank Board Resolution No. 81-710, also issued in November 1981, although the court never states that this is the source of the express contract it found. This document too cannot serve the role it has been assigned because it merely required that Glendale furnish an opinion, satisfactory to the agency, from an independent accountant justifying under GAAP the use of the purchase method of accounting. A276.

This Bank Board resolution nowhere states that goodwill will be counted as capital for regulatory purposes. And, even if it is deemed to do so through its requirement for a justification of the purchase method of accounting, the resolution certainly nowhere states that the governing agency is going to permit Glendale to treat goodwill as capital for 40 years.

Glendale did produce the required letter from its accountants, and it was acceptable to the agency. See A277. But the Claims Court never pointed to anything in that letter stating that the Government will allow Glendale to count goodwill to meet regulatory capitalization requirements, and will continue to do so for 40 years. Rather, the court merely noted that the opinion letter furnished by Glendale explains that a large sum of goodwill will be amortized over 40 years. A277.

Even if these documents had contained language regarding regulatory treatment of goodwill, they cannot properly be converted into an express contract guaranteeing that Glendale can count goodwill for regulatory capital purposes for 40 years, regardless of any changes Congress may enact in the law -- a subject that **none** of them addresses.

The Claims Court has also incorrectly used Bank Board forbearance letters and resolutions as documents constituting express contracts with Glendale. These documents merely state prosecutorial and regulatory decisions, and do not create a contract. See Flagship Federal Savings Bank v. Wall, 748 F. Supp. 742, 748 (S.D. Cal. 1990) ("the forbearance letter was not a contract but a statement by the [Bank Board] that it would not prosecute * * *").

Bank Board resolutions are not contract documents; they were regulatory agency decisions issued in informal agency adjudications approving applications by thrifts to consummate mergers that could not have been completed without first obtaining regulatory approval (see 12 U.S.C. 1464 (1988)). The Fourth Circuit accepted this very point in Charter, 976 F.2d at 211, finding that "resolutions issued by the [Bank Board] in connection with the mergers merely granted that agency's approval of the merger and the accounting practices employed by [the thrift] in connection therewith," and did not constitute a contract. The Bank Board resolution here is devoid of language indicating any intent by the agency to enter into a contract.

The important distinction between a governmental act stating a regulatory policy and an agreement constituting a contract binding on the Government was illustrated by the Supreme Court in National Railroad Passenger Corp. v. Atchison, Topeka & Santa Fe Railway, 470 U.S. 451, 465-69 (1985). There, Congress changed an existing statute and mandated higher payments for specified rail employee privileges. Despite the existence of the prior statute, with use of the word "contract," the Court held that no contractual rights had been created because the repealed provision had merely stated a regulatory policy. Nothing in the relevant language evidenced an intent by Congress to bind the United States contractually. Id. at 465-70.

The principle applied in National Railroad was nothing new or startling. Over a century ago, the Supreme Court recognized that there can be no contract right to a regulatory scheme, regardless of a party's expectations to the contrary. See Welch v. Cook, 97 U.S. 541 (1878). There, the District of Columbia had enacted legislation declaring that all real property used for manufacturing purposes would be exempt from taxes for ten years. When the legislation was repealed, a private party brought suit on the ground that he had expended large sums in improving his property in reliance upon the legislation. The Supreme Court rejected the claim because "there is no pledge that [the legislation] shall not be repealed at any time." Id. at 542. Accord Wisconsin & Michigan Ry. Co. v. Powers, 191 U.S. 379, 386-87 (1903).

Given the long-running, pervasive nature of the regulation of the thrift industry and the fact that the regulation was constantly shifting, it is particularly unreasonable to treat agency statements of prosecutorial and regulatory policy in this field as creating contracts binding on the Government. As the Supreme Court explained in the context of rejecting a taking claim against retroactive application of changes in the federal pension regulatory scheme: "Those who do business in the regulated field cannot object if the legislative scheme is buttressed by subsequent amendments to achieve the legislative end." Connolly v. PBGC, 475 U.S. 211, 227 (1986).

Thus, the Bank Board forbearance letter and resolution involving Glendale were merely statements of then-current prosecutorial and regulatory policy; they cannot properly be transformed into contracts binding upon the Government for up to 40 years regardless of future congressional action.

The Claims Court, however, believed that the Bank Board forbearance letter and resolution became incorporated into the Supervisory Action Agreement under that document's integration clause. A279. However, that clause by its terms provided only that interpretations of the agreement "or understanding[s] agreed to in writing by the parties" become part of the agreement. A279. Under the integration clause, all of these materials then became the entire agreement between the parties and superseded prior agreements, except the Merger Agreement and the simultaneously issued Bank Board forbearance and resolution.

The integration clause by its plain wording meant that the Supervisory Action Agreement entered into by the FSLIC was not meant to supersede policies that a higher authority -- the Bank Board -- was stating with regard to the merger. That fact hardly converts those Bank Board documents from statements of then-current regulatory policy into contract terms, which as explained above is otherwise contrary to established law.

The Supervisory Action Agreement itself undermines the Claims Court's ruling because it contained a clause providing that: "Nothing in this Agreement shall require any unlawful action or inaction by either of the parties hereto." A280. This clause incorporates into the agreement between Glendale and the FSLIC the requirement that the law be followed, regardless of the rest of the agreement terms.

At the time of the acquisition of First Federal by Glendale, this clause caused no problem because nothing in that agreement was contrary to then-existing regulatory requirements. But once FIRREA was passed, it would be unlawful for OTS to grant an exemption from the goodwill restrictions.

Consequently, any contract with Glendale expressly recognized and accommodated the possibility of future changes in the applicable law, and the parties were bound by what those future changes would provide. Glendale therefore cannot establish that it had a contract guaranteeing it a particular form of regulatory treatment for up to 40 years despite supervening later legislation.

B. Winstar

By contrast with Glendale, the Claims Court in Winstar found no express contract regarding goodwill; instead, it found a contract implied-in-fact. This conclusion too is deeply flawed.

There actually was an agreement between the Government and Winstar regarding the acquisition of Windom Savings. An Assistance Agreement, entered into in July 1984, set the obligations assumed by the respective parties. A61-91. That agreement included a promise by the FSLIC to make a cash contribution to assist the merger, and to indemnify United against certain legal liabilities. Those obligations were fulfilled and **by its clear terms the Assistance Agreement terminated in July 1986**. A86.

Additionally, the Assistance Agreement prohibited the accounting treatment that Winstar now seeks. As in Glendale, the agreement provided that "[n]othing in this Agreement shall require any unlawful action or inaction by either party." A87. As explained above, permitting the accounting scheme that Winstar now wants would require an action made unlawful by FIRREA.

Further, as noted earlier, a Net Worth Maintenance Stipulation was provided for by Bank Board Resolution No. 84-363, which explicitly required compliance with capital regulations "as now or **hereafter** in effect * * *." A158 (emphasis added). The capital regulations have been amended to comply with FIRREA's capital requirements. Thus, the resolution covering Winstar contemplated the very type of changes that were made, and Winstar pledged to meet them.

The Winstar Assistance Agreement thus cannot possibly be the source of the asserted continuing contract right found here by the Claims Court. Apparently for that reason, that court looked to other documents to create an intent by the parties to contract. See A39. However, this type of contract creation is prohibited when there actually was an agreement between the parties.

The terms of a document ultimately executed by the parties -- the 1984 Winstar Assistance Agreement -- determine the contract terms actually agreed upon. See Calamari & Perillo, The Law of Contracts (3d ed., 1987) at 135 ("the final agreement made by the parties supersedes tentative terms discussed in earlier negotiations. Consequently, in determining the content of the contract, earlier tentative agreements and negotiations are inoperative"). Thus, the Claims Court could not look to other documents -- such as internal Bank Board staff memoranda -- as it did to find contract terms.

More importantly, the existence of an express contract -- the now-expired Assistance Agreement -- "precludes the existence of an implied-in-fact contract dealing with the same subject." Lichtefeld-Massaro, Inc. v. United States, 17 Cl. Ct. 67, 72 (1989) (citing Klebe v. United States, 263 U.S. 188, 192 (1923)).

The trial court here never explained how it avoided this rule. Instead, the court relied upon a July 1984 forbearance letter from the Bank Board to show an intent by the Government to be bound by an obligation regarding regulatory treatment of goodwill.

As explained immediately above, such a document does not give rise to contract rights; it merely represented a statement of then current agency policy. It in no way purported to provide an amendment to the Assistance Agreement, which was the complete integration of the parties' agreement and which expired in July 1986.

In addition, the Claims Court quoted what it viewed as the key part of that forbearance letter. A39. The letter contains no statement whatsoever concerning the long-term counting of goodwill for regulatory capitalization purposes. Accordingly, there was no contract on this point.

C. **Statesman**

The Statesman transaction is governed primarily by the March 1988 Assistance Agreement between the FSLIC and the Statesman plaintiffs, pursuant to which the FSLIC contributed $60 million to Statesman Bank. The terms of the Assistance Agreement provided that $26 million of that amount (the "capital credit") constituted RAP goodwill to be credited to Statesman's regulatory capital. A273.

Nothing in the Assistance Agreement, nor anything else in the documents material to this transaction, provides that this policy would continue notwithstanding subsequent changes in applicable law. Indeed, the Statesman Assistance Agreement contains the same governing law provision as in Glendale and Winstar, providing that no unlawful action or inaction is required of the parties. A280. Once FIRREA was passed, a contract right obliging OTS to continue to count RAP goodwill fully as regulatory capital would have required OTS to act unlawfully. The notion that Statesman retained any such right, notwithstanding the changes in law effected by FIRREA, is therefore inconsistent with the parties' agreement.

Significantly too the Statesman Assistance Agreement nowhere provides that the $25.8 million in supervisory goodwill created from the various Statesman thrift acquisitions is to be treated in any particular fashion for regulatory purposes.

For this reason, apparently, the Claims Court again looked to Bank Board Resolution No. 88-169 to supply contract terms of this nature. See A278. That Bank Board resolution provided that Statesman Bank would report to the Bank Board and the FSLIC in accordance with GAAP, except that supervisory goodwill could be amortized over a period not to exceed 25 years. A274.

This Bank Board resolution, like that in Glendale, is not a contract document; it is simply a manifestation of regulatory approval of the Statesman transaction, and is devoid of language indicating an intent by the Bank Board to be contractually bound.

The Claims Court found, however, that the Assistance Agreement's integration clause (A278) incorporated the Bank Board resolution as part of that agreement, and therefore made the resolution's provisions binding on the parties. But if the Bank Board resolution is deemed to be part of the Assistance Agreement, then any contract right it confers is also subject to the proviso that the agreement requires no unlawful action or inaction of the parties.

* * * * * *

In sum, the most striking thing about the contract claims made by the plaintiffs and the conclusions by the Claims Court is that the essential language clearly reflecting the contract rights that plaintiffs assert is simply not there. This Court is being asked to imagine the key contract terms. The actual language of the relevant documents reveals that plaintiffs did not have contracts with the Government providing for a particular governmental treatment of goodwill for regulatory purposes for an extended period. In the absence of such contract provisions, the thrifts' cases collapse and no further issues need be reached.

II. IN REQUIRING GREATER THRIFT CAPITALIZATION AND RESTRICTING USE OF GOODWILL, CONGRESS IN NO WAY BREACHED ANY CONTRACT RIGHTS HELD BY PLAINTIFFS.

As explained already, plaintiffs contend that the Government agreed to contract rights barring Congress for periods ranging from 25 to 40 years -- or until the year 2021 -- from reacting to a nationwide crisis in the thrift industry and amending the rules governing goodwill as applied to all thrifts.

Even if we are mistaken in our first point that the thrifts here did not have contracts concerning a particular form of regulatory treatment for goodwill, the very arguments accepted by the Claims Court were recently rejected by the District of Columbia Circuit in Transohio Savings, supra, and the Fourth Circuit in Charter, supra. As those opinions demonstrate, plaintiffs' arguments fail because Supreme Court precedent requires that a contract purporting to bar changes by Congress must be unequivocally expressed in order even possibly to be cognizable. There is not the slightest hint in the record here that the thrifts had the necessary unmistakable contract provision, and none of them has ever pointed to one.

1. The Supreme Court long ago instructed that "governmental [regulatory] powers cannot be contracted away." North American Commercial Co. v. United States, 171 U.S. 110, 137 (1898). The Court has consistently held that the Contract Clause in the Constitution does not require governments "to adhere to a contract that surrenders an essential attribute of its sovereignty." United States Trust Co. v. New Jersey, 431 U.S. 1, 23 (1977).[3]

Justice Brennan explained that to hold otherwise undermines one of the fundamental premises of our popular democracy by barring, through contracts with private individuals, subsequent legislatures from acting for the public welfare. United States Trust, 431 U.S. at 45 (Brennan, J., dissenting). See also Home Building & Loan Ass'n v. Blaisdell, 290 U.S. 398, 434-44 (1934).

Thus, "the exercise of the police power cannot be limited by contract for reasons of public policy * * * and it is immaterial upon what consideration the contracts rest, as it is beyond the authority of the State * * * to abrogate this power so necessary to the public safety." Northern Pacific Railway v. Minnesota,

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[3] While the Contract Clause does not apply to the Federal Government, the Supreme Court has suggested that the Contract Clause imposes more rigorous restrictions on the states than the Fifth Amendment imposes on the Federal Government. See PBGC v. R.A. Gray & Co., 467 U.S. 717, 732-33 (1984). Thus, if the restrictions imposed by the Contract Clause do not prohibit states from exercising regulatory powers, the Fifth Amendment certainly does not place such limits on the Federal Government.

208 U.S. 583, 598 (1908). Accord City of El Paso v. Simmons, 379 U.S. 497, 508-09 (1965). Indeed, in Veix v. Sixth Ward Building & Loan Ass'n, 310 U.S. 32 (1940), the Supreme Court rejected a Contract Clause challenge to a state statute altering the scheme of regulation of a thrift. The Court explained that the regulations governing the thrift had always remained "subject to the paramount police power." Id. at 38.

2. Assuming that Congress can nevertheless under the right circumstances waive its regulatory powers, the Supreme Court has held that, as a matter of contract interpretation, Congress will not be deemed to have done so if there is any possible question regarding its intent. See Bowen v. Public Agencies Opposed to Social Security Entrapment, 477 U.S. 41, 52 (1986) (POSSE); Merrion v. Jicarilla Apache Tribe, 455 U.S. 130, 148 (1982); United States v. Cherokee Nation, 480 U.S. 700, 707 (1987).

The D.C. Circuit has described this rule succinctly: "Without regard to its source, sovereign power, even when unexercised, is an enduring presence that governs all contracts subject to the sovereign's jurisdiction, and will remain intact unless surrendered in unmistakable terms." Western Fuels-Utah, Inc. v. Lujan, 895 F.2d 780, 789 (D.C. Cir.), cert. denied, 498 U.S. 811 (1990). Consequently, "contractual arrangements, including those to which a sovereign itself is [a] party, remain subject to subsequent legislation by the sovereign." POSSE, 477 U.S. at 52.

As the Eleventh Circuit recently held in determining whether contracts confer upon thrifts "a fixed right to treat supervisory goodwill as regulatory capital or a revocable one," courts must apply the rule of construction "that one who wishes to obtain a contractual right against the sovereign that is immune from the effect of future changes in law must make sure that the contract confers such a right in unmistakable terms." Guaranty Financial Services, Inc. v. Ryan, 928 F.2d 994, 1000-01 (11th Cir. 1991).

Further, these principles "take on added force when the arrangement pursuant to which the Government is claimed to have surrendered a sovereign power is one that serves to implement a comprehensive social welfare program affecting millions of individuals throughout our Nation." Guaranty, 928 F.2d at 1000. This statement is fully applicable to the thrift regulatory system. That system provides a mechanism for both federal thrift deposit insurance and governance of this industry, which is so crucial in providing funds for housing for millions of Americans.

This line of Supreme Court precedent was described by Chief Judge Mikva writing for the D.C. Circuit in Transohio Savings as the "unmistakability doctrine," and it provided the basis for that court to reject claims virtually identical to those raised here. There, the D.C. Circuit described the development of the unmistakability doctrine, and noted that "[t]he Supreme Court has applied the unmistakability requirement most forcefully in cases involving the government's regulatory power, as opposed to the government's power to ease its financial burdens." 967 F.2d at 619.

The D.C. Circuit explained that, because of legislative developments in the mid-1980s, thrifts should have been well aware of the possibility that capital requirements and goodwill accounting rules would change. 967 F.2d at 619-620. Hence, even though the thrift in that case -- Transohio Savings -- was found to have a contract with the Government that contained provisions concerning treatment of goodwill, the D.C. Circuit concluded that the thrift "in effect wagered the chance that the rules would be changed against the potential return if they were not," and that the thrift gained substantial advantages from the Government's allowance of liberal accounting rules during the years before FIRREA was passed. Id. at 620.

In light of the unmistakability doctrine, the D.C. Circuit ruled in Transohio Savings that the thrift there had no contract right to a set form of regulatory treatment regardless of statutory changes made in reaction to a monumental financial disaster in the industry.

Although stated in the context of a substantive due process discussion, the D.C. Circuit's Transohio Savings analysis is fully applicable in the cases at bar because here too there is no unmistakable language in any statute, regulation, or contract surrendering the Federal Government's authority to amend the regulatory scheme governing the thrifts' treatment of goodwill or capital in general.

In Charter, the Fourth Circuit agreed with the reasoning of the D.C. and Eleventh Circuits, and rejected a claim by a thrift that it is entitled to the contract remedy of rescission because of the changes wrought by FIRREA regarding goodwill. The thrift there too claimed that regulatory approvals of thrift acquisitions under the prior statutory scheme represented contracts regarding long-term regulatory treatment of the goodwill that was created. The Fourth Circuit was skeptical that any contract had been created, but it then assumed a contract's existence in order to deal with the legal issues. 976 F.2d at 210.

The Fourth Circuit found it controlling that the Bank Board "never expressly waived its right to enforce future regulations governing supervisory goodwill." Charter, 976 F.2d at 212. Although, as in the cases at bar, the Bank Board approved the thrift's accounting treatment of goodwill, the agency "made no explicit promise to [the thrift] of continued approval throughout the life of the amortization period." Ibid. Under these circumstances, the Fourth Circuit refused to "enlarge the scope of guarantees given to [the thrift]." Ibid.

The Claims Court here disagreed (A288) with the D.C. Circuit's reasoning on the ground that the unmistakability doctrine applies merely to determine if contract rights have been created, but not to the "effect of the government's breach of a contract." The Claims Court's criticism of the D.C. Circuit analysis is puzzling since the latter court used the doctrine in Transohio Savings to do exactly what the Claims Court said it was designed for. Chief Judge Mikva explained that, although the thrift there had a contract with the Government, that contract could not be interpreted to include a right to be free from bearing the impact of legislative changes in the regulatory scheme. See 967 F.2d at 619.

Thus, the D.C. and Fourth Circuits tested the terms of the contracts they found or presumed against the unmistakability standard, and concluded that nothing in those contracts could be deemed to be clear enough to create the claimed contract rights.

The trial court here quoted (A286) stirring language concerning the obligation of the Government to honor contracts and its responsibility to its citizens. We agree with these statements. But the Claims Court failed to recognize that Congress was honoring its responsibilities by changing the thrift regulatory scheme to meet a dangerous crisis in the nation's financial system. When Congress enacted FIRREA, no contract rights were breached because the only ones that existed were limited to the operations under the existing regulatory scheme, and thus were not continued in the event that Congress did precisely what it did.

Moreover, in light of the pervasive regulation of the thrift industry and the constant changes in the regulatory scheme, it is difficult to credit claims by the thrifts that they believed they had contract terms binding regulatory treatment of goodwill without explicit terms so providing. As this Court's ruling in California Housing, 959 F.2d at 958-59, makes clear, plaintiffs cannot show a reasonable expectation that the thrift regulatory scheme would remain static for up to 40 years. Accord Charter, 976 F.2d at 213 (noting that, because of highly regulated nature of thrift industry, the thrift there "certainly was cognizant of the regulatory intrusions into this business").

3. Further, as the D.C. Circuit also explained in Transohio Savings, 967 F.2d at 620-24, the agreements claimed here by the thrifts should not be interpreted as the Claims Court did because the Bank Board and the FSLIC lacked authority to exempt thrifts from changes in the statutory law that covers all thrifts. Congress alone can surrender its authority, either through an unmistakably worded statute or possibly an explicit statutory delegation to an agency giving it the power to do so. See Transohio Savings, 967 F.2d at 621; Peterson v. Dept. of the Interior, 899 F.2d 799, 811 n.17, 813 n.18 (9th Cir.), cert. denied, 498 U.S. 1003 (1990).

Any argument that agency actions regarding the thrifts somehow estopped Congress from changing legislative capital requirements clearly fails under recent Supreme Court precedent. See Office of Personnel Management v. Richmond, 496 U.S. 414 (1990). An agency promise that it will refrain from enforcing against a party subsequently enacted statutory requirements would plainly be ultra vires. See Federal Crop Insurance Corp. v. Merrill, 332 U.S. 380, 383-84 (1947); Amino Brothers Co. v. United States, 372 F.2d 485, 491 (Ct. Cl.), cert. denied, 389

U.S. 846 (1967) ("[t]he Government cannot make a binding contract that it will not exercise a sovereign power").

Consequently, as the D.C. Circuit details (Transohio Savings, 967 F.2d at 623-24), the thrift regulatory agencies should not be found to have bound Congress unless their enabling statutes delegated such authority. Although the FSLIC could enter into contracts, the relevant statutes were devoid of even the slightest hint that Congress had surrendered its right to legislate or had delegated such power to the regulatory agencies. See former 12 U.S.C. 1464, and 1729, 1730a(e) (1986). See also Flagship, 748 F. Supp. at 748; S. Rep. 97-536, 97th Cong., 2d Sess. 48 (1982), reprinted in 1982 USCCAN 3054, 3102; H.R. Conf. Rep. 74-955, 74th Cong., 1st Sess. 13 (1935) (12 U.S.C. 1729(f) only authorized FSLIC monetary assistance).

Moreover, as the D.C. Circuit noted, "the Bank Board statute, like the law in POSSE, contains an express reservation of '[t]he right to alter, amend or repeal this chapter." Transohio Savings, 967 F.2d at 623, quoting Section 30 of the Federal Home Loan Bank Act (47 Stat. 741 (1932)).

The Fourth Circuit in Charter, 976 F.2d at 212, pointed out the unlikelihood that the Bank Board had any intent to attempt to contract away Congress' power. Since "[c]apital requirements have been an evolving part of the regulatory scheme since its inception," the Bank Board "would have expected changes in statutory requirements, including capital requirements. We find it doubtful, then, that the [Bank Board] intended to secure to [the thrift] the use of supervisory goodwill over a fifteen to twenty-five year period." Ibid.

The lack of an intent by the FSLIC to enter into the type of contracts that plaintiffs claim is also demonstrated by a statutory provision that restricted the power of that body to grant financial assistance to thrifts if the amount of assistance would be greater than the cost of liquidating the institution. See 12 U.S.C. 1729(f)(4)(A) (1988) (now repealed). In light of this provision, it is highly unlikely that the FSLIC meant to sign binding contracts whereby the United States would assume a risk, if Congress later changed thrift capitalization rules, of having to pay contract breach damages that might often exceed the cost of closing the thrift.

The Claims Court disagreed with the analysis adopted by the Fourth Circuit in Charter. The Claims Court noted emphatically that Congress had given the FSLIC and the Bank Board the power to enter into binding contracts. A290. While true, this point does not demonstrate that these agencies could sign contracts that would exempt certain thrifts from changes in the legislative regulatory scheme.

Further, the Claims Court relied upon (A290) statutory language providing that the FSLIC could "in its sole discretion and upon such terms and conditions as [FSLIC] may prescribe" guarantee a thrift against loss from a merger. See 12 U.S.C. 1729(f)(2)(A). But that section merely served to exempt such FSLIC determinations from review under the Administrative

Procedure Act (5 U.S.C. 701(a)(2)); it did not give away to the FSLIC Congress' authority to legislate for the future for all thrifts.

The Claims Court nevertheless says (A286-90) that the thrifts' contracts did not prevent Congress from acting, and thus no unmistakable delegation from Congress was needed. But this logic is odd since the Claims Court's conclusion is that the prior banking regulatory agencies did enter into binding contracts that would be breached if Congress changed the underlying statutory scheme. The agencies thus, according to the Claims Court, bound the United States to an obligation to keep the regulatory system for these thrifts in place for up to 40 years, or face the consequences of a breach of contract.

4. The force of the unmistakability doctrine is reinforced here by the "sovereign acts" doctrine, which also protects the full ability of Congress to legislate in the public interest.

Over a century ago, this Court's predecessor held that general acts of Congress cannot be deemed to violate Government contracts with private parties. Deming v. United States, 1 Ct. Cl. 190, 191 (1865), appeal dismissed, 76 U.S. 145 (1870).

It is now fully established that the United States and its agencies are immune from contractual liability when the Government has acted in its sovereign regulatory capacity, regardless of whether such actions infringe existing contractual rights or create additional monetary burdens on private parties who have contracted with the government. See, e.g., Horowitz v. United

States, 267 U.S. 458, 461 (1925) ("Whatever acts the government may do, be they legislative or executive, so long as they be public and general, cannot be deemed specially to alter, modify, obstruct or violate the particular contracts into which it enters with private persons").

This Court has consistently followed Horowitz by finding the United States immune from liability on contract theories as long as the act challenged was "public and general," and not taken merely to avoid obligations to a particular party. See, e.g., Atlas Corp. v. United States, 895 F.2d 745, 754-55 (Fed. Cir.), cert. denied, 498 U.S. 811 (1990); Tony Downs Foods Co. v. United States, 530 F.2d 367 (Ct. Cl. 1976); Amino Brothers Co., 372 F.2d at 491.

The sovereign acts doctrine dovetails with the unmistakability principle to protect the sovereign power of the Government to legislate for the general public welfare. It covers FIRREA and its implementation because they are sovereign acts -- regulatory actions taken to regulate all thrifts -- for the protection of depositors nationwide in order to benefit the general welfare.

The Claims Court concluded, however, that this doctrine is not applicable here because the purpose of FIRREA's new restrictions on use of goodwill "was to take away plaintiffs' rights to use supervisory goodwill because the Congress felt its use was no longer good policy." A55.

The Claims Court's reasoning makes it appear that the goodwill restrictions were directed only at those thrifts that had contracts guaranteeing long-term recognition of goodwill for regulatory purposes. But this view is too narrow. The FIRREA goodwill restrictions apply to <u>all</u> thrifts, whether they previously had goodwill created or may undertake transactions that create goodwill in the future, and whether or not they had contracts assertedly freezing the prior regulatory treatment of goodwill. And, the key question under the sovereign acts doctrine is not whether a particular party is affected by the governmental action at issue; it is whether that party was the only one targeted.

The intent of the FIRREA restrictions was <u>not</u> specifically to eliminate contract rights allowing goodwill for regulatory capital purposes. Rather, it was a far more general regulatory purpose designed to restrict thrifts in their use of goodwill, whether contracts existed or not.

Moreover, there can be no doubt that Congress' action to restrict use of goodwill was rational. As described above, Congress determined that the use of accounting gimmickry for intangible assets such as goodwill and inadequate thrift capitalization were key causes of the thrift crisis. It made perfect sense to change the governing scheme.

Accordingly, the FIRREA goodwill restrictions were general sovereign acts performed for the public good, and neither arbitrary nor unreasonable.

5. The Claims Court tried (A46-52) to avoid POSSE and the unmistakability doctrine by asserting that the factual situation there is distinguishable from those here. The court focused on the fact that the subject in POSSE -- participation by state and local government workers in the Social Security system -- was one that Congress could govern by regulation rather than contract. This argument fails because the legal principles relied upon by the Supreme Court in POSSE are clearly of general application, and have been applied by the other circuits in a variety of circumstances. See, e.g., Education Assistance Corp. v. Cavazos, 902 F.2d 617, 629 (8th Cir.), cert. denied, 498 U.S. 896 (1990) (applying POSSE principles in case involving changes in rules governing student loan program); Western Fuels, 895 F.2d at 789 (applying POSSE principles in case involving mining leases voluntarily entered into with the Government by private parties); Peterson, 899 F.2d at 807 (applying POSSE principles to case involving voluntary contracts for water rights).

The Claims Court also noted (A46) that the original statute at issue in POSSE contained a reservation of Congress' ability to change the statutory scheme. 477 U.S. at 51-52. While, as discussed in Transohio, 967 F.2d at 623-24, the Bank Board statute contained a similar reservation, the Supreme Court's discussion in POSSE of its precedents did not focus on this factor as decisive, and made clear that the Court had declined to find that a sovereign waives its right to exercise its regulatory powers unless such a right has been expressly reserved. 477 U.S.

at 52. Accord Transohio Savings, 967 F.2d at 621 (and cases cited there); Peterson, 899 F.2d at 808.

Thus, the factual point relied upon by the Claims Court is incorrect and irrelevant for the analysis here. At the same time, we note that, unlike in the cases at bar, the contract at issue in POSSE actually contained a clear clause permitting the action by the contracting parties that Congress then eliminated. See 477 U.S. at 48. POSSE was therefore a more difficult case than these are.

6. The Claims Court also pointed out (A51) that the Supreme Court has instructed that the United States is not free under the Due Process Clause simply to repudiate its contracts and debts. It is not clear how this rule assists the thrifts here in proving that the contracts they assert contained the necessary terms, such as a guarantee of the same regulatory treatment for 40 years.

In any event, FIRREA does not violate this principle since what the Due Process Clause prohibits is a debt repudiation made solely to reduce public expenditures. See POSSE, 477 U.S. at 55 (Congress does not have "the power to repudiate its own debts * * * simply in order to save money"); Peterson, 899 F.2d at 808 n.16, 813 n.20.

The primary instance in which this principle has been applied is Lynch v. United States, 292 U.S. 571 (1934). There, the Supreme Court invalidated, on substantive due process grounds, legislation repudiating the Government's otherwise clear obligation to pay war risk insurance benefits to veterans. In a key paragraph, Justice Brandeis explained for the Court that there was no suggestion that Congress "abrogate[d] these contracts in the exercise of the police or any other power." Id. at 580.

Lynch therefore merely stands for the proposition that the United States cannot simply repudiate a debt because it has become inconvenient to pay.

Shortly thereafter, a similar analysis was used in the special circumstances of Perry v. United States, 294 U.S. 330 (1935). The Supreme Court there concluded that legislation authorizing redemption of United States Liberty Bonds in currency rather than in gold violated Article I, Section 8, clause 2 of the Constitution, which authorizes Congress to "borrow money on the credit of the United States," and the Fourteenth Amendment, which protects the validity of "the public debt." 294 U.S. at 350-54. The Court rejected the view that obligations of the United States could be ignored if their "fulfillment [becomes] inconvenient." Id. at 350.

As explained in POSSE, 477 U.S. at 55, in Lynch and Perry, Congress tried to repudiate a debt through statutory changes in order to save money. No debt of the United States is being repudiated here. Rather Congress restructured the entire regulatory scheme governing thrift capitalization. Stricter capitalization requirements and their application to all thrifts were imposed in FIRREA for reasons other than simply to save money owed to private parties having binding contracts with the Government. The thrift regulatory scheme was drastically changed as an exercise of federal police power in an effort to alter thrift management practices to ensure that the dangerous crisis in the thrift industry could be resolved and not recur.

The substantive due process limits on Congress' power to affect contractual obligations of the United States thus in no way help the thrifts' claims regarding the contents of their asserted contracts. It is significant for this case that there is a similarity between substantive due process principles and the sovereign acts doctrine. The Supreme Court has explained in rejecting substantive due process attacks that a statute "readjusting rights and burdens is not unlawful solely because it upsets otherwise settled expectations. * * * This is true even though the effect of the legislation is to impose a new duty or liability based upon past acts." PBGC v. R.A. Gray Co., 467 U.S. 717, 729 (1984). As shown above, the sovereign acts doctrine also protects the Government from liability when it enacts a general statute that adversely affects some parties. Therefore, although Lynch and Perry make clear that the Due Process Clause does not allow legislation aimed at a particular group simply in order to save money, because the actions by Congress here fit within the sovereign acts doctrine, the rule in those cases is not implicated here.

7. The Claims Court believed (A281) that our position means that any agreements between plaintiffs and the prior regulatory

agencies were illusory and of little worth. This notion loses sight of the fact that the purpose of the agreements was to acquire thrifts; the accounting and regulatory treatment of goodwill was, at most, only one aspect of those transactions.

The fact remains that the plaintiffs' applications to consummate transactions were approved by the Bank Board on terms that granted them highly favorable regulatory practices, and in some instances with substantial contributions of public money. Plaintiffs then received the benefit of those favorable regulatory terms until FIRREA became effective, which for some of them was nearly a decade.

Thus, the benefits of plaintiffs' agreements with the agency regulators were hardly illusory. The thrifts received substantial benefits even with the later changes made by FIRREA. In any event, the fact remains that the Government simply did **not** contract for a fixed regulatory scheme for periods up to 40 years, signing away Congress' power to legislate and regulate for the public welfare.

* * * * * *

Plaintiffs also raise other contract remedies, such as rescission, and make claims for just compensation based on their assertion of contract rights. See A30-33, 53-56, 1287-92. The Claims Court did not reach those claims because of its determination that plaintiffs' contracts had been breached. If we are correct that plaintiffs did not have contract rights to a particular form of regulatory treatment for long periods regardless of changes in the statutory scheme, then, as the Fourth Circuit found in Charter, 976 F.2d at 210-13, there is no need to consider rescission. Further, as the D.C. Circuit found in Transohio Savings, 967 F.2d at 613-14, just compensation claims are without merit because plaintiffs have been deprived of no constitutionally cognizable property rights.

Consequently, if the Court accepts our arguments, it should also order judgment for the United States on all of plaintiffs' contract and just compensation claims.

CONCLUSION

For the foregoing reasons, the decisions of the Claims Court should be reversed, and judgment entered for the United States on the contract breach claims in each of the three cases covered by this appeal. If the Court reaches this result, it should also direct judgment for the United States on all of plaintiffs' contract and just compensation claims.

Respectfully submitted,

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OCTOBER 15, 1993

CERTIFICATE OF SERVICE

I hereby certify that on this 15th day of October 1993, I served the foregoing Replacement Brief of Defendant United States upon counsel by causing copies to be mailed, first class postage prepaid, to:

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DOUGLAS LETTER
Appellate Litigation Counsel

EXECUTIVE OFFICE OF THE PRESIDENT

01-Sep-1995 07:01pm

TO: (See Below)

FROM: Alan B. Rhinesmith
Office of Mgmt and Budget, HTF

SUBJECT: While you were away -- HTF Division Report

As you know, I was away for a good portion of the time you have been out, but my overall assessment is similar to Ken's: things have been generally slow, with a couple of exceptions.

Treasury/DC

--Weekly conference calls with Treasury (Thompson) on pending DC issues have been on hold, although each Thursday Marcia has called Margaret and Erica to verify that there was no need for one. Regarding the Congressional/House leadership, we have first drafts of all papers, and should have a complete analysis package ready for you on your return.

DeSeve is meeting with John Hill on September 7th to discuss Child Welfare alternatives with the new court-appointed administrator, Jerome Miller. We were informed by OMB staff, who in turn were informed by Joe Wholey, who was invited to sit in on it. Other meetings may have occurred or may be scheduled as well, about which you may learn from other channels (if so, we appreciate any intelligence).

Meanwhile, Bill Dorotinsky (an examiner in the OMB Health Division) is working on a temporary basis with the Assistance Authority for approximately three weeks. He is not officially detailed to the Authority, but will assist them in coordinating with the District Council's budget deliberations with District agencies. This will prepare both the Authority and the Council for Congressional inquiries regarding the FY 96 budget when the appropriations process begins in earnest in mid-September. The Director approved this detail, although we continue to have some misgivings about the appearance of OMB involvement in DC budget deliberations.

--Treasury expects its conference to occur possibly as early as the week of the 11th. Some in Treasury believe that additional resources will be found for the Department; others, including HTF staff, are more skeptical. None of the reports or the floor debates suggest that Congress will increase the Treasury mark above the House level.

--Treasury 1997 Budget: They will not have a formal submission on time, but can provide a letter from the Secretary along with major features. Treasury Budget Office expects the Department to come in at or under guidance -- primarily due to the fact that guidance was based on the 1996 Presidential request level, while the 1997 Departmental Budget request will build on much lower likely 1996 enacted. We are not expecting any major initiatives, with the exception of a fairly significant bump for Customs Hard Line. We are working with Customs to make sure that any proposed investments make sense and fit within some overall definable strategy.

Financial Institutions

--SBA's Small Business Investment Company (SBIC) Program: FIB staff have drafted a memo from you to Cassandra Pulley on the SBIC program. The memo expresses our opposition to expanding the program rapidly and requests that SBA provide us with detailed information on options for containing program growth, improving program administration, and operating the program within demand constraints. FIB staff met with Treasury staff (Mozelle Thompson's office) last week and Treasury agrees with most of our concerns and may want to sign the memo as well.

--SBA's Export Working Capital Program: HTF staff are reviewing testimony by SBA and the Export-Import Bank for a September 7th hearing on their "harmonized" loan guarantee programs, which provide small and large exporters with identical loan programs. Reforms to SBA's 7(a) program, passed by the House and Senate Small Business Committees, would lower SBA's export loan guarantee percentage to 75-80 percent, making it different from Ex-Im's 90 percent guarantee. Both agencies would like to recommend maintaining SBA's program at 90 percent, so the program can continue to be "seamless." You will be getting an e-mail on this on Tuesday with more details.

--FEMA Energy Conservation and Disaster Relief: HTF staff met with Energy and Science Division staff to discuss the Alliance to Save Energy report on the "greening" of disaster relief. We agreed to meet with FEMA and SBA to discuss the report, its recommendations, and what, if anything, could be done administratively to implement recommendations.

--Consolidated earthquake office: OMB staff (GGF and ES) have reviewed a proposal received from OSTP on this subject. OSTP would like to set up an office for earthquake research. Comments have been provided to OSTP staff, who are continuing to refine the strategy.

--Long Island Fires: The fires on Long Island, which started the weekend of August 26,27, required a fire suppression grant from FEMA. The fires were brought under control quickly enough that a disaster declaration was neither necessary nor requested by NY State.
Some questions came up regarding the "Federal Government's" response to the wildfires on Long Island. Fingers were initially pointed at FEMA, but all concerned parties seem to agree that the problem was with the Forest Service's initial reluctance to send the promised planes to the scene.

RTC/Appeals Court Decision: On Wednesday August 30, the Federal Appeals Court for the Federal Circuit ruled that the disallowance by statute (FIRREA) of the use of "goodwill" as capital, which had been granted by FSLIC to thrift institutions that had acquired insolvent thrifts, constituted a breach of contract by the Government. This decision potentially exposes the Government to billions of dollars of additional costs for the thrift crisis cleanup. About 90 suits from the owners of failed thrifts are pending.

At the request of Jack Lew, we are attempting to determine the size and timing of these potential additional costs. Some of our contacts are on vacation, so this is an ongoing effort. Despite the press reports estimating up to $20 billion of additional costs to the Government, the actual timing and size of the costs are both very unclear. If Justice chooses not to appeal to the Supreme Court, payments could begin within three or four months following negotiation of settlements.

However, nearly everyone expects Justice to appeal. An appeal likely would be heard in the 1996 term of the Supreme Court, so a decision would not occur until the Spring of 1997. Under this scenario, outlays for damages likely would not start until early FY 1998.

The size of the additional cost also is very indeterminate. The suits against the Government seek damages based on new, untested theories. Indeed, the determination of damages could lead to additional litigation. The $20 billion cost estimate in the press, which is based on damages sought in the suits, likely is a worst-case estimate. We will do a more complete E-mail when we no more.

Housing

-- Reconciliation: Bad news, if true: Both House and Senate Banking Committee appear to be increasingly pessimistic about the propects for getting more than $800 to $900 million in CBO-scoreable savings out of the BIF-SAIF merger and other non-HUD items (particularly if they also give up on flood insurance). Therefore, they may set their sights on $1 to $1.5 billion in savings from HUD. Only advantage might be as leverage to get some of the elements of MTM authority, if they can be pulled out and scored as potential savings; would require language directing CBO to use a revised baseline including significant default costs. A long shot still. HUD is putting together its own list of reconciliation possibilities; we have seen those for FHA Multifamily, but not the whole list yet.

-- Cities Analysis: Information will be released this coming week. A Presidential event is scheduled for Wednesday, Sept. 6th, with some mayors and county officials; is being handled by WH Intergovernmental. Starting the following day, the data will be released in a series of local events in metro. areas all over the country. Nearly all agencies responded -- some late -- to the second request for data, including info. on impacts and 1995 area allocations. On August 30th, HUD (Katz) and WH Intergovernmental (Bromberg) met again to discuss the mode of release and whether comparisons should be with 1995 enacted or President's plan. Emily argued, that despite the weakly expressed preference of local officals for 1995 as the base for comparison, it was more advantageous to emphasis differences with the President's plan over 7 years -- much larger differences. HUD, it seems, remains nervous that reporters will ask about the 1995 figures and assume that the apparent magnitude of the cuts is being exaggerated by comparison with a President's plan that doesn't add up. WH IG has okayed a one-page narrative format and accompanying table for each metro. area; the intro. to the narrative emphasizes that the President's plan achieves a balanced budget. Joseph Firschein and Winnie Chang (on Phil Dame's staff) did an enormous amount of

96 Budget + House bill

Will circulate to WH list

Other T. Agencies

excellent work to prepare and clean the information and, in some cases, to cajole examiners and their agencies to respond.

-- Distributional Analysis: You will probably get a fuller report on this from others. The next in a series of meetings under Apfel's lead is scheduled for Wednesday, Sept. 6. This is also the target date for the "marriage" of Treasury and HHS models. HUD is communicating directly with HHS about its housing assistance. Some issues have arisen, but I believe that Paul Leonard and Wendell Primus can work these out directly.

-- Appropriations: Senate Subcommittee markup scheduled for Sept. 11th. We obtained an August 28th draft of Stephan's appropriations bill language for HUD (missing some items), still in progress. Kohashi is ambitious and will do lot's of authorizing. Mark includes the industry proposal for Preservation, which is costly and otherwise undesirable. Also includes $1 billion PH demolition funding and language that would allow HUD to bring down many more non-viable projects and replace with vouchers. Another provision would create a 30 PHA demo. allowing shift to vouchers. Creates an MTM "demo" similar to that drafted for Stephan by HUD with our help (see next item). We understand that many elements of the bill are still in flux. The final scoring of the House appropriations bill produced surprising number of differences with CBO -- Branch is working with CBO staff to resolve.

--Mark to Market: We reviewed a draft of the HUD "compromise", which HUD was preparing for Kohashi. Edits that we suggested were intended to ensure a rescoring of the baseline by CBO to show greater defaults resulting from limits on project-basing of future subsidies. Informal conversation with CBO is encouraging. HUD also has MTM on its list of possible reconciliation items, although the prospects are problematic.

-- 1997 Budget Planning: As you know, budgeting for 1997 is in the earliest stages at HUD. You have in your in box a draft Housing branch memo on 1997 budget strategy and principles for evaluating proposals. The Branch is planning to meet with you on Sept. 13th. A meeting with Bruce and Mike Stegman is being set up for the following day. We need to accelerate HUD's process and also work to see that it doesn't go off track (see Urban Policy, below).

-- HUD 1995 Operating Plan: The Branch reviewed and cleared a revised operating plan that allocated $1.15 billion in unspecified reductions from Annual Contributions for Assisted Housing. All but $100 million of this took the form of gimmicks that yield no outlay savings. Compared to our scoring of this at the time planning guidance was prepared, this adds about $170 million to HUD's 1997 outlays. Of course, our planning guidance also assumed enactment of the President's 1996 budget; so, with expected Congressional cuts, HUD still has some outlay leeway in 1997.

-- Urban Policy: As you know, on August 9th, the Secretary wrote to the President calling for money off the top to fund a 1997 urban policy initiative. We understand that there have been additional conversations on an urban initiative between the Secretary and the President and between the Secretary and Sec. Rubin. Apparently, the discussion with Rubin included possible tax options for Reconciliation; the one item along this line cited in the POTUS memo is for a commercial investment tax credit modelled after the Low-income Housing Tax Credit. This is also something that Repub. Senator Hutchinson has introduced. We have not heard of any West Wing reaction to the Cisneros memo.

Magaziner's first brainstorming meeting with you and others is scheduled for Thursday, Sept. 7th. NPR staff helped design a workshop for the Conference of Mayors' Seattle meeting, Aug. 24-26th, on the VP's promised "performance partnership with the cities." NPR staff reported that the Seattle workshop was a success, with roughly 20 cities represented. We can expect some of these to come forward with proposals to negotiate Performance Agreements.

-- SBA/CDBG Disaster Loan Policy: Following your decision on this memo, Joseph as talked to HUD CPD staff. We don't anticipateany problem in including either appropriations language or guidance to recipients in future disaster allocations to limit CDBG use for loans so that won't undercut SBA underwriting standards.

Talk w/ Dwight

-- HUD Performance Measures: HUD has given us responses to our "final" proposals. You have a separate memo and summary of unsettled issues. Jim Jordan and others in the branch are prepared to review these with you next week. So that we can bring this to closure in time for HUD to include measures with its budget submission, it would be helpful for you and Dwight Robinson to talk as soon as possible and come to agreement on each measure.

-- HUD Performance Agrement: NPR and OMB staff met with HUD reps. to kick off drafting of the HUD 1996 Performance Agreement (details in separate e-mail). The measures negotiated for the 1997 Budget provide a good starting point. Agreement was reached on general content and timetable. HUD will draft by end of September, with the goal of having it signed in the first quarter. Other agencies are being approached by NPR to begin preparing their 1997 Agreements.

-- Shutdown Planning: Memos from Rivlin and Dellinger were sent to HUD. During the week of August 21st, we confirmed with HUD that FHA would be forced to stop insuring new mortgages in the absence of appropriations. (At the time, Bob Damus was compiling a list of middle-class benefits that would be lost in a shutdown, for possible Rivlin use on CNN.) Ginnie Mae acting President Kevin Chavers called to relay press inquiries about effect of shutdown on Ginnie Mae issuances and intervention in a default. It appears that Ginnie can still issue securities to fulfill previous commitments (commitment being the point of obligation), especially if no goverment employee is needed to execute. Agency plans due Sept. 6th.

-- Homeless Survey: This national survey, to be conducted by Census, now has fully funding from the agencies who make up the Interagency Council on the Homeless. OMB cleared the first part of the survey design/questions on August 29th.

-- Chicago: The Secretary will testify September 5th in Chicago before the House Committee on Government Oversight and Reform Subcommittee on Human Resources and Intergovernmental Relations. We cleared testimony August 30th (and can make a copy available to you if you wish). The Secretary will testify that HUD worked for 29 months to turn the Chicago situation around before taking over management. He will say that HUD did not seek a court-appointed receiver because the problems went beyond mismanagement, arguing that HUD "needed to engage the political forces and elected officials in the transformation." HUD also will argue that getting a receiver on board takes too long. After 3 months of review, HUD reports that the problems of Chicago are even greater than envisioned. Demolition of Henry Horner high-rises began in August; displaced residents have choice of Section 8, scattered site homes, or moving to other public housing. HUD "will approach DOL and HHS with the hope of establishing a welfare-to-work strategy for CHA residents." The Secretary stresses the transitional nature of HUD's involvement and says that its goal is to "ensure that a 'Chicago solution' is found." A/S Joe Shuldiner continues to chair an executive advisory council appointed jointly by the Secretary and the Mayor to formulate policy and strategic plans. HUD has not yet found a permanent management team to run the reconsistuted Authority.

--Welfare Reform: Something to watch and worry about -- Senator Gramm would amend Dole's bill to block grant HUD housing assistance and eliminate the HUD staff that currently administer the assistance. We are monitoring the welfare reform debates in case this or similar proposals are incorporated.

-- Matching of Tenant Incomes: Three years after it received legislative authority in Reconciliation to implement this match, HUD is finally planning to pilot test the matching process at seven locations in November. Once fully implemented, expect to gain $600 million in higher tenant payments and a corresponding reduction in HUD subsidy costs without raising rent as a percent of income. We have been pushing HUD along for some time now. JIm and Katherine have worked with HUD staff to design the pilot. Finally, some light at the end of the tunnel -- but the delay will still cost HUD precious 1997 outlays relative to our previous estimates.

Personnel

Two new staff have started in Financial Institutions: Ed Brigham, the new Branch Chief, and Bill Wiggins, the new SEC/CFTC examiner. Ed Chase is leaving Housing to go to Justice/GSA. I am recruiting for new examiners to replace Ed and Alice Cho. With respect to support staff, Sharon Thomas is currently detailed to Justice but we expect DOJ to pick her up on a permanent basis shortly and we have already posted to fill a support staff vacancy for Financial Institutions.

Distribution:

TO: Robert E. Litan

CC: Karin L. Kizer
CC: Kenneth L. Schwartz
CC: Susan M. Carr
CC: Elizabeth M. DiGennaro
CC: Harry G. Meyers
CC: Francis S. Redburn
CC: Edward Brigham
CC: Alan B. Rhinesmith
CC: Diane G. Limo

OMB
Jack
Lew

~~[illegible]~~

~~Mikva~~ // ~~Chaters~~
/ // Katzen

why did the Ct do This?

How we got into This pickle.
What we're doing abt IT?

Bob Litan –

5-3/20

1) memo?
2) What are the implications?
how much money?

1ST CASE of Level 1 printed in FULL format.

WINSTAR CORPORATION, UNITED FEDERAL SAVINGS BANK, STATESMAN SAVINGS HOLDING CORP., THE STATESMAN GROUP, INC. and AMERICAN LIFE AND CASUALTY INSURANCE COMPANY, and GLENDALE FEDERAL BANK, FSB, Plaintiffs-Appellees, v. THE UNITED STATES, Defendant-Appellant.

WINSTAR CORP. v. UNITED STATES

92-5164

UNITED STATES COURT OF APPEALS FOR THE FEDERAL CIRCUIT

1995 U.S. App. LEXIS 24416

August 30, 1995, Decided

PRIOR HISTORY: [*1] Appealed from: U.S. Court of Federal Claims. Chief Judge Smith.

COUNSEL: Charles J. Cooper, Shaw, Pittman, Potts & Trowbridge, of Washington, D.C., argued for plaintiffs-appellees, Winstar Corporation, United Federal Savings Bank, Statesman Savings Holding Corp., The Statesman Group, Inc., and American Life and Casualty Insurance Company. With him on the brief were Michael A. Carvin, Robert J. Cynkar and Vincent J. Colatriano. Jerry Stouck, Spriggs & Hollingsworth, of Washington, D.C., argued for plaintiffs-appellees, Glendale Federal Bank, FSB. With him on the brief were Joe G. Hollingsworth, Donald W. Fowler and Charles J. Fromm.

Douglas Letter, Appellate Litigation Counsel, Department of Justice, of Washington, D.C., argued for defendant-appellant, The United States. With him on the brief was Frank W. Hunger, Assistant Attorney General. Scott R. McIntosh and William Kanter, Attorneys, Department of Justice, of Washington, D.C., represented the defendant-appellant, The United States.

William H. Butterfield, McGuire, Woods, Battle & Boothe, of Washington, D.C., was on the brief for Amicus Curiae, The Electronic Industries Association, The Shipbuilders Council of America, Inc. and [*2] Litton Industries, Inc.

Clarence T. Kipps, Jr. and Kevin C. Dwyer, Miller & chevalier, Chartered, of Washington, D.C., were on the brief for the Amicus Curiae, Aerospace Industries Association of America, Inc. Also on the brief were Professor Emeritus John Cibinic, Jr., The National Law Center, Washington, D.C., Kathleen A. Buck, Kirkland & Ellis, of Washington, D.C. and Mac S. Dunaway and Gary E. Cross, Dunaway & Cross, of Washington, D.C.

Herbert L. Fenster, McKenna & Cuneo, of Washington, D.C., was on the brief for Amicus Curiae, Chamber of Commerce of The United States of America. With him on the brief were Tami Lyn Azorsky and Margaret C. Rhodes. Also on the brief was Robin S. Conrad, National Chamber Litigation Center, Inc., of Washington, D.C. Of counsel were Hugo Teufel, III and Mark A. Rowland.

Don S. Willner, Willner & Zabinsky, of Portland, Oregon, was on the brief for Amicus Curiae, C. Robert Suess, Leo Sherry, Richard A. Green, Irving Roberts and Foster, Paulsell & Baker, Inc. With him on the brief were Thomas M. Buchanan and Eric W. Bloom, Winston & Strawn, of Washington, D.C.

Melvin C. Garbow and Peter T. Grossi, Jr., Arnold & Porter, of Washington, [*3] D.C., were on the brief for Amicus Curiae, Amwest Savings Association and The Adam Corporation/Group; The Globe Savings Bank, FSB and Phoenix Capital Group, Inc.; and Old Stone Corporation. Of counsel were Peter M. Barnett, Linda B. Coe and Matthew Frumin.

Billie J. Ellis, Jr., Kelly, Hart & Hallman, of Fort Worth, Texas, was on the brief for Amicus Curiae, Keystone Holdings, Inc. and American Savings Bank, F.A.

Daniel J. Goldberg, Housley, Goldberg & Kantarian, P.C., of Washington, D.C., was on the brief for Amicus Curiae, Coast Federal Bank, Union Federal Savings Bank of Indianapolis, Union Federal Savings Bank of Frankton and Union Holding Company, Inc.

John C. Millian, Gibson, Dunn & Crutcher, of Washington, D.C., was on the brief for Trinity Ventures, Ltd. and Castle Harlan, Inc. With him on the brief were Wesley G. Howell, Jr., Gibson, Dunn & Crutcher, of New York, New York and John K. Bush, Gibson, Dunn & Crutcher, of Washington, D.C.

Paul Blankenstein and John K. Bush, Gibson, Dunn & Crutcher, of Washington, D.C., were on the brief for Amicus Curiae, Dollar Bank, F.S.B.

Laurence H. Tribe, of Cambridge, Massachusetts, was on the brief for Amicus Curiae, [*4] AmBase Corporation and carteret Bancorp, Inc. With him on the brief was Brian Stuart Koukoutchos, of Bedford, Massachusetts, Harvey Silverglate and Andrew Good, Silverglate & Good, of Boston, Massachusetts, Wesley G. Howell, Jr., Gibson, Dunn & Crutcher, of New York, New York and John C. Millian, Gibson, Dunn & Crutcher, of Washington, D.C.

Thomas M. Buchanan and Eric W. Bloom, Winston & Strawn, of Washington, D.C., were on the brief for Amicus Curiae, Franklin Financial Group, Inc., Franklin Federal Savings Bank, and Charter Federal Savings Bank.

Lloyd N. Cutler, Wilmer, Cutler & Pickering, of Washington, D.C., was on the brief for Amicus Curiae, The Long Island Savings Bank, FSB and The Long Island Savings Bank of Centerach FSB. With him on the brief were William B. Richardson, Jr., Michael S. Helfer and Lydia R. Pulley. Also on the brief were Michael J. Chepiga and Eric S. Kobrick, Simpson, Thacher & Bartlett, of New York, New York. Russell E. Brooks, Milbank, Tweed, Hadley & McCloy, of New York, New York, represented the Amicus Curiae, The Long Island Savings Bank, FSB.

Timothy K. Irvine, General Counsel, Franklin Federal Bancorp, of Austin, Texas, was on the brief [*5] for Amicus Curiae, Franklin Federal Bancorp.

JUDGES: Before ARCHER, Chief Judge, * and RICH, NIES, NEWMAN, MAYER, MICHEL, PLAGER, LOURIE, CLEVENGER, RADER, and SCHALL, Circuit Judges. ** Opinion for the court filed by Chief Judge ARCHER, in which Circuit Judges RICH, NEWMAN, MAYER, MICHEL, PLAGER, CLEVENGER, RADER, and SCHALL join. Dissenting opinions filed by Circuit Judges NIES, and LOURIE.

* Chief Judge Archer assumed the position of Chief Judge on March 18, 1994.

** Circuit Judge Bryson joined the Federal Circuit on October 7, 1994, and has not participated in the disposition of this appeal.

OPINIONBY: ARCHER

OPINION:
ARCHER, Chief Judge.

The United States appeals the decisions n1 of the United States Court of Federal Claims n2 granting plaintiffs Winstar Corporation and United Federal Savings Bank, No. 90-8C, plaintiffs Statesman Savings Holding Corporation, the Statesman Group Incorporated and American Life and Casualty Company, No. 90-773C, and plaintiff Glendale Federal Bank, No. 90-772C, summary judgment on the liability portion of their breach of contract claims against the United States. The cases were consolidated for purposes of this interlocutory appeal. [*6] We affirm.

- - - - - - - - - - - - - - - - - - -Footnotes- - - - - - - - - - - - - - - - - - -

n1 Winstar Corp. v. United States, 21 Cl. Ct. 112 (1990) (finding an implied-in-fact contract but requesting further briefing on contract issues) (Winstar I); 25 Cl. Ct. 541 (1992) (finding contract breached and entering summary judgment on liability) (Winstar II); Statesman Savings Holding Corp. v. United States, 26 Cl. Ct. 904 (1992) (granting summary judgment on liability to Statesman and Glendale).

n2 The Federal Courts Administration Act of 1992, Pub. L. No. 102-572, @ 902(a), 106 Stat. 4506, 4516, changed the name of the former United States Claims Court to the "United States Court of Federal Claims." Except where the context requires otherwise, we refer to the trial court by its new name.

- - - - - - - - - - - - - - - - - -End Footnotes- - - - - - - - - - - - - - - - - -

I

In its Winstar decisions, the Court of Federal Claims found that an implied-in-fact contract existed between the government and Winstar and that the government breached this contract when Congress enacted the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 [*7] (FIRREA), Pub. L. No. 101-73, 103 Stat. 183 (codified in relevant part at 12 U.S.C. @ 1464). Similarly, in the Statesman decision the Court of Federal Claims found that plaintiffs Statesman Savings Holding Corporation, the Statesman Group Incorporated and the American Life and Casualty Insurance Company (together "Statesman") and plaintiff Glendale Federal Bank ("Glendale") had express contracts with the government and citing its Winstar decision, found that these contracts were breached by the enactment of FIRREA.

The Court of Federal Claims certified its decisions in these three related cases for interlocutory appeal pursuant to 28 U.S.C. @ 1292(b) after determining that the decisions involved controlling questions of law as to which there is substantial ground for difference of opinion and that an immediate appeal may materially advance the termination of these and other related cases. We granted the appeal. 979 F.2d 216 (Fed. Cir. 1992). After an initial split panel decision of this Court reversed the Court of Federal Claims, 994 F.2d 797 (Fed. Cir. 1993), we vacated the panel opinion and agreed with the plaintiffs' suggestion to consider these cases in banc.

II [*8]

A. During the Great Depression of the 1930s, 40 percent of the nation's $ 20 billion in home mortgages went into default, 1700 of the approximately 12,000 thrift institutions failed, and depositors in these thrifts lost $ 200 million. H.R. Rep. No. 54(I), 101st Cong., 1st Sess. 292 (1989), reprinted in 1989 U.S.C.C.A.N. 86, 88-89 (House Report). Congress took several measures in response. First, Congress created the Federal Home Loan Bank Board (Bank Board) to channel funds to thrifts in order to prevent foreclosures and to allow thrifts to make loans on residences. House Report at 292, 1989 U.S.C.C.A.N. at 88; see Federal Home Loan Bank Act, Pub. L. No. 72-304, 47 Stat. 725 (1932) (codified as amended at 12 U.S.C. @@ 1421-1449 (1988)). Next, Congress added the Home Owners' Loan Act, which authorized the Bank Board to charter and regulate federal savings and loan associations. Pub. L. No. 73-43, 48 Stat. 128 (1933) (codified as amended at 12 U.S.C. @@ 1461-1468 (1988)). Then, to further restore public confidence in thrift institutions, Congress in the National Housing Act of 1934 provided federal deposit insurance for depositors. Pub. L. No. 73-479, 48 Stat. 1246 (1934) (codified [*9] as amended at 12 U.S.C. @@ 1701-1750g (1988)). This act also established the Federal Savings and Loan Insurance Corporation (FSLIC), an agency under the Bank Board's authority that regulated all federally insured thrifts.

Among the regulatory requirements promulgated and enforced by the agencies were capital requirements, which were minimum reserves of capital that a thrift had to maintain. Failure to comply with minimum regulatory capital requirements had severe repercussions for a thrift. The agencies had a variety of measures that could be taken against noncomplying thrifts. In the most serious cases, the government could seize the thrift and place it into receivership where it might later be sold or liquidated. This drastic remedy was rarely necessary, however, because of the relative health of the thrift industry until the thrift crisis of the late 1970s and early 1980s.

In the late 1970s and early 1980s high interest rates resulted in sharply higher costs of funds for thrifts. The thrifts' main assets were long-term, fixed-rate mortgages taken during times of lower interest rates. As a result the revenues produced by these mortgages were exceeded by the rapidly rising costs [*10] of attracting short-term deposits. Thrifts that were locked into long-term low interest rate loans simply could not meet their deposit obligations. This interest rate mismatch was one of the principal causes of numerous thrift failures. Eighty-one thrifts failed in 1981, 252 in 1982, and 102 in 1983. House Report at 296, 1989 U.S.C.C.A.N. at 92.

cause of bank problems early 80s - unnec

With all of these bank failures and the likelihood of more occurring, the FSLIC faced deposit insurance liabilities that threatened to exhaust its insurance fund. See Olympic Fed. Sav. & Loan Ass'n v. Director, OTS, 732 F. Supp. 1183, 1185 (D.D.C. 1990). As an alternative to liquidating failing thrifts and expending the FSLIC's insurance funds, the Bank Board and FSLIC encouraged healthy thrifts to merge with the failing ones. In these supervisory mergers, the regulators provided direct assistance and other incentives necessary for the healthy thrifts to maintain their financial well-being after the mergers and in this way the regulators tried to avoid paying off the failing thrifts' deposits out of the FSLIC's insurance fund. Among the incentives offered by the FSLIC and the Bank Board was the use of the purchase method of accounting [*11] under which "supervisory goodwill" resulting from the merger would be treated as satisfying part of the merged thrift's regulatory capital requirements. See Bank Board Memorandum R-31b (1981). Another incentive was the use of "capital credits" that also could be counted toward the regulatory capital requirements.

both relevant?

The purchase method of accounting is a generally accepted accounting practice (GAAP) for mergers, which accounts for the surplus of the purchase price over the fair market value of the acquired organization as goodwill, an intangible asset. As explained by the Court of Federal Claims:

Under [the purchase method of accounting,] . . . the book value of the acquired thrift's assets and liabilities was adjusted to fair market value at the time of the acquisition. Any excess in the cost of the acquisition (which included liabilities assumed by the acquirer) over the fair market value of the acquired assets was separately recorded on the acquirer's books as "goodwill." . . . Goodwill was considered an intangible asset that could be amortized on a straightline basis over a number of years.

Winstar I, 21 Cl. Ct. at 113. In the context of a supervisory merger, [*12] the difference between the fair market value of the failing thrift's liabilities assumed by an acquirer and the fair market value of the failing thrift's assets was considered "supervisory goodwill." The Bank Board and the FSLIC allowed the merged thrifts to count this supervisory goodwill toward the minimum regulatory capital requirements and to amortize this goodwill over periods of up to 40 years. This permitted the healthy thrift to assume the deposit liabilities of the failing thrift and to maintain capital compliance without having to put up large amounts of its own money and without requiring large amounts of monetary assistance from the government.

The capital credits incentive used by the Bank Board and the FSLIC to encourage mergers with failing thrifts involved the FSLIC's contribution of cash to the merged thrifts. The regulators allowed a portion or all of this cash contribution to be treated as partial satisfaction of the merged thrift's regulatory capital requirements. In addition, this cash contribution in some instances would not be treated as an asset in determining supervisory goodwill generated by the merger.

Allowing acquirers of failing thrifts to treat supervisory [*13] goodwill and capital credits as regulatory capital stimulated many acquisitions that would otherwise not have taken place because of the difficulty of meeting the minimum capital requirements. Indeed this was the precise intention of the Bank Board and FSLIC -- supervisory mergers could not have occurred without the approval by the regulatory agencies of these accounting treatments. As former Bank Board Chairman Richard Pratt stated in testimony before Congress:

The Bank Board was caught between a rock and a hard place. While it did not have sufficient resources to close all insolvent institutions, at the same time, it had to consolidate the industry, move weaker institutions into stronger hands and do everything possible to minimize losses during the transition period. Goodwill was an indispensable tool in performing this task. The GAAP approach to purchase method accounting mergers provided a bridge which allowed the Bank Board to encourage the necessary consolidation of the industry, while at the same time husbanding the financial resources which were then available to it.

Savings and Loan Policies in the Late 1970s and 1980s: Hearings Before the House Comm. on [*14] Banking, Finance and Urban Affairs, 101st Cong., 2d Sess., No. 176, at 227 (1990).

B. Winstar, Statesman and Glendale acquired insolvent, failing thrifts under this policy of encouraging thrift mergers. In each case, they received the government's approval and assistance. In each case, the government saved millions of dollars that it would have had to pay to the insured depositors if the failing thrifts had been liquidated instead of being acquired.

1. In September of 1981, Glendale Federal Bank was approached by First Federal Savings and Loan Association of Broward County (Broward) about a possible merger. Glendale was a federal savings and loan association based in California. It was a profitable thrift, which was in full regulatory compliance. Broward was a federal savings and loan association based in Florida that had incurred significant losses. Broward's liabilities exceeded its assets by approximately $ 734 million. Glendale submitted a merger proposal to the FSLIC. Glendale proposed to use the purchase method of accounting to record the supervisory goodwill resulting from this accounting as an intangible asset amortizable over periods up to 40 years. After lengthy negotiations [*15] over the terms and conditions, the FSLIC agreed to provide assistance to the merged entity and to recommend approval of the merger transaction to the Bank Board.

In its resolution approving the merger plan between Glendale and Broward, the Bank Board imposed the condition that Glendale provide an opinion letter satisfactory to the Board's supervisory agent from its independent accountants justifying the use of the purchase method of accounting, specifically describing any goodwill arising from the merger, and substantiating the reasonableness of the amounts attributable to goodwill and the resulting amortization periods and methods. The Bank Board resolution also gave the FSLIC authority to enter into a Supervisory Action Agreement (SAA) with Glendale. The SAA with Glendale was signed in November of 1981 and Glendale promptly consummated its merger with Broward. As required by the Bank Board resolution, Glendale later provided its accountants' justification and opinion letter satisfactory to the Bank Board, which stated that "$ 18,000,000 of the resultant goodwill . . . will be amortized on a straight line basis over 12 years" and that the "remaining goodwill of $ 716,666,000 will [*16] be amortized on a straight line basis over 40 years." By the government's estimates, the Glendale-Broward merger saved the government approximately three quarters of a billion dollars.

2. In 1987 Statesman approached the FSLIC about acquiring a subsidiary of an insolvent state-chartered FSLIC insured savings and loan in Florida, First Federated Savings Bank (First Federated). The FSLIC responded to the inquiry by indicating that Statesman would have to acquire all of First Federated if the government was to assist. Further, it would require that Statesman's acquisition of First Federated be combined with the acquisition of three other financially troubled thrifts in Iowa. n3 After a year of negotiating the FSLIC and Statesman agreed on the terms of a complex plan whereby Statesman would acquire the four thrifts.

- - - - - - - - - - - - - - - - - - - -Footnotes- - - - - - - - - - - - - - - - - - - -

n3 The three thrifts were First Federal Savings Bank of Waterloo, Iowa, Peoples Federal Savings and Loan Association of Waterloo, Iowa, and Perpetual Savings and Loan Association of Waterloo, Iowa.

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[*17]

Like the merger of Glendale, Statesman's merger plan called for the use of the purchase method of accounting. The Statesman plan called for an investment by Statesman and its co-investor American Life and Casualty Company of $ 21 million into Statesman's Savings Holding Company, which in turn would purchase $ 21 million of stock in a newly-formed federal stock savings bank named Statesman Bank for Savings. The Statesman Bank for Savings would then merge with the four failing thrifts.

As part of the transactions, the FSLIC and Statesman entered into an Assistance Agreement calling for the FSLIC to provide a $ 60 million cash contribution to the Statesman Bank for Savings. Under the Assistance Agreement and the Bank Board Resolution approving the merger, $ 26 million of this cash contribution (including $ 5 million represented by a debenture that Statesman was required to pay back) was to be permanently credited to Statesman's regulatory capital (i.e., as a capital credit) for purposes of meeting minimum regulatory capital requirements. Statesman's merger is the only one of the three at issue in this appeal that involves a capital credit.

The Bank Board resolution permitted use of [*18] the purchase method of accounting. Supervisory goodwill arising from the merger acquisitions in the amount of $ 25.8 million was recognized as a capital asset for purposes of meeting regulatory capital requirements and Statesman was allowed to amortize that goodwill over 25 years. The Bank Board granted authority to the FSLIC to enter into the Assistance Agreement with Statesman and required Statesman to provide an opinion letter from its independent accountants to justify its use of the purchase method of accounting and supervisory goodwill. Statesman provided the opinion letter to the agency's satisfaction. By the government's estimates, the cost of the Statesman merger to the government was $ 50 million less than the cost of liquidating the four thrifts.

3. In 1983 a Minnesota-based thrift, Windom Federal Savings and Loan Association (Windom), was in danger of failing. The board of directors of Windom determined that its failure could not be avoided without assistance from the FSLIC. The FSLIC estimated that liquidating the federally insured thrift could cost $ 12 million dollars and it pursued an alternative to paying this money out of its insurance fund. It chose to solicit [*19] bids for the acquisition of Windom.

Winstar Corporation was a holding company formed by investors for the purpose of acquiring Windom. Winstar in turn formed a new wholly-owned, federal stock savings bank, United Federal Savings Bank, to merge with Windom. Winstar's plan contemplated financing the merger by cash contributions by both the investors and the FSLIC. The plan also called for use of the purchase method of accounting and recording supervisory goodwill as an intangible asset which initially was to amortized over a period of 40 years (later changed to 35 years). After negotiating the terms with Winstar Corporation and its investors, the FSLIC recommended to the Bank Board that it approve the merger plan. The Bank Board approved the merger again subject to Winstar providing an opinion letter from its independent accountants justifying the use of the purchase method of accounting and detailing the resulting supervisory goodwill. As a part of the transaction, FSLIC signed an Assistance Agreement with Winstar Corporation and the Bank Board issued a forbearance letter. The forbearance letter stated that intangible assets resulting from use of the purchase method of accounting [*20] "may be amortized . . . over a period not to exceed 35 years by the straight-line method." By the government's estimates, the Winstar-Windom merger saved the government $ 7 million over what liquidation of Windom would have cost.

C. In spite of these and similar actions taken by the Bank Board and the FSLIC, thrifts continued to fail and the public confidence in the thrift industry continued to erode during the late 1980s. In response to this crisis in the savings and loan industry, Congress in 1989 passed FIRREA. FIRREA substantially modified the overall thrift regulatory scheme. As pertinent here, it (1) abolished the FSLIC and transferred its functions to other agencies; (2) created a new thrift deposit insurance fund under the Federal Deposit Insurance Corporation (FDIC); (3) eliminated the Bank Board and replaced it with the Office of Thrift Supervision (OTS), an office within the Department of Treasury, and made the OTS Director responsible for the regulation of all federally insured savings associations and the chartering of federal thrifts; and (4) established the Resolution Trust Corporation (RTC), which was charged with closing certain thrifts. See 12 U.S.C. @@ 1437 [*21] note, 1441a, 1821.

Among the legislative reforms of FIRREA was the requirement that the OTS "prescribe and maintain uniformly applicable capital standards for savings associations." 12 U.S.C. @ 1464(t)(1)(a). In addition, Congress expressly restricted the continued use of supervisory goodwill to satisfy regulatory capital requirements. *

FIRREA required federally insured thrifts to satisfy three new minimum capital standards: "tangible" capital, "core" capital, and "risk-based" capital. 12 U.S.C. @ 1464(t). Under FIRREA supervisory goodwill could not be included at all in satisfying minimum tangible capital. The amount of supervisory goodwill that could be included in satisfying "core" capital decreased each year after FIRREA's enactment and was entirely phased out on December 31, 1994. Finally, thrifts were required to maintain "risk-based" capital in an amount substantially comparable to that required by the Comptroller of the Currency for national banks. 12 U.S.C. @ 1464(t)(2)(C). Although supervisory goodwill could be used for this purpose, FIRREA limited its amortization to a period of no more than 20 years. 12 U.S.C. @ 1464(t)(9)(B).

FIRREA did not specifically cover capital [*22] credits or otherwise exclude FSLIC cash contributions from capital for purposes of determining compliance with any of the minimum capital requirements. The OTS, however, equated capital credits with "qualifying supervisory goodwill" within the meaning of the statute and promulgated a regulation that treated capital credits in the same manner as supervisory goodwill. 12 C.F.R. @ 567.1(w). Probably ignore this — just do other

As a result of FIRREA and the OTS regulation, many thrifts that were previously in full compliance with the regulations on capital requirements failed to satisfy the new capital standards and immediately became subject to seizure. Glendale initially remained in compliance with the three new capital standards of FIRREA even though it was required to exclude all the unamortized supervisory goodwill that resulted from its merger with Broward for purposes of calculating its tangible capital and was required to accelerate the amortization of supervisory goodwill in calculating its required core and risk-based capital requirements. However, Glendale had to implement costly new measures to compensate for the exclusion of much of its supervisory goodwill from regulatory capital. Later, in March 1992, Glendale [*23] fell out of compliance with the risk-based capital standard.

After FIRREA, Statesman immediately fell below the three new capital standards established by the Act. As a result, the OTS appointed the RTC as receiver for Statesman in July of 1990. Winstar also fell into noncompliance as soon as the FIRREA capital requirements became effective. Winstar was placed in receivership by the OTS in May of 1990.

D. The plaintiffs filed suit in the Court of Federal Claims alleging that under FIRREA the preclusion or limited availability to them of supervisory goodwill (and capital credits in the case of Statesman) for satisfying regulatory capital constituted a breach of contract or, in the alternative, a taking of their contract rights without compensation in violation of the Fifth Amendment. The plaintiffs claimed that the government was contractually obligated to recognize supervisory goodwill generated by the mergers (and capital credits) as an intangible capital asset for purposes of their compliance with minimum regulatory capital standards. The plaintiffs also claimed that they were entitled to amortize that supervisory goodwill for the agreed periods established at the time of their [*24] acquisitions of failing thrifts. Under their contract claims, plaintiffs asserted that FIRREA, and the regulations thereunder, as applied to them, breached those contract obligations. All of the plaintiffs filed summary judgment motions on the issue of liability. What's the

The government defended on the grounds that there were no contractual rights as alleged and that in any event the alleged agreements were subject to statutory and regulatory changes. Relying principally on Bowen v. Public Agencies Opposed to Social Security Entrapment (POSSE), 477 U.S. 41, 91 L. Ed. 2d 35, 106 S. Ct. 2390 (1986), the government argued that the thrifts impermissibly sought to enjoin Congress' power to legislate and the agencies' power to regulate. The government further argued that the sovereign acts doctrine, as stated in Horowitz v. United States, 267 U.S. 458, 461, 69 L. Ed. 736, 45 S. Ct. 344 (1925), precluded recovery for any contractual rights breached by FIRREA.

The Court of Federal Claims granted summary judgment to the plaintiffs on the issue of liability under the contract claims and did not reach the constitutional takings claims. The court found that binding contracts were made between plaintiffs and the FSLIC in each of the three merger transactions. [*25] It held that these contracts were breached when the regulatory capital requirements of FIRREA, and the regulations, were applied to plaintiffs. The Court of Federal Claims distinguished POSSE on the grounds that the case did not involve bargained for contract rights but rather involved an entitlement program. The court also distinguished POSSE because the relief sought was an injunction to prevent the government from acting in its sovereign capacity, whereas plaintiffs only claimed damages for breach of their contracts. Finally, the Court of Federal Claims found that FIRREA, in specifically limiting the use of supervisory goodwill that had previously been contractually authorized, was not a sovereign act but rather was aimed directly at thrifts with contracts like those of the plaintiffs. Thus, the court concluded that the government could not rely on the sovereign acts doctrine to shield it from liability.

III

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Franchise ~~directly~~ in conflict?

Ask Carter
1) What's the gov't's Lit arg?
2) What now?
3) Chances for success?

We review the Court of Federal Claims' grant of summary judgment under a de novo standard of review, with justifiable factual inferences being drawn in favor of the party opposing summary judgment. Anderson v. Liberty Lobby, Inc., 477 U.S. 242, 255, 91 L. Ed. 2d 202, 106 S. Ct. 2505 (1986). [*26] On appeal both parties ask for entry of judgment in their favor based on the uncontested facts of record.

A. The Court of Federal Claims found that all the thrifts had contracts with the government that contained terms allowing the use of supervisory goodwill (and in Statesman's case, capital credits) to satisfy a portion of their regulatory capital requirements and that this intangible asset could be amortized over extended periods of time. In the Glendale and Statesman cases, the court determined there were express contracts with these terms, and in Winstar's case, that there was an implied-in-fact contract with these terms. The government initially contends that no such contractual terms existed.

Contract construction is a question of law that we review de novo. Hughes Communications Galaxy, Inc. v. United States, 998 F.2d 953, 957 (Fed. Cir. 1993). A principal objective in deciding what contractual language means is to discern the parties' intent at the time the contract was signed. Arizona v. United States, 216 Ct. Cl. 221, 575 F.2d 855, 863 (Ct. Cl. 1978).

1. We agree with the Court of Federal Claims that the government had an express contractual obligation to permit Glendale [*27] to count the supervisory goodwill generated as a result of its merger with Broward as a capital asset for regulatory capital purposes. Similarly, as the trial court determined, under this agreement Glendale was entitled to amortize the major portion of that goodwill on a straight line basis for a period of 40 years, and the balance for 12 years.

The government contends that the FSLIC's SAA with Glendale is the only document evidencing Glendale's contract with the FSLIC and that it contains no promise relating to goodwill or its amortization. As noted by the Court of Federal Claims, however, Glendale's contract was not limited to the SAA itself, but also included the contemporaneous resolutions and letters issued by the FSLIC and the Bank Board. The SAA's integration clause provided:

This Agreement, together with an interpretation thereof or understanding agreed to in writing by the parties, constitutes the entire agreement between the parties thereto and supersedes all prior agreements and understandings of the parties in connection herewith, excepting only the Agreement of Merger and any resolutions or letters issued contemporaneously herewith by the [Bank Board] or the [*28] FSLIC, provided, however, that in the event of any conflict, variance, or inconsistency between this Agreement and the Agreement of Merger, the provisions of this Agreement shall govern and be binding on all parties insofar as the rights, privileges, duties, obligations, and liabilities of the FSLIC are concerned.

(Emphasis added.)

One of these contemporaneous documents, which was relied on by the Court of Federal Claims, was Bank Board Resolution 81-710. The FSLIC needed the Bank Board's approval before it could enter into the SAA with Glendale and approve the merger. The FSLIC and Glendale had negotiated the terms of the Broward merger, including Glendale's proposed use of supervisory goodwill and

Glendale's obligation to absorb Broward's deposit liabilities. After negotiating terms satisfactory to both parties, the FSLIC recommended to the Bank Board that it approve the merger and authorize the FSLIC to execute the SAA with Glendale.

Resolution 81-710 provided the Bank Board's approval, with certain conditions that Glendale was required to satisfy to the Bank Board's satisfaction, including the following:

Not later than sixty days following the effective date [*29] of the merger, Glendale shall furnish an opinion from its independent accountant, satisfactory to the Supervisory Agent, which (a) indicates the justification under generally accepted accounting principles for the use of the purchase method of accounting for its merger with Broward, (b) specifically describes, as of the Effective Date, any goodwill or discount of assets arising from the merger to be recorded on Glendale's books, and (c) substantiates the reasonableness of amounts attributed to goodwill and the discount of assets and the resulting amortization periods and methods . . . .

The Resolution continued:

Glendale shall submit a stipulation that any goodwill arising from this transaction shall be determined and amortized in accordance with [Bank Board] Memorandum R-31b . . . .

Memorandum R-31b (1981) was the Bank Board's "guidelines" on how an acquiring thrift could count the excess of the acquired thrift's purchase price over the acquired thrift's fair market value as an intangible asset under the purchase method of accounting. n4

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n4 The Memorandum provided that:

An application from an association requesting approval for a business combination to be accounted for by the purchase method of accounting, from which intangible assets will result, should include a description of any resulting intangible assets and the plan for their amortization. This description should discuss the nature and results of management's analysis of the underlying intangible assets and the resulting amortization periods and methods.

In accordance with applicable accounting principles, the Memorandum limited the period of amortization to 40 years or less.

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[*30]

Thus, in Resolution 81-710, the Bank Board clearly evidenced its approval of the terms of the merger, including the terms that the purchase method of accounting would be employed in accounting for the merger, that goodwill arising from the merger would be recorded on Glendale's books, and that such goodwill would be amortized for reasonable periods under reasonable methods, provided these accounting treatments were justified to the satisfaction of the Bank Board's supervisory agent. In this connection, the Court of Federal Claims observed:

It is also uncontroverted that the government manifested its approval of the terms set forth in the opinion letter prior to the effective date of the Supervisory Action Agreement. In a letter from H. Brent Beesley, then-Director of FSLIC, to [Bank Board] dated November 19, 1981, FSLIC recommended the use of the purchase method of accounting for the merger. Beesley explicitly referred to a Peat, Marwick, Mitchell & Co. opinion letter dated November 10, 1981 setting forth the specific amount of supervisory goodwill projected to be amortized pursuant to the merger, assuming the use of the purchase method of accounting.

26 Cl. Ct. [*31] at 910.

After the merger, Glendale submitted the required letter from its independent accountants to the Bank Board's supervisory agent. The letter confirmed as of the date of closing the amount of goodwill resulting from the merger under the purchase method of accounting and reiterated the amortization periods and the amounts of goodwill to be amortized under each period.

Pursuant to the provisions of the Agreement of Merger between [Glendale] and Broward dated November 20, 1981 and the Supervisory Action Agreement between [Glendale] and the Federal Savings and Loan Insurance Corporation (FSLIC) dated November 20, 1981, upon the effective date of November 20, 1981, [Glendale] accounted for the acquisition using the "Purchase Method" of accounting. . . .

. . . .

. . . $ 18,000,000 of the resultant goodwill is associated with the savings deposit base and will be amortized on a straight line basis over 12 years, the estimated life of the savings deposit base. The remaining goodwill of $ 716,666,000 will be amortized on a straight line basis over 40 years as [Glendale] believes that the remaining goodwill has an indefinite life since it is related to expansion [*32] of operations into an entirely new market area.

The letter further opined that the accounting and methodology for calculating supervisory goodwill were in accordance with generally accepted accounting principles. Glendale satisfied the conditions for merger approval set out in Resolution 81-710 by submitting both the independent accountants' opinion and the stipulation that the accounting was in accordance with Memorandum R-31b. Moreover, there is no dispute that these submissions were satisfactory to the Bank Board's supervisory agent as required by that Resolution.

We conclude based on all of the contemporaneous documents, which under the integration clause of the SAA collectively constituted the "Agreement" of the parties, that the Bank Board and the FSLIC were contractually bound to recognize the supervisory goodwill and the amortization periods reflected in the approved accountants' letter. It is clear from the documents that this was the intent of the parties. Glendale consummated its merger with Broward on this understanding and in doing so saved the government hundreds of millions of dollars.

Our conclusion is supported by other evidence and by the [*33] circumstances surrounding the transaction. If the parties did not intend to use supervisory goodwill for regulatory capital purposes there would simply be no reason for the extensive negotiations and the conditions regarding its use. It is not disputed that if supervisory goodwill had not been available for purposes of meeting regulatory capital requirements, the merged thrift would have been subject to regulatory noncompliance and penalties from the moment of its creation. n5 Moreover, the recitals of the SAA state that "Glendale proposes to enter into an agreement of merger with [Broward]" and that Broward "is in danger of default and that the nature and/or amount of such assistance would be less than the losses FSLIC would sustain upon the liquidation of [Broward]." Without the use of supervisory goodwill, the merged thrifts would have been in a failing position resulting in the losses the FSLIC sought to avoid. Finally, it is appropriate to observe that no healthy thrift would consummate a transaction that immediately put it in regulatory noncompliance.

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n5 Prior to the merger, Glendale was a healthy, fully capitalized thrift. Glendale asserts, and the government does not disagree, that after merging with Broward Glendale's regulatory net worth would have been negative $ 460 million if supervisory goodwill had not been counted as a capital asset.

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[*34]

We consider the government's argument that the Bank Board Resolution was merely a statement of "then-current prosecutorial and regulatory policy" to be of little significance. Once specific terms as to the amount of supervisory goodwill and its amortization periods under that regulatory policy were incorporated in a negotiated arm's length contract, both parties were bound to them. While it is true as the government argues that a statement of policy, for instance as set forth in Memorandum R-31b, could be changed (which it later was), the contract could not be changed except by mutual consent.

The government makes two additional arguments why the Court of Federal Claims' interpretation was wrong. First it contends that the SAA expired by its terms in November 1991, prior to the alleged breach. We view the expiration provision as only relating to executory provisions set out in the SAA, which obligated the FSLIC to make certain payments to the merged thrift for a limited period of time. This provision of the SAA in any event does not negate other obligations under the merger plan, including the specific time periods for amortization of goodwill.

The government's second argument is [*35] based on the clause contained in the SAA, which provides that: "Nothing in this Agreement shall require any unlawful action or inaction by either of the parties hereto." The government contends this clause contemplates possible future changes in the law. The proper reading of this clause, however, is that neither party is required to act to the extent that some portion of the contract inadvertently violated the law as it existed at the time the contract was entered into. In any case, the clause clearly is not an escape hatch that allows the federal government to avoid performance of its contractual obligations without penalty by passing a law prohibiting its own performance.

2. The Statesman transaction involved the acquisition by merger of four failing thrifts, and thus the accompanying documentation was more complex than that in the Glendale transaction. The Court of Federal Claims determined an

express contract existed between the plaintiffs and the government which permitted the use of supervisory goodwill and capital credits in meeting regulatory capital levels, and which established the amortization period for such goodwill. We agree.

In connection with the acquisition of [*36] the four thrifts, Statesman signed an Assistance Agreement with the FSLIC. The Assistance Agreement contained express terms that allowed capital credits to be used to satisfy regulatory capital. Not surprisingly, the Court of Federal Claims stated that "the government readily concedes that an express contract existed, at least in regard to the $ 26 million capital credit extended by the government to Statesman." 26 Cl. Ct. at 912. A similar concession has been made by the government in its appeal brief, which states:

The terms of the Assistance Agreement provided that $ 26 million of that amount (the "capital credit") constituted RAP goodwill to be credited to Statesman's regulatory capital.

Thus, although the government maintains these terms were not insulated against changes in the law, there can be no doubt that contractual promises regarding capital credits were made.

The Statesman documents regarding the treatment of supervisory goodwill are, in substance, the same as those in the Glendale transaction. The Assistance Agreement contained an integration clause that incorporated contemporaneous resolutions of the Bank Board. The Bank Board's Resolution 88-169 approved [*37] the Statesman merger plan and authorized the FSLIC to enter into the Assistance Agreement. In contrast to the Glendale resolution, however, Resolution No. 88-169 expressly approved and described the accounting treatments to be used in the Statesman merger transaction, as follows:

The Acquisition and the Mergers shall be accounted for, and [Statesman] shall report to the Bank Board and the FSLIC, in accordance with generally accepted accounting principles prevailing in the savings and loan industry, as accepted, modified, clarified, or interpreted by applicable regulations of the Bank Board and the FSLIC, except to the extent of the following departures from generally accepted accounting principles:

(a) Twenty-one million dollars of the initial contribution by the [FSLIC] to [Statesman], and five million dollars of the principal amount of the Subordinated Debenture issued to the FSLIC, pursuant to @ 6 of the Assistance Agreement, shall be credited to the regulatory capital account of [Statesman]; and

(b) The value of any unidentifiable intangible assets resulting from accounting for the Acquisition and the Mergers in accordance with the purchase [*38] method of accounting may be amortized by [Statesman] over a period not in excess of twenty-five (25) years by the straight line method . . . .

As stated in the government's appeal brief:

The Bank Board resolution also permitted use of the purchase method of accounting for the acquisitions. Thus, Statesman was allowed to amortize $ 25.8 million more in supervisory goodwill for 25 years.

As it did in the Glendale transaction, the Bank Board reserved its approval of this accounting treatment until Statesman furnished within ninety days, "an analysis accompanied by a concurring opinion from its independent certified public accountants" which

shall (a) specifically describe, as of the Effective Date, any intangible assets, including goodwill and the discount and premiums arising from the Acquisition and the Mergers, to be recorded on New Federal's books, and (b) substantiate the reasonableness and conformity with regulatory requirements of the amounts attributed to intangible assets, including goodwill and the discount and premiums, and the related amortization periods and methods . . . .

The government concedes that this condition was met to [*39] the Board's satisfaction.

We conclude that the government was contractually obligated to recognize the capital credits and the supervisory goodwill generated by the merger as part of the Statesman's regulatory capital requirement and to permit such goodwill to be amortized on a straight line basis over 25 years.

3. The Court of Federal Claims concluded that Winstar had an implied-in-fact contract that obligated the government to allow Winstar to treat supervisory goodwill as a capital asset for regulatory capital purposes to be amortized over a 35 year period. Because we are satisfied that an express agreement existed between the FSLIC and Winstar, on the same terms found by the Court of Federal Claims, we do not reach the question of whether there could also be an implied-in-fact contract.

In July 1984 Winstar entered into an Assistance Agreement with the FSLIC. The Assistance Agreement stated that "the purpose of this Agreement [is] to provide a means by which the failure of [Windom] may be prevented, the savers and other creditors of [Windom] may be protected against losses . . . , [United] and Winstar may receive the benefits and assume the risks contracted for, and [*40] expenses to [the FSLIC] may be reduced." While this purpose recognized there was a mutual exchange of benefits and risks in the agreement, Winstar's Assistance Agreement, like Glendale's SAA, did not directly cover the treatment of supervisory goodwill. Again, however, this Assistance Agreement contained an integration clause which made "the Merger Agreement and any resolutions or letters issued contemporaneously with [the Assistance Agreement]" part of the contract between the parties.

Among the documents evidencing the government's contractual obligation is a forbearance letter of the Bank Board issued in July of 1984 to the Winstar investors. The forbearance letter in the first paragraph states the purpose is to "confirm the understanding that," after which it proceeds to enumerate several terms of the Winstar transaction. Paragraph 2 of those terms provides:

For purposes of reporting to the Board, the value of any intangible assets resulting from accounting for the merger in accordance with the purchase method may be amortized by [Winstar] over a period not to exceed 35 years by the straight-line method . . . .

The other documentation in the Winstar transaction [*41] is substantially identical to that in the Glendale transaction with respect to accounting treatment for the merger. For example, there is a contemporaneous Bank Board resolution, Resolution 84-363, approving the Winstar merger and giving the FSLIC the authority to proceed. That resolution required Winstar to provide an opinion "from its independent public accountants, satisfactory to the Supervisory Agent and to the Office of Examinations and Supervision" describing the use of goodwill and substantiating its reasonableness and conformity with regulatory requirements. It is not contested that Winstar satisfied the conditions in Resolution 84-363 to the Bank Board's satisfaction.

We conclude that the documentation in the Winstar transaction establishes an express agreement allowing Winstar to proceed with the merger plan approved by the Bank Board, including the recording of supervisory goodwill as a capital asset for regulatory capital purposes to be amortized over 35 years. Other circumstances, such as those discussed above in connection with the Glendale transaction, are consistent with this conclusion and demonstrate that it was the intention of the parties to be bound by the accounting [*42] treatment for goodwill arising in the merger. Likewise, we find the government's arguments regarding the expiration of the Assistance Agreement and the Agreement's "unlawful action" provision unpersuasive for the same reasons as in the Glendale transaction.

Finally, the government argues the Net Worth Maintenance Stipulation signed by Winstar required Winstar to abide by any changes in the law regarding regulatory capital. We agree to the extent the Stipulation requires Winstar to maintain its capital at levels set by the bank regulators. Winstar, like other thrifts, was bound to keep in compliance with banking regulations and laws regarding capital levels except to the extent the Bank Board expressly agreed to forbear from enforcing its regulations against it. This stipulation by Winstar to maintain its regulatory net worth at whatever level the regulators set does not, however, eclipse the government's own promise that Winstar could count supervisory goodwill in meeting the regulatory requirements with which it had promised to comply.

B. There can be little question that the application of FIRREA and the regulations thereunder to deny or restrict plaintiffs' contractual rights [*43] to use supervisory goodwill with the associated amortization periods, and for Statesman's capital credits, in partial satisfaction of their capital requirements was a breach of the FSLIC's and the Bank Board's agreements with them. FIRREA greatly reduced the amount of supervisory goodwill that could be used to meet regulatory capital requirements. See 12 U.S.C. @ 1464(t). The OTS by regulation treated capital credits in the same manner as supervisory goodwill, see 12 C.F.R. @ 567.1(w), thereby restricting the use of such credits for regulatory capital purposes. n6

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n6 Because we affirm the Court of Federal Claims' decision in this case, we need not reach the question of whether FIRREA contemplated that capital credits would be treated as a form of supervisory goodwill.

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Failure to perform a contractual duty when it is due is a breach of the contract. Restatement (Second) of Contracts @ 235(2) (1981). The three plaintiff thrifts negotiated contracts with the bank regulatory agencies that allowed [*44] them to include supervisory goodwill (and capital credits) as assets for regulatory capital purposes and to amortize that supervisory goodwill over extended periods of time. When the plaintiffs satisfied the conditions imposed on them by the contracts, the government's contractual obligations became effective and required it to recognize and accept the purchase method of accounting for the mergers and the use of supervisory goodwill and capital credits as capital assets for regulatory capital requirements.

After FIRREA and its implementing regulations, the bank regulatory agencies limited these assets as acceptable regulatory capital and limited the amortization periods. As a result, Winstar and Statesman were immediately thrown into noncompliance with the new regulatory capital requirements and were seized by federal regulators within approximately six months. Glendale survived the new capital standards but at considerable detriment. We conclude the government failed to perform its contractual obligations under plaintiffs' contracts.

C. The government makes two additional arguments why the thrifts' claims must fail. It contends (1) that the contracts failed to secure unmistakably [*45] the government's contractual obligations in the face of legislative change (the "unmistakability doctrine") and (2) that the government's contractual obligations were relieved by the enactment of "public and general" legislation by the Congress (the "sovereign acts doctrine"). The Court of Federal Claims analyzed each of these arguments extensively in its opinions and found neither to be persuasive. We agree with, and adopt, the substance of these analyses. See Winstar I, 21 Cl. Ct. at 115-17; Winstar II, 25 Cl. Ct. at 544-53; Statesman, 26 Cl. Ct. at 916-24.

1. The government contends that interpreting the contracts at issue as guaranteeing certain accounting treatments in spite of Congress' enactment of FIRREA is a restriction on the government's power to legislate. The Supreme Court's decision in POSSE, 477 U.S. at 52, is cited for the proposition that in interpreting contracts to which the government is a party, the contract should not be construed as waiving the government's power to legislate unless it says so in unmistakable terms. In POSSE the Court, quoting Merrion v. Jicarilla Apache Tribe, 455 U.S. 130, 147-48, 71 L. Ed. 2d 21, 102 S. Ct. 894 (1982), stated:

We have emphasized [*46] that "without regard to its source, sovereign power, even when unexercised, is an enduring presence that governs all contracts subject to the sovereign's jurisdiction, and will remain intact unless surrendered in unmistakable terms." Therefore, contractual arrangements, including those to which a sovereign itself is party, "remain subject to subsequent legislation" by the sovereign.

POSSE, 477 U.S. at 52 (citations omitted). In its briefs on appeal and in the proceedings below, the government also relied heavily on the opinion of the District of Columbia Circuit in Transohio Sav. Bank v. Director, Office of Thrift Supervision, 296 U.S. App. D.C. 231, 967 F.2d 598 (D.C. Cir. 1992). (As explained below, Transohio was modified by the District of Columbia Circuit after the in banc arguments in the instant cases.) Because none of the thrifts can point to express language in their contracts preserving their contractual rights in the face of legislative change, the government concludes that the contracts must yield to the later enacted FIRREA capital requirements.

The Court of Federal Claims in its first Winstar opinion, 21 Cl. Ct. at 115, viewed POSSE as being inapposite because the [*47] government "mischaracterizes the plaintiffs' claim as one which improperly seeks to bind the government's power to regulate." Rather, the court noted that plaintiffs sought only money damages, which did not implicate the government's power to regulate. Thereafter, in its Winstar II opinion considering the government's motion for clarification, the Court of Federal Claims held that POSSE did not preclude finding a binding contract that had been breached by the government, explaining its holding as follows:

> Contrary to the assertions of the government, the Court's holding in POSSE in no way precludes this court from finding the existence of a contract between the government and plaintiffs. As is evident from its opinion, the Court in POSSE recognized that the government has the power to enter into contracts which confer vested rights - rights which the government has a duty to honor. See Perry v. United States, 294 U.S. 330, 351, 79 L. Ed. 912, 55 S. Ct. 432 (1935) ("To say that the Congress may withdraw or ignore [its] pledge, is to assume that the Constitution contemplates a vain promise, a pledge having no other sanction than the pleasure and convenience of the pledgor. This Court [*48] has given no sanction to such a conception of the obligations of our Government."); Lynch v. United States, 292 U.S. 571, 580, 78 L. Ed. 1434, 54 S. Ct. 840 (1934) ("Congress was free to reduce gratuities deemed excessive. But Congress was without power to reduce expenditures by abrogating contractual obligations of the United States. To abrogate contracts, in the attempt to lessen government expenditure, would be not the practice of economy, but an act of repudiation.").
>
> In POSSE, however, unlike the case here, no such vested rights were created as the basic elements of contract formation were absent. In contracts involving the government, as with all contractual relationships, rights vest and contract terms become binding when, after arms length negotiation, all parties to the contract agree to exchange real obligations for real benefits. In POSSE, the Court determined that such vested contract rights did not exist. POSSE, 477 U.S. at 52, 54-55. Although the Court did not explicitly so state, the facts of POSSE make it clear that the provisions of the original Social Security Act were not promulgated after negotiation, arms length or otherwise, between Congress and the plaintiffs who [*49] filed suit. As is the case with all legislation, the only "negotiations" or bargaining involved in the enactment of the original Social Security Act and its amendments took place in the halls of Congress. The "rights" at issue in POSSE, then, were solely government-created. They were really policy decisions made by the democratic political process. There was no legal consideration for the creation of these "rights." At any time, the government could revoke them without legal consequence because the plaintiffs had not bargained for their creation.

25 Cl. Ct. at 545-46 (footnotes omitted) (emphasis in original). The Court of Federal Claims returned to the government's unmistakability argument again in its opinion in the Statesman case. By this time the District of Columbia Circuit had issued its opinion in Transohio, which the government argued supported the unmistakability argument it had made in Winstar.

In Transohio, the plaintiff was a healthy thrift that merged with a failing one upon signing an Assistance Agreement with the FSLIC. After FIRREA was enacted, Transohio sought a preliminary injunction to enjoin the government from applying FIRREA's [*50] provisions against the use of supervisory goodwill as regulatory capital. It argued that FIRREA would breach the government's Assistance Agreement and that there would be a taking of Transohio's property under the Fifth Amendment.

The D.C. Circuit affirmed the district court's denial of the injunction because Transohio was unlikely to succeed on the merits. Transohio, 967 F.2d at 601. While noting the district court had no jurisdiction over the breach of contract claims, the D.C. Circuit analyzed whether Transohio had any contractual property rights that were protected under the due process clause of the Fifth Amendment. Id. at 617. The court agreed there was a contract right for the treatment of goodwill, id. at 618 ("We think the documents strongly suggest that, in addition to money, the agencies gave Transohio some ability to count as regulatory capital the intangible assets created by its mergers."), but concluded that the unmistakability doctrine precluded an interpretation of the contract that would guarantee such treatment against legislative change. Id. at 620. Because the thrift's contract and taking claims were both dependent on the existence of a binding [*51] contract, the court stated there was no need to remand the case to consider the thrift's monetary claims in the Court of Federal Claims. Id. at 614.

The government argued to the Court of Federal Claims that Transohio was persuasive precedent against interpreting the thrift agreements as allowing recovery for contractual breach in the face of legislative change. The Court of Federal Claims was unpersuaded and criticized the Transohio court's use of the unmistakability doctrine as one of contract interpretation rather than one of contract creation.

The purpose animating the unmistakability doctrine makes it clear that the doctrine controls how contractual rights with the government are created, i.e., whether the government has agreed in unmistakable terms to be contractually bound. The doctrine never has been understood as controlling, as the government has alleged in the Winstar-related cases, the effect of the government's breach of a contract. See United States Trust Co. v. New Jersey, [431 U.S. 1, 23, 52 L. Ed. 2d 92, 97 S. Ct. 1505 (1977)] ("The [unmistakability] doctrine requires a determination of the State's power to create irrevocable contract rights in the first place, [*52] rather than an inquiry into the purpose or reasonableness of the subsequent impairment."). The doctrine solely goes to whether a party possesses contractual rights which are binding and for which damages may be given.

Thus, in Winstar and the instant cases, there has been little serious dispute that the government granted the acquiring thrifts, in the clearest possible terms, the right to certain types of regulatory capital treatment. Likewise, the acquiring thrifts have never contended in this court that the government is bound to specifically perform on this obligation. Rather, the dispute has primarily raged over the question of breach. Namely, whether the government must pay damages or provide restitution for its breach, or whether it is excused from such damages by an interpretation of POSSE or the sovereign acts doctrine. The historical understanding of the unmistakability doctrine is not applicable to this issue.

26 Cl. Ct. at 920.

We agree with the Court of Federal Claims' view on the unmistakability doctrine. The terms of a government contract, like any other contract, do not change with the enactment of subsequent legislation absent a specific contractual [*53] provision providing for such a change. Further, we conclude the Court of Federal Claims properly rejected the government's argument based on POSSE that its sovereign power to legislate is at issue here. As the Court of Federal Claims observed:

It is critical to this case . . . that plaintiffs are not claiming that the government contractually bound Congress not to change its regulations. Rather, plaintiffs claim that in their particular transaction with the government, it was agreed that they would be permitted to treat supervisory goodwill in a particular way for a fixed number of years. Thus, while Congress' power to regulate is not impaired, the government may be compelled to pay for the results of its actions, especially when in so doing the government actually is paying because it received a benefit.

Winstar I, 21 Cl. Ct. at 116.

The thrifts did not ask for, and the Court of Federal Claims could not provide, injunctive relief that would have enjoined the thrift regulators from applying the FIRREA requirements to the thrifts. See Kanemoto v. United States Dep't of Justice, 41 F.3d 641, 644 (Fed. Cir. 1994). Rather the thrifts sought money damages for [*54] breach of contract by the government. Money damages, in contrast to injunctive relief, presents little threat to the government's sovereign powers, other than the obvious financial incentive to honor its contracts. The Supreme Court's decision in POSSE is predicated on the need to protect the sovereign's legislative power and that concern is inapplicable where money damages alone are at issue. Hughes Communications, 998 F.2d at 958 (distinguishing POSSE and other unmistakability cases as cases seeking to enjoin the sovereign power to legislate from cases in the Court of Federal Claims where the plaintiff seeks only money damages). In sum, Congress was always free to deem supervisory goodwill a bad idea and legislate it out of existence. Where that legislation breached the government's prior contractual obligations regarding the treatment of supervisory goodwill, however, the government remains liable in money damages for the breach.

Significantly, after the Winstar and Statesman cases were argued to this court sitting in banc, the D.C. Circuit in a later proceeding in the Transohio case reconsidered its earlier position. See Transcapital Fin. Corp. v. Director, [*55] Office of Thrift Supervision, No. 93-5260 (D.C. Cir. Jan. 27, 1995). The court recognized that its prior decision concerned only the denial of injunctive relief, and stated that its "analysis has no bearing one way or the other on the merits of [Transohio's] claim for compensation in the Federal Court of Claims [sic]." Slip op. at 4 (emphasis in the original). Thus the Transohio decision, as modified, complements our decision. In Transohio, the thrift sought to enjoin the government on the basis of its contractual rights and the court ruled it could not do so. In the present case, the thrifts seek only money damages with no request to enjoin the government. Accordingly, the sovereign's power to legislate is not here at issue, only money damages because the FIRREA legislation has breached the contracts.

We are also persuaded, as the Court of Federal Claims held, that the Bank Board and the FSLIC, as the principal regulators of the thrift industry, were fully empowered to enter into the contracts at issue here. Since its inception, the FSLIC has had the power "to make contracts." 12 U.S.C. @ 1725(c)(3) (repealed). The FSLIC and its supervisory agency, the Bank Board, [*56] have had the authority both to extend assistance to acquirers of insolvent FSLIC-insured thrifts, 12 U.S.C. @ 1729(f)(2)(A) (repealed), and to set minimum capital limits on a case-by-case basis, 12 U.S.C. @ 1730(t)(2) (repealed). Although the FSLIC's authority to provide assistance could not exceed the cost of liquidating the thrift, in each of the transactions on appeal the government was saving millions of dollars over the cost of liquidation.

2. Finally, the government argues that FIRREA was a public and general sovereign act and that the government's contractual performance is excused when it is precluded by such an act. Citing the leading case on the sovereign acts doctrine, Horowitz v. United States, 267 U.S. 458, 461, 69 L. Ed. 736, 45 S. Ct. 344 (1925), the government contends that FIRREA was a public and general act that excused its contractual performance. We agree, however, with the Court of Federal Claims that the relevant sections of FIRREA are not public and general sovereign acts. Therefore, the sovereign acts doctrine does not apply.

"The United States when sued as a contractor cannot be held liable for an obstruction to the performance of the particular contract resulting from its public [*57] and general acts as a sovereign." Horowitz, 267 U.S. at 461 (citations omitted). The sovereign acts doctrine is a part of every contract with the government, whether the contract explicitly provides for it or not. Hughes Communications, 998 F.2d at 958. Horowitz makes clear that the sovereign acts doctrine is intended to level the playing field between the government and its contractors. "In this court the United States appear simply as contractors; and they are to be held liable only within the same limits that any other defendant would be in any other court. Though their sovereign acts performed for the general good may work injury to some private contractors, such parties gain nothing by having the United States as their defendants." Horowitz, 267 U.S. at 461 (quoting Jones v. United States, 1 Ct. Cl. 383, 384 (1865)).

Not every governmental action, however, qualifies as a sovereign act within the meaning of the doctrine. Only those "public and general acts as a sovereign" qualify. While presumably all government action is enacted for the good of the public, government action whose principal effect is to abrogate specific contractual rights does not immunize [*58] the government from contractual liability under the doctrine. Everett Plywood Corp. v. United States, 227 Ct. Cl. 415, 651 F.2d 723, 731-32 (Ct. Cl. 1981); Sun Oil Co. v. United States, 215 Ct. Cl. 716, 572 F.2d 786, 817 (Ct. Cl. 1978). As noted by the Court of Federal Claims in its Winstar II decision:

> Where the government abrogates through a limited and focused action specific government obligations to a particular class of individuals or entities it has contracted with, the government is not afforded immunity. In these instances, the government acts not in its capacity as sovereign, but in its capacity as contractor.

25 Cl. Ct. at 551 (citations omitted).

The Court of Federal Claims determined with respect to the Winstar transaction:

> The pertinent sections of FIRREA at issue here, 12 U.S.C. @@ 1464(t)(3)(A) and (9)(B), preclude the application of the sovereign acts doctrine. Their very purpose was to take away plaintiffs' rights to use supervisory goodwill because the Congress felt its use was no longer good policy. Courts assessing sovereign act claims have not granted immunity where the sole purpose of the government action is to reverse an earlier policy decision later deemed [*59] unwise.

Id. at 552 (citations and footnotes omitted). The government argues the Court of Federal Claims erred in concluding that the pertinent FIRREA sections were directed only at thrifts with agreements with the FSLIC. In its brief, the government contends "the FIRREA goodwill restrictions apply to all thrifts, whether they previously had goodwill created or may undertake transactions that create goodwill in the future, and whether or not they had contracts assertedly freezing the prior regulatory treatment of goodwill." (Emphasis in original.)

govt arg

The relevant provisions of FIRREA are 12 U.S.C. @@ 1464(t)(3)(A) and 1464(t)(9)(A)-(C). Section 1464(t)(9)(A) defines "core capital" as that "defined by the Comptroller of the Currency for national banks, less any unidentifiable intangible assets . . . ." Goodwill is one form of an "unidentifiable intangible asset." An exception to the rule against intangible assets being includable in core capital is set forth in the transition rule at @ 1464(t)(3)(A). That section provides "notwithstanding paragraph 9(A), an eligible savings association may include qualifying supervisory goodwill in calculating core capital." 12 U.S.C. [*60] @ 1464(t)(3)(A). The section then provides a table that limits the amount of qualifying supervisory goodwill until it is totally phased out in 1995. Section 1464(t)(9)(C) provides the definition of "tangible" capital, which excludes all intangible assets, including supervisory goodwill. Section 1464(t)(9)(B) defines "qualifying supervisory goodwill" as supervisory goodwill existing on April 12, 1989 and limits the amortization period of qualifying supervisory goodwill to the shorter of 20 years or the remaining amortization period in effect on April 12, 1989.

The statute plainly singles out supervisory goodwill for special treatment, albeit treatment less harsh than other forms of intangible assets. Supervisory goodwill only results from a supervisory merger, a merger that necessarily required the participation of the FSLIC. n7 Thus, thrifts that underwent a supervisory merger, like appellants, are singled out for special treatment by the statute. The statute specifically limits their ability to include certain assets in their calculation of capital. Although there is no doubt Congress passed this legislation out of concern about the use of "accounting gimmicks" behind the insured [*61] deposits, the legislation quite specifically abrogates agreements the government had made at an earlier time when it had suggested and approved the use of such "gimmicks" to avoid bailing out failing thrifts.

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n7 See House Report at 432, 1989 U.S.C.C.A.N. at 228:

The Committee intends the term "supervisory goodwill" to mean goodwill resulting from the acquisition, merger, consolidation, purchase of assets or other business combination of any savings association where the market value of the assets acquired was less than the market value of the liabilities at the time of the transaction and where the accounting treatment of the goodwill has been approved by the Federal Home Loan Bank Board.

- - - - - - - - - - - - - - - - - -End Footnotes- - - - - - - - - - - - - - - - - -

The legislative history behind FIRREA demonstrates that those debating the bill in Congress knew that some thrifts claimed to have contractual rights regarding the use of supervisory goodwill and that the subject provisions would breach those contracts. Three members of the House Committee on Banking, Finance [*62] and Foreign Affairs stated in response to the House version of FIRREA:

Unfortunately, [FIRREA] was amended by the Full Committee to phase out the treatment of goodwill for capital purposes over a five year period. Simply put, the Committee has reneged on the agreements that the government entered into concerning supervisory goodwill.

. . . Clearly, the agreements concerning the treatment of goodwill were part of what the institutions had bargained for. Just as clearly, the Committee is abrogating those agreements.

House Report at 498, 1989 U.S.C.C.A.N. at 293-94 (additional views of Reps. Annunzio, Kanjorski, and Flake). Representative Ackerman argued that "[FIRREA] would abrogate written agreements made by the U.S. Government to thrifts that acquired failing institutions by . . . no longer counting goodwill as capital after a 4-year transition period. In effect, the Government is saying 'thanks for your help, but we don't need you anymore, so we're breaking our promise.'" 135 Cong. Rec. H2783 (daily ed. June 15, 1989). These remarks, which are by no means exhaustive, illustrate that many in Congress were concerned about FIRREA's repudiation of the supervisory [*63] goodwill promises made in the thrift agreements.

One of the dissents argues that because the pertinent sections were part of a "comprehensive piece of national legislation" enacted by Congress, the sections are general and public acts that excuse the government's contractual performance. We disagree. First, the portions of FIRREA at issue in this case are not any less directed at thrifts that had supervisory mergers because they are part of "comprehensive" legislation. By definition, the pertinent sections apply only to supervisory goodwill, which could only occur as a result of a supervisory merger, that was in existence on April 12, 1989. The legislation plainly singles out thrifts that underwent supervisory mergers for special treatment.

Second, we do not find the dissent's attempt to distinguish Sun Oil and Everett Plywood as cases limited to agency action persuasive. There is no reason to distinguish action by the legislative branch from that of the executive branch. Indeed, the agencies in the executive branch receive their power to enter into the contracts from the legislative branch. The contracts the agencies properly enter into are not binding only at the grace [*64] of the legislative branch. Thus the Horowitz case makes no distinction between the acts of the coordinate branches of government. See 267 U.S. at 461 ("be they legislative or executive").

Finally, we know of no authority for this dissent's position that the government has a sovereign right to disavow its contractual obligations through comprehensive national legislation. Such a proposition is not supported by Horowitz and cannot be reconciled with the decisions of the Supreme Court in Lynch v. United States, 292 U.S. 571, 78 L. Ed. 1434, 54 S. Ct. 840 (1934) and Perry v. United States, 294 U.S. 330, 79 L. Ed. 912, 55 S. Ct. 432 (1934). These decisions belie the notion that the government may repudiate its contracts by merely claiming it is acting in its "sovereign" capacity.

We accept, as did the Court of Federal Claims, that FIRREA was enacted for the public welfare--presumably all legislation is. We are convinced, however, that the FIRREA provisions at issue here targeted thrifts that had undergone supervisory mergers, financed in part with supervisory goodwill, with the approval and assistance of the federal government. Moreover, the undisputed reason for limiting the use of the supervisory goodwill was precisely the [*65] reason the government used it in the first place--it is a money equivalent, not money. The government has plainly sought to render its own performance impossible. This is not a public and general act. The sovereign acts doctrine does not apply.

CONCLUSION

There is nothing extraordinary about the contracts in these cases save for their subject matter and the potential liability to the government. It is well established that the government may enter into contracts with private individuals as parties. See Perry v. United States, 294 U.S. 330, 353, 79 L. Ed. 912, 55 S. Ct. 432 (1935) ("The right to make binding obligations is a competence attaching to sovereignty.") (footnote omitted). Our decision is consistent with long standing precedent that when the government enters into such contracts, "its rights and duties therein are governed generally by the law applicable to contracts between private individuals." Lynch v. United States, 292 U.S. 571, 579, 78 L. Ed. 1434, 54 S. Ct. 840 (1934) (footnote omitted); see also Perry, 294 U.S. at 352 ("When the United States, with constitutional authority, makes contracts, it has rights and incurs responsibilities similar to those of individuals who are parties to such instruments.").

We [*66] conclude the thrifts' contracts are enforceable against the government and that the government bargained to allow the thrifts to count certain intangible assets created in their mergers as capital assets for specified periods of time. The government later exercised its sovereign prerogative to enact legislation to limit the use of these intangible assets towards meeting capital requirements. Although the government was free to legislate, it remains liable for breach of contract where its legislation is directed at repudiating its prior contractual agreements. We conclude FIRREA repudiated the government's agreements with the plaintiff thrifts. Accordingly, we affirm the liability judgments of the Court of Federal Claims.

AFFIRMED

DISSENTBY: NIES; LOURIE

DISSENT:
NIES, Circuit Judge, dissenting.

Following in banc rehearing, additional briefing, and Chief Judge Archer's thoughtful opinion, I have reviewed my position in this appeal which is set out at 994 F.2d 797-813. However, I cannot agree that Congress "breached" contracts between the plaintiffs and the "government," that is, the Bank Board and FSLIC, by enacting FIRREA. The majority's holding impermissibly fuses "the [*67] two characters which the government possesses as a contractor and as a sovereign." Horowitz v. United States, 267 U.S. 458, 461, 69 L. Ed. 736, 45 S. Ct. 344 (1925). In my view, the plaintiffs can assert only a claim for an alleged taking of their property by the legislation, a claim which remains to be litigated. This is not a mere technicality. The amount of damages for a "taking" by legislation and for breach of contract are significantly different.

Further, I disagree that a breach of contract occurred even accepting that the Bank Board and the FSLIC were contractually bound to recognize supervisory goodwill * and particular amortization periods. While the regulators agreed to allow the thrifts to use their proposed accounting methods, that is as far as any contract with the "government" went. In the case of private parties, the burden of a change in the law is borne by the party on which it falls, unless responsibility is otherwise assigned in the contract. Contracting parties in that situation "gain nothing by having the United States as their defendants." Id. As delineated in my prior opinion, no clause can be found in the contracts under which the Bank Board and the FSLIC promised to pay if [*68] Congress decided to step in and do away with the "purchase method of accounting," a euphemism for spinning straw into gold, and other accounting gimmicks. In this highly regulated industry, the thrifts did not negotiate contracts that freed them from the risk of a change in regulations.

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* The "purchase method of accounting," in some circumstances, may be "generally accepted accounting practice," but the thrifts could not use that practice to create nonexistent capital as a basis on which they could make loans. The bank regulators had to approve the practice for the thrifts to be able to use this practice for such purposes.

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No one forced the plaintiffs into the acquisitions of failing S&L's. Each acted voluntarily for the purpose of making money, a legitimate purpose, but not one the public must underwrite. It turned out for some that the bargains they struck were disastrous. That was due to their management's bad judgment, coupled with their decision to use the optional accounting practices.

I see no reason [*69] for reprinting my prior lengthy opinion to make minor editorial changes, e.g., change "we" to "I" throughout. While vacated as a court decision, it remains in the books for anyone to read who may be interested. I will simply incorporate it here by reference.

LOURIE, Circuit Judge, dissenting.

I respectfully dissent.

I have no quarrel with the majority's conclusion that the government had a contractual obligation to permit the thrifts to count supervisory goodwill as regulatory capital and to accept the particular amortization periods. Moreover, there can be little doubt concerning the essential unfairness in Congress's denial of those contractual rights in its enactment of FIRREA.

However, I believe that the sovereign acts doctrine is a barrier to the thrifts' recovery under a breach of contract theory. In Horowitz v. United States, the Supreme Court held that "the United States when sued as a contractor cannot be held liable for an obstruction to the performance of [a] particular contract resulting from its public and general acts as a sovereign." Horowitz v. United States, 267 U.S. 458, 461, 69 L. Ed. 736, 45 S. Ct. 344 (1925). An embargo placed by the Railroad Administration on shipments [*70] of silk by freight did not obligate the government for breach of its contract to ship silk which the Ordnance Department had sold to the petitioner. This case is no different in principle.

The majority holds that the enactment of certain sections of FIRREA was not a "public and general" act because "legislation whose principal effect is to abrogate specific contractual rights does not immunize the government from contractual liability under the doctrine." In support of this principle, the majority cites Everett Plywood Corp. v. United States, 227 Ct. Cl. 415, 651 F.2d 723, 731-32 (Ct. Cl. 1981) and Sun Oil Co. v. United States, 215 Ct. Cl. 716, 572 F.2d 786, 817 (Ct. Cl. 1978). The majority also quotes the Court of Federal Claims' decision in Winstar II stating that the government is not afforded immunity when it "acts not in its capacity as sovereign, but in its capacity as contractor." Winstar Corp. v. U.S., 25 Cl. Ct. 541, 551 (1992). In addition, the majority refers to Lynch v. United States, 292 U.S. 571, 78 L. Ed. 1434, 54 S. Ct. 840 (1934), and Perry v. United States, 294 U.S. 330, 79 L. Ed. 912, 55 S. Ct. 432 (1935).

Neither Everett nor Sun Oil, however, involved an act of general legislation as the asserted ground of contract breach. [*71] Everett dealt with an agency's termination of a single logging contract. The Everett court specifically stated that "it would have been an entirely different case if Congress had passed a law immediately prohibiting all cutting in public forests." Everett, 651 F.2d at 732. Similarly, in Sun Oil the Secretary of the Interior denied a single drilling permit; there was no question of an alleged breach by legislation. In both Everett and Sun Oil the agency action was directed to a single contract, not all government contracts having a particular provision. Furthermore, unlike the legislation at issue in Lynch and Perry, FIRREA's change in the regulatory treatment of supervisory goodwill did not repudiate a debt of the United States. No authority of which I am aware suggests that a comprehensive piece of national legislation such as FIRREA is not a "public and general" sovereign act of government.

The majority, like the Court of Federal Claims, states that only certain sections of FIRREA are relevant to the issue at hand. Of course, defining the relevant governmental action narrowly focuses on the impact that FIRREA had on the particular parties before us. [*72] However, it also mischaracterizes the true nature of the governmental action. Congress did not act only against certain thrifts or contracts; it acted to deal with the entire thrift system in order to save it. Doing so required dealing with the problem of underfunded thrifts to which the treatment of goodwill was integrally related.

Furthermore, I cannot see how Congress was acting in its contractual capacity, rather than in its role as sovereign, when it enacted FIRREA. The government was not buying goods or services when it acted. The legislation was intended to eliminate, nationally, practices that Congress thought were inconsistent with sound banking practice or that otherwise threatened the government's ability to insure the depositors of the thrifts. FIRREA, in fact, reshaped the entire thrift industry on a national level. Thus, one can hardly characterize Congress's act of passing FIRREA as "contractual" rather than sovereign. Moreover, the enactment of FIRREA was public and general; it was broadly directed to the good of the general public, to the country's financial system, rather than to a specific contract that it disapproved.

That some members of Congress argued that [*73] enactment of certain provisions of FIRREA would break promises made to the thrifts does not mean that Congress's passage of FIRREA was not a sovereign act; it only states the problem and indicates the understandable distress felt by those members. Nor do such statements overcome the government's sovereign right to enact comprehensive national legislation for the common good without liability for breach of particularly affected contracts. Thus, while the thrifts certainly were victimized when they made commitments in reliance on accounting treatment agreed to by the regulatory agencies, I am unable to conclude that the government was powerless to enact appropriate legislation in order to restructure the U.S. thrift industry.

We are going to seek cert
~~D~~ Not made
Feldman/Bender
Knew we were going to lose - from argument
(20 mos)

Assumed we would be
No off'l piece
But unanimity.

File - by ca Dec
resp - 30 days (quickly - want it now)
by Jan - mt make conf in Jan
Probably granted

Prob Then April
possible short briefing schedule
possible - if gr. late January
Feb - not This term.
?? Should get it decided - help to know

Prob. This term.

80 cases pending - almost all in fed. claims.

In othe circs, we won.
P. sued seeking injunctions.
Circuits - we won
4c - closest to This one - also sought restitution (not just injunction)

That's closest case in terms of K.
~~Charter~~ - 4C - also K relief
6 + 11 - injunction cases
~~Transohio~~ - best reasoned - Alb's
Shouldn't make a diff whether K case
or injunction K?
= Direct conflict w/ Charter / same w/ Transohio

~~Hear Ct.~~
Financial
costs?
~~Chance of success?~~

loss in 10c - only $6 m.
9th circ - waiting for Fed Cir
$24 m

Could have damages trials in this case
Rulings in other cases.
Mandate issues in abt 2 mos.
Ask them to stay mandate - hold up dams trial.
Assume - stays mandate - won't do dam trial
sit on 80 others

Chances in SCt
Letter - optimistic
Paul Bender/Feldman - less 80

K rt - very unusual
basically ks to commit hand
amt of $ involved
give mid-level off'ls abil to bind Cong.

Change 1st ¶. - if same result in other
other ~~cours~~
(almost all in Fed Cir

Almost imposs to figure out the $ amt

as to many of these
// We have strong arg - these suits going down anyway -
dams are 0

80 - in dams trials, many would end up 0

Claims - about 20 billion.
Not realistic.

If lost in SCt
try a few, see how we do.

10TH STORY of Level 1 printed in FULL format.

The Washington Post

August 31, 1995, Thursday, Final Edition

SECTION: A SECTION; Pg. A01

LENGTH: 954 words

HEADLINE: Thrift Cleanup Costs May Soar; Court Rules Congress Wrongly Changed Rules

BYLINE: Jerry Knight, Washington Post Staff Writer

BODY:

A federal appeals court yesterday handed taxpayers a belated bill for the savings and loan debacle that could add $ 10 billion to $ 20 billion to the price of the $ 120 billion thrift cleanup.

The court ruled that Congress went too far in 1989 when it changed the accounting rules for S&Ls -- causing many of them to go from apparently healthy to terminally ill overnight.

The government now has to pay damages to three savings and loans that were affected by Congress's decision and that filed the lawsuit, the U.S. Court of Appeals for the Federal Circuit ruled. The District-based court has not yet awarded damages. The three are seeking more than $ 1.5 billion in damages.

Eighty-eight similar cases are pending in federal courts that could multiply the potential cost many times over, said a spokesman for the Office of Thrift Supervision, the federal regulatory agency.

Because so much money is at stake, the Justice Department plans to ask the Supreme Court to overturn the 9 to 2 decision by the appeals court, government attorneys said.

Any damages won by the thrifts would have to be paid directly by the Treasury Department from a special fund that picks up the cost of all lawsuits against the government, said a spokesman for the Federal Deposit Insurance Corp. (FDIC).

Yesterday's decision was a rebuke to Congress for its handling of the S&L crisis as well as a major defeat for government lawyers who have been fighting lawsuits over Congress's change in S&L accounting rules ever since the law was passed.

"The court said Congress has the right to legislate, but they don't have the right to abrogate what has been agreed to. . . . " said Washington attorney Joe L. Hollingsworth of Spriggs & Hollingsworth, the firm representing one of three S&Ls in the case.

"The government really struck out on this one," said Alexandria banking consultant Bert Ely. "The government has been appealing all along and losing at every level."

In the early 1980s, hundreds of S&Ls were getting in financial trouble because of rising interest rates, and the Federal Savings and Loan Insurance Corp. did not have enough money to pay off depositors of thrifts that failed.

To avoid paying for the problem, S&L regulators -- with the approval of Congress -- came up with a plan for healthy thrifts to take over failing ones. Ordinarily, the government would put up cash to pay the buyers for the losses of the failed thrifts, but since there was no cash, regulators agreed to a plan that would disguise the losses.

The old losses were carried on the books as "goodwill," which made the S&Ls look healthy. Though goodwill is a standard accounting practice, it was criticized as an "accounting gimmick" after Congress figured out that goodwill covered up billions of dollars of problems.

In the 1989 S&L cleanup bill, Congress set up the Resolution Trust Corp., which spent $ 120 billion rescuing depositors in failed thrifts.

The law also imposed many new restrictions on the industry designed to prevent future S&L excesses.

The law required thrifts to change their accounting to reflect their true financial health. Many of those showed massive losses as the result of the accounting change, and subsequently went out of business. Owners of others were forced to pour in more money to keep them afloat.

Dozens of institutions affected by the law went to court, arguing that Congress had given them a contract that let them use the accounting method, and could not later change the rules.

Yesterday, the appeals court agreed. "There is nothing extraordinary about the contracts in these cases save for their subject matter and the potential liability to the government," said the decision by Chief Judge Glenn L. Archer Jr.

Justice Department lawyers argued that the government had a sovereign right to change laws.

But Charles Cooper of Shaw, Pittman, Potts & Trowbridge, which represented two thrifts in the case, said, "The circuit court is simply rejecting this notion. The federal government can not simply renege on its solemn contractual obligation."

Eighty-eight other thrifts are now in line to join the case, Cooper said. It is too late for perhaps hundreds of others that never joined a suit -- many of which failed years ago -- because the six-year statute of limitations on suits challenging the 1989 law expired Aug. 10.

Cooper estimated the potential cost to the government at $ 2.5 billion to $ 7.5 billion in damages from the pending cases, but congressional banking experts have been warned that depending on how the court decides to calculate damages, the price tag could easily reach $ 20 billion.

The Justice Deparment and regulatory agencies did not comment on the appeals court decision.

Federal Deposit Insurance Corp. Chairman Ricki Helfer warned Congress earlier this year that the government was facing huge damages in the case. Some lawmakers have suggested that Congress pass legislation to settle the case before damages are assessed and avoid adding to the bill.

The biggest plaintiff in the case, Glendale Federal Bank of California, by itself is seeking $ 1.5 billion. Much smaller amounts are at stake with the other two thrifts in the case, Winstar Corp. of Minnesota and Statesman Holding Corp. of Iowa. Statesman invested more than $ 30 million in four failing S&Ls, only to be shut down by the government after Congress changed the accounting rules, Cooper said.

If the Supreme Court rejects the appeal, the case will return to the U.S. Court of Claims. "Then the issue will be only what is the amount of damages owed," said Hollingsworth. "We had a contract. It was breached and we are owed money. The only question is how much."

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