

QUESTION PRESENTED

Whether the federal government can deliberately repudiate, without liability, specifically negotiated, unambiguous, and express contractual commitments for which it has received valuable consideration simply by changing the law.

PARTIES BELOW

The parties to the proceeding in the court whose judgment is under review were Winstar Corporation, United Federal Savings Bank, Statesman Savings Holding Corp., The Statesman Group, Inc., and American Life and Casualty Insurance Company.

Respondents have already provided the Court, in their brief in opposition to the government's petition for writ of certiorari, with the information required under Rule 29.6 of the Rules of this Court.

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**BRIEF FOR RESPONDENTS
WINSTAR CORPORATION AND
THE STATESMAN GROUP, INC., ET AL.**

This case is actually three separate cases, consolidated by the Court of Federal Claims for purposes of an interlocutory appeal of the court's order granting plaintiffs' (respondents here) motions for partial summary judgment as to liability on their claims of breach of contract. Pet. App. 150a-152a. This brief is filed on behalf of the respondents in two of the consolidated cases - Winstar Corporation ("Winstar") and The Statesman Group, Inc., and its affiliated entities (collectively "Statesman"). Respondent in the third consolidated case, Glendale Federal Bank, FSB, is represented by separate counsel and is filing its own brief.

STATEMENT

In upholding the trial court's finding of contract liability against the government, a nine-judge majority of the *en banc* Federal Circuit concluded that "[t]here is nothing extraordinary about the contracts in these cases save for their subject matter and the potential liability to the government." Pet. App. 45a. Applying straightforward and venerable principles of contract law, the Federal Circuit concluded, as had the trial court, that in acquiring insolvent savings and loan institutions ("thrifts"), respondents had "negotiated contracts with the bank regulatory agencies that allowed 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." Pet. App. 30a. Winstar and Statesman fulfilled their obligations under their contracts with the government, but the government did not. Because the thrift regulators, acting pursuant to regulations implementing the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 ("FIRREA"), Pub. L. No. 101-73, 103 Stat. 183 (codified in relevant part at 12 U.S.C. § 1464), repudiated their agreements and largely eliminated the bargained-for supervisory goodwill and capital credits from the thrifts' regulatory capital, "Winstar and Statesman were immediately

thrown into noncompliance with the new regulatory capital requirements and were seized by federal regulators within approximately six months." *Id.* The government's repudiation of its agreements with respondents was nothing more, nor less, than an old-fashioned breach of contract, and the only thing remarkable about this case are the arguments advanced by the government to avoid its liability for the damages it has caused to respondents.

Throughout its opening brief, the government casts respondents Winstar and Statesman, and the transactions giving rise to their claims, in a false light. Noting that during the thrift crisis of the 1980s many troubled thrifts sought "to grow rapidly" as "the easiest way to regain profitability," Pet. Br. 2, quoting H.R. Rep. No. 54, 101st Cong., 1st Sess., pt. 1, at 298-99 (1989) ("House Report"), the government portrays respondents Winstar and Statesman as "thrifts [that] engaged in . . . acquisitions of, failing thrifts" and that sought "[i]n connection with their transactions," the Federal Home Loan Bank Board's ("Bank Board") "formal approval" and "valuable government cash and non-cash financial assistance." Pet. Br. 14. The government also attempts to portray the thrift regulators - the Federal Savings and Loan Insurance Corporation ("FSLIC") and the Bank Board - as financially disinterested in the acquisitions, passively providing the necessary "regulatory approval of the Bank Board for the acquisition," Pet. Br. 6, and "permit[ting respondents] to use 'goodwill' to satisfy federal regulatory capital requirements" until FIRREA finally curtailed such "shadowy" accounting "gimmicks." Pet. Br. 4-5.

One would scarcely conclude from a reading of the government's brief that the thrift regulators' commercial interests as the *insurer* of the deposits of the acquired thrifts were vitally at stake in these transactions; that the regulators aggressively urged Winstar and Statesman - neither of which were previously involved in the savings and loan industry - to acquire the insolvent thrifts; that the key inducement, the essential *quid pro quo*, for Statesman's and Winstar's acquisitions was the regulators' express contractual promise to accord regulatory capital treatment to supervisory goodwill

(and Statesman's capital credit) for the specified periods; that the government's use of regulatory capital "forbearances" such as supervisory goodwill to facilitate acquisitions of failed thrifts was designed to (and did) save the *regulators*, not the acquirers, huge sums of money; that the regulators aggressively promoted the use of supervisory goodwill and capital credits because they lacked the cash that would otherwise have been necessary either to liquidate or to facilitate acquisitions of failed thrifts; and that the regulators' transactions with Winstar and Statesman saved the government tens of millions of dollars. The government's account of the transactions giving rise to this case is misleading, and a somewhat extended counter-statement of the case is required to correct it.

1. The causes and extent of the financial crisis in the thrift industry in the 1980s are amply described by the court of appeals in both the panel majority opinion (Pet. App. 57a-61a) and the *en banc* majority opinion (Pet. App. 4a-7a). It suffices here to say that by 1984, when Winstar acquired an insolvent thrift from the FSLIC, hundreds of savings and loan institutions had failed and the FSLIC was *in extremis*. Historically, the FSLIC and the Bank Board had "resolved" failed thrifts either by liquidation or by offering enough cash or other tangible financial assistance to induce a healthy institution or investor to acquire the failed thrift. The cost to the FSLIC insurance fund of facilitating the acquisition of a failed thrift usually ran about 70 percent of the cost of liquidating the thrift,¹ Because of the unprecedented number of thrift failures in the early 1980s, "the FSLIC faced deposit insurance liabilities that threatened to exhaust its insurance fund," Pet. App. 5a, and it was forced to offer favorable regulatory capital forbearances instead of cash and other tangible financial assistance to induce healthy institutions and

¹ Housing and Urban Recovery Act of 1982: Hearings Before the Subcommittee on Housing and Community Development of the House Committee on Banking, Finance and Urban Affairs, 97th Cong., 2d Sess. 1490, 1501 (Mar. 24, 1982) (statement of Richard T. Pratt, Chairman, Bank Board) ("Pratt testimony").

private investors to acquire insolvent thrifts.² The primary regulatory capital forbearance offered by the regulators was "supervisory goodwill," which was created under the "purchase method" of accounting for a thrift acquisition, and was measured as the amount by which the cost of the acquired thrift (which included any liabilities assumed by the acquirer) exceeded the fair market value of the acquired assets. As the court of appeals explained:

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 forty 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.*

Pet. App. 6a (emphasis added). The FSLIC and the Bank Board also permitted some acquirers to count all or a portion of the cash contributed by the FSLIC to the deal as a direct and commonly *permanent* credit to the acquired thrift's regulatory capital. This regulatory forbearance was called, not surprisingly, a "capital credit."

The FSLIC and the Bank Board thus used supervisory goodwill and capital credits, as Bank Board Chairman Pratt

² The Bank Board developed an entire menu of cash substitutes used to induce acquisitions of insolvent thrifts. The substitutes were even standardized to expedite the processing of these transactions, and to diminish staff time in negotiating these deals. The Bank Board issued a memorandum, denominated SP-37(a), to its Principal Supervisory Agents, providing a standard list of non-cash accounting forbearances. J.A. 180-207. Memorandum SP-37(a) made clear that "[t]he basic purpose in granting forbearances is to give realistic incentives to potential acquirers of problem institutions." J.A. 182. The suggested forbearances included separate language effectuating the use of supervisory goodwill and regulatory capital credits. *See* J.A. 194, 195.

testified in 1982, "as a means of conserving FSLIC's insurance fund." Pratt testimony at 1502.³ And it worked. By offering regulatory capital forbearances, FSLIC and the Bank Board "stimulated many acquisitions that would otherwise not have taken place" absent much greater cash contributions by FSLIC. Pet. App. 7a. As a result, the average cost to FSLIC of facilitating the acquisition of an insolvent thrift was reduced to less than 20 percent of the estimated liquidation cost. Pratt testimony at 1501.

Congress was fully informed of the Bank Board's use of supervisory goodwill and capital credits in lieu of cash to facilitate acquisitions of insolvent thrifts. Indeed, the Bank Board's "consistent policy of forbearance toward capital deficient thrifts" and its "development and use of regulatory accounting principles.., that served to artificially inflate the value of thrift capital," were undertaken "with Congressional consent." S. Rep. No. 19, 101st Cong., 1st Sess. 9 (1989).

2. a. After "year-long negotiations between Statesman and FHLBB and FSLIC," Pet. App. 109a, Statesman acquired four deeply insolvent thrifts in March 1988. In 1987 FSLIC had solicited 96 financial institutions and 41 private investors to bid on the four thrifts, but Statesman was the only party to submit a proposal. C.A. App. 69 (under seal).⁴ Thus, had a deal with Statesman not been consummated, the government's only alternative would have been liquidation.

Statesman agreed to invest \$21 million in the merged institutions, and the government agreed to make a \$60 million capital infusion. Even after these capital infusions had been made, however, the merged institution acquired by Statesman

³ In congressional testimony in 1990, former Chairman Pratt recalled that supervisory goodwill had been "an indispensable tool" in the Bank Board's efforts to consolidate "weaker institutions into stronger hands.., while at the same time husbanding the financial resources which were then available to it." Pet. App. 7a, quoting Savings and Loan Policies in the Late 1970s and 1980s: Healings Before The House Comm. on Banking, Finance, and Urban Affairs, 101st Cong., 2d Sess. 176, 227 (1990).

⁴ "C.A. App." refers to the appendix filed jointly by the parties in the Court of Appeals.

was still insolvent, with a *negative* tangible net worth of almost \$9 million. In other words, Statesman invested \$21 million in a thrift that not only failed to satisfy, on a tangible capital basis, the government's minimum regulatory capital standards, but was deeply insolvent and thus subject to seizure by the thrift regulators on the very day that they delivered it to its new owners. Pet. App. 64a.

Statesman agreed to this seemingly foolish acquisition because it bargained for and received from the government express contractual promises (1) that the supervisory goodwill created by the transaction - a figure ultimately calculated to be \$25.8 million - could be reported by the thrift as regulatory capital and amortized over a period of 25 years, and (2) that \$26 million of FSLIC's cash contribution could be recorded as a direct and permanent capital credit to the thrift's regulatory capital. Pet. App. 10a. In return for these regulatory capital forbearances, the FSLIC and the Bank Board received what they believed to be a "permanent" disposition of four of their serious problem thrifts at a cost to the insurance fund far lower than the cost of liquidation.

The value to the government of these regulatory capital forbearances was enormous and readily quantifiable. Indeed, shortly after the Statesman deal was closed, Bank Board Chairman Wall touted it to Congress as costing the government "\$50 million less than the cost to the FSLIC of liquidating the four institutions." Oversight on the Condition of the Financial Services Industry: Hearings Before The Senate Comm. on Banking, Housing, and Urban Affairs, 100th Cong., 2d Sess. 356 (1988). J.A. 487. In other words, Statesman agreed to shoulder \$50 million of the government's cost of resolving four of its failed thrifts. The value of the supervisory goodwill and capital credit to Statesman, on the other hand, derived not from any inherent worth, but solely from the government's promise to count them as regulatory capital, a promise that only the government could make.

Statesman took the government at its word, and fully performed its end of the bargain. Indeed, Statesman's new thrift far exceeded the thrift regulators' most optimistic projections. Under Statesman's management the thrift's tangible

net worth increased more than \$6 million - from negative \$9 million to just under negative \$3 million. Yet, on July 5, 1990, the thrift regulators declared Statesman's thrift to be "in an unsafe and unsound condition to transact business," C.A. Supp. App. 1071, despite the plain fact that the thrift was by then far safer and sounder than it was a scant 20 months earlier, when the government turned it over to Statesman. The government seized the much-improved thrift, along with Statesman's \$21 million.

The government changed its mind about the soundness of the thrift's financial condition because it changed its mind about allowing the thrift to report its bargained-for supervisory goodwill and capital credit as regulatory capital. Pursuant to FIRREA, the Bank Board's successor agency, the Office of Thrift Supervision ("OTS"), promulgated new minimum capital standards that largely eliminated the thrift's ability to report its goodwill and capital credit as regulatory capital - the central *quid pro quo* for Statesman's agreement to acquire the insolvent thrifts on the financial terms negotiated by the parties. If the government had honored its contractual obligations to Statesman, the thrift would have satisfied - with millions to spare - all three of the new minimum regulatory capital standards established by FIRREA. Pet. App. 113a-114a. Thus, as the Court of Federal Claims concluded, "but for the enactment of FIRREA, Statesman would be operating today." Pet. App. 114a.

b. In late 1983 FSLIC and the Bank Board began soliciting bids for the acquisition of Windom Federal Savings & Loan Association, an insolvent thrift institution whose failure was imminent and whose liquidation would cost FSLIC an estimated \$12 million. Pet. App. 184a. Winstar, which was organized by private investors for the sole purpose of acquiring the thrift, submitted the winning bid, which saved FSLIC more than half the estimated cost of liquidating the thrift. Pet. App. 185a. Pursuant to the parties' acquisition agreement, Winstar invested approximately \$2.8 million in the thrift, while the FSLIC contributed approximately \$5.6 million. Pet. App. 194a. Even with these capital contributions, the acquired thrifts tangible net worth was approximately *negative* \$6.7

million. Accordingly, the "linchpin of the parties' agreement," as the trial court noted, was the government's express promise that the goodwill resulting from the transaction - slightly over \$10.6 million - could be reported as regulatory capital: "[T]he promise of continued treatment of goodwill as a capital asset that could be amortized over 35 years was a negotiated and critical term of this particular transaction. It was critical because it was clear that without it no purchaser would have engaged in this transaction." Pet. App. 154a.

Winstar's thrift failed to satisfy FIRREA's new minimum capital standards. In May of 1990, OTS placed the thrift in receivership. Pet. App. 14a.

c. The record of these cases thus makes clear that using favorable regulatory capital forbearances to induce Winstar and Statesman to acquire failed thrifts was *the government's idea*. Far from the disinterested regulators portrayed in the government's brief, FSLIC's commercial and financial interests as a deposit insurer were vitally at stake in these transactions, and it needed to sell the failed thrifts to Statesman and Winstar far more than Statesman and Winstar needed to buy them. The FSLIC and the Bank Board offered supervisory goodwill and capital credits as substitutes for the cash that they did not have, and they aggressively encouraged Statesman and Winstar to accept these regulatory capital forbearances as *consideration*, the *quid pro quo* for assuming liabilities that far exceeded the assets acquired. And the Statesman and Winstar transactions saved the insurance fund, by FSLIC's own reckoning, almost \$60 million over the cost of liquidating the insolvent institutions. Pet. App. 11a-12a. In light of these facts, it is hardly surprising that Circuit Judge Newman, in dissenting from the panel majority's decision below, was moved to remark that the government's disavowal of its contractual obligations in this case "comes with poor grace, not only in view of the government's encouragement of these arrangements when they were made, but also because performance was accepted by the government for several years." Pet. App. 95a.

3. Statesman and Winstar filed suit against the United States in the Court of Federal Claims, seeking monetary relief

on contractual and constitutional theories. The trial court granted, in separate opinions, both Statesman's and Winstar's motions for summary judgment as to liability. Pet. App. 106a-152a (*Statesman*); Pet. App. 153a-182a (*Winstar*). The Court held that the government had entered into an express contract with Statesman, and an implied-in-fact contract with Winstar, regarding the regulatory capital treatment of supervisory goodwill (and in *Statesman*, the capital credit), and that the government had breached its contractual obligations. In light of its finding of liability on respondents' contract claims, the court did not reach respondents' claims under the Takings Clause and the Due Process Clause of the Fifth Amendment. The court rejected the government's arguments that the "sovereign acts" doctrine and the "unmistakability" doctrine shielded the government from monetary liability. The court consolidated the *Statesman* and *Winstar* cases with the similar *Glendale* case and certified its decisions for interlocutory appeal to the Federal Circuit.

4. A divided panel of the Federal Circuit, over Judge Newman's dissent, reversed the trial court's liability rulings in favor of Statesman and Winstar. Pet. App. 53a-88a; 89a-103a (Newman, J., dissenting). The panel decision was vacated, however, when the full court granted respondents' petitions for rehearing *en banc*. Pet. App. 105a. The *en banc* Federal Circuit affirmed the trial court's contract liability rulings by a 9 to 2 vote. Pet. App. 1a-52a. The court of appeals painstakingly reviewed *de novo* the contract documents governing the transactions and concluded, as the trial court had, that the regulatory capital treatment of supervisory goodwill (and of Statesman's capital credit) was a specifically bargained for and agreed upon term of the contracts between the parties.

With respect to the Statesman transaction, the court of appeals first noted that the government had conceded that the "Assistance Agreement" executed by the parties contained an express term allowing Statesman to report its \$26 million capital credit as regulatory capital. The court of appeals found the government's promise concerning supervisory goodwill specifically described in the resolution issued by the Bank

Board in connection with the transaction. The Bank Board's resolution, which also reiterated the government's promise concerning Statesman's \$26 million capital credit, expressly provided that in "report[ing] to the Bank Board and the FSLIC [t]he value of any unidentifiable intangible assets [*i.e.*, goodwill] resulting from accounting for the Acquisition . . . in accordance with the purchase method of accounting may be amortized by [Statesman] over a period not in excess of twenty-five (25) years by the straight line method." Pet. App. 25a-26a. The Federal Circuit rejected the government's argument that the Bank Board's resolution did not constitute a contract document, noting that the Assistance Agreement contained an integration clause that expressly incorporated contemporaneous resolutions of the Bank Board. Pet. App. 25a. Accordingly, the Federal Circuit concluded that the government was contractually bound to permit Statesman to report its supervisory goodwill and capital credit as regulatory capital on the specified terms.

With respect to the Winstar transaction, the court of appeals found that the government had expressly promised to treat Winstar's supervisory goodwill as regulatory capital, and thus it did not need to reach the question whether such a promise could be implied-in-fact. Although the Assistance Agreement did not contain a specific provision relating to supervisory goodwill, it did contain an integration clause specifically incorporating into the parties' contract any "resolutions or letters issued contemporaneously" by the Bank Board. A "forbearance" letter issued by the Bank Board in connection with the transaction specifically "confirmed the understanding" of the parties that "[f]or purposes of reporting to the Board," Winstar would be entitled to amortize its goodwill "over a period not to exceed 35 years by the straight-line method." Pet. App. 28a.

Having found express contractual commitments by the government concerning the regulatory capital treatment of respondents' supervisory goodwill and capital credit, the Federal Circuit readily and correctly concluded that the government's repudiation of those commitments constituted a breach of its contractual obligations. The court of appeals also

rejected the government's claim that its contractual commitments concerning regulatory capital were negated under the so-called "unlawful action" clause of the parties' agreement when FIRREA was enacted.

The Federal Circuit turned next to the government's sweeping claim that respondents' contracts failed to satisfy the requirements of the "unmistakability doctrine." Relying primarily on this Court's decision in *Bowen v. Public Agencies Opposed to Social Security Entrapment*, 477 U.S. 41 (1986) ("*POSSE*"), the government argued that because respondents' contracts did not contain an express provision guaranteeing that the government would continue to honor the regulatory capital forbearances notwithstanding a legislative change such as FIRREA, the contracts should not be construed as unmistakably waiving Congress' sovereign power to legislate. Quoting liberally from the trial court's analysis of the unmistakability doctrine, the Federal Circuit reasoned that the government's argument was based upon the false premise that respondents sought to bind "Congress not to change its regulations." Pet. App. 37a. Respondents, however, were not seeking to "enjoin[] the thrift regulators from applying the FIRREA requirements to the thrifts." Pet. App. 37a. Rather, they sought only monetary relief for the harm that they suffered when FIRREA's requirements *were applied* to them. Thus, the court of appeals concluded that upholding the government's contract liability to respondents would not threaten Congress' sovereign power to legislate. Pet. App. 38a.⁵

5 With respect to the distinct government promise regarding the treatment of Statesman's \$26 million capital credit, the Federal Circuit also noted that "FIRREA did not specifically cover capital credits or otherwise exclude FSLIC cash contributions from capital for purposes of determining compliance with any of the minimum capital requirements," Pet. App. 13a, but did not need to address the significance of this fact in light of its rejection *in toto* of the government's claim to immunity. The distinctive nature of the government's commitments regarding capital credits, as well as the fact that FIRREA did not abrogate those commitments, is discussed at length in the brief filed in this case by *amici* Coast Federal Bank, Union Federal Savings Bank of Indianapolis, Union Holding Company, Inc., Meadows Resources, Inc., and Republic Holding Company.

With specific reference to this Court's decision in POSSE, the Federal Circuit agreed with the trial court that "the unmistakability doctrine . . . controls how contractual rights with the government are *created, i.e.*, whether the government has agreed in unmistakable terms to be contractually bound." Pet. App. 35a-36a (emphasis in original). Because Winstar's and Statesman's contracts granted them, "in the clearest possible terms, the right to certain types of regulatory capital treatment," the requirements of the unmistakability doctrine were satisfied. Pet. App. 36a.

Finally, the Federal Circuit rejected the government's defense under the "sovereign acts doctrine," which excuses the government from contract liability when its performance is precluded by "a public and general sovereign act." Pet. App. 39a. FIRREA's provisions concerning supervisory goodwill did not qualify as "public and general" sovereign acts because they specifically targeted respondents' agreements and similar contracts. FIRREA's provisions restricting the regulatory capital treatment of supervisory goodwill, while no doubt enacted for the public good, "specifically abrogate[d] 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." Pet. App. 43a. Because the government had "plainly sought to render its own performance impossible," the sovereign acts doctrine did not insulate it from damages liability. Pet. App. 45a.

Judge Nies and Judge Lourie filed separate dissents. Judge Nies continued to adhere to the views expressed in her majority opinion for the panel. (The other member of the panel majority, Judge Rich, changed his mind on reconsideration and joined the *en banc* majority.) Judge Nies believed that the majority had erred in failing to distinguish between the "government" and Congress in concluding that the enactment of FIRREA had breached respondents' contracts. Pet. App. 47a. Judge Lourie concluded that the sovereign acts doctrine precluded respondents' recovery for breach of contract because FIRREA 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." Pet. App. 51a.

INTRODUCTION AND SUMMARY OF ARGUMENT

Respondents' claim is simple and straightforward, a point that tends to be obscured by the heft of this brief and of the briefs filed by our many *amici*. Winstar and Statesman were induced by the government's thrift regulators to acquire at great expense deeply insolvent thrifts on the basis of the government's contractual commitment to accord the acquired institutions certain specifically negotiated and clearly expressed regulatory capital forbearances. Respondents fully performed their contractual obligations, but the government did not, causing respondents substantial damage. If it is still true, as it always has been, that "in the performance of its voluntary engagements with its citizens [the government] should conform to the same standard of honorable conduct as it exacts of them," *Heil v. United States*, 273 F. Supp. 729, 731 (S.D.N.Y. 1921) (Hand, J.), then the courts below did not err in holding the government liable in damages for its breach.

The government's defense, in contrast, is sophisticated and complex, and its many facets take many pages to rebut. It boils down, however, to a claim that our law attaches *no consequence whatever* to the government's deliberate repudiation of specific contractual commitments that formed the principal *quid pro quo* for Statesman's and Winstar's costly acquisitions. Indeed, the government says that it is even entitled under the law to keep the multi-million dollar investments that it solicited from Statesman and Winstar and then seized along with the thrifts. No federal case supports the government's claim.

The government's argument opens with the contention that the specifically negotiated, unambiguous, and express contractual promises concerning respondents' regulatory capital forbearances were not sufficiently "unmistakable" to create binding obligations on the government. They were not unmistakable, the government says, because the parties' contracts did not contain language expressly "contracting away [Congress's] right to exercise future sovereign regulatory authority"; that is, the contracts did not include language "either commit[ing] Congress not to enact new legislation

requiring a different treatment of respondents' capital or grant[ing] respondents a prospective immunity from any such legislative change." Pet. Br. 19, 36.⁶ The government quickly adds, however, that even if respondents' contracts did contain express provisions satisfying the government's version of the "unmistakability doctrine," respondents still lose. Any such express contractual promise would be *ultra vires*, and thus "invalid and unenforceable," *id.* 37, because the Bank Board did not have "an express delegation of authority from Congress" to enter into "an agreement that binds future Congresses not to change regulatory schemes or that immunizes private parties from the effects of such changes." *Id.* 36. In the next breath, however, the government notes that respondents' case would not really be improved even if we could produce such an extraordinary statutory delegation of authority to the thrift regulators. Any such delegation would itself be *ultra vires*, for under the "reserved powers doctrine" the government's "sovereign regulatory authority" cannot be "'bargained away, and is inalienable even by express grant'" of the legislature itself. *Id.* 38, quoting *Atlantic Coast Line R.R. v. City of Goldsboro*, 232 U.S. 548, 558 (1914).

Thus, the government's arguments add up to this: under the unmistakability doctrine a government agency's contractual commitment concerning its regulatory authority must be expressed in unmistakable terms, although such a promise, no matter how unmistakable, will nonetheless be invalid and unenforceable under the reserved powers doctrine. Obviously, the government is confused about the legal principles governing its contractual undertakings.

The government's confusion stems from its insistence that respondents' claims for contract damages are to be

⁶ In its briefing to the Federal Circuit, the government offered even more specific insight into its version of the unmistakability doctrine, asserting that it could not be held liable to respondents in the absence of "an unambiguous contract provision stating that [the thrift agency] 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." Replacement Reply Brief of Defendant-Appellant United States at 9.

analyzed as if respondents were seeking an order invalidating FIRREA's restrictions on supervisory goodwill and enjoining the government to specifically perform its contractual obligations according to their terms. Every case cited by the government in support of its unmistakability and reserved powers contentions involved either a Contract Clause or a Due Process Clause challenge to the constitutional *validity* of a statute that impaired the government's performance of its pre-existing contractual obligations. A decision upholding the constitutional challenge in these cases would have voided the legislation impairing the government's contractual obligation, thus requiring the government to abide by its agreement according to its terms. In other words, successful assertion of a Contract Clause or Due Process Clause challenge to a law impairing a prior government contractual obligation is tantamount to an award of specific performance;⁷ the contract obligation effectively overrides subsequent contrary legislation, thus "binding [the government] to a future course of conduct" at least with respect to the contracting parties. *United States Trust Co. v. New Jersey*, 431 U.S. 1, 23 (1977).

It was in this context, as the government acknowledges (Pet. Br. 38), that the "reserved powers doctrine" was developed to ensure that "the obligation of contracts does not *prevent* the State from exercising such powers as are vested in it for the promotion of the common weal, or are necessary for the general good of the public" *Manigault v. Springs*, 199 U.S. 473, 480 (1905) (emphasis added). This Court described the reserved powers doctrine succinctly in *United States Trust*: "[T]he Contract Clause does not require a State *to adhere* to a contract that surrenders a central attribute of its sovereignty." 431 U.S. at 23 (emphasis added). In other

⁷ Michael L. Zigler, Note, *Takings Law and the Contract Clause: A Takings Law Approach to Legislative Modifications of Public Contracts*, 36 *Stan. L. Rev.* 1447, 1462 (1984) ("[T]he contract clause effectively grants public contract holders a constitutional right to specific performance [A]nalysis under the contract clause is limited to declaring the statute unconstitutional. The provision does not authorize the courts to award damages in lieu of requiring the state to adhere to the original terms of the contract.")

words, a contractual obligation does not constitutionally "prevent" a State from enacting contrary legislation under its police powers, nor does it constitutionally require a State "to adhere to" its contractual obligation in the face of such legislation. In this context, the Contract Clause leaves a contracting State in the same shoes as any other contracting party - it may elect to breach its contractual obligation and pay damages.⁸

The courts below well understood this point. As the *en banc* Federal Circuit put it: "[C]ongress 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." Pet. App. 38a.

The alleged rationale for the government's novel version of the "unmistakability doctrine" is derived directly from the reserved powers doctrine. Because government promises of specific regulatory treatment in the future may frustrate the ability of government to take contrary regulatory action deemed in the public interest, the requirement that such promises be expressed in unmistakable terms "helps to ensure that public officials who enter into contracts - and others who

⁸ "When a man makes a contract, he incurs, by force of the law, a liability to damages, unless a certain promised event comes to pass The [common] law seems to have regarded it as technically in the election of the promisor to perform or to pay damages." *Globe Refining Co. v. Landa Cotton Oil Co.*, 190 U.S. 540, 543 (1903). Restatement (Second) of Contracts ch. 16, intro, note (1981) ("The traditional goal of the law of contract remedies has not been compulsion of the promisor to perform his promise but compensation of the promisee for the loss resulting from breach In general, therefore, a party may find it advantageous to refuse to perform a contract if he will still have a net gain after he has fully compensated the injured party for the resulting loss."); E. Allan Farnsworth, *Contracts* 840 (2d ed. 1990) ("[A]long with the celebrated freedom to make contracts goes a considerable freedom to break them as well.").

review them - are fully aware of the serious step they are taking." Pet. Br. 11.

In this case, the public policy considerations underlying the reserved powers doctrine and the government's unmistakability doctrine are wholly inapplicable. Respondents are not challenging the constitutional validity of FIRREA's goodwill provisions, nor are they seeking to require the government "to adhere to [its] contract" regarding supervisory goodwill and capital credits. It is too late for that; the government has applied FIRREA's goodwill provisions to respondents' thrifts and, consequently, has regulated them out of existence. In other words, the government elected to breach, and respondents seek only to be compensated for their injury. The issue in this case, therefore, is not whether the government's regulatory capital promises were "unmistakable" enough to constitutionally immunize respondents from application of FIRREA's goodwill provisions, but rather whether the government is constitutionally immune from damages liability for its breach of express regulatory capital promises for which it sought and received valuable consideration. The government can cite no constitutional provision, and no case, supporting its claim of immunity from contract damages for its repudiation of its agreements with Statesman and Winstar.

In the pages that follow, we demonstrate that the federal thrift regulators, knowingly and with full authority, entered into contracts with Statesman and Winstar that anticipated the possibility of future regulatory changes and expressly agreed, in as unmistakable a fashion as possible, that the regulatory accounting treatment promised in these agreements would govern over any future regulatory change.

We further demonstrate that no attribute of the government as sovereign immunizes the government from liability in damages for its abrogation of its contractual obligations to Statesman and Winstar. The "sovereign acts" doctrine ensures that the federal government, as a contracting party, is accorded the *same* treatment under the law as is accorded to private contracting parties; if a private party would have been liable under the contract, then so also is the government. Accordingly, the Federal Circuit was correct in concluding

that the doctrine "does not relieve the government from liability where it has specifically undertaken to perform the very act from which it later seeks to be excused." *Hills Materials Co. v. Rice*, 92 F.2d 514, 516 n.2 (Fed. Cir. 1992).

ARGUMENT

I. THE GOVERNMENT UNMISTAKABLY AGREED TO ACCORD REGULATORY CAPITAL TREATMENT TO RESPONDENTS' SUPERVISORY GOODWILL AND CAPITAL CREDIT FOR SPECIFIED TIME PERIODS.

1. "All contracts are to be construed to accomplish the intention of the parties." *The Binghamton Bridge*, 70 U.S. (3 Wall.) 51, 74 (1865).⁹ The intent of contracting parties is often no less obvious from the economic realities surrounding a transaction than it is from the contract documents themselves. Courts are thus naturally reluctant to interpret a contract in a manner that renders the bargain illusory or economically irrational for one of the parties.¹⁰

The contract interpretation advanced by the government in this case is no less at war with common sense than it is

⁹ See *id.* at 76 ("[T]he main canon of interpretation of a contract, is to ascertain what the parties themselves meant and understood.") *Bradley v. Washington, Alexandria, and Georgetown Steam Packet Co.*, 38 U.S. (13 Pet.) 89, 96-97 (1839) ("It is a principle recognized and acted upon by all courts of justice, as a cardinal rule in the construction of all contracts, that the intention of the parties is to be inquired into; and if not forbidden by law, is to be effectuated."). See also Restatement (Second) of Contracts § 201 cmt. c (1981) ("[T]he primary search is for a common meaning of the parties The objective of interpretation in the general law of contracts is to carry out the understanding of the parties").

¹⁰ See, e.g., *Russell v. Sebastian*, 233 U.S. 195, 208 (1914) (rejecting State's argument that plaintiff gas company had made extensive investment in plants and reservoirs "without any assurance that the laying of the distributing system could be completed, or that it could even be extended far enough to afford any chance of profit"); *Appleby v. Delaney*, 271 U.S. 403, 413 (1926) (city's contract interpretation rejected because "[i]t is not reasonable to suppose that the [plaintiffs] would pay \$12,000... and leave to the city authorities the absolute right completely to nullify the chief consideration").

with the written agreements executed by the parties. According to the government, the parties' written agreements in this case "contain no undertaking by FSLIC that its parent body - the Bank Board - or Congress would not change [thrift capital] requirements or the treatment of goodwill under them," and that the courts below therefore simply "hypothesiz[ed] an intent by the thrift regulators' to agree "that goodwill would continue to be treated as capital in the future." Pet. Br. 15. The government thus represents to this Court that when it shook hands with Statesman and Winstar on these transactions in 1988 and 1984, all parties fully understood and intended that the Bank Board was entitled under their contracts to exclude supervisory goodwill from regulatory capital *at that very moment*. The parties intended, in other words, that the government was "agreeing to abide by its promises only so long as it unilaterally decided to keep those promises." Pet. App. 128a. Given that supervisory goodwill was the only thing standing between respondents' thrifts and "immediate liquidation," Pet. App. 64a, the common sense of the matter, as the trial court below put it, is that "no purchaser would have engaged in [these] transaction[s]" without "the promise of continued treatment of goodwill as a capital asset that could be amortized over [the specified number of] years." Pet. App. 190a.

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11 The government resists this conclusion on two grounds. First, the government notes that Statesman and Winstar "obtained the benefits of the Bank Board policy permitting them to count goodwill as capital" for 20 months and five years, respectively. Pet. Br. 42-43. But the fact that the government honored its contractual commitments for a brief period of time does not ameliorate, let alone eliminate, the harm that its repudiation caused to respondents. More fundamentally, the government's brief periods of performance under its contracts does not alter the fact that its alleged contract obligation - to perform at its "unrestricted pleasure" -was simply no obligation at all. Pet. App. 128a.

The government also points out that Statesman and Winstar "received substantial infusions of federal cash" as consideration in the transactions. Pet. Br. 43. The government forgets that it, not Statesman and Winstar, was the insurer of the deposits of the insolvent thrifts. The government's cash contributions were necessary to cover, though only partially, the losses already suffered by the federally insured insolvent thrifts. Statesman's and Winstar's combined capital

The truth is that precisely because of the historically volatile nature of the government's regulation of thrift capital standards (they "changed three times in 1982 alone," Pet. App. 57a), Statesman and Winstar painstakingly negotiated over many months regulatory capital forbearances that would make their acquisitions viable. And they insisted that the parties' regulatory capital agreements be incorporated, repeatedly, in the contract documents governing the transactions - a process that would have been meaningless if, as the government now absurdly contends, these provisions were merely superfluous acknowledgments of the government's regulatory policy at the time.

The government's assertion that it made no promises and assumed no risks in connection with its transactions is expressly belied by the "Assistance Agreement" that it executed. This document provides: "It is the purpose of this Agreement to provide a means by which . . . the [FSLIC] may receive the benefits and *assume the risks contracted for*, and expense to the [FSLIC] may be reduced." J.A. 409 (*Statesman*) (emphasis added). As we demonstrate below, the government clearly and expressly assumed in these transactions the risk that future regulatory changes would prevent fulfillment of its regulatory capital promises.¹²

investment of almost \$24 million was a direct contribution to the *government* losses as deposit insurer. And if these transactions had not been consummated, the government estimates that its losses on the insolvent thrifts would have run another \$60 million. Thus, the reality of these transactions is that Winstar and Statesman contributed almost \$24 million to the government for the privilege of assuming almost \$60 million of additional government liabilities.

12 The government, citing three decisions, argues that courts have held that documents similar to those at issue here were not sufficient to establish the existence of enforceable contracts regarding the regulatory accounting treatment of supervisory goodwill and regulatory capital credits. Pet. Br. 22 n.12. Leaving aside the fact (as explained *infra* n.21) that the decisions cited by the government are readily distinguishable, the government ignores numerous other cases in which courts, examining documents either very similar to, or even less explicit than, the documents evidencing the transactions at issue here, have concluded that the government did enter into such contracts for particular accounting treatment. *See, e.g., RTC v. FSLIC*, 25 F.3d 1493 (10th Cir. 1994); *Far West Fed. Bank v. Director*,

2. a. *Statesman*.

In 1988 Statesman and the government executed a lengthy "Assistance Agreement," as well as a separate "Regulatory Capital Maintenance Agreement." The Assistance Agreement contains an integration clause providing that "[t]his Agreement, together with any resolutions adopted by the Bank Board and documents delivered at closing which contain written interpretations or understandings of the parties, constitutes the entire agreement between the parties . . . , excepting only . . . any resolutions or letters . . . issued by the Bank Board . . . in connection with the approval of the Acquisition" J.A. 407-08. In light of this language, the courts below uniformly found (Pet. App. 25a, 62a, 121a), that two other documents - a "Resolution" and a "Forbearance Letter" executed by the Bank Board in connection with the approval of the acquisition - set out contract terms governing the transaction equal in legal force to those in the Assistance Agreement. 13

The government concedes that the Assistance Agreement expressly committed the government to count \$26 million of FSLIC's cash contribution as regulatory capital. Pet. Br. 34. Specifically, the Assistance Agreement provides:

For the purposes of reports to the Bank Board \$26 million of the contribution [made by FSLIC] shall be credited to [Statesman's] regulatory capital account and shall constitute regulatory capital (as defined in § 561.13 of the Insurance Regulations).

OTS, 787 F. Supp. 952 (D.Or. 1992); *Carteret Sav. Bank v. OTS*, 762 F. Supp. 1159 (D.N.J. 1991), *vacated on other grounds*, 963 F.2d 567 (3d Cir. 1992); *Hansen Sav. Bank v. OTS*, 758 F. Supp. 240 (D.N.J. 1991); *Security Fed. Sav. Bank v. Director, OTS*, 747 F. Supp. 656 (N.D. Fla. 1990); *Security Sav. & Loan Ass'n v. Director, OTS*, 761 F. Supp. 1277 (S.D. Miss. 1991), *aff'd in part, rev'd in part on other grounds*, 960 F.2d 1318 (5th Cir. 1992); *Sterling Sav. Ass'n v. Ryan*, 751 F. Supp. 871 (E.D. Wash. 1990), *rev'd on other grounds*, 959 F.2d 241 (9th Cir. 1992).

13 The Assistance Agreement also contained an "Accounting Principles" section, which expressly provided that the accounting treatment of the transaction would be governed by the "resolution or action in the Bank Board approving or relating to the Acquisition" J.A. 402.

J.A. 362a. The government argues, however, that this provision obligated it to accord regulatory capital treatment to Statesman's \$26 million capital credit only until it decided not to. Seizing upon the parenthetical statement providing that the capital credit shall constitute regulatory capital "(as defined in § 561.13 of the Insurance Regulations)," the government argues that its regulatory capital promise "depended entirely upon existing regulations and that the same treatment would not necessarily be accorded if changes were made in -- the governing regulations or statute." Pet. Br. 34, 35.

The government's interpretation of this provision, which renders Statesman's bargain entirely illusory, does not represent the intentions of the contracting parties. First, by incorporating by reference the definition of regulatory capital contained in the FSLIC's regulation, the parties' agreement incorporated the content of the regulation as it existed at the time of the contract. *See Craft Machine Works, Inc. v. United States*, 926 F.2d 1110, 1115 (Fed. Cir. 1991); *Hughes Communications Galaxy, Inc. v. United States*, 998 F.2d 953, 957-58 (Fed. Cir. 1993); *Hills Material Co. v. Rice*, 982 F.2d 514 (Fed. Cir. 1992). *See also Wood v. Lovett*, 313 U.S. 362, 369-70 (1941); *Van Hoffman v. Quincy*, 71 U.S. (4 Wall.) 535, 550 (1867). Moreover, the government's suggested interpretation is directly contradicted by other express provisions in the contract.

As previously noted, Statesman fully understood that regulatory capital standards could be changed by the government. Accordingly, it insisted that the "Accounting Principles" provision of the Assistance Agreement specifically provide that the government's contractual commitment concerning the regulatory accounting treatment of the transaction would govern over any conflicting present *or future* "regulations of the [FHLBB] or [FSLIC]." Because the Accounting Principles clause directly refutes the government's construction of the parties' agreement, and because the government's discussion of this key provision omits a critical sentence, we set the clause out at length, emphasizing the two key sentences:

Section 17. *Accounting Principles*. Except as otherwise provided, any computations made for purposes of this Agreement shall be governed by GAAP, except that where such principles conflict with the terms of the Agreement, applicable regulations of the Bank Board or the CORPORATION, or any resolution or action of the Bank Board approving or relating to the Acquisition, the Mergers or to this Agreement, then this Agreement, such regulations, or such resolution or action shall govern. In the case of any ambiguity in the interpretation or construction of any provision of this Agreement, such ambiguity shall be resolved in a manner consistent with such regulations and the Bank Board's resolution or action relating to the Acquisition, the Mergers or of this Agreement. *If there is a conflict between such regulations and the Bank Board's resolution or action relating to the Acquisition, the Mergers or to this Agreement, the Bank Board's resolution or action shall govern. For purposes of this section, the accounting principles and governing regulations shall be those in effect on the Effective Date, as subsequently changed, amended, clarified or interpreted by the Bank Board*

J.A. 402-03. (emphasis added). Thus, the emphasized sentences of the Accounting Principles clause clearly provide that the Bank Board's Resolution and Forbearance Letter govern over any conflicting capital regulations, including "subsequently changed" or "amended" regulations.

The government's answer to the obvious import of the two emphasized sentences of the Accounting Principles clause is to hide the first one from this Court. The government's discussion of this clause (in connection with Winstar's virtually identical Accounting Principles clause), omits any reference to the first emphasized sentence, and quotes the second emphasized sentence standing alone. *See* Pet. Br. 31.

The government then invites this Court to interpret the second emphasized sentence as though the sentence preceding it did not exist, arguing that it shows "that the parties recognized that Bank Board policies could change, and that whatever new policies were adopted would, from then on, govern future accounting by" Statesman. *Id.* When the two sentences, however, are read together, as intended by the parties, it is clear that the clause means precisely the opposite of the government's suggested interpretation. Indeed, a candid reading of the Accounting Principles clause can yield no conclusion other than that reached by Circuit Judge Newman in dissenting from the panel majority's opinion below: "[T]he 'Accounting Principles' clauses in the Winstar and the Statesman agreements reflect the parties' recognition that the accounting principles might in the future be 'subject to clarification, interpretation or amendment', and provide that '[i]f there is a conflict between such regulations and the Bank Board's resolution or action . . . , the resolution or action shall govern.'" Pet. App. 101a.

The Bank Board Resolution referred to in the Accounting Principles clause set forth the parties' agreement concerning the regulatory capital treatment of both the \$26 million capital credit and supervisory goodwill. The key provision of the Resolution warrants quotation in full:

[T]he 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 excepted, 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 [*i.e.*, goodwill] resulting from accounting for the Acquisition and the Mergers in accordance with the purchase method of accounting may be amortized by [Statesman] over a period not in excess of twenty-five (25) years by the straight line method.

J.A. 458-59 (emphasis added).

Similarly, the Forbearance Letter issued by the Bank Board in connection with the transaction reiterated the government's agreement to allow Statesman to count \$26 million of FSLIC's cash contribution as "a credit to [Statesman's] regulatory capital." The letter specified that "for regulatory accounting purposes, [Statesman] may book such contribution as a direct addition to its regulatory capital." J.A. 476.

The government dismisses the Bank Board's Resolution and Forbearance Letter as obligating only Statesman; they contain "no promises" by the government concerning regulatory capital, but rather "merely state[s] the requirements for Statesman to capitalize goodwill under then-current regulatory capital policy." Pet. Br. 33. One need look no farther than the Forbearance Letter's name to refute the government's remarkable argument. It was the government, after all, that was *forbearing* from enforcing certain otherwise applicable requirements of its then-current regulatory capital policies in order "to give realistic incentives to potential acquire[r]s of problem institutions." J.A. 182; *see* note 2, *supra*. The letter opens with the statement that "the following forbearances are hereby *granted*," and closes with an express reservation of all of the Bank Board's statutory authority "[o]ther than actions to enforce the regulatory requirements *waived* in accordance with paragraphs 1-5" J.A. 475-80 (emphases added). Likewise, the Bank Board Resolution contains a number of

provisions expressly waiving specified regulatory requirements.¹⁴ Indeed, in the very provision of the Resolution governing the regulatory capital treatment of Statesman's capital credit and supervisory goodwill, the Bank Board expressly agrees to the specified "departures" from its otherwise applicable regulatory accounting requirements.

Finally, the parties' Regulatory Capital Maintenance Agreement ("RCMA") expressly confirms that the government's Resolution and Forbearance Letter obligated it to accord the specified regulatory accounting forbearances. Executed by Statesman and FSLIC "[i]n consideration of the mutual promises contained [t]herein," J.A. 418, the RCMA expressly required Statesman to maintain the regulatory capital of the acquired thrifts "at the level . . . required by § 563.13(b) of the Insurance Regulations . . . or any successor regulation, as now or thereafter in effect." But the RCMA also specifically provided that Statesman's "Required Regulatory Capital shall be calculated . . . [to] include . . . Regulatory Capital amounts *permitted by the FSLIC in the Assistance Agreement and in the forbearances issued in connection with the transactions . . .*" J.A. 418-19 (emphasis added).

In light of the foregoing express contractual provisions, the Federal Circuit, quoting the trial court, concluded that "the government granted [Statesman], in the clearest possible terms, the right to certain types of regulatory capital treatment." Pet. App. 36a. Indeed, far from placing itself at the regulatory mercy of the government, as the government would have it, Statesman can justly be accused of overkill in its insistence that the government's regulatory capital promises - a key term of the transaction for both sides - be expressed in

¹⁴ See J.A. 449 ("the Bank Board... hereby waives and deems inapplicable" certain regulations); *id.* 452 ("good cause exists for a waiver of the requirements of certain regulations"); *id.* ("the terms of this Resolution, and not the requirements set forth in [specified regulations] shall govern" the transaction); *id.* 455 ("the Bank Board... hereby deems inapplicable and waives" certain regulations); *id.* 473 ("the Bank Board hereby waives the laws of any state" that interfere in certain ways with the insurance activities of Statesman's affiliates).

the parties' written contracts.¹⁵ The conclusion is thus inescapable that the parties' agreement placed "the risk of a change in the governing law" (Pet. Br. 35) squarely on the government, rather than Statesman.¹⁶

15 The importance and content of the government's regulatory accounting forbearances is also reflected in the negotiating record of the transaction, as well as in the government's own internal analysis of the deal. For example, Statesman's acquisition proposal explicitly required that "[t]wenty one million dollars of the cash contribution to be made to [Statesman] pursuant to an assistance agreement to be entered into between the FSLIC and Statesman is to be a credit to [Statesman's] regulatory capital; therefore, for regulatory accounting purposes, [Statesman] will book such contribution as a direct addition to its net worth." J.A. 215-16. Similarly, the Business Plan submitted as part of Statesman's proposal expressly "assume[d] the acquisition will be accounted for using the purchase method of accounting, applied by the 'push down' method" J.A. 232. *See also* J.A. 240. Similar explicit statements regarding Statesman's intentions were made in the holding company application submitted to FSLIC. *See* J.A. 245-46. Similarly, the government's internal documents analyzing the transaction make clear that the promised regulatory accounting forbearances were critical to its consummation and success. *See, e.g.*, FHLBB Memorandum (J.A. 280) ("It is the FSLIC's intention that \$21 million of the cash contribution to be made to [Statesman] pursuant to an assistance agreement to be entered into between the FSLIC and [Statesman] is to be a credit to [Statesman's] regulatory capital; therefore, for regulatory accounting purposes, [Statesman] may book such contribution as a direct addition to its regulatory capital."); FHLBB Memorandum: Viability and Revised Bid Costing (C.A. App. 58) (under seal) ("Statesman will mark-to-market all assets and liabilities . . . under use of purchase accounting."); *id.* (C.A. App. 61) (under seal) ("\$21 million of the FSLIC cash assistance . . . is a direct contribution to net worth"); FHLBB Issues Memorandum (C.A. App. 70) (under seal) ("\$21 million of FSLIC's assistance will count towards regulatory net worth.").

16 The government claims, Pet. Br. 35, that its contractual commitments concerning regulatory capital were negated under the so-called "unlawful action" clause of the parties' agreement. The clause provides: "Nothing in this Agreement shall require any unlawful action or inaction by either of the parties hereto." Pet. App. 23a. The Federal Circuit, like the trial court (Pet. App. 125a-129a), correctly interpreted this clause as protecting against any inadvertent violation of law existing when the contract was entered, rather than supplying "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." Pet. App. 23a-24a. The same answer applies to the standard provision in the Assistance Agreement requiring Statesman to comply "with all applicable statutes, regulations, orders of and restrictions imposed by the United States or any state, municipality, or other

b. *Winstar*.

Many of Winstar's contract documents are remarkably similar to those at issue in *Statesman*, and so many of the points previously made in answer to the government's arguments with respect to *Statesman* are equally applicable here. The Winstar Assistance Agreement contains an Accounting Principles provision that is virtually identical to the corresponding provision in the *Statesman* agreement (quoted at length above). See J.A. 108-09. The Assistance Agreement also contains a similar integration clause, incorporating into the parties' agreement the Bank Board's contemporaneous Resolution and Forbearance Letter.¹⁷ J.A. 112. The Bank Board's Forbearance Letter, in turn, "confirm[ed] the understanding" of the parties that "[f]or purposes of reporting to the Board, the value of any intangible assets [*i.e.*, goodwill] 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." J.A. 123. As in *Statesman*, the Bank Board's Forbearance Letter in the Winstar transaction plainly expresses commitments on behalf of the government - to "forbear" and "waive" enforcement of otherwise applicable regulatory capital requirements. See J.A. 124. And the Accounting Principles clause in Winstar's Assistance Agreement, as in *Statesman*, makes clear that "in the event of regulatory change, the negotiated forbearances and accounting procedures would govern." Pet. App. 102a (Newman, J., dissenting).

The government seizes upon the language stating that the Accounting Principles clause applies only to "computations made for the purposes of this Agreement," arguing that because the Assistance Agreement contained no provision relating to supervisory goodwill, "no computations regarding

political subdivision," which specifically referenced such things as "equal employment opportunities" and "environmental standards." J.A. 407.

¹⁷ Every court that has considered similar integration language has confirmed that it expressly incorporates Bank Board forbearance letters and resolutions into the parties' contractual arrangement. See Pet. App. 121a-122a (listing cases). See also *RTC v. FSLIC*, 25 F.3d at 1499.

goodwill or capital requirements had to be or were 'made for the purposes of this Agreement.' " Pet. Br. 30-31. Here again, however, the government ignores the agreement's integration clause, which expressly incorporated into the Assistance Agreement the Bank Board's Forbearance Letter, which expressly permits Winstar to count its supervisory goodwill as amortizing regulatory capital for 35 years. Nor does the government explain what "computations made for the purposes of this Agreement" the clause could possibly be referring to if not regulatory capital computations.

Finally, the government notes (Pet. Br. 31-32) that the Bank Board Resolution required Winstar to file a "Net Worth Maintenance Stipulation" requiring Winstar to maintain its "net worth . . . at a level consistent with that required by . . . the Insurance Regulations, *as now or hereafter in effect.*" J.A. 78 (emphasis added). The Resolution thus contemplated, according to the government, "that regulatory capitalization requirements might be changed, and Winstar pledged to comply with those changes." Pet. Br. 32.

To be sure, the Resolution required Winstar to pledge to maintain the thrift's net worth at the "*level*" - that is, the *amount* as a percentage of assets - required under then-existing or later regulations. The Resolution did not contemplate, however, that the *calculation* of regulatory capital, or more accurately, the status of supervisory goodwill as an asset included in that calculation, would change. Indeed, Winstar fulfilled its obligation to provide the required Net Worth Maintenance Stipulation, and it was included in the parties' Assistance Agreement. Specifically, Winstar pledged to maintain its "Net Worth at an amount not less than the minimum amount prescribed in § 563.13 of the Insurance Regulations." J.A. 96. The Assistance Agreement then defines the term "net worth" as follows: "Regulatory Net Worth as defined in § 561.13 of the Insurance Regulations *and as computed in accordance with the accounting principles required by this Agreement.*" J.A. 94 (emphasis added).

Winstar's contract documents thus plainly reflect the parties' agreement that Winstar could count supervisory

goodwill as regulatory capital for 35 years and that the government assumed the risk of future regulatory change.¹⁸

c. In sum, both the Federal Circuit and the Court of Federal Claims, which are especially entrusted with issues of government contract interpretation and enforcement, concluded from all the evidence that Statesman and Winstar specifically bargained for and received an express government promise to accord regulatory capital treatment to supervisory goodwill and capital credit for specified periods. This interpretation plainly accords with the intentions of the contracting parties, and the government's disingenuous attempt to suggest otherwise does it no credit.¹⁹

18 The regulatory capital terms set out in the contract documents are consistently reflected in other documents related to this transaction. For example, the acquisition proposal documents prepared by Winstar clearly indicated that the resulting institution would "record the assets (other than FSLIC assistance) and liabilities acquired at the date of consummation of the combination at their fair value and the difference will be allocated to goodwill and amortized on the straight-line basis over a period not to exceed 35 years." C.A. App. 205. *See also* J.A. 40-42. Similarly, the government's internal documents analyzing the transaction recognized the regulatory capital forbearance as a key feature of the deal. *See, e.g.*, FHLBB Memorandum: Viability Analysis (J.A. 37) (listing as assumption that "[p]urchase accounting is applied to the assets of Windom . . . Goodwill is amortized over 40 years."); FHLBB Memorandum (J.A. 46) (listing as assumption that "[g]oodwill is amortized over 35 years"); FHLBB S-Memorandum (J.A. 62) (noting "that the proposed acquisition requires the use of the purchase method of accounting, and that loan discounts and intangible assets will be amortized under regulatory accounting principles."); FHLBB Memorandum (J.A. 49) ("We concur . . . that the purchase method of accounting is appropriate for the acquisition of Windom Further, we have no objection to the accounting forbearance outlined for purposes of reports to the FHLBB.").

19 Relying on the termination provisions in the *Winstar* and *Statesman* Assistance Agreements, the government also argues that whatever contractual commitments it made to respondents have by now terminated. Pet. Br. 32, 35 n.25. The Court of Appeals quite correctly rejected this argument. Pet. App. 23a, 29a. The government's argument ignores the actual language of the Assistance Agreements, which provide that the Assistance Agreements would, "[e]xcept as otherwise specifically provided., in th[e] Agreements," terminate, in the case of *Statesman*, five years after the effective date of the agreement or, in the case of *Winstar*, two years after the effective date of the agreement. *See* J.A. 405 (emphasis added). *See also* J.A. 110. As the Court of Appeals held, such termination

3. a. The government relies upon the "unmistakability doctrine" for its claim that its contracts with Statesman and Winstar should be construed to create no obligation whatever on its part. According to the government, the unmistakability doctrine is a kind of "clear statement" rule of contract interpretation, designed to ensure that a government promise "contracting away the government's right to exercise future sovereign regulatory authority" is expressed in the "clearest possible terms." Pet. Br. 18-19. The rationale of the rule is that courts should be reluctant to interpret government contracts to prohibit the government from taking regulatory actions that may be deemed "necessary or advisable at a later time." Pet. Br. 18. To satisfy the unmistakability doctrine in this case, respondents would have to produce, according to the government, an express promise "either committ[ing] Congress not to enact new legislation requiring a different treatment of respondents' capital or grant[ing] respondents a prospective immunity from any such legislative change." Pet. Br. 36.

Throughout the course of this case, the government has stood silent in response to our repeated requests that it point to a single government contract - from any time in our Nation's history, involving any federal agency - that contains an express provision stating that the government's contract obligations will override any future statutory obligations imposed by Congress. We cannot find one either. One need know no more than this to know that the government's understanding of the unmistakability doctrine is wrong.

Indeed, if the government's version of the unmistakability doctrine is correct, then the many cases in which this Court has enforced contracts against the United States despite subsequent changes in the law must be wrong. For example, in *Perry v. United States*, 294 U.S. 330 (1935), this

provisions did not "negate other obligations under the merger plan, including the specific time periods for amortization of goodwill." Pet. App. 23a. Finally, even if the government's strained reading of the termination provision is correct, the Statesman Assistance Agreement did not expire until 1993, four years *after* the passage of FIRREA.

Court held that a government bond promising the payment of principal and interest in gold was a binding contractual obligation that could not be abrogated by subsequent legislation. Similarly, in *Lynch v. United States*, 292 U.S. 571 (1934), the Court held that war risk insurance policies issued pursuant to statute were contracts that could not be abrogated by subsequent statutes without compensating the beneficiary. In neither *Perry* nor *Lynch* did the government contract at issue contain even a reference, unmistakable or otherwise, to Congress or its sovereign powers, let alone a provision "commit[ting] Congress not to enact new legislation." Pet. Br. 36. And, in both *Perry* and *Lynch* the Court made clear that the government is bound by its express contractual undertakings no less than an individual would be. See *Perry*, 294 U.S. at 352 ("When the United States, with constitutional authority, makes contracts, it . . . incurs responsibilities similar to those of individuals who are parties to such instruments."); *Lynch*, 292 U.S. at 579 ("When the United States enters into contract relations, its rights and duties therein are governed generally by the law applicable to contracts between private individuals."). See also *Sinking Fund Cases*, 99 U.S. (9 Otto) 700, 719 (1879) ("The United States are as much bound by their contracts as are individuals."); *United States v. Klein*, 80 U.S. (13 Wall.) 128, 144 (1872) ("It is as much the duty of the government as individuals to fulfill its obligations.").

In truth, the government's notion of contract unmistakability misappropriates the nomenclature of a venerable and sensible rule of construction - that contract rights against the government cannot be presumed, but must be "expressed in terms too plain to be mistaken," *Jefferson Branch Bank v. Skelly*, 66 U.S. (1 Black) 436, 446 (1862) - and attaches it to an extraordinary claim of governmental immunity from liability for any contract breach occasioned by an act of Congress. The origins of the doctrine can be traced back to the early 1800s. In the leading case, *Providence Bank v. Billings*, 29 U.S. (4 Pet.) 514 (1830), a bank claimed that its charter from the State created a contract right precluding the State from taxing it. Chief Justice Marshall rejected the bank's claim that the charter impliedly prohibited taxation because

the taxing power could be exercised so as to destroy the charter. *Id.* at 561-62. Because the charter did not contain "a promise, either express or implied, not to tax the bank," *id.* at 560, the Court held that such a contractual promise "ought not to be presumed in a case in which the deliberate purpose of the State to abandon it does not appear." *Id.* at 561. Nowhere did the Court suggest that anything more "unmistakable" than an express promise not to tax would be required to bind the government.

Indeed, in *Jefferson Branch Bank v. Skelly, supra*, this Court held that a bank's charter created a contract right exempting the bank from taxation imposed by subsequent statute. The charter provision at issue provided that a certain percentage of the bank's profits were to go to the State "in lieu of all taxes."²⁰ Certainly this language - though unmistakable in the common sense of the term - does not satisfy the unmistakability rule advanced by the government. Yet this Court construed the charter provision to have contractually bound the state "in terms too plain to be mistaken." *Jefferson Branch Bank*, 66 U.S. (1 Black) at 446.

These cases are the direct ancestors of the three cases cited by the government in support of its version of the unmistakability doctrine - *POSSE*, *Merrion v. Jicarilla Apache Tribe*, 455 U.S. 130 (1982), and *United States v. Cherokee Nation*, 480 U.S. 700 (1987). *Merrion* involved leases granted by the Apache Tribe for the extraction of oil and gas deposits on reservation land. The Tribe later imposed a severance tax on oil and gas production covered by the leases, and the lessees sought to enjoin imposition of the tax on the ground that their leases exempted them from such taxes. The leases, however, were silent on the question of severance taxes. As the Court concluded:

We could find a waiver of the Tribe's taxing power only if we *inferred it from silence* in the leases. To presume that a sovereign forever waives the right to

²⁰ *Piqua Branch v. Knoop*, 57 U.S. (16 How.) 369, 378 (1854). The Court's opinion in *Jefferson Branch Bank* does not set out the specific charter provision at issue, but it cites to the *Piqua Branch* decision, which does.

exercise one of its sovereign powers unless it expressly reserves the right to exercise that power in a commercial agreement turns the concept of sovereignty on its head

455 U.S. at 148 (emphasis added).

Quoting the above passage from *Merrion*, the Court in *POSSE* reiterated that a contractual waiver of the government's right to exercise sovereign powers cannot be inferred from contractual silence on the issue. *POSSE* involved a purported contract between the Department of Health and Human Services ("HHS") and the State of California governing the State's participation in the social security system. The agreement was expressly made subject to the provisions of the Social Security Act, which at the time the agreement was entered permitted states to withdraw from participation in the program. A subsequent amendment to the Act prohibited states from withdrawing from the system. This Court held that neither the Act nor the State's contract obliged the government to permit the State's withdrawal because Congress had expressly reserved in the statute the "right to alter, amend, or repeal" any of its provisions. 477 U.S. at 52. Thus, the Act itself obviously "created no contractual rights," and because the contract conformed to the Act, it too created no contractual right to withdraw. *Id.* *POSSE* thus stands for the common sense rule of construction that neither the government nor anyone else is contractually bound in the face of statements that expressly negate any intention to be bound. *POSSE* expressly reaffirmed, however, that "the Federal Government, as sovereign, has the power to enter contracts that confer vested rights, and the concomitant duty to honor those rights." *Id.*

Finally, in *Cherokee Nation*, the Tribe claimed that a treaty granting it title to a river bed also conveyed the federal government's navigational servitude, although the treaty was silent on the point. Citing *POSSE*, this Court rejected the claim, stating that such a waiver of "sovereign authority will not be implied but instead must be 'surrendered in unmistakable terms.'" *Id.* at 707, quoting *POSSE*, 477 U.S. at 52.

The consistent teaching of these cases is that an "unmistakable" promise is simply a clearly expressed promise. None of the cases even distantly suggests that in order to bind the government to a clearly expressed promise, it must be coupled with a further promise that Congress will not enact contrary legislation. Thus, while it is certainly true that the courts below expressly declined in this case to apply the government's version of the unmistakability doctrine, they faithfully applied this Court's version of the doctrine. *See also The Binghamton Bridge*, 70 U.S. (3 Wall.) at 75-77.²¹

21 The government cites (Pet. Br. 22 n.12) three cases that, it says, properly applied the unmistakability doctrine to contracts similar to those at issue here. *See Charter Fed. Sav. Bank v. OTS*, 976 F.2d 203 (4th Cir. 1992), *cert. denied*, 113 S. Ct. 1643 (1993); *Transohio Sav. Bank v. Director, OTS*, 967 F.2d 598 (D.C. Cir. 1992); *Guaranty Fin. Serv., Inc. v. Ryan*, 928 F.2d 994 (11th Cir. 1991). In contrast to the Government's portrayal of those cases, however, both *Guaranty* and *Charter* represent straightforward applications of the principles discussed in *POSSE*.

In *Guaranty* the government expressly reserved its right to change applicable regulations and apply them to the thrift. 928 F.2d at 999. And the Fourth Circuit in *Charter* expressly distinguished that case from *Winstar* and *Statesman*, noting that *Charter* did not involve a written contract of any kind between the plaintiffs and the government. 976 F.2d at 211 n.12. That the *POSSE* doctrine precluded relief in cases in which there was no contract to begin with or in which the contract included an express reservation of authority to alter the terms of performance does not mean that it precludes relief here, where the parties' contracts clearly express the government's promise with respect to the regulatory capital forbearances at issue and which contain no similar language of reservation. Finally, the D.C. Circuit's application of the unmistakability doctrine in *Transohio* was limited to claims seeking injunctive relief, not compensation. Although the first *Transohio* decision had adopted the United States' erroneous view of contract interpretation in a case seeking injunctive relief, the second *Transohio* decision determined that rule may be inapplicable in a Tucker Act action for damages: "[T]he *Transohio* opinion, including the statement that 'Transohio cannot prevail on its takings claim on the merits,' 967 F.2d at 614, was solely concerned with *Appellants' ability to obtain injunctive relief*, as is evident from the opinion's repeated explanations that Transohio 'did not receive from the banking regulators a right that *defeats Congress' power to change the law on goodwill accounting*.' *Id.* at 613; *see id.* at 601, 624. That analysis has no bearing one way or the other on the *merits of Appellants' claim for compensation* in the Federal Court of Claims." *Transcapital Fin. Corp. v. Director, OTS*, 44 F.3d 1023, 1025 (D.C. Cir. 1995) (emphases added).

b. In the introduction to our argument (*supra* at 13-17), we demonstrated that the rationale of the government's unmistakability doctrine, and of the reserved powers doctrine developed by this Court in the context of Contract Clause challenges, is wholly inapplicable to this case. Respondents do not seek an order invalidating FIRREA's goodwill provisions or otherwise requiring the government to abide by its contractual obligations. Nor do respondents seek the return of their thrifts; that egg cannot now be unscrambled. Respondents seek only monetary relief for their injuries, which "presents little threat to the government's sovereign powers." Pet. App. 37a.

The government argues, however, that "[t]he unmistakability doctrine protects against requiring the public to pay in damages for the privilege of changing government policy, just as it protects against injunctions precluding such alterations altogether." Pet. Br. 11. While requiring the government to respond in damages for a contract breach occasioned by a statutory or regulatory change would not *prevent* the exercise of sovereign authority, the government argues that the threat of a damages award would nonetheless "carr[y] the danger that needed future regulatory action will be deterred." Pet. Br. 21.

The law, however, attaches an obligation to pay damages not to "the privilege of changing government policy," but rather to the privilege of breaching a solemn contractual obligation. The purpose of the law of contracts is to "deter" breaches of contractual obligations secured by consideration. The government claims, however, that it is entitled, as sovereign, to make a contractual promise that in no way deters it from later breaching that promise. Mr. Hamilton answered this claim succinctly two centuries ago: "It is in theory impossible to reconcile the idea of a promise which obliges, with the power to make a law which can vary the effect of it." *Perry*, 294 U.S. at 351 n.2 (quoting Alexander Hamilton, "Report On Public Credit" (1795), in 3 *The Works of Alexander Hamilton* 518-19 (John C. Hamilton ed. 1850)).

Moreover, the assumption that allowing contract damages recovery in this case would financially harm the government ignores the extraordinary financial benefit that the government received from respondents in exchange for the contractual promises that the government has now broken. Thus, far from harming the government, damages relief is necessary to prevent a government windfall.²² Similarly, upholding the government's claimed constitutional right to breach its contract obligations without liability would effectively expand the government's sovereign power beyond constitutional bounds. The thrift regulators could not have *forced* Statesman and Winstar to acquire the insolvent thrifts. Nor could they have forced respondents to donate almost \$24 million to help the government defray the cost of recapitalizing its insolvent thrifts. Allowing the government now to repudiate, without liability, its contractual commitments to respondents would enable the government to accomplish through broken promises that which it could not have required through the compulsion of straightforward legislation.²³

"The right to make binding obligations is a competence attaching to sovereignty." *Perry*, 294 U.S. at 353. The federal government, like any other contracting party, may elect to breach its contract obligations, but it must pay damages, like any other contracting party. *See* note 8, *supra*. The government's contrary claim misapprehends the nature of its own

²² Allowing the government to breach its regulatory capital promises without consequence would effectively shift to respondents and others like them the dominant financial burden for the government's change in regulatory policy, solely because they took the government at its word. Far from being a necessary or legitimate element of sovereign power, the government's alleged entitlement to breach without damages liability runs counter to the basic purpose of the Takings Clause; namely, "to bar Government from forcing some people alone to bear public burdens which, in all fairness and justice, should be borne by the public as a whole." *Armstrong v. United States*, 364 U.S. 40, 49 (1960).

²³ The government acknowledges (Pet. Br. 41 n.34) that it can claim no legitimate, let alone overriding, interest in "repudiat[ing] its own debts . . . simply in order to save money." *POSSE*, 477 U.S. at 55. The only governmental interest at stake, however, in this action for damages relief is money. It is thus clear that there is no serious "public policy" basis for denying respondents' claims.

accountability under our constitutional system. As the trial court below put it:

The assertion that, in order to freely regulate, the government must have the power to disregard the rights and interests of its citizens is a novel proposition that finds no support . . . in our constitutional tradition. Sovereign power is always restricted, in one sense, by the rights of individuals. However, in our Nation that has never been seen as an improper restriction on regulatory power. Rather, it is the foundation upon which all law and regulation are built.

Pet. App. 168a.²⁴

4. The reserved powers doctrine, as we have previously discussed (*supra* at 15-17), was developed by this Court to ensure that a State's contractual obligations did not limit, under the Contract Clause, a future exercise of the State's police powers in the area of health, safety, and public morals. *See, e.g., United States Trust*, 431 U.S. at 21-24. The Court has consistently recognized, however, that a State's "power to enter into effective financial contracts cannot be questioned," even though enforcing such contracts according to their terms necessarily entails restrictions on the State's taxing and spending powers. *Id.* at 24. *See also Energy Reserves Group v. Kansas Power & Light Co.*, 459 U.S. 400, 412-13 n.16 (1983) ("In almost every case, the Court has held a governmental unit to its contractual obligations when it enters financial or

²⁴ *See also* Pet. App. 103a ("That the government may be empowered to legislate in this way, and that a desired public policy is served, does not mean that it can be done without liability to those with whom the government had made a different commitment. The government is not exonerated of responsibility with respect to specific commercial contracts to which it is a party, whether the breach is by executive or legislative action.") (Newman, J., dissenting); *id.* 192a-193a ("[W]hile Congress' power to regulate is not impaired, the government may be compelled to pay for the result of its actions, especially when in doing so the government actually is paying because it received a benefit The fact that the government was free to change its regulatory scheme is not inconsistent with the possibility that there exists a contract here under which the government may have obligations to the plaintiffs in this case.").

other markets."). The government concedes this point, recognizing that the government cannot "renege on purely financial contractual obligations." Pet. Br. 41; *see id.* at n.9 (noting that the price term and other financial elements of a government contract "do not implicate sovereign regulatory authority").

The contracts at issue here involved *commercial* transactions in which both parties were motivated by their own *economic* interests. The government's regulatory capital promises were made for financial reasons and they were breached for financial reasons. As the government itself emphasizes, goodwill was eliminated as regulatory capital under FIRREA because it "is not cash 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." Pet. Br. 5, quoting 135 Cong. Rec. 11,795 (1989).

Thus, in 1989 the government rejected goodwill as regulatory capital for precisely the same reason that it embraced goodwill as regulatory capital in its transaction with Statesman - because it is not *cash*. As a substitute for cash, goodwill was used by the government as "an indispensable tool" in the government's effort to induce respondents' acquisitions on terms that "husband[ed] FSLIC's] financial resources" from the enormous expense of liquidating or recapitalizing the insolvent thrifts. *See* note 3, *supra*. Later, that very same goodwill became quite dispensable to the government solely because it would be "valueless" if the government ever had to liquidate the thrifts that it had sold to respondent. So the government repudiated the very regulatory capital promises that had induced respondents' acquisition and ordered respondents either to replace the supervisory goodwill and capital credit with hard cash or to return the thrifts, along with their multi-million investments, to the government. In short, by repudiating its regulatory capital promises, the government retroactively transferred to respondents the government's obligation, as deposit insurer, to make good on the losses suffered by the acquired thrifts.

The government's regulatory capital promises in this case are thus no less financial, and its breach no less consequential, than if the government had induced respondents' supervisory acquisitions with a promissory note rather than intangible capital, and then canceled the note and seized the thrifts as undercapitalized. Accordingly, the reserved powers doctrine would not in any event shield the government from enforcement of its regulatory capital promises according to their terms. *See, e.g., Lynch*, 292 U.S. at 579; *Perry*, 294 U.S. at 352. *See also Hodel v. Irving*, 481 U.S. 704 (1987); *Ruckelshaus v. Monsanto Co.*, 467 U.S. 986 (1984); *Choate v. Trapp*, 224 U.S. 665 (1912).

5. In sum, Statesman and Winstar specifically bargained for and received express regulatory capital promises from the thrift regulators in return for their agreements to infuse substantial sums of money into the acquired thrifts and to assume liabilities that far exceeded the thrifts' assets. Statesman and Winstar took care to ensure that the government's regulatory capital promises were expressly contained in "documents [that] were integrated and cross-referenced, in textbook compliance with the rules of contract." Pet. App. 95a (Newman, J., dissenting). The intent of the contracting parties regarding regulatory capital is clear from the contract documents, the negotiating records, the government's internal analyses of the transactions, the parties' course of dealing until enactment of FIRREA, and common sense. No doctrine of contract construction, including the unmistakability doctrine, requires a court to interpret an agreement in a manner that negates the clear intent of the contracting parties, as the government invites this Court to do here. Indeed, Congress found these and similar contracts unmistakable enough; during consideration of FIRREA, both supporters and opponents of the legislation in Congress understood and acknowledged that FIRREA's goodwill provisions would violate existing

government contracts like respondents.²⁵ And the Comptroller General warned Congress that enactment of those provisions would expose the government "to potentially enormous financial liability" for both breach of contract and uncompensated takings. Comptroller General Op. B-240860 (Aug. 27, 1990) (J.A. 515). The government assumed the risk of future regulatory change, and now it must pay damages for its breach.

II. THE THRIFT REGULATORS HAD EXPRESS STATUTORY AUTHORITY TO ENTER INTO STATES-MAN'S AND WINSTAR'S CONTRACTS.

It is true, as the government states, that nothing in the laws relating to thrift institutions "grant[ed] FSLIC or the Bank Board the authority to commit Congress not to modify - the governing statutes." Pet. Br. 41. Indeed, we are certain

²⁵ See, e.g., H.R. Rep. No. 54, 101st Cong., 1st Sess., pt. 1, 432 (1989) (defining supervisory goodwill, and then noting that "[a]ny other goodwill resulting from the acquisition, merger, consolidation, purchase of assets or other business combination that is not covered by a *specific contractual understanding or agreement with the Bank Board* is not included as a component of capital") (emphasis added); *id.* at 497-98 (additional views of Mr. Annunzio, Mr. Kanjarski, and Mr. Flake) ("The Committee's [treatment of supervisory goodwill] is the same as the government asking a man to enlist in the Army for hazardous duty overseas and then suing him for deserting his wife and children Simply put, the Committee has reneged on the agreements that the government entered into concerning supervisory goodwill."); *id.* at 507-08 (additional views of Mr. LaFalce) ("Those institutions which carry intangible assets on their books do so generally under written agreements they have entered into with the U.S. government, agreements which generally state that they cannot be superseded by subsequent regulations."); *id.* at 534 (additional views of Representatives Hiler, Ridge, Bartlett, Dreier, McCandless, Saiki, Baker, and Paxon). See also 135 Cong. Rec. H2706 (daily ed. June 15, 1989) (statement of Rep. Crane) (FIRREA "would require these S&Ls to write off this goodwill in a scant five years. This legislation violates the present agreements that these institutions made with the Federal Government."); *id.* at H2783 (daily ed. June 15, 1989) (statement of Rep. Ackerman) (FIRREA "would abrogate written agreements made by the U.S. Government to thrifts that acquired failing institutions In effect, the Government is saying, 'Thanks for your help, but we don't need you anymore, so we're breaking our promise.' "); *id.* at H2717 (daily ed. June 15, 1989) (Statement of Rep. Rostenkowski) ("The contracts between the savings and loan owners when they acquired failing institutions in the early 1980's are not contracts written in stone.").

that there is no provision in the *United States Code* granting such a power to any federal agency. And we cannot imagine that such a law would be upheld if one did exist. As we have demonstrated above, however, the unmistakability doctrine, properly understood, requires nothing more to bind the government than a clearly expressed contractual promise, not a further commitment that the promise will either be honored by Congress or specifically enforced despite enactment of contrary legislation. Thus, the fact that the thrift laws do not contain a provision delegating to the thrift regulators' authority to make such a commitment is quite beside the point.

There is no doubt that the thrift regulators had ample statutory authority to enter into the contracts at issue here. As the court of appeals noted, the FSLIC has always had express statutory power "[t]o make contracts." Pet. App. 39a (quoting 12 U.S.C. § 1725(c)(3) (1988) (repealed by FIRREA)).²⁶ That nothing more is required is a central premise of the Tucker Act, whose purpose, according to Judge Learned Hand, was "to assume liability for the acts of such of [the government's] agents as had the power in the discharge of their duties to assume or refuse engagements on the faith of which other citizens should rely." *Heil*, 273 F. Supp. at 731.

III. THE SOVEREIGN ACTS DOCTRINE DOES NOT EXCUSE THE GOVERNMENT'S LIABILITY IN DAMAGES FOR ITS BREACH OF ITS CONTRACTUAL OBLIGATIONS.

1. As a final safe harbor from liability for its contract breach, the government offers the sovereign acts doctrine, which excuses the government from contract liability when its

²⁶ See also 12 U.S.C. § 1729(f)(2)(A), (3) (1988) (repealed by FIRREA) (granting authority to FSLIC, "in its sole discretion and upon such terms and conditions as [it] may prescribe," to agree to specified forms of assistance in order to facilitate the merger or acquisition of a failing institution); 12 U.S.C. § 1725(d) (1988) (repealed by FIRREA) (authorizing FSLIC "to borrow money, and to issue notes, bonds, debentures, or other such obligations upon such terms and conditions as the [Bank Board] may determine.").

performance is "incidentally" impaired by its *unrelated* "public and general acts as a sovereign." *Horowitz v. United States*, 267 U.S. 458, 461 (1925). The Federal Circuit concluded that the sovereign acts doctrine did not apply in these cases primarily because it was "convinced . . . 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." Pet. App. 45a. As a result, no "public and general" sovereign act was involved that could trigger the immunity of the doctrine.

The government quarrels with this conclusion of the Federal Circuit on several, equally unmeritorious, grounds. The government first contends that FIRREA qualifies as a "public and general" sovereign act because it "instituted a comprehensive overhaul of the regulation of the entire thrift industry," Pet. Br. 44, and so was enacted "to govern regulatory policy and to advance the general welfare." Pet. Br. 45. The Federal Circuit provided the complete answer to this argument, observing that the relevant provisions of FIRREA were not any less targeted at the parties to supervisory mergers because they were packaged in a much larger, "comprehensive" piece of legislation. Pet. App. 44a. Moreover, the court of appeals pointed out that the good motives of Congress in enacting FIRREA did not somehow distinguish the relevant parts of FIRREA and make them "general" for purposes of the sovereign acts doctrine; presumably every act of Congress is intended to advance the public welfare. Pet. App. 45a. *See United States Trust*, 431 U.S. at 29 ("a State cannot refuse to meet its legitimate financial obligations simply because it would prefer to spend the money to promote the public good rather than the private welfare of its creditors").

The government further argues that the Federal Circuit's rejection of the sovereign acts doctrine - based on the conclusion that FIRREA's "principal effect is to abrogate specific contractual rights," Pet. App. 40a - is wrong because FIRREA provided a "transition" that phased out supervisory goodwill over several years rather than eliminating it all at once. Pet. Br. 45-46. As a result, the government claims,

FIRREA actually placed thrifts like Statesman and Winstar in a *better* position than other institutions. *Id.* at 45.

Taken at face value, such an argument turns a blind eye to the actual impact of FIRREA, as well as to the text and legislative history of the statute itself. For Winstar and Statesman, there was no "transition" period; their thrifts were seized within a few months of the date on which FIRREA's restrictions on supervisory goodwill became effective. The government certainly will have a hard time convincing Statesman and Winstar that FIRREA placed them in a *better* position than anyone else.

At bottom, the government strains to avoid the clear focus of FIRREA and its legislative history on the goodwill contracts - as the *in banc* Federal Circuit, and Judge Newman dissenting from the panel decision, explained, Pet. App. 41a-44a, 95a-98a - by employing a *non sequitur*. The fact that the restrictions on the use of supervisory goodwill were phased in hardly negates the undeniable fact that those restrictions were targeted at this particular intangible asset created only by contracts with the government.

2. To apply the sovereign acts doctrine as the government urges here would transform the doctrine into a radical instrument of government lawlessness, at war both with this Court's precedents and with the attributes of sovereignty itself. As previously discussed, this Court has long recognized that "the right to make binding obligations is a competence attaching to sovereignty." *Perry*, 294 U.S. at 353. Consequently, the Federal Circuit was correct in describing the bounds of the sovereign acts doctrine: "[W]e know of no authority for . . . [the proposition] that the government has a sovereign right to disavow its contractual obligations through comprehensive national legislation." Pet. App. 45a. *See also Freedman v. United States* 320 F.2d 359, 366 (Ct. Cl. 1963) ("The doctrine of 'public and general' 'sovereign acts,' laid down in *Horowitz* . . . does not relieve the Government from liability where it has specially undertaken to perform the very act from which it later seeks to be excused."); *Hills Materials Co. v. Rice*, 982 F.2d 514, 516 n.2 (Fed. Cir. 1992). To the

contrary, "Congress was without power to reduce expenditures by abrogating contractual obligations of the United States." *Lynch*, 292 U.S. at 580.

The issue addressed by the sovereign acts doctrine, it must be remembered, arises only in circumstances where the "dual capacities" of the government as sovereign and as a participant in commerce are manifestly distinct. In *Horowitz*, for example, a government agency that had entered a contract to sell surplus silk could not comply with Horowitz' request to ship the silk by freight due to a subsequent rail embargo. In denying Horowitz' claim against the government for loss caused by the resulting delay in shipment, this Court explained:

The two characters which the government possesses as a contractor and as a sovereign cannot be thus fused 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).

The operating premise of the sovereign acts doctrine is that, where the federal government is acting in distinct capacities as sovereign and as a contractor, in its role as a contractor it is entitled to be treated as if it were a private contracting party - no better, no worse. It follows that to determine whether the government's breach of a contract is excused under the sovereign acts doctrine, "a citizen or corporate body must by supposition be substituted in its place, and then the question be determined whether the action will lie against the supposed defendant." *Jones v. United States*, 1 Ct. Cl. at 385. In *Horowitz*, the silk contract contained no provision concerning shipment by freight or otherwise allocating the risk of a future event like the embargo, and so Horowitz would not

have been entitled to recover his loss against a private contractor. As a result, he was not entitled to recovery against the government.

Under this analysis, when a contracting party - whether a private party or a government agency - in effect assumes the risk that a change in the law will not occur, and that change does occur so as to impair contract performance, the party that assumed that risk will be liable in damages. Nothing in the sovereign acts doctrine either bars the government as a contractor from assuming such a risk or subsequently operates to immunize it from the consequences of such an obligation, whether or not the legislation involved is "public and general." In *Perry*, for example, Congress acted pursuant to its power "to regulate the value of money," 294 U.S. at 350, to declare provisions in not only government contracts, but in *any* contract, requiring payment in gold to be "against public policy." *Id.* at 349. It is difficult to imagine a statute with broader application. Yet the Court rejected the notion that this power allowed Congress to "disregard the obligations of the Government at its discretion," *id.* at 350, or to otherwise "alter or repudiate the substance of its own engagements." *id.* at 351. So, too, in *Lynch*, the law breaching the government's contract was a repeal of "[a]ll laws granting or pertaining to" certain insurance policies. 292 U.S. at 575. Though Congress clearly had the power to issue such insurance, *id.* at 579, at the same time "Congress was without power to reduce expenditures by abrogating contractual obligations of the United States." *Id.* at 580.²⁷

²⁷ See also *Hills Materials*, 982 F.2d at 516 n.2 ("[T]he [sovereign acts] doctrine certainly does not prevent the government as contractor from affirmatively assuming responsibility for specific sovereign acts."); *Amino Bros. Co. v. United States*, 372 F.2d 485, 491 (Ct. Cl.), *cert. denied*, 389 U.S. 846 (1967) ("The government cannot make a binding promise that it will not exercise a sovereign power, but it can agree in a contract that if it does so, it will pay the other contracting party the amount by which its costs are increased by the Government's sovereign act.").

In its contracts with Statesman and Winstar, the government agreed to assume precisely this risk that future regulatory changes would not interfere with the promised regulatory treatment of supervisory goodwill and capital credits. Accordingly, the sovereign acts doctrine can erect no bar to the government's liability in damages to Statesman and Winstar for its breaches of the contracts with them.

The inapplicability of the sovereign acts doctrine is even more apparent when, as is the case here, a clear distinction cannot be drawn as to whether the government is acting in its sovereign or regulatory capacity on the one hand, or its capacity as a participant in commerce on the other. Indeed, the blurring of this distinction with the rise of the modern regulatory state has long been recognized.²⁸ The contracts with Statesman and Winstar provide a clear example. A government agency, acting as an insurer, and animated by financial concerns similar to those of any other insurer, needed to relieve itself of the vast liability created by insolvent thrifts that was driving the agency itself into insolvency. As a result, the agency entered the marketplace to find buyers for those thrifts who would assume that liability - clearly a commercial endeavor.²⁹ Yet certain of the contractual promises made to effect these transactions, part of the price paid by the agency, were promises to accord specified *regulatory* treatment to respondents' supervisory goodwill and capital credit, promises that obviously could not have been made by a private party. Only the government could have made such a contractual promise, and only the government could have breached it.

²⁸ See, e.g., *Sunswick Corp. v. United States*, 75 F. Supp. 221, 228 (Ct. Cl.), *cert. denied*, 334 U.S. 827 (1948) ("We know of no reason why the Government may not by the terms of its contract bind itself for the consequences of some act on its behalf which, but for the contract, would be nonactionable as an act of the sovereign.").

²⁹ This point is discussed more fully in the brief filed in this case by *amici* Keystone Holdings, Inc. and American Savings Bank, F.A.

Surely the sovereign acts doctrine does not permit the government to escape damages liability for rendering impossible (by changing the law) its own performance of a contractual promise that only it could have made. Excusing a deliberate breach of such a governmental promise would contradict rather than serve the purpose of the sovereign acts doctrine. As one commentator recently put it:

In such cases, the party that entered into the contract - the government as lawgiver or regulator - and the party that impaired the contract by enacting a sovereign act - the government as lawgiver or regulator - are the same. Instead of providing the government with as much protection under contract law as private parties enjoy, shielding the regulatory state from contract liability would allow the government as lawgiver or regulator to breach its contracts freely.

Recent Cases, 109 Harv. L. Rev. 1162, 1167 (1996).

3. Finally, the government does not even try to justify the unconscionably unfair consequences of applying the sovereign acts doctrine in this case. The government, as a direct result of its repudiation of its contractual obligations, seized Statesman's and Winstar's thrifts, along with the substantial cash capital infusions (\$21 million and \$2.8 million, respectively) that they had made in the thrifts in direct reliance on the government's promises. The government would invoke the sovereign acts doctrine not only to excuse its breach, but also to retain Statesman's and Winstar's money as well. No sovereign acts case, of course, supports such a result.

To the contrary, American law is far more solicitous of elementary notions of fairness than the government is willing to admit. Even when an agency's contractual promise cannot be enforced - for example, because it was unlawful or unauthorized at the time it was made - the benefits conferred on the government and costs incurred by the private party in reliance on the promise must be reimbursed, on application of *a quantum meruit* or *quantum valebant* analysis, to put the contracting parties "substantially in the position they would

have occupied without the attempted contract" *New York Mail & Newspaper Transp. Co. v. United States*, 154 F. Supp. 271, 276 (Ct. Cl.), *cert. denied*, 355 U.S. 904 (1957).

For example, in *United States v. Amdahl Corp.*, 786 F.2d 387, 393 (Fed. Cir. 1986), the Federal Circuit held that the government must return the value of benefits received even under a contract that was properly terminated by the government for illegality:

Where a benefit has been conferred by the contractor on the government in the form of goods or services, which it accepted, a contractor may recover at least on a *quantum valebant* or *quantum meruit* basis for the value of the conforming goods or services received by the government prior to the rescission of the contract for invalidity.³⁰

Clearly Statesman and Winstar are entitled, at a minimum, to return of the money and other benefits they provided to the government in reliance on promises that were validly made, but whose performance was later rendered impossible by contrary legislation.

³⁰ See also *Prestex Inc. v. United States*, 320 F.2d 367, 373 (Ct. Cl. 1963) ("Even though a contract be unenforceable it is only fair . . . that the Government pay for goods delivered or services rendered and accepted under it."); *Yosemite Park & Curry Co. v. United States*, 582 F.2d 552, 560 (Ct. Cl. 1978) ; [W]hile... the Government could [not] be bound by . . . Agreement, . . . the Government bargained for, agreed to pay for, and received the benefit of [the contractor's] services"; *Ocean Technology, Inc. v. United States*, 19 Cl. Ct. 288, 293 (1990) ("It would be manifestly unfair, at this late date, for [the government] to retain the benefits of the [contractor's product] . . . while renouncing its contractual obligations.").

CONCLUSION

For the foregoing reasons, the judgment below should be affirmed.

Respectfully submitted,

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