KIRKLAND & ELLIS LLP

MEMORANDUM

June 2, 2004

Validity of Proposed Section 1710.30

This memorandum addresses the validity of 12 C.F.R. § 1710.30, a proposed amendment to the corporate governance regulations promulgated by the Office of Federal Housing Enterprise Oversight ("OFHEO"). The proposed amendment provides as follows:

> In connection with standards of Federal or state law (including the Revised Model Corporation Act) or NYSE rules that are made applicable to an Enterprise by §§ 1710.10, 1710.11, 1710.12, 1710.17, and 1710.19 of this part, the Director, in his or her sole discretion, may modify such standards upon written notice to the Enterprise.

We believe that this proposed amendment is unlawful on both substantive and procedural grounds.

1. Substantive Grounds

Under the Administrative Procedure Act ("APA"), administrative agencies must act "'in accordance with law,' 5 U.S.C. § 706(2)(A)—which means, of course, *any* law, and not merely those laws that the agency itself is charged with administering." *FCC v. NextWave Personal Communications, Inc.*, 537 U.S. 293, 300 (2003) (emphasis in original). While agencies may enact their own regulations, to the extent authorized by their organic statutes and otherwise in accordance with law, they have no power to "modify" the laws otherwise enacted by Congress or state legislatures. In other words, if the agency wants to impose a new obligation on Fannie Mae, it must do so pursuant to its *own* regulatory authority (to the extent permissible), and not by "modifying" the obligations otherwise imposed by federal or state law, which the agency has no power to do. The fact that the agency has chosen to incorporate such federal and/or state laws into its own regulations is immaterial: the agency can always seek to modify its own regulations, but cannot modify those otherwise applicable laws. Indeed, the agency's suggestion that it has the power to "modify" substantive provisions of federal and state law applicable to Fannie Mae violates not only the APA, but basic principles of separation-of-powers and federalism.

2. Procedural Grounds

With respect to procedure, the proposed amendment is invalid because (even assuming that OFHEO had the power to "modify" the substantive standards of federal or state law), the agency could not exercise such power merely "upon written notice" to Fannie Mae. Rather, because any such "modification" is clearly substantive (as opposed to interpretative) in nature, it would have to be promulgated pursuant to notice-and-comment rulemaking under the APA. *See* 5 U.S.C. § 553(5); *see also National Family Planning & Reprod. Health Ass'n, Inc. v. Sullivan*, 979 F.2d 227, 234-35, 241-42 (D.C. Cir. 1992). That requirement applies not only to the promulgation of regulations in the first instance, but also to repeals, amendments, and modifications of such regulations. *See, e.g., Alaska Professional Hunters Ass'n v. FAA*, 177 F.3d

1030, 1033-34 (D.C. Cir. 1999); *Paralyzed Veterans of Am. v. D.C. Arena*, 117 F.3d 579, 586 (D.C. Cir. 1997). Thus, a modification of the substantive standards governing Fannie Mae under OFHEO's corporate governance regulations would require notice-and-comment rulemaking. The requirements for notice-and-comment rulemaking under the APA are very specific, and mere "written notice" to the regulated entity will not suffice. *National Family Planning,* 979 F.2d at 235.

Christopher Landau