

OPINION

REVIEW & OUTLOOK

Godzilla Defeats the Thing

Federal Judge Royce Lamberth did a service for taxpayers on Tuesday by dismissing claims against the federal government brought by private investors trying to profit once again from Fannie Mae and Freddie Mac. The judge saw through a plaintiffs' argument that combined dubious legal reasoning with junk economics.

The two mortgage giants would have failed without a 2008 federal bailout that eventually poured \$188 billion into the firms. But investment funds including Perry Capital and Fairholme that own shares in Fannie and Freddie have argued that they now deserve to reap the rewards of the taxpayer rescue.

These shareholders point out that dividends paid to the Treasury for the rescue have totaled more than \$218 billion—apparently exceeding the rescue funds. They argue that Treasury has used a 2012 amendment to the bailout agreement to unfairly collect all of Fan and Fred's profits.

Nobody has written more about this Administration's legal abuses than we have, but Judge Lamberth appears to be right on this one. His ruling cites the "plain meaning" of the 2008 law under which the government put Fan and Fred into federal conservatorship, which says that "no court may take any action to restrain or affect the exercise of powers or functions" of the company's conservator. The senior jurist suggests that if investors have a gripe, it's with Congress for writing the law.

Judge Lamberth is arguably being too kind to the plaintiffs, because the \$188 billion in direct support was hardly the only public assistance to Fan and Fred. According to Larry Wall, a researcher at the Federal Reserve Bank of Atlanta, "The claim that the taxpayers and Treasury have been fully repaid for their support of Fannie Mae and Freddie Mac is based on an accounting calculation that does not withstand economic analysis."

He adds that, among other problems, this claim "attributes no value to the government guarantee to absorb whatever losses arose in the pre-conservatorship book of business, and arguably reflects Treasury setting too low of a dividend rate on its senior preferred stock. Moreover, the profits that are being used to pay the dividends did not arise from the con-

tributions of private shareholders but rather entirely reflect risks borne by the Treasury and taxpayers."

Judge Lamberth blocks a revival of the old Fannie Mae scam.

Every nickel the mortgage monsters earn comes courtesy of the taxpayers. The firms have two principal businesses: guaranteeing bundles of mortgages sold to other investors, and investing in mortgages themselves. Neither business would exist without Uncle Sugar.

As Alex Pollock of the American Enterprise Institute has noted, "What is the value of a guaranty from a guarantor with hugely negative capital? Zero. It is solely the fact that the government guarantees Fannie and Freddie's obligations that gives this business any revenue or profit at all."

But even the mortgage-guarantee business hasn't been generating profits for Fannie, say Andy Laperriere and his colleagues at Cornerstone Macro. They note that its "net earnings are completely due to its large portfolio of mortgages it holds. These earnings come from earning a spread on its mortgages compared to its cost of borrowing. So how does an insolvent company borrow at close to a risk-free rate and earn a spread on its massive portfolio of mortgages? Only because of the government support, of course."

If Judge Lamberth's ruling withstands appeal, it will have the side benefit of breaking up the political constituency that has sustained the economically disastrous policy at the core of Fannie and Freddie. The two firms were designed to serve Washington and Wall Street. The politicians collected campaign contributions from Fan and Fred while using the firms to allocate credit. Meanwhile, Fan and Fred investors and banks were able to profit from the implied government guarantee.

The shareholders in the suit are mainly big-money speculators who hope to make a killing on the upside if the politicians revive Fan and Fred. Gambling on politics is their right, but it's a little rich to then whine when the politicians they're canoodling with decide to confiscate their taxpayer-guaranteed profits.

This brawl has been like watching Godzilla vs. The Thing. With private subsidy-seekers perhaps out of the picture, taxpayers may now have a better shot at beating Godzilla.

ObamaCare's Wonderland

One of the four major legal challenges to ObamaCare advanced in Oklahoma on Tuesday, as a federal district court struck down the federal subsidies that are nowhere authorized in the Affordable Care Act. The order is stayed pending appeal to the Tenth Circuit Court of Appeals, so all the more reason for the Supreme Court to resolve the legal turbulence posthaste.

In *Oklahoma v. Burwell*, Judge Ronald White held that the Administration cannot ignore the plain text of the Affordable Care Act—which limits insurance subsidies to exchanges established by states—by sending out these dollars through the 36 federal exchanges too. He writes that "the court is upholding the Act as written. Congress is free to amend the ACA to provide for tax credits in both state and federal exchanges, if that is the legislative will."

A panel of the D.C. Circuit Court of Appeals came to the same conclusion in the *Halbig* case, though it was later vacated by the en banc court. The Fourth Circuit upheld the fed-

eral subsidies in a separate case, *King*, which has been appealed to the Supreme Court. Judge White's opinion reads almost like an amicus brief to the High Court, sparring with the reasoning of the opinions and dissents in those earlier cases.

Judge White also invokes a 1998 Tenth Circuit precedent called *Sundance Associates v. Reno*, which held that neither judges nor regulatory agencies possess "the authority to rewrite a poor piece of legislation (if, indeed, that is what it is). That responsibility lies solely with Congress." The alternative "leads us down a path toward Alice's Wonderland, where up is down and down is up, and words mean anything."

The White House would prefer that ObamaCare remain in such a legal wonderland for as long as possible, but multiple federal courts have made conflicting rulings. The relevant questions are now squarely in front of the Supreme Court, and for the sake of the law and the future of health policy the Justices should accept an appeal of the *King* case for their term that begins next week.

What's at Stake in Hong Kong

The size of the pro-democracy protests in Hong Kong this week surprised even their organizers. Some 10,000 people were expected to take part, but protesters from all ages and incomes have emerged by the hundreds of thousands. And their numbers continue to swell.

Why? For 30 years Hong Kong residents have asked for a say in their system of government. And for just as long China has told them to focus on business and be patient. The desire for self-government is natural when a society becomes as affluent as Hong Kong. But talk to the protesters and another theme emerges: saving the qualities that make their city unique. They want democracy as a bulwark against the influx of mainland authoritarian values.

The experience of Hong Kong under Chinese rule shows that the subsidiary institutions of a free society—rule of law, civil liberties, an independent civil society, free markets—can't survive long in the face of authoritarian assault. The British colonial government bequeathed the software of freedom to the city. After the handover in 1997, some of us hoped that China would emulate Hong Kong. Instead China is slowly bringing Hong Kong down to its level.

Take the Independent Commission Against Corruption, formerly one of the city's most respected institutions. Under the leadership of Simon Peh and Timothy Tong, a security official who worked on legislation to restrict civil liberties in 2003, the ICAC took on a mainland mien. Two months ago the ICAC launched an investigation into several opposition figures.

Meanwhile, Beijing has stepped up its use of local front groups such as the Federation of Trade Unions, which can be relied on to turn out largely elderly crowds for anti-democracy protests. State-run newspapers serve as China's mouthpieces in the city and run smear

campaigns against opposition figures. Beijing has forged links with local mafia "triads," which have attacked several journalists and politicians. Its hackers attack the computers of pro-democracy groups.

The decision to deploy riot police to use tear gas against peaceful students on Sunday reflects the local government's increasingly hard line under Chief Executive Leung Chun-ying. During the 2012 selection process, Mr. Leung was accused by a former colleague of having advocated the use of riot police against protesters in 2003. Immediately after the handover, Mr. Leung also denounced legislators for criticizing government officials.

The good news is that Hong Kong still has a few bulwarks against Beijing's attempts to rule by fear. The Bar Association condemned the police use of tear gas as excessive and disproportionate, as did the leaders of Hong Kong University.

Officials have repeatedly called for the judiciary to be "patriotic" and work in tandem with the executive branch, but so far judges have defended their independence. After police arrested student leader Joshua Wong on Friday night and held him for 40 hours without charge, a High Court judge found his detention unreasonable and granted a writ of habeas corpus.

Chinese intimidation and cronyism may not bother Hong Kong's wealthiest residents, who are used to cutting deals and making money in China. But it horrifies ordinary Hong Kong residents, many of whom fled the mainland looking for something better.

That solidarity may protect Hong Kong. The tighter Beijing squeezes, the more disgusted the city becomes with its tactics. With their understanding that democracy is about both political choice and moral values, the people of Hong Kong are today in the vanguard of the global fight for freedom.

LETTERS TO THE EDITOR

On American Democracy and a Patriotic Education

In Donald Kagan's opinion, as expressed in "Democracy Requires a Patriotic Education" (op-ed, Sept. 27), "neither family nor nation can flourish without love, support and defense." I agree.

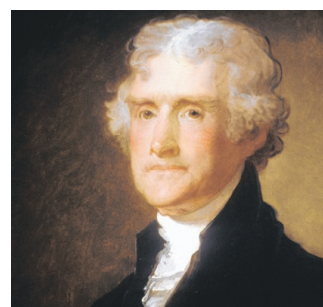
But I would argue that feelings cannot be taught. Parents don't instruct their children to love them, and teachers cannot educate students to love their country. What the most effective adults do is provide the environment, tools and exemplary behavior for young people to develop their own responses. Education may indeed produce patriotism, but teaching students how to feel borders on indoctrination. Feelings like love, respect and patriotism are earned, not taught.

KATHERINE BALCH
Fanwood, N.J.

That "democracy requires a patriotic education" is painfully clear. And more painful is how clear it is that the country has moved in the opposite direction. I see our colleges dwell on slavery and colonialism instead of what this coun-



Plato and Aristotle by Raphael, and Thomas Jefferson by Gilbert Stuart.



Getty Images (2)

try has achieved in providing life, liberty and the pursuit of happiness. I see our leaders make apologies for our past. By the way, our past includes building a free representative democracy. Perfect? No. But where else would you want to be born? If you can name a place, move.

After college, I see our politicians educating our citizens with campaigns like "the war on women," the "1%," "you did not build it," demonizing many industries, and that it is your "right" to all kinds of services. These campaigns are negative, they divide. They teach people to hate and ask for free stuff.

The time has come for our country to brag about our culture and accomplishments as we educate our citizens. Yes, we need to acknowledge our

mistakes, but only after it is clear that we are patriotic Americans.

GUY RANDOLPH
Savannah, Ga.

Donald Kagan's speech about patriotism reminded me that when I was in school, from kindergarten through high school (I graduated in 1963), we started every day with the Pledge of Allegiance. Every classroom in America had an American flag standing in the corner—48 stars before Hawaii and Alaska joined the Union. When did we stop saying the Pledge in our schools (public and private)? This country gives us more rights and freedoms than any nation on earth; it would behoove us to acknowledge that every day.

ANN C. LYNN
Scottsdale, Ariz.

We Don't Need Perfect Knowledge to Act on the Climate

Steven E. Koonin's essay "Climate Science Is Not Settled" (Review, Sept. 20) isn't an accurate reflection of the current state of climate science. We have spent our careers developing computer models of the climate system, comparing models with observations and studying the causes of climate change. Over our lifetimes a human-caused warming signal has emerged from the background noise of natural climate variability. This warming signal is discernible not only over the land surface, but also in the Earth's oceans, lower atmosphere, and snow and ice cover. Our best understanding—from observations, basic physics and models—is that the global climate changes observed over the last century are largely human driven. They aren't

"comparable to the intrinsic, natural variability of the climate system itself."

Models will always have important uncertainties in the size, rate and regional details of the climatic shape of things to come. These uncertainties are dealt with openly and transparently in the climate-science community and aren't relegated to "hushed sidebar conversations at academic conferences." They are quantified in all documents of the recent assessment of the Intergovernmental Panel on Climate Change.

Uncertainties in projections of 21st century climate change shouldn't be an excuse for policy inaction. The longer we delay concerted action to reduce emissions of greenhouse gases, the more difficult it will be to avoid dangerous interference

with the climate system. Time is a luxury we don't have.

We welcome the constructive collaboration of the physics community in improving our understanding of the human fingerprint on climate. This collaboration has a long and rich history. Many climate scientists are trained physicists, who decided to work on an important problem that impacts every person on this planet. We invite Dr. Koonin to join their ranks. Actively advancing scientific understanding of human-caused climate change and its consequences is a much tougher task than pronouncing judgment on the maturity and credibility of climate science.

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We Ignore Mortgage Crisis's Lessons

Regarding "Mortgage Lending Poses Puzzle" (U.S. News, Sept. 22), low mortgage supply is the direct result of the past five years of overregulation litigation and government intervention. Mortgage lenders aren't going to deviate from the current ultraconservative underwriting standards as long as the current administration is shaking down the big banks for billions of dollars for supposedly making bad loans before the financial crisis (even though many of these loans met the underwriting and documentation guidelines in effect at the time the loans were made).

FNMA and FHLMC are now owned by Uncle Sam, and mortgage lenders must measure the risk of being forced to repurchase mortgages sold to these government-sponsored enterprises for what in many cases are absurd techni-

calities. If clear guidelines for borrower qualification and the required documentation related thereto are met, then mortgage lenders should be provided with comfort that there won't be a future indemnification request from the GSEs should the loan default or otherwise. No such comfort exists today, hence the ultratight standards.

Many individuals with high credit scores and enough money for a down payment are frozen out of today's market for minor technicalities. While this helps explain why a number of opportunistic folks are working hard to make nonqualified mortgage lending a bigger piece of the market, such efforts aren't a substitute for a more rational approach to loan-indemnification policies by the GSEs.

DAVID C. FLEIG
Sugar Land, Texas

Mr. Lew's Counterproductive Policy

Regarding your editorial "Can Jack Lew Add?" (Sept. 24): The cynicism in Treasury Secretary Jack Lew's "unilateral diktat designed solely with an election in mind," as you put it, is that even an untutored outsider like myself realizes that these new regulations will have exactly the opposite effects of those proclaimed by Mr. Lew. They will put a damper on business investment and profits which will be compensated for by increasing cutbacks, increasing the trend from full-time employment to part time and outright layoffs.

For all those struggling workers trying to keep their and their families' heads above water, it will increase anxieties, but not, the administration hopes, before the November elections.

For those elections, the administration would like to implant the image of the fat capitalist lounging in his chair, puffing his cigar while the sacks of money flow up to him from his struggling worker ants below, with the administration as Sir Galahad. Perhaps this cynical image will carry the day in November. What happens after that matters not.

FREDERIC WILE
New York

Jack Lew's new regulations to limit corporate inversions are shortsighted. The new regulations aim to limit inversions by limiting corporations from bringing back foreign earnings tax free by requiring foreign parent companies to be engaged in actual business activities in the foreign country, but don't prevent foreign companies using debt to strip earnings from their U.S. subsidiaries via interest payments.

RALPH JEDDA
Peoria, Ariz.

Airbnb World's Fine, Until There's a Claim

The article "The Hidden Income Inside Your Home" (Journal Report, Sept. 22) doesn't mention liability. I am guessing personal-injury lawyers are salivating over the Airbnb environment when a guest has a slip or fall. There goes the house and the retirement portfolio. And good luck filing a claim with your existing insurance carrier if you didn't buy a liability rider or forgot to mention that you were using your house for a commercial activity.

HARRY POPE
Long Beach, Calif.

Minority Rights Not In the Constitution

In his Bookshelf review of Erwin Chemerinsky's "The Case Against the Supreme Court" (Sept. 25), Terry Eastland writes: "It appears that in every case in which the rights of the minority and the right of the majority to govern are pitted against each other in a lawsuit, Mr. Chemerinsky believes that minority rights should win." This demonstrates that Mr. Chemerinsky is merely an ideologue.

Nowhere does the Constitution recognize majority or minority rights, or that one set of rights should be protected against another. The Constitution establishes and defends individual rights, which are the same for both minorities and the majority. According to the philosophy of the Constitution, only "negative rights" were to be recognized and protected. A negative right isn't a right to be provided with something, but the right not to be harmed or interfered with in the pursuit of it.

The concepts of minority and majority rights are modern notions that belong in the category of "group or positive rights," which declare a right of one group to be provided for by another. The Constitution and the Declaration of Independence rejected such poly-logistic philosophy as a violation of individual rights.

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