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**UNITED STATES DISTRICT COURT  
NORTHERN DISTRICT OF CALIFORNIA  
OAKLAND DIVISION**

PEOPLE OF THE STATE OF CALIFORNIA )  
*ex rel.* EDMUND G. BROWN, JR., )  
ATTORNEY GENERAL )

Plaintiff,

v.

FEDERAL HOUSING FINANCE AGENCY, )  
EDWARD DeMARCO, in his capacity as )  
Acting Director of FEDERAL HOUSING )  
LOAN MORTGAGE CORPORATION; )  
CHARLES E. HALDEMAN, JR., in his )  
capacity as Chief Executive Officer of )  
FEDERAL HOME LOAN MORTGAGE )  
CORPORATION; FEDERAL NATIONAL )  
MORTGAGE ASSOCIATION; MICHAEL J. )  
WILLIAMS, in his capacity as Chief )  
Executive Officer of FEDERAL NATIONAL )  
MORTGAGE ASSOCIATION )

Defendants.

CASE NO. 4:10-CV-03084-CW

**DEFENDANTS’ MOTION TO DISMISS  
AND SUPPORTING MEMORANDUM  
OF POINTS AND AUTHORITIES**

DATE: December 2, 2010

TIME: 2:00 pm

COURTROOM: Courtroom #2

JUDGE: The Honorable Claudia Wilken

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COUNTY OF SONOMA, )  
)  
Plaintiff, )  
)  
v. )  
)  
FEDERAL HOUSING FINANCE AGENCY;) )  
EDWARD DeMARCO, in his capacity as )  
Acting Director of FEDERAL HOUSING )  
FINANCE AGENCY; FEDERAL HOME )  
LOAN MORTGAGE CORPORATION; )  
CHARLES E. HALDEMAN, JR. in his )  
capacity as Chief Executive Officer of )  
FEDERAL HOME LOAN MORTGAGE )  
CORPORATION; FEDERAL NATIONAL )  
MORTGAGE ASSOCIATION; MICHAEL J. )  
WILLIAMS, in his capacity as Chief )  
Executive Officer of FEDERAL NATIONAL )  
MORTGAGE ASSOCIATION, )  
)  
Defendants. )

**Case No. 4:10-CV-03270-CW**

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SIERRA CLUB, )  
)  
Plaintiff, )  
)  
v. )  
)  
FEDERAL HOUSING FINANCE AGENCY;) )  
EDWARD DeMARCO, in his capacity as )  
Acting Director of FEDERAL HOUSING )  
FINANCE AGENCY; )  
)  
Defendants. )

**Case No. 4:10-CV-03317-CW**

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1 **MOTION TO DISMISS AND NOTICE OF HEARING**

2 **TO ALL PARTIES AND THEIR ATTORNEYS OF RECORD:**

3 PLEASE TAKE NOTICE that on December 2, 2010 at 2:00 p.m., or such other date and  
4 time as the Court may direct, in Courtroom 2 of the U.S. District Court, 1301 Clay Street, Oakland,  
5 CA 94612, Defendants will appear to argue this motion to dismiss three related actions pending in  
6 this Court — *California v. Federal Housing Finance Agency* (No. 4:10-cv-03084-CW), *County of*  
7 *Sonoma v. Federal Housing Finance Agency* (No. 4:10-cv-03370-CW), and *Sierra Club v. Federal*  
8 *Housing Finance Agency* (No. 4:10-cv-03317-CW).

9 By this motion, Defendants Federal Housing Finance Agency, Federal Home Loan  
10 Mortgage Corp., Federal National Mortgage Association, DeMarco, Haldeman, and Williams  
11 respectfully ask the Court to dismiss the actions in their entirety and with prejudice, pursuant to  
12 Fed. R. Civ. P. Rules 12(b)(1) and 12(b)(6). Defendants have submitted contemporaneously  
13 herewith the Declaration of Scott Border and a Request for Judicial Notice covering many of the  
14 non-legal sources cited herein.

15 **MEMORANDUM OF POINTS AND AUTHORITIES**

16 **INTRODUCTION**

17 In these actions, Plaintiffs seek to enjoin the federal regulator and Conservator of Fannie  
18 Mae and Freddie Mac (the “Enterprises”) from undertaking the central mission entrusted to it by  
19 Congress — the prompt identification and mitigation of risks and practices inconsistent with the  
20 safe and sound conduct of the Enterprises’ financial operations.

21 Plaintiffs advocate financing energy-related home-improvement projects through liens that,  
22 as to properties with outstanding mortgages, shift the risk of default from the provider of the home-  
23 improvement funds to the mortgage holder. Cal. Am. Compl. ¶ 21.<sup>1</sup> Shifting risk from another  
24 creditor to the mortgage holder in this way makes mortgage loans and mortgage-related assets  
25 riskier and less valuable. Plaintiffs not only admit this fact, they embrace it — Plaintiff California  
26 quantifies the incremental “risk” such programs pose, computing the diminution in the value of an

27 \_\_\_\_\_  
28 <sup>1</sup> Plaintiff Sonoma County operates a PACE program. Plaintiffs California and Sierra Club do not, but assert that their citizens and members respectively may benefit from such programs.

1 “average” mortgage encumbered by Plaintiffs’ programs. Cal. Am. Compl. ¶ 41.<sup>2</sup> Other facets of  
2 PACE programs exacerbate those already-serious financial risks. For example, no uniform  
3 underwriting criteria apply, and many PACE programs apply credit standards that are plainly  
4 insufficient to meet any credible standard of financial prudence.

5 Fannie Mae and Freddie Mac hold more than \$5 *trillion* in mortgage-related assets, but  
6 would be insolvent and in receivership but for quarterly infusions of taxpayer capital contributed by  
7 the U.S. Treasury. Hence, even a minor diminution in the value of a small fraction of mortgages in  
8 the Enterprises’ portfolios could deplete the Enterprises’ net worth, disrupting the enormously  
9 costly federal effort to stabilize the Enterprises and leaving taxpayers at even greater risk of  
10 financial loss. In effect, Plaintiffs would export much of the financial risk associated with  
11 California PACE programs to taxpaying residents of other states.

12 Assessment and management of such risks is the primary responsibility of the Federal  
13 Housing Finance Agency (“FHFA”), which presently acts in two relevant statutory capacities with  
14 respect to the Enterprises. *First*, FHFA is the congressionally appointed supervisory regulator of  
15 Fannie Mae and Freddie Mac. As such, FHFA is charged with the responsibility to ensure that the  
16 Enterprises operate safely and soundly. *Second*, FHFA is also the Conservator of Fannie Mae and  
17 Freddie Mac. As Conservator, FHFA directs the Enterprises’ operations with a mandate to  
18 “preserve and conserve the [Enterprises’] assets and property.”

19 On July 6, 2010, after meeting with stakeholders and studying programs such as those run  
20 by Plaintiffs (known generically as Property Assessed Clean Energy, or “PACE,” programs) for  
21 more than a year, FHFA issued a Statement expressing “significant safety and soundness concerns”  
22 with PACE programs and directing the Enterprises to take certain “prudential actions” to “protect  
23 their safe and sound operations” in light of the risks. The Enterprises, under FHFA’s  
24 conservatorship, have since announced that they will no longer purchase mortgages subject to a  
25 PACE obligation.

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28 <sup>2</sup> Plaintiffs’ assertion that the incremental risk is “miniscule,” Cal. Am. Compl. ¶ 41, is not  
correct. *See* fn. 37 *infra*.

1 Plaintiffs' lawsuits claim that "FHFA has effectively precluded PACE programs in  
 2 California." Cal. Am. Compl. ¶ 4. They demand that the Court "set aside FHFA's July 6, 2010  
 3 Statement" and "enjoin[] Fannie Mae or Freddie Mac from taking any adverse action against any  
 4 mortgagee [that] is participating, or may participate, in [such] program[s] under California law, or  
 5 other action that has the effect of chilling [such] programs in California." *Id.* at Prayer ¶¶ 2, 5. In  
 6 essence, Plaintiffs ask the Court (i) to enjoin FHFA from doing its statutory job — as regulator and  
 7 as Conservator — of taking the risks associated with PACE programs into account in supervising  
 8 and directing the Enterprises' operations, and (ii) to force the Enterprises to bear those risks.

### 9 SUMMARY OF THE ARGUMENT

10 In response to their identification of a serious financial risk, Defendants acted responsibly,  
 11 appropriately, and legally. FHFA did what Congress had expressly directed it to do — FHFA  
 12 diligently investigated and analyzed an emerging risk to the safety and soundness of the financial  
 13 institutions it supervises. FHFA then engaged with state and local authorities regarding FHFA's  
 14 concerns, sought changes to the programs (including necessary consumer protections and energy  
 15 retrofit standards) and ultimately directed the Enterprises to take reasonable and prudential actions  
 16 to protect their safe and sound operations in light of that risk. The Enterprises, in conservatorship,  
 17 did what their federal charters authorized and what safe and sound financial practice dictated —  
 18 they took reasonable steps to protect their portfolios from the risks posed by PACE programs.  
 19 Hence, Defendants are confident that any evenhanded review of FHFA's actions as regulator and  
 20 Conservator challenged in this litigation would determine that those actions were soundly  
 21 conceived, legally authorized, adequately supported, and reasonably implemented.

22 The Court need not undertake such a review; indeed, Congress has mandated that it cannot.  
 23 Three specific statutory provisions divest all courts of any jurisdiction to grant the relief Plaintiffs  
 24 seek:

- 25 • 12 U.S.C. § 4617(f) mandates that "*no court may take any action to*  
 26 *restrain or affect the exercise of powers or functions of the Agency as*  
*conservator*";
- 27 • 12 U.S.C. § 4635(b) mandates that "*no court shall have jurisdiction to*  
 28 *affect, by injunction or otherwise, the issuance or enforcement of any*  
*notice or order*" under certain statutory provisions implicated here; and,

- 1           • 12 U.S.C. § 4623(d) mandates that “*no court shall have jurisdiction to*  
2           *affect, by injunction or otherwise, the . . . effectiveness of any . . . action*  
3           *of the Director*” under the relevant statutory provisions.

4 Hence, this action must be dismissed under Rule 12(b)(1) for want of subject-matter jurisdiction, an  
5 absolute bar to judicial review that neither Defendants nor the Court can waive.

6           Moreover, even if Congress had not divested the Court of jurisdiction to hear Plaintiffs’  
7 claims, those claims would all still be subject to dismissal under Rule 12(b)(6) for failure to state a  
8 claim upon which relief could be granted:

- 9           • Plaintiffs’ state-law claims for purported unfair competition and  
10           interference with prospective economic advantage fail because the  
11           provisions of state law upon which Plaintiffs rely are pre-empted by  
12           federal law. Moreover, Plaintiffs have not alleged, and cannot  
13           plausibly allege, the factual elements that are a prerequisite to their pre-  
14           empted state-law claims.
- 15           • Plaintiffs’ claim for a declaratory judgment that their programs involve  
16           “assessments” and not “loans” and that Defendants’ mischaracterized  
17           the PACE program is non-justiciable because it would resolve a purely  
18           semantic dispute of no legal consequence. The Enterprises’ Uniform  
19           Security Instrument (“USI”) requires borrowers to discharge any liens  
20           that have priority over the mortgage loan, regardless of whether they  
21           result from an “assessment” or a “loan.” In any event, Plaintiffs  
22           themselves have publicly, repeatedly, and authoritatively confirmed  
23           that their programs *do* involve “loans.”
- 24           • Plaintiffs’ claims that FHFA’s actions contravene the Administrative  
25           Procedure Act (“APA”) fail because Plaintiffs are not in the zone of  
26           interests protected by the statute under which FHFA acted, the Housing  
27           and Economic Recovery Act of 2008 (“HERA”), and because FHFA  
28           has not issued any rule or regulation subject to notice and comment  
            under the APA.
- Plaintiffs’ National Environmental Policy Act (“NEPA”) claim fails  
            because jurisdiction is lacking, because nothing FHFA did constitutes  
            “major federal action,” and because NEPA’s procedural requirements  
            did not attach since FHFA is not empowered to subordinate safety and  
            soundness to environmental considerations, no matter how laudable.

            Plaintiffs offer no specific allegations as to the individual defendants sued in their official  
capacities: Messrs. DeMarco, Haldeman, and Williams. This failure provides independently  
sufficient grounds for dismissal of all claims as to those defendants.<sup>3</sup>

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<sup>3</sup> The collective term “Defendants” is used throughout this brief for convenience and without  
waiver of this facial defect in Plaintiffs’ allegations as to the individuals.

**STATEMENT OF FACTS**

**A. Statutory Powers and Obligations of FHFA**

FHFA is an independent federal agency created by HERA to supervise and regulate Fannie Mae, Freddie Mac and the Federal Home Loan Banks (“Banks”). 12 U.S.C. § 4501 *et seq.*; California Amend. Compl. ¶ 14; Sierra Club Compl. ¶ 21. Congress established FHFA in 2008 in the wake of a national crisis in the housing market. A key purpose of HERA was to create a single federal regulator with all of the authorities necessary to oversee critical components of our country’s secondary mortgage markets — Fannie Mae, Freddie Mac, and the Banks. 12 U.S.C. § 4511(b)(2). “[HERA] combined the staffs of the Office of Federal Housing Enterprise Oversight (OFHEO), the Federal Housing Finance Board (FHFB), and the [government sponsored enterprise] mission office at the Department of Housing and Urban Development (HUD).” *About FHFA*, FEDERAL HOUSING FINANCE AGENCY, <http://www.fhfa.gov/Default.aspx?Page=4> (“*About FHFA*”) (last visited Oct. 14, 2010).

Fannie Mae and Freddie Mac are government sponsored enterprises that facilitate the secondary market in residential mortgages by purchasing loans from mortgage lenders, thereby freeing up capital for additional mortgage lending. Cal. Am. Compl. ¶¶ 10, 12, 3; Sonoma Compl. ¶¶ 7, 9. Fannie Mae and Freddie Mac are presently in conservatorship and being operated by FHFA in its capacity as Conservator.<sup>4</sup> The Enterprises hold or securitize and guarantee the mortgages they acquire. Fannie Mae and Freddie Mac together own or guarantee about half of all residential home mortgages. Cal. Am. Compl. ¶ 3; Sonoma Compl. ¶¶ 7, 9; Sierra Club Compl. ¶ 11. As of June 2008, the Enterprises’ combined debt and obligations totaled \$6.6 trillion — exceeding the national debt by \$1.3 trillion.<sup>5</sup>

As their regulator, FHFA oversees the operations of the Enterprises in an effort to assure that they operate in a financially safe and sound manner; remain adequately capitalized; and comply with their respective authorizing statutes, as well as all rules, regulations, guidelines, and orders

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<sup>4</sup> We refer in this brief to Fannie Mae and Freddie Mac in conservatorship as “the Enterprises.”

<sup>5</sup> *About FHFA*.

1 issued under law. 12 U.S.C. § 4513(a). To carry out its statutory mission, FHFA is empowered  
 2 with an array of supervisory, examination, and enforcement tools. For example, HERA empowers  
 3 the Director of FHFA to “issue any regulations or guidelines or orders as necessary to carry out the  
 4 duties of the Director,” including but not limited to ensuring that the Enterprises are adequately  
 5 capitalized and operating safely. 12 U.S.C. §§ 4526(a), 4511(b)(2), 4513(a). Guidelines and  
 6 orders, as opposed to regulations, are not subject to the notice and comment provisions of the APA.  
 7 *See* 12 U.S.C. § 4526. Under HERA’s authority, the FHFA Director issues policy guidance and  
 8 directives to Fannie Mae, Freddie Mac, and the Banks addressing specific safety and soundness  
 9 concerns, including the guidance and directives Plaintiffs challenge here.<sup>6</sup>

10 Congress, in order to facilitate the prompt and effective exercise of the FHFA’s supervisory  
 11 and regulatory expertise, sharply limited judicial oversight of the FHFA’s supervision and  
 12 regulation of the Enterprises. Specifically, drawing directly from the supervisory and regulatory  
 13 scheme long in place with respect to the federal financial institution regulatory agencies, Congress  
 14 directed that “no court shall have jurisdiction to affect, by injunction or otherwise,” either (a) “the  
 15 issuance or enforcement of any notice or order” under certain of HERA’s supervisory provisions, or  
 16 (b) “the issuance or effectiveness of any . . . action of the Director” under a different but  
 17 overlapping set of HERA’s supervisory provisions. 12 U.S.C. §§ 4635(b), 4623(d).

## 18 **B. The Conservatorships**

19 Immediately following passage of HERA in July 2008, FHFA, the Department of the  
 20 Treasury (“Treasury”), and the Federal Reserve undertook a comprehensive financial review of the  
 21 Enterprises.<sup>7</sup> At the same time, the national housing market was deteriorating. On September 6,  
 22

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23  
 24 <sup>6</sup> *See, e.g.*, OFHEO Policy Guidance PG-00-001, Minimum Safety and Soundness Requirements  
 25 (December 19, 2000), *available at* <http://www.fhfa.gov/webfiles/1336/pg00001.pdf> (subsequently  
 26 issued as regulation: Safety and Soundness Regulation, 67 Fed. Reg. 55691 (Aug. 30, 2002),  
*available at* [http://www.fhfa.gov/webfiles/1880/20020830\\_Final\\_Rule\\_FR.pdf](http://www.fhfa.gov/webfiles/1880/20020830_Final_Rule_FR.pdf)). *See also* 12  
 U.S.C. § 4511.

27 <sup>7</sup> Remarks by Treasury Secretary Henry M. Paulson, Jr. on the Role of the GSEs [*i.e.*, the  
 28 Enterprises] in Supporting the Housing Recovery before the Economic Club of Washington (Jan. 7,  
 2009) (“Paulson Remarks”), *available at* <http://ustreas.gov/press/releases/hp1345.htm> (Border Decl.  
 Ex. 1).

1 2008, the Director placed Fannie Mae and Freddie Mac into conservatorship “for the purpose of  
2 reorganizing, rehabilitating or winding up the[ir] affairs.” 12 U.S.C. § 4617(a)(2). It quickly  
3 became apparent that the Enterprises could not continue to operate without infusions of billions of  
4 taxpayer dollars by Treasury.<sup>8</sup> Treasury entered into Preferred Stock Purchase Agreements with the  
5 Conservator, which was acting on behalf of the Enterprises, to ensure that the Enterprises  
6 maintained positive net worths and avoided receivership, which would have worsened the financial  
7 crisis. The Conservator is authorized to draw on that Agreement at the end of each quarter to make  
8 up any deficiency in the Enterprises’ net worth.<sup>9</sup> Through August 31, 2010, Treasury has advanced  
9 \$148 billion to the Enterprises through the Conservators’ draws.<sup>10</sup> Any losses incurred through  
10 December 31, 2012 will be backed up by the Treasury: that is, by taxpayers across the United  
11 States.<sup>11</sup>

12 As Conservator, FHFA is charged with taking any action “necessary to put the regulated  
13 entity into sound and solvent condition” and “appropriate to carry on the business of the regulated  
14 entity and preserve and conserve the assets and property of the regulated entity.” 12 U.S.C.  
15 § 4617(b)(2)(D). HERA provides the Conservator with extensive powers to accomplish its  
16 statutory mission. FHFA “by operation of law, immediately succeed[ed] to all rights, titles and  
17 powers, and privileges of the shareholders, directors, and officers of the regulated entity” and is  
18 empowered to (i) take over the assets of and operate the regulated entity; (ii) collect all obligations  
19 and money due the regulated entity; (iii) perform functions of the regulated entity consistent with  
20 appointment of the Conservator; and (iv) exercise such incidental powers as may be necessary to  
21 carry out all powers and authorities specifically granted. 12 U.S.C. § 4617(b)(2)(A), (B), (J).

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23  
24 <sup>8</sup> Paulson Remarks, *supra* fn.7.

25 <sup>9</sup> FHFA, Data as of October 1, 2010 on Treasury and Federal Reserve Purchase Programs for  
26 GSE [*i.e.*, Enterprise] and Mortgage-Related Securities at 1-2 (Oct. 1, 2010), *available at*  
<http://www.fhfa.gov/webfiles/17990/TreasFED10012010.pdf> (Border Decl. Ex. 2).

27 <sup>10</sup> *Id.* at 2.

28 <sup>11</sup> Treasury Issues Update on Status of Support for Housing Programs (updated Jan. 5, 2010),  
[http://www.financialstability.gov/latest/pr\\_1052010b.html](http://www.financialstability.gov/latest/pr_1052010b.html) (Border Decl. Ex. 3).

1 Congress has directed that the Conservator's powers are to be exercised without interference  
 2 from any state or federal agency, or any court, mandating that "no court may take any action to  
 3 restrain or affect the exercise of powers or functions of the Agency as conservator," 12 U.S.C.  
 4 § 4617(f), and that "[w]hen acting as conservator or receiver, the Agency [is] not subject to the  
 5 direction or supervision of any other agency of the United States or any State in the exercise of the  
 6 rights, powers and privileges of the Agency." *Id.* § 4617(a)(7).

7 Pursuant to its statutory authority, the Conservator has assumed the power of the  
 8 Enterprises' Boards of Directors and management.<sup>12</sup> One of the central goals of the  
 9 conservatorships is the mitigation of losses, and in that regard the Conservator has made improving  
 10 underwriting standards and the quality of assets purchased a principal focus.<sup>13</sup> As a result, the loans  
 11 purchased since the appointment of the Conservator have had much lower rates of serious  
 12 delinquency. The risks associated with continued housing market price declines, especially on  
 13 loans originated in four particularly hard-hit states (including California), present a continuing and  
 14 difficult challenge for FHFA and the Enterprises.<sup>14</sup> Indeed, because of continuing losses associated  
 15 with pre-conservatorship purchases, as well as forecasted losses not yet realized, FHFA continues to  
 16 designate both Enterprises as presenting "critical supervisory concerns."<sup>15</sup>

### 17 C. PACE Programs

18 PACE programs permit local governments to offer individual property owners government  
 19 loans to fund energy retrofits to their homes. Homeowners repay the amount borrowed, with

20 \_\_\_\_\_  
 21 <sup>12</sup> Statement of FHFA Director James B. Lockhart at 7 (Sept. 7, 2008), *available at*  
 22 <http://www.fhfa.gov/webfiles/23/FHFASStatement9708final.pdf>.

23 <sup>13</sup> "Current State of the Government Sponsored Enterprises," Statement of Edward DeMarco,  
 24 Acting Director, Federal Housing Finance Agency, Before the U.S. House of Representatives  
 25 Subcommittee on Capital Markets, Insurance and Government Sponsored Enterprises at 6-7 (May  
 26 26, 2010) ("DeMarco Stmt.") at 6-7, *available at* <http://www.fhfa.gov/webfiles/15790/52610>  
 27 [DeMarcoTestimony.pdf](http://www.fhfa.gov/webfiles/15790/52610/DeMarcoTestimony.pdf) (California house prices declined from peak through 4Q09 by 39%)  
 28 (Border Decl. Ex. 4); Conservator's Report on the Enterprises' Financial Performance, Second  
 Quarter 2010, at 12 (Aug. 26, 2010), *available at*  
<http://www.fhfa.gov/webfiles/16591/ConservatorsRpt82610.pdf> (in 2009, 24% and 32% of the total  
 credit losses by the Enterprises were for mortgages originating in California) (Border Decl. Ex. 5).

<sup>14</sup> Demarco Stmt., *supra* fn.13, at 6.

<sup>15</sup> Demarco Stmt., *supra* fn.13, at 6.

1 interest, over a period of years through “contractual assessments” added to their property tax bill.<sup>16</sup>  
 2 Over the last two years, more than 20 states have passed legislation authorizing local governments  
 3 to set up PACE-type programs.

4 California PACE programs began “multiplying rapidly” across the state in 2008. Cal. Am.  
 5 Compl. ¶¶ 21-22. Plaintiff Sonoma County (“Sonoma”) is one of over 200 California  
 6 municipalities that have authorized implementation of a PACE program. Sierra Club Compl. ¶ 6.  
 7 Sonoma launched a pilot PACE program in March 2009. As of July 2010, Sonoma had financed  
 8 over 1,000 PACE loans.<sup>17</sup> Sonoma has continued its PACE program after FHFA issued its July 6  
 9 Statement.<sup>18</sup> In California, the liens that result from PACE program loans have priority over  
 10 mortgages, including pre-existing first mortgages.<sup>19</sup> The PACE lender “steps ahead” of the  
 11 mortgage holder in priority of its claim against the collateral, adversely increasing the risk of the  
 12 existing mortgage to its holder, a class that includes not only the Enterprises but also such investors  
 13 as pension funds and mutual funds. Such liens “run” with the property. As a result, the mortgage  
 14 holder becomes the effective guarantor of the PACE loan. A mortgagee foreclosing on a property  
 15 subject to a PACE lien must pay off any outstanding assessments and remains responsible for the  
 16 principal and interest payments that are not yet due. If a home is sold before the homeowner repays  
 17 the municipality, the purchaser of the home assumes the obligation to pay the remainder. Sonoma  
 18 Compl. ¶ 16.<sup>20</sup>

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21 <sup>16</sup> Cal. Am. Compl. ¶¶ 1, 21; Sonoma Compl. ¶¶ 14, 17 18; Sierra Club Compl. ¶ 2. *See also*  
 22 Cal. Streets & Hwy Code § 5898.14; Cal. Gov. Code § 53311 *et seq.*

23 <sup>17</sup> Cal. Am. Compl. ¶ 22; Sonoma Compl. ¶ 28.

24 <sup>18</sup> *See* Sonoma Compl. ¶ 46 (indicating that Sonoma continues to operate its PACE program)..

25 <sup>19</sup> Cal Am. Compl. ¶¶ 21, 33; Sonoma Compl. ¶ 16. Lien-priming is not inherent in PACE  
 financing; Maine has authorized PACE programs that do not include it. Me. Rev. Stat. tit. 35-A,  
 § 10156 (2010) (“A PACE mortgage is not entitled to any special or senior priority.”).

26 <sup>20</sup> When a homeowner is delinquent on the payment of property tax assessments, the mortgage  
 27 lender receives notice and must pay the arrearage to prevent a tax sale and avoid losing the lien on  
 28 the secured property. If a mortgage lender is not in control of the sale of the property, the lender  
 could lose its entire monetary interest in the property; there is no incentive in a tax sale to garner  
 more than the amount of the tax arrears.

1 Unlike traditional assessments, PACE loans are voluntary: that is, homeowners opt in,  
2 submit applications, and contract with the municipality's PACE program. Each participating  
3 property owner controls the use of the funds, owns the energy retrofit fixtures, and must repair the  
4 fixtures — with no county assistance — should they become inoperable while the liability remains.  
5 There are no uniform requirements for homeowner participation in these programs as each locality  
6 sets its own terms and requirements. There are also currently no national standards for certification  
7 of contractors or for the level of energy savings required to qualify for PACE financing. Moreover,  
8 nothing in PACE requires that uniform underwriting standards be implemented by the local  
9 programs, such as minimum total loan-to-value ratios that take into account either (i) total debt or  
10 other liens on the property, or (ii) the possibility of subsequent declines in the value of the  
11 property.<sup>21</sup> Nor does PACE employ standard homeowner creditworthiness requirements other than  
12 that the homeowner not be in bankruptcy or in default on the mortgage or taxes.<sup>22</sup> Some local  
13 PACE programs do communicate to homeowners that participation in PACE may violate the terms  
14 of their mortgage documents.<sup>23</sup> For this reason, some municipalities require participants to obtain  
15 the lender's consent prior to participation. Sonoma Consent Agreement at 4.

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18  
19 <sup>21</sup> Placer County Application at 2-3 (requiring that loan not exceed 10% of property value but no  
20 provision for decline in property values), [http://www.mpowerplacer.org/forms/  
21 Placer%20Application%20Written%20Form.pdf](http://www.mpowerplacer.org/forms/Placer%20Application%20Written%20Form.pdf) (“Placer App.”) (last visited Oct. 14, 2010)  
22 (Border Decl. Ex. 6); Sonoma County Application at 3 (retrofit costs must be “reasonable” relative  
23 to current property value, but no requirement of excess equity), [http://www.drivecms.com/uploads/  
24 sonomacountyenergy.org/application.pdf](http://www.drivecms.com/uploads/sonomacountyenergy.org/application.pdf) (“Sonoma App.”) (last visited Oct. 14, 2010) (Border  
25 Decl. Ex. 7).

26 <sup>22</sup> *See, e.g.*, Placer App., *supra* fn.21, at 2-3 (requiring only that property owner be current on  
27 property taxes and mortgage (with no defaults on taxes for the past three years and no default on  
28 mortgage for the past five years), that property owner not be in bankruptcy, that property owner not  
have a civil court record indicating failure to make payments within past five years, and that  
property not be subject to involuntary liens); Sonoma App., *supra* fn.21, at 3 (requiring only that  
property owner be current on property taxes and mortgage, that property owner not be in  
bankruptcy, and that property not be subject to involuntary liens).

<sup>23</sup> *See, e.g.*, Yucaipa Loan Application at 7, [http://www.yucaipa.org/cityPrograms/EIP/  
PDF\\_Files/Application.pdf](http://www.yucaipa.org/cityPrograms/EIP/PDF_Files/Application.pdf) (last visited Oct. 14, 2010) (Border Decl. Ex. 8); Sonoma App., *supra*  
fn.21, at 9.

**D. The Defendants’ Concerns Regarding PACE Programs**

As PACE programs were being considered by more states, Defendants began to evaluate their impact on the Enterprises’ portfolios. On June 18, 2009, FHFA issued a letter and background paper raising concerns about PACE programs, such as the programs at issue here, that retroactively created first liens. FHFA set forth the negative impact of such programs on the Enterprises, who, as holders of large portfolios of mortgage-related assets, are forced to take on the increased risk of default and exposure resulting from PACE loans, without any control over the underwriting of these loans. FHFA also explained that such programs may have negative consequences — not just for the Enterprises as mortgage holders, but also for “consumers facing increased mortgage interest rates, more restrictive borrower underwriting standards and reductions in both the availability and size of mortgage loans in areas with such programs.”<sup>24</sup> To discuss the risks to lenders and the Enterprises as well as borrowers, FHFA met with PACE stakeholders all over the country, including the California Attorney General and Sonoma County. FHFA also caucused with other federal financial-institution regulators, the White House National Economic Council, and the Departments of Energy and Housing and Urban Development. The intention of these discussions and the year-long effort by FHFA was to develop a structure for PACE that would address lenders’ and financial regulators’ concerns while providing consumers with safe access to energy efficiency lending.<sup>25</sup> Despite the significant efforts of those involved, a resolution that addressed the concerns of FHFA and other financial regulators has not been reached.

On May 5, 2010, in response to continuing questions about PACE programs, the Enterprises issued advisories (“Advisories”) to lenders and servicers of mortgages owned or guaranteed by the Enterprises.<sup>26</sup> Fannie Mae’s Advisory provided:

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<sup>24</sup> Letter from James B. Lockhart III, Director, FHFA, to Neil Milner, President and CEO, Conference of State Bank Supervisors, *et al.*, at 2 (June 18, 2009), *available at* <https://www.efanniemae.com/sf/guides/ssg/relatedsellinginfo/pdf/fhfaeltapletter.pdf> (attached as 9).

<sup>25</sup> *See also* FHFA, Legal and Market Issues Related to Energy Loan Tax Assessment Programs (ELTAPs) (Sept. 10, 2009) (attached to Sept. 17, 2009 letter from Alfred M. Pollard to Rodney A. Dole, County of Sonoma) (Border Decl. Ex. 10).

<sup>26</sup> Fannie Mae Lender Letter LL-2010-06 (May 5, 2010), *available at* <https://www.efanniemae.com/sf/guides/ssg/annltrs/pdf/2010/ll1006.pdf> (Border Decl. Ex. 11);

(Footnote Continued on Following Page)

1 Fannie Mae has received a number of questions from seller-servicers  
 2 regarding government-sponsored energy loans, sometimes referred to  
 3 as [PACE] loans. PACE loans generally have automatic first lien  
 4 priority over previously recorded mortgages. The terms of the Fannie  
 5 Mae/Freddie Mac Uniform Security Instruments prohibit loans that  
 have senior lien status to a mortgage. As PACE programs progress  
 through the experimental phase and beyond, Fannie Mae will issue  
 additional guidance to lenders as may be needed from time to time.

6 Freddie Mac's Advisory provided:

7 The purpose of this Industry Letter is to remind Seller/Servicers that an  
 8 energy-related lien may not be senior to any Mortgage delivered to  
 9 Freddie Mac. Sellers/Servicers should determine whether a state or  
 locality in which they originate mortgages has an energy loan program  
 and whether a first lien is permitted.

10 The May 5 Advisories referred to Fannie Mae's and Freddie Mac's jointly developed master  
 11 uniform security instruments ("USIs"), which prohibit liens senior to that of the mortgage.<sup>27</sup>

12 Shortly after the May 5 Advisories were issued, FHFA received a number of inquiries,  
 13 including from the California Attorney General, seeking FHFA's position.<sup>28</sup> On July 6, 2010,  
 14 FHFA affirmed its long-standing concerns with the assessment regime, the absence of enforceable  
 15 consumer protections, and the lack of national energy retrofit standards by issuing a Statement (the  
 16 "Statement") that, consistent with the views expressed in the Enterprises' Advisories, provided:<sup>29</sup>

17 After careful review and over a year of working with federal and state  
 18 government agencies, the Federal Housing Finance Agency (FHFA)  
 19 has determined that certain energy retrofit lending programs present  
 20 significant safety and soundness concerns that must be addressed by  
 Fannie Mae, Freddie Mac and the Federal Home Loan Banks . . . .

21 (Footnote Cont'd From Previous Page)

22 Freddie Mac Industry Letter (May 5, 2010), *available at*  
[http://www.freddiemac.com/sell/guide/bulletins/pdf/](http://www.freddiemac.com/sell/guide/bulletins/pdf/iltr050510.pdf)  
 23 [iltr050510.pdf](http://www.freddiemac.com/sell/guide/bulletins/pdf/iltr050510.pdf) ((Border Decl. Ex. 12).

24 <sup>27</sup> The relevant provision appears in Section 4. *See* Freddie Mac Form 3005, California Deed of  
 Trust, *available at* <http://www.freddiemac.com/uniform/doc/3005-CaliforniaDeedofTrust.doc>;  
 25 Fannie Mae Form 3005, California Deed of Trust, *available at* [https://www.efanniemae.com/sf/](https://www.efanniemae.com/sf/formsdocs/documents/secinstruments/doc/3005w.doc)  
 formsdocs/documents/secinstruments/doc/3005w.doc (Border Decl. Ex. 13).

26 <sup>28</sup> Letter from Edmund G. Brown, Jr. to Edward DeMarco (May 17, 2010) (Border Decl. Ex. 14);  
 Letter from Edmund G. Brown, Jr. to Edward DeMarco (June 22, 2010) (Border Decl. Ex. 15).

27 <sup>29</sup> California Amend. Compl. ¶ 4 (July 6 Statement "affirmed" May 5 Letters); Sonoma Compl. ¶  
 28 (July 6 Statement "confirms" May 5 Letters); Sierra Club Compl. ¶ 12 (July 6 Statement "echoes"  
 May 5 Letters).

1 First liens established by PACE loans are unlike routine tax  
2 assessments and pose unusual and difficult risk management challenges  
3 for lenders, servicers and mortgage securities investors. The size and  
4 duration of PACE loans exceed typical local tax programs and do not  
5 have the traditional community benefits associated with taxing  
6 initiatives.

7 FHFA urged state and local governments to reconsider these programs  
8 and continues to call for a pause in such programs so concerns can be  
9 addressed. First liens for such loans represent a key alteration of  
10 traditional mortgage lending practice. They present significant risk to  
11 lenders and secondary market entities, may alter valuations for  
12 mortgage-backed securities and are not essential for successful  
13 programs to spur energy conservation.<sup>30</sup>

14 Given the safety and soundness issues raised by first-lien PACE programs, the Statement  
15 directed that the May 5 Advisories “remain in effect” and that the Enterprises “should undertake  
16 prudential actions to protect their operations,” including: (i) adjusting loan-to-value ratios;  
17 (ii) ensuring that loan covenants require approval/consent for any PACE loans; (iii) tightening  
18 borrower debt-to-income ratios; and, (iv) ensuring that mortgages on properties with PACE liens  
19 satisfy all applicable federal and state lending regulations. However, FHFA opted to protect  
20 homeowners who had already obtained a PACE loan with a priority first lien, directing that any  
21 prohibition against such liens in the Enterprises’ USIs be waived.

22 Also on July 6, 2010, the Office of the Comptroller of the Currency (“OCC”), the Federal  
23 Deposit Insurance Corporation (“FDIC”), and the National Credit Union Administration (“NCUA”)  
24 issued statements supporting FHFA’s position. The OCC released a “Supervisory Guidance”  
25 informing national banks that they should “carefully consider [PACE] programs’ impact on both  
26 banks’ current mortgage portfolios and ongoing mortgage lending activities,” and suggested steps  
27 “to mitigate exposures and protect collateral positions.”<sup>31</sup> The FDIC noted that it “shares the  
28 FHFA’s concerns about the lack of appropriate underwriting and consumer protection

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30 FHFA Statement on Certain Energy Retrofit Loan Programs (July 6, 2010), *available at* <http://www.fhfa.gov/webfiles/15884/PACESTMT7610.pdf> (Border Decl. Ex. 16).

31 OCC Bulletin 2010-25, Property Assessed Clean Energy (PACE) Programs (July 6, 2010), *available at* <http://www.occ.treas.gov/ftp/bulletin/2010-25.html> (Border Decl. Ex. 17).

1 standards.”<sup>32</sup> The NCUA issued a “Regulatory Alert” to “All Federally Insured Credit Unions,”  
2 warning that “[i]n addition to potentially affecting loans held in your credit union’s portfolio,  
3 certain PACE loan programs could also adversely affect earnings and liquidity.”<sup>33</sup>

4 On August 31, 2010, the Enterprises issued further guidance to their sellers and servicers.<sup>34</sup>  
5 This guidance provided that the Enterprises would not purchase mortgages secured by properties  
6 subject to a first-lien PACE obligation. They also provided guidelines for refinancing of mortgages  
7 secured by properties subject to PACE obligations originated before July 6, 2010.

8 In sum, Defendants have four primary concerns about PACE programs.<sup>35</sup>

9 *First*, and most significantly, first-lien PACE programs pose material financial risks to the  
10 Enterprises (and thereby present serious safety and soundness issues that FHFA must address)  
11 because they retroactively subordinate first mortgages, effectively shifting the risk of default from  
12 PACE financiers to mortgage holders such as the Enterprises.<sup>36</sup> Plaintiffs do not deny that this  
13 feature of PACE programs makes mortgage assets riskier and therefore less valuable. Rather, they  
14 acknowledge the incremental risk but attempt to trivialize Defendants’ safety and soundness  
15 concern with a series of facially implausible and erroneous calculations purporting to show that the  
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18 <sup>32</sup> FDIC, Financial Institution Letter FIL-37-2010, Alert on FHFA Statement Relative to  
19 Concerns with Certain Energy Lending Programs (July 6, 2010), *available at* <http://www.fdic.gov/news/news/financial/2010/fil10037.pdf> (Border Decl. Ex. 18).

20 <sup>33</sup> National Credit Union Administration, Regulatory Alert No. 10-RA-10, Potential Risks of  
21 Property Assessed Clean Energy Loans (July 2010), *available at* <http://www.ncua.gov/news/express/xfiles/10-RA-10.pdf> (Border Decl. Ex. 19).

22 <sup>34</sup> Fannie Mae Announcement SEL-2010-12 (Aug. 31, 2010), *available at*  
23 <https://www.efanniemae.com/sf/guides/ssg/annltrs/pdf/2010/sel1012.pdf> (Border Decl. Ex. 20);  
24 Freddie Mac Bulletin No. 2010-20 (Aug. 31, 2010), *available at* <http://www.freddiemac.com/sell/guide/bulletins/pdf/bll1020.pdf> (Border Decl. Ex. 21);

25 <sup>35</sup> *See also* FHFA, Legal and Market Issues Related to Energy Loan Tax Assessment Programs  
26 (ELTAPs) (Sept. 10, 2009) (attached to Sept. 17, 2009 letter from Alfred M. Pollard to Rodney A. Dole, County of Sonoma).

27 <sup>36</sup> Retroactive legislative alteration of an existing security interest is so unusual that the Supreme  
28 Court has held that it may “result in a complete destruction of the property right of the secured party,” and that accordingly “there is substantial doubt whether [it] comports with the Fifth Amendment.” *U.S. v. Security Indus. Bank*, 459 U.S. 70, 75, 78 (1982).

1 risk to the Enterprises, now in conservatorship, and thereby to taxpayers, is “miniscule.” *See* Cal.  
 2 Am. Compl. at ¶ 41.<sup>37</sup>

3 *Second*, PACE programs lack sound and consistent underwriting standards, consumer  
 4 disclosures, and assessment of a borrower’s ability to pay, thereby posing significant risk not only  
 5 to mortgage holders such as the Enterprises, but also to homeowners.<sup>38</sup> For example, PACE statutes  
 6 authorize loans based on assessed value — known as collateral base lending — a key element in the  
 7 subprime financial crisis and a reason why the recent Dodd-Frank Act reminded lenders and  
 8 secondary market parties about the need to focus not on property but on borrower “ability to  
 9 repay.”<sup>39</sup> *Third*, PACE-funded projects may not generate sufficient energy savings to justify their  
 10 cost on a cash-flow basis or to increase the value of the underlying property commensurately with  
 11 the expenditure, but there is no recognized standard for determining the likely economic

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 14  
 15 <sup>37</sup> Plaintiffs equate the “risk” to the mortgage holder with the maximum reduction in proceeds  
 16 that the presence of a PACE obligation would cause the mortgagee to realize in a foreclosure sale.  
 17 Cal. Am. Compl. at ¶ 41. Plaintiffs assert that, so defined, the “risk” would equal “one year’s worth  
 18 of PACE assessments,” purportedly because “there is no acceleration of the entire amount financed  
 19 [in a PACE loan] for failure to a pay a [PACE] assessment.” *Id.* But any rational purchaser will  
 20 treat his “assum[ption] [of] the continuing obligation to pay the [PACE] assessments” — *i.e.*, his  
 21 assumption of the remaining PACE obligation — as a cost, and will reduce his cash bid  
 22 accordingly. *See id.* Because reducing the purchaser’s bid reduces the mortgagee’s proceeds, the  
 23 “risk” to the mortgagee, as Plaintiffs quantify it, must include the entire PACE obligation, not just  
 24 the amount in default. Hence, Plaintiffs underestimate the incremental risk significantly.

25 <sup>38</sup> PACE financing is available to homeowners without appropriate or uniform underwriting  
 26 standards, such as minimum total loan-to-value ratios or adequate consumer credit requirements.  
 27 *See, e.g.*, Placer App., *supra* fn. 21, at 2-3 (requiring that financing cannot exceed 10 percent of  
 28 property value, but no requirement that there be excess equity to allow for declines in property  
 value); Sonoma App., *supra* fn. 21 (improvement costs must be “reasonable” to current property  
 value, but no excess equity requirement; property owner must be current on taxes and mortgage,  
 and not in bankruptcy, but not other credit requirements applicable).

<sup>39</sup> *See* Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, §  
 1402, 124 Stat. 1376, 2139 (2010) (to be codified at 15 U.S.C. § 1639b (“It is the purpose of this  
 section . . . to assure that consumers are offered and receive residential mortgage loans on terms that  
 reasonably reflect their ability to repay the loans . . .”). *Id.* at § 1639c (requiring creditors to take  
 into consideration borrowers’ ability to repay, including the “consumer’s credit history, current  
 income, expected income the consumer is reasonably assured of receiving, current obligations,  
 [and] debt-to-income ratio.”).

1 consequences of retrofit projects.<sup>40</sup> *Fourth*, while the Enterprises do business in all parts of the  
 2 United States, PACE financing terms and program standards are not uniform throughout the  
 3 country.<sup>41</sup> The patchwork of municipalities with PACE programs, each posing its own set of  
 4 financial risks to mortgage holders (particularly the risk of borrower default), presents a safety and  
 5 soundness concern due to the Enterprises' large holdings of mortgage-related assets.

## ARGUMENT

### II. LEGAL STANDARD

8 FHFA respectfully requests that all claims of the three Plaintiffs against all Defendants be  
 9 dismissed under Federal Rule of Civil Procedure 12(b)(1) for lack of subject matter jurisdiction and  
 10 Federal Rule of Civil Procedure 12(b)(6) for failure to state a claim.

11 Subject matter jurisdiction is a threshold requirement; without it, a court cannot hear a  
 12 claim. *See Morongo Band of Mission Indians v. Cal. State Bd. of Equalization*, 858 F.2d 1376,  
 13 1380 (9th Cir. 1988). The party asserting jurisdiction must establish that it exists over each claim.  
 14 *See Kokkonen v. Guardian Life Ins. Co. of Am.*, 511 U.S. 375, 377 (1994). General grants of  
 15 jurisdiction do not apply where a specific statute precludes it. *First Nat'l Bank of Scotia v. United*  
 16 *States*, 530 F. Supp. 162, 166-68 (D.D.C. 1982) ("none of the general jurisdictional statutes cited in  
 17 the complaint are operative here, because those provisions confer jurisdiction upon this Court only  
 18 to the extent that Congress has previously carved out a role for the district courts in the more  
 19 focused and controlling statutory scheme set forth in 12 U.S.C. § 1818").

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21 <sup>40</sup> As late as June 8, 2010, the Department of Energy issued a request for information regarding  
 22 residential energy retrofits and noted that this was a leading problem for consumer acceptance of  
 23 retrofit borrowing. Department of Energy, National Energy Rating Program for Homes, Request  
 24 for Information at 4 (June 8, 2010), *available at* [http://apps1.eere.energy.gov/buildings/  
 25 publications/pdfs/corporate/rating\\_rfi\\_6\\_2\\_10.pdf](http://apps1.eere.energy.gov/buildings/publications/pdfs/corporate/rating_rfi_6_2_10.pdf) (Border Decl. Ex. 22).

26 <sup>41</sup> The Department of Energy has identified "best practices" for PACE programs. Department of  
 27 Energy, Guidelines for Pilot PACE Financing Programs (May 7, 2010), *available at*  
 28 [http://www1.eere.energy.gov/wip/pdfs/arra\\_guidelines\\_for\\_pilot\\_pace\\_programs.pdf](http://www1.eere.energy.gov/wip/pdfs/arra_guidelines_for_pilot_pace_programs.pdf) (Border Decl.  
 Ex. 23). Not only are these best practices not mandatory, they also assume that standard  
 underwriting practices are inadequate for PACE. *Id.* at 1 ("These best practice guidelines are  
 significantly more rigorous than the underwriting standards. currently applied to land-secured  
 financing districts."). FHFA indicated to Department of Energy that the best practices were still  
 insufficiently rigorous to protect the borrowers.

1 A complaint must be dismissed under Rule 12(b)(6) for failure to state a claim if it (a) does  
 2 not allege a cognizable legal theory or (b) alleges insufficient facts under a cognizable legal theory.  
 3 *See Balistreri v. Pacifica Police Dep't*, 901 F.2d 696, 699 (9th Cir. 1990). A case must be  
 4 dismissed where the complaint fails to state a “claim to relief that is plausible on its face.”  
 5 *Ashcroft v. Iqbal*, 556 U.S. \_\_\_, 129 S. Ct. 1937, 1949 (2009) (quoting *Bell Atlantic Corp. v.*  
 6 *Twombly*, 550 U.S. 540, 570 (2007)). While the Court must assume the truth of all properly  
 7 pleaded allegations of fact, “conclusory allegations of law and unwarranted inferences are  
 8 insufficient to defeat a motion to dismiss.” *Ove v. Gwinn*, 264 F.3d 817, 821 (9th Cir. 2001).  
 9 Stripped of unsupported legal conclusions, the factual allegations must do more than “create[] a  
 10 suspicion of a legally cognizable right of action”; they must “raise a right to relief above the  
 11 speculative level.” *Twombly*, 550 U.S. at 555 (internal quotations, citations, and alterations  
 12 omitted).

### 13 **III. THE COURT LACKS JURISDICTION OVER PLAINTIFFS’ CLAIMS**

14 Three specific statutory provisions — 12 U.S.C. § 4617(f), 12 U.S.C. § 4635(b), and 12  
 15 U.S.C. § 4623(d) — expressly preclude jurisdiction over Plaintiffs’ claims.

#### 16 **A. Section 4617(f) Withdraws Jurisdiction over Plaintiffs’ Claims Because the** 17 **Relief Sought Would Affect the Exercise of FHFA’s Powers as Conservator of** 18 **the Enterprises**

19 The first such provision, 12 U.S.C. § 4617(f), mandates that “no court may take any action  
 20 to restrain or affect the exercise of powers or functions of the [FHFA] as a conservator.” The plain  
 21 language of § 4617(f) and the rationale behind its enactment both support its application here.

#### 22 **1. The Plain Language of § 4617(f) Bars Jurisdiction over Plaintiffs’ Claims**

23 Congress modeled HERA’s conservatorship provisions on the corresponding provisions of  
 24 the statutes governing federal banking agencies. *See* H. Comm. on Fin. Servs., 110th Cong.,  
 25 Detailed Summary of H.R. 3221 (2008). The jurisdictional bar provision that applies to FHFA  
 26 conservatorships, § 4617(f), is materially identical to the provision applicable to FDIC  
 27 conservatorships, § 1821(j), which states that “no court may take any action, except at the request of  
 28 the [FDIC] by regulation or order, to restrain or affect the exercise of powers or functions of the

1 [FDIC] as a conservator or a receiver.” *Compare* 12 U.S.C. § 4617(f) with § 1821(j). Hence,  
2 decisions applying § 1821(j) provide particularly useful guidance in applying § 4617(f).

3 In affirming a dismissal for lack of jurisdiction, the D.C. Circuit has confirmed that the  
4 materially identical language of § 1821(j) is to be applied specifically as enacted:

5 [Section] 1821(j) does indeed bar courts from restraining or affecting  
6 the exercise of powers or functions of the FDIC as a conservator or a  
7 receiver unless it has acted or proposes to act beyond, or contrary to, its  
8 statutorily prescribed, constitutionally permitted, powers or functions.  
9 Congress undoubtedly did not contemplate anything like the parade of  
10 possible violations of existing laws — civil and criminal — that  
creative judges can conjure up, but *given the breadth of the statutory  
language, untempered by any persuasive legislative history pointing in  
a different direction, the statute would appear to bar a court from  
acting in virtually all circumstances.*

11 *Nat’l Trust for Historic Preservation in U.S. v. FDIC*, 21 F.3d 469, 472 (D.C. Cir. 1994) (Wald, J.  
12 concurring) (internal brackets, quotation marks, and citation omitted; emphasis added).

13 The § 4617(f) jurisdictional bar applies “regardless of [Plaintiffs’] likelihood of success on  
14 the merits of [any] underlying claims.” *Freeman v. FDIC*, 56 F.3d 1394, 1398-99 (D.C. Cir. 1995)  
15 (applying § 1821(j)). Indeed, the jurisdictional bar would apply even if it were (incorrectly)  
16 assumed that Plaintiffs could otherwise state a viable claim. *See Nat’l Trust for Historic  
17 Preservation in the U.S. v. FDIC*, 995 F.2d 238, 240 (D.C. Cir. 1993) (“We do not think it possible,  
18 in light of the strong language of § 1821(j), to interpret the FDIC’s ‘powers’ and ‘authorities’ to  
19 include the limitation that those powers be subject to — and hence enjoined for non-compliance  
20 with — any and all other federal laws.”), *vacated by* 5 F.3d 567 (D.C. Cir. 1993), *but reinstated in  
21 relevant part by* 21 F.3d 469 (D.C. Cir. 1994). And it makes no difference whether FHFA has acted  
22 (or could act) under its powers as a Conservator or its authority as a supervisory regulator. FHFA  
23 acts in both capacities, and is vested with “discretion regarding whether it will wear one hat or the  
24 other, or both.” *Nat’l Trust*, 21 F.3d at 471 (applying § 1821(j)). Regardless of the “hat” or hats  
25 worn by FHFA in issuing the Statement, setting the Statement aside would affect the FHFA’s  
26 exercise of its powers as Conservator.

1                                    **a.        Plaintiffs’ Requested Relief Would Inevitably Restrain and**  
 2                                    **Severely Affect the Exercise of the Conservator’s Power to**  
 3                                    **Preserve and Conserve Enterprise Assets**

4                                    Because the Conservator is statutorily bound to “preserve and conserve the assets and  
 5 property” of the Enterprises, by enacting HERA Congress prescribed that the Conservator must be  
 6 accorded broad latitude to make its own supervisory judgments about financial risk (such as  
 7 judgments as to the type and magnitude of risks that PACE loans pose), to determine how to  
 8 mitigate such risks, and to direct the Enterprises to manage their portfolios accordingly. *See* 12  
 9 U.S.C. § 4617(b)(2)(B), (D), (J). As the Eastern District of Virginia held last year, “[i]n granting  
 10 the conservator broad, sweeping authority over Freddie Mac’s assets, Congress made it clear that it  
 11 left to the FHFA . . . the discretion to decide how best to manage the assets of Freddie Mac.” *In re*  
 12 *Federal Home Loan Mortg. Corp. Derivative Litig.*, 643 F. Supp. 2d 790, 798 (E.D. Va. 2009).

13                                    Here, all of the injunctive relief that Plaintiffs seek would “affect the exercise of powers or  
 14 functions of [FHFA] as a conservator,” and is therefore precluded by § 4617(f). Principally,  
 15 Plaintiffs seek to enjoin the Enterprises (and, thus necessarily the Conservator) from “taking any . . .  
 16 action . . . that has a chilling effect on the implementation of PACE programs,” particularly from  
 17 “taking any adverse action against any mortgagee . . . participating . . . in a PACE program.”<sup>42</sup> But  
 18 if the Conservator cannot take “any adverse action against a mortgagee participating in a PACE  
 19 program,” then the Conservator must treat such mortgagees as if they were *not* participating in  
 20 PACE programs. Thus, Plaintiffs’ relief, if granted, would preclude the Conservator from taking  
 21 *any* account of the added risks that PACE loans pose to mortgages acquired by the Enterprises; this  
 22 would restrain and affect the Conservator’s ability to exercise its statutory power “to preserve and  
 23 conserve [Enterprise] assets.” The vague request to bar “any adverse action,” likewise might pose  
 24 unintended consequences.

25                                    Such injunctive relief “violates the heart of what is commonly termed [the] ‘anti-injunction  
 26 provision’” of the § 1821(j)/4617(f) jurisdictional bar. *Bank of Am. Nat’l Ass’n v. Colonial Bank*,

27 \_\_\_\_\_  
 28 <sup>42</sup> All of the injunctive relief Plaintiffs seek is fairly subsumed within that request. Regardless, all  
 of their requests for injunctive relief fail for the same reasons.

1 604 F.3d 1239, 1244 (11th Cir. 2010) (applying § 1821(j)). While it is true that certain of Plaintiffs’  
2 injunctive requests are formally directed at Fannie Mae and Freddie Mac, FHFA in its statutory  
3 capacity as Conservator “operates” those Enterprises. 12 U.S.C. § 4617(b)(2)(B). Any injunctive  
4 restraint on the Enterprises would, as a matter of law, therefore restrain and affect the exercise of  
5 the Conservator’s statutory authority to “operate” Fannie Mae and Freddie Mac and “to perform all  
6 functions” of the Enterprises in their “name[s].” *Id.* Hence, the jurisdictional bar of § 4617(f) is not  
7 limited to claims pleaded directly against the Conservator. As the Third Circuit explained:

8 [T]he plain language of the statute is not so limited [as to apply only to  
9 claims formally pled against a conservator or receiver]. Rather, the  
10 statute, by its terms, can preclude relief even against a third party, . . .  
11 where the result is such that the relief “restrain[s] or affect[s] the  
12 exercise of powers or functions of . . . a conservator or a receiver.”  
13 After all, an action can “affect” the exercise of powers by an agency  
14 without being aimed directly at it.

15 *Hindes v. FDIC*, 137 F.3d 148, 160 (3d Cir. 1998) (citations omitted) (holding that § 1821(j) barred  
16 jurisdiction over claim that FDIC acted improperly as regulator because the relief sought would  
17 limit FDIC’s ability to act as receiver).

18 All of Plaintiffs’ requests for declaratory relief also founder on the jurisdictional bar of  
19 § 4617(f), which, like the parallel § 1821(j), is not limited to requests for injunctions. Rather, such  
20 provisions also bar any “declaratory judgment that would effectively ‘restrain’ the [conservator].”  
21 *Kuriakose v. Federal Home Loan Mortgage Corporation*, 674 F. Supp. 2d 483, 493-94 (S.D.N.Y.  
22 2009) (quoting *Freeman*, 56 F.3d at 1399 (applying § 1821(j)); see also *Hindes*, 137 F.3d at 166 (3d  
23 Cir. 1998) (explaining that § 1821(j) “precludes injunctive *and declaratory relief* which would  
24 restrain or affect the powers” of a conservator or receiver) (emphasis added). Plaintiffs first ask the  
25 Court to declare that the PACE loans are, in fact, “assessments,” notwithstanding that Plaintiffs  
26 themselves have stated repeatedly and authoritatively that their programs involve “loans.” See § V  
27 *infra*. To the extent that such a declaration would have any legal consequence, it would restrain and  
28 affect the Conservator’s power to “preserve and conserve” assets — regardless of semantic labels,  
the Conservator cannot blind itself to the real risks PACE programs pose to the Enterprises’  
portfolios. Plaintiffs’ requests for declaratory judgments that FHFA violated the APA or NEPA are  
also barred. As the D.C. Circuit explained in confirming that the analogous provision of § 1821(j)

1 barred a claim that an FDIC receiver’s planned sale of a building would violate another generally  
2 applicable federal statute, the National Historic Preservation Act, “We do not think it possible, in  
3 light of the strong language of § 1821(j), to interpret the FDIC’s ‘powers’ and ‘authorities’ to  
4 include the limitation that those powers be subject to — and hence enjoined for *non-compliance*  
5 *with — any and all other federal laws.*” *Nat’l Trust*, 995 F.2d at 240 (emphasis added). Not only  
6 does § 4617(f) preclude jurisdiction directly, but it also triggers the APA provision foreclosing APA  
7 claims where another “statute[] preclud[es] judicial review.” 5 U.S.C. § 701; *see also id.* § 702.

8 **2. The Policy Rationale behind § 4617(f) Supports Its Application Here**

9 In § 1821(j) cases, courts have explained the policies supporting the jurisdictional bar. As  
10 the Fifth Circuit noted in 1991, Congress enacted the § 1821(j) jurisdictional bar so that  
11 conservators and receivers could “act in a quick and decisive manner in reorganizing, operating, or  
12 dissolving” troubled financial institutions. *281-300 Joint Venture v. Onion*, 938 F.2d 35, 39 (5th  
13 Cir. 1991) (applying § 1821(j)). Indeed, as the D.C. Circuit explained four years later, “[a]lthough  
14 [the § 1821(j)] limitation on courts’ power to grant equitable relief may appear drastic, it fully  
15 accords with the intent of Congress . . . to enable the [federal banking agencies] to expeditiously  
16 wind up the affairs of literally hundreds of failed financial institutions throughout the country.”  
17 *Freeman*, 56 F.3d at 1398 (citing H.R. Rep. No. 101-54(I), 101st Cong., 1st Sess. 291, 307,  
18 *reprinted in* 1989 U.S.C.C.A.N. 86, 87, 103).

19 Here, those same policies apply. Given the importance of housing finance to the overall  
20 economy, it is imperative that all courts respect Congress’s determination that the Conservator’s  
21 ability to exercise its powers, functions, and discretion to respond decisively and efficiently to  
22 challenges as they arise, without becoming exposed to entangling litigation at each step, is  
23 paramount. Indeed, given the magnitude and complexity of the Fannie Mae and Freddie Mac  
24 conservatorships, the need for the FHFA Conservator to act decisively and efficiently is not only  
25 more acute but also more enduring than in even the largest banking-agency conservatorships or  
26 receiverships.

1           **B.       HERA Separately Withdraws Jurisdiction Because the Relief Plaintiffs Seek**  
2           **Would Undermine FHFA’s Supervisory Authority**

3           In addition to withdrawing jurisdiction to grant relief that would “affect the exercise of  
4 powers or functions of [FHFA] as a conservator,” 12 U.S.C. § 4617(f), Congress also included  
5 provisions in HERA that withdraw court jurisdiction over actions that would interfere with FHFA’s  
6 regulatory supervision of the Enterprises. *See* 12 U.S.C. §§ 4635(b), 4623(d). These provisions are  
7 closely analogous to a provision applicable to the federal banking agencies, 12 U.S.C. § 1818(i)(1),  
8 and they apply both during “ongoing administrative proceeding[s]” and prior to their  
9 commencement. As the Third Circuit explained, “by its terms[,] section 1818(i),” and, thus, its  
10 HERA analogues, are “not restricted to precluding judicial review which would interfere with an  
11 ongoing administrative proceeding.” *Hindes*, 137 F.3d at 164. Indeed, “[t]he fact that no  
12 administrative action [i]s pending . . . is irrelevant to th[e] determination” that jurisdiction is  
13 withdrawn. *Board of Governors v. DLG Fin. Corp.*, 29 F.3d 993, 999 (5th Cir. 1994)

14           **1.       The Plain Language of Section 4635(b) Bars Relief That Would Affect**  
15           **FHFA’s Issuance and Enforcement of Supervisory Notices and Orders**

16           In 12 U.S.C. § 4635(b), Congress mandated that “no court shall have jurisdiction to affect,  
17 by injunction or otherwise, the issuance or enforcement of . . . any notice or order” under several  
18 HERA provisions. Because of the risks first-lien PACE loans pose to mortgage-related assets, the  
19 Enterprises’ treatment of such assets implicates many of FHFA’s supervisory and enforcement  
20 powers, including those powers specifically referenced in § 4635(b).

21           At its core, § 4635(b) withdraws jurisdiction over actions that would affect the “issuance or  
22 enforcement of notices or orders” under the entirety of “subchapter II,” *i.e.*, 12 U.S.C. §§ 4611-  
23 4624.<sup>43</sup> One of the “subchapter II” provisions, 12 U.S.C. § 4624(c), states that “the Director may,  
24 by order, require [an Enterprise], under such terms and conditions as the [FHFA] determines to be  
25 appropriate, to dispose of or acquire any asset,” provided that “the Director determines that such  
26 action is consistent with the purposes of [HERA].” Another section, 12 U.S.C. § 4624(b), provides  
27 that “the Director may, by order, make temporary adjustments to the established standards [for

28           <sup>43</sup> Sections 4619, 4620, and 4621 have been repealed and are therefore not relevant here.

1 Enterprise portfolio holdings], such as during times of economic distress or market disruption.”  
 2 Here, all of the relief Plaintiffs seek would affect FHFA’s issuance or enforcement of notices or  
 3 orders under provisions covered by § 4635(b); jurisdiction to grant it is therefore lacking.

4 **a. The July 6 Statement Stands as an Order or Presages an Order**  
**Reiterating Its Terms**

5 Section 4635(b) is triggered here because the Statement stands as, or could lead to, an  
 6 “order” issued under one of the HERA provisions enumerated in § 4635(b).

7 If it is assumed (as Plaintiffs assert) that the Statement represents final agency action, then  
 8 the Statement must be deemed a declaratory order. Under the APA, “‘order’ means the whole or a  
 9 part of a final disposition, whether affirmative, negative, injunctive, or declaratory in form, of an  
 10 agency in a matter other than rule making.” 5 U.S.C. § 551(6).<sup>44</sup> The APA provides that an agency  
 11 “in its sound discretion, may issue a declaratory order to terminate a controversy or remove  
 12 uncertainty.” *Id.* § 554(e). One obvious purpose of FHFA’s issuance of the July 6 Statement was to  
 13 terminate the brewing controversy as to whether PACE programs present significant safety and  
 14 soundness concerns; another was to remove uncertainty as to whether FHFA would direct the  
 15 Enterprises to take any prudential actions regarding PACE programs (and, if so, what such actions  
 16 would be). Plaintiffs themselves assert that the Statement bears all indicia of finality. Hence, to the  
 17 extent the Statement is deemed final agency action, it fits neatly within the APA definition of a  
 18 “declaratory order.”

19 But even if the Statement is *not* itself deemed a declaratory order, it is readily foreseeable  
 20 that FHFA might re-issue the same guidance in declaratory-order form — it is not uncommon for an  
 21 administrative agency to transform its informal supervisory guidance into a formal declaratory  
 22

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23  
 24 <sup>44</sup> It is true that under the APA, by definition, “orders” result from “adjudication.” *See* 5 U.S.C.  
 25 § 551(7). But here, it is indisputable that the Statement addresses the conduct of a small number of  
 26 parties — the Enterprises and the Home Loan Banks — that all had ample notice and opportunity to  
 27 be heard. Under the governing case law, that is sufficient to meet the APA definition of  
 28 adjudication. *See American Airlines, Inc. v. Dep’t of Transp.*, 202 F.3d 788, 798 (5th Cir. 2000)  
 (“informal” process by which agency issued declaratory order that “interpreted the rights of a small  
 number of parties properly before it” properly deemed adjudicative); *Sierra Club v. Peterson*, 185  
 F.3d 349, 366-67 (rejecting parties’ “vehement assertions” that agency actions were not  
 adjudicatory and therefore could not have led to an “order”).

1 order. *See, e.g., British Caledonian Airways, Ltd. v. Civil Aeronautics Bd.*, 584 F.2d 982, 984-85  
2 (D.C. Cir. 1978) (describing process by which agency first sent a “letter to the industry” containing  
3 “precise and definite” guidance, which certain entities treated as “a non-binding advisory notice,”  
4 then “issued [a] Declaratory Order [that] generally reaffirmed the industry letter.”).

5 **b. The § 4635(b) Jurisdictional Bar Applies Regardless of Whether**  
6 **the Statement Is Deemed a Declaratory Order**

7 Whether the Statement is or could lead to an order, any such order would be issued pursuant  
8 to 12 U.S.C. § 4624 (b) or (c), provisions that trigger the § 4635(b) jurisdictional bar.

9 The stated basis for the Statement and its operative provisions conform precisely to  
10 § 4624(c), which states that “the Director may, by order, require [an Enterprise], under such terms  
11 and conditions as the [FHFA] determines to be appropriate, to dispose of or acquire any asset,” if  
12 “the Director determines that such action is consistent with the purposes of [HERA].” By  
13 “direct[ing]” the Enterprises to take certain “prudential actions” regarding mortgages subject to  
14 PACE loans, FHFA attached “terms and conditions [that FHFA] deems appropriate” to the  
15 acquisition of such assets. The Statement notes that the directive to take those prudential actions  
16 deals with “significant safety and soundness concerns that must be addressed,” meeting the  
17 § 4624(c) requirement that FHFA “determine that such action is consistent with the purposes of  
18 [HERA].”

19 The Statement also falls within the scope of § 4624(b), which provides that “the Director  
20 may, by order, make temporary adjustments to the established standards [for Enterprise portfolio  
21 holdings], such as during times of economic distress or market disruption.” The “prudential  
22 actions” FHFA “directs” in the statement reflect “adjustments to the established standards” for  
23 Enterprise portfolio holdings — Plaintiffs allege that the Statement precludes the Enterprises from  
24 purchasing mortgages subject to PACE loans — and the Statement was indisputably issued “during  
25 [a] time[] of economic distress.”

26 And, as noted *supra*, even if the Statement itself is not deemed a declaratory order, it is  
27 readily foreseeable that FHFA would reiterate the directives in the Statement as a more formal  
28 declaratory order issued pursuant to § 4624(b) or (c). Hence, regardless of whether the Statement is

1 itself deemed an “order,” all the relief Plaintiffs seek would “affect” the “issuance or enforcement  
2 of a[n] . . . order” issued pursuant to § 4624, thereby triggering the § 4635(b) jurisdictional bar.

3 **c. Section 4635(b) Bars All Forms of Relief Plaintiffs Seek**

4 Plaintiffs principally ask this Court to enjoin Fannie Mae and Freddie Mac (and thus,  
5 necessarily, FHFA) from “taking any . . . action . . . that has the effect of chilling PACE programs in  
6 California,” particularly from “taking any adverse action against any mortgagee . . . participating  
7 . . . in a PACE program.” *See* Cal. Am. Compl. at Prayer ¶ 2. Enjoining any action that would have  
8 “the effect of chilling PACE programs” would surely “affect” FHFA’s ability to “enforce[]” the  
9 directives set forth in the July 6 Statement through direct enforcement of the Statement or through  
10 the issuance of a more formal declaratory order reiterating the same directives. Because all of the  
11 injunctive relief Plaintiffs seek would affect the issuance or enforcement of an order under § 4624,  
12 it is barred by § 4635(b).

13 As to Plaintiffs’ declaratory relief claims, as noted *supra*, jurisdiction withdrawal provisions  
14 like § 4635(b) “[n]ot only . . . bar injunctive relief,” but also bar any “declaratory judgment that  
15 would effectively ‘restrain’ the [conservator].” *Freeman*, 56 F.3d at 1399. As we explained *supra*  
16 in the § 4617 context, the declaratory relief Plaintiffs seek would have the effect of an injunction.  
17 Hence, under § 4635(b) the Court has no jurisdiction to consider such relief.

18 **2. The Plain Language of a Second, Similar Section — § 4623(d) — Bars**  
19 **Jurisdiction over Claims That Would Affect Other Supervisory Action**

20 A second jurisdiction withdrawal provision, § 4623(d), extends the reach of the  
21 jurisdictional bar beyond notices and orders in some circumstances, mandating that “no court shall  
22 have jurisdiction to affect, by injunction or otherwise, the issuance or effectiveness of *any* . . .  
23 *action of the Director*” pursuant to any of the subchapter II sections, *i.e.*, §§ 4611-24. 12 U.S.C.  
24 § 4623(d) (emphasis added). Among other things, those sections authorize the Director to “require”  
25 a “significantly undercapitalized” Enterprise “to terminate, reduce, or modify any activity that the  
26 Director determines creates excessive risk.” 12 U.S.C. § 4616(b)(4). The Enterprises were placed  
27 into conservatorship as a result of their significant undercapitalization, and the directives set forth in  
28 the July 6 Statement fit well within the authority granted and the actions prescribed under  
§ 4616(b)(4). Accordingly, § 4623(d) bars jurisdiction over all of Plaintiffs’ claims.

3. **The Policy Rationale behind Sections 4635(b) and 4623(d) Supports Their Application Here**

As with the conservatorship provisions, Congress modeled the supervisory and enforcement provisions of HERA on corresponding provisions of the statutes governing federal banking regulatory agencies. Accordingly, decisions articulating the policy basis behind the banking agency jurisdiction withdrawal provision, § 1818(i)(1), equally illuminate the policy behind the jurisdiction withdrawal provisions that apply here to FHFA in its regulatory capacity, §§ 4635(b) and 4623(d).

Several such decisions explain that Congress intended expert federal financial agencies such as the OCC, FDIC, and FHFA to have wide latitude in supervisory matters, and that Congress therefore chose to permit judicial intervention at limited times and in limited circumstances only.

As the Fifth Circuit explained in the 1978 *Groos* decision, the relevant statutory “provisions establish a closely meshed administrative structure through which the [financial regulatory agencies] may curtail unsafe . . . practices.” *Groos Nat’l Bank v. Comptroller of the Currency*, 573 F.2d 889, 894 (5th Cir. 1978) (addressing title 12 provisions applicable to OCC, including 12 U.S.C. § 1818). The court further explained that the statute “as a whole provides a detailed framework for regulatory enforcement and for orderly review of the various stages of enforcement; and [the jurisdictional bar provision] in particular evinces a clear intention that *this regulatory process is not to be disturbed by untimely judicial intervention.*” *Id.* (emphasis added). *See also Henry v. Office of Thrift Supervision*, 43 F.3d 507, 513 (10th Cir. 1994).

The District Court for the District of Columbia, in the 1982 *First Nat’l* case, explained the same reasoning in greater detail:

The statutory scheme . . . grants federal agencies such as the [OCC], the [FDIC] and the Federal Reserve Board wide[-]ranging supervisory and enforcement authority over our nation’s banking system. . . . These agencies are charged with the task of overseeing that banking system for the protection of the public and the national economy as a whole . . . .

*First Nat’l Bank of Scotia*, 530 F. Supp. at 166 (internal quotation marks and citations omitted).

The court continued:

Given the magnitude of the public and private interests that are impacted by such extensive agency regulation of financial institutions, it is not surprising that Congress has seen fit to prescribe a specific statutory mechanism for obtaining judicial review of agency

enforcement actions in this area. . . . Aside from the[] carefully delineated circumstances where federal district courts are granted jurisdiction over [such] controversies, Congress has categorically determined that “no court shall have jurisdiction to affect by injunction or otherwise the issuance or enforcement of any notice or order under this section, or to review, modify, suspend, terminate, or set aside any such notice or order.” . . . [Hence,] both common sense and the language of the statute preclude this Court from exercising jurisdiction over [plaintiffs’ claims for declaratory and injunctive relief under the APA].

*Id.* at 166-68. *See also RTC v. Ryan*, 801 F. Supp. 1545, 1550 (S.D. Miss. 1992); *Leuthe v. Office of Fin. Inst. Adjudication*, 977 F. Supp. 357, 360-61 (E.D. Pa. 1997).

As these decisions confirm, litigating the propriety of the supervisory activities of expert financial regulatory agencies like FHFA outside of the statutorily prescribed review process (which Plaintiffs do not even purport to invoke here) would subvert the regulatory mission of these agencies — the precise result Congress wished to avoid. Accordingly, the policy rationale behind the § 4635(b) and § 4623(d) jurisdictional bars fully supports dismissal of the Plaintiffs’ claims.

**IV. PLAINTIFFS’ STATE LAW CLAIMS FAIL BECAUSE THEY ARE PREEMPTED**

California and Sonoma each bring a state law claim against the Enterprises. California alleges that the Enterprises (*i.e.*, the Conservator) have engaged in acts that constitute unfair competition as defined by California Business & Professional Code § 17200 (California’s Unfair Competition Law, or “UCL”).<sup>45</sup> Cal. Am. Compl. ¶¶ 59-60. The alleged acts “include, but are not limited to” (a) “characterization of PACE assessments as loans without support for such characterization under California law,” and (b) “claims that PACE assessments providing first-lien priority are contrary to Fannie Mae’s and Freddie Mac’s Uniform Security Instruments.” *Id.* ¶ 60. Sonoma alleges that the Enterprises have interfered with prospective contractual relationships between Sonoma and its residents by treating assessments as loans and by “taking, or threatening to take, certain adverse actions against residents who participate in [PACE].” Sonoma Compl. ¶ 66. As a result, Sonoma alleges, the County and its residents are being deprived of economic and

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<sup>45</sup> Cal. Bus. & Prof. Code § 17200 provides that “unfair competition shall mean and include any unlawful, unfair or fraudulent business act or practice . . . .”

1 environmental benefits. *Id.* ¶ 67. The Court need not address the dubious merits of these claims  
 2 because federal law preempts California’s UCL claim and Sonoma’s claim for interference with  
 3 prospective contractual relations.

4 **A. Plaintiffs’ State Law Claims Are Preempted Because They Conflict with**  
**HERA’s Delegation of Safety and Soundness Authority to FHFA**

5 Under conflict preemption doctrine, “[a] state law, whether arising from statute or common  
 6 law, is preempted if it creates an ‘obstacle to the accomplishment and execution of the full purposes  
 7 of Congress.’” *Chae v. SLM Corp.*, 593 F.3d 936, 943 (9th Cir. 2010) (quoting *Crosby v. Nat’l*  
 8 *Foreign Trade Council*, 530 U.S. 363, 373 (2000)).<sup>46</sup> In this case, Plaintiffs are not entitled to a  
 9 presumption against preemption because “the State regulates in an area where there has been a  
 10 history of significant federal presence.” *Bank of America*, 309 F.3d at 558 (quoting *United States v.*  
 11 *Locke*, 529 U.S. 89, 108 (2000)). Just like the regulation of national banks, to which the  
 12 presumption does not apply, the safety and soundness of the Enterprises is an area with a history of  
 13 significant federal presence, now delegated to FHFA.<sup>47</sup>

14 Here, Plaintiffs seek to enjoin conduct of the Enterprises that is exclusively within the power  
 15 of FHFA to supervise and as to which FHFA has issued an express directive. A state lawsuit must  
 16 be dismissed if the relief sought would frustrate federal law. *See, e.g., Martinez*, 598 F.3d at 557-58  
 17 (affirming dismissal of § 17200 claim because it was preempted by the National Bank Act, as  
 18 interpreted by the OCC in regulations and an interpretive letter); *Montgomery v. Bank of America*  
 19 *Corp.*, 515 F. Supp. 2d 1106, 1114 (C.D. Cal. 2007) (granting motion to dismiss § 17200 claim  
 20 because “plaintiff’s attempt to require defendants to set overdraft fees in a manner that conflicts  
 21 with the [National Bank Act] and the regulations promulgated thereunder necessitates the  
 22 conclusion that plaintiff’s claims are barred by the doctrine of conflict preemption.”).

23  
 24  
 25  
 26 <sup>46</sup> *See also Martinez v. Wells Fargo Home Mortgage*, 598 F.3d 549, 555 (9th Cir. 2010) (“State  
 27 attempts to control the conduct of national banks are void if they conflict with federal law, frustrate  
 28 the purposes of the National Bank Act, or impair the efficiency of national banks to discharge their  
 duties.” (quoting *Bank of America v. San Francisco*, 309 F.3d 551, 561 (9th Cir. 2002)).

<sup>47</sup> *See* 12 U.S.C. §§ 1451 *et seq.* (Freddie Mac charter), 1716 *et seq.* (Fannie Mae charter).

1 By conferring broad authority on FHFA to exercise its discretion in supervising the  
 2 Enterprises,<sup>48</sup> Congress directed that FHFA would be the arbiter of safety and soundness judgments  
 3 governing the Enterprises, notwithstanding any conflicting state law.<sup>49</sup> In its July 6, 2010  
 4 Statement, FHFA explained its safety and soundness concerns relating to first-lien PACE programs  
 5 and directed the Enterprises to undertake prudential action to protect their assets.<sup>50</sup> By seeking to  
 6 enjoin the Enterprises from taking “adverse action” against PACE participants and from  
 7 “interfering” with PACE programs, Plaintiffs effectively demand a court order requiring the  
 8 Enterprises to purchase mortgages with PACE first liens and thereby to take on all of the associated  
 9 risks — with no compensation. In other words, they ask this Court to hold that state law compels  
 10 the Enterprises to ignore FHFA’s concerns and directives. This outcome would undermine FHFA’s  
 11 Congressionally delegated authority and permit fifty states to regulate the Enterprises in accordance  
 12 with their other goals and interests. The creation of state-imposed obligations regarding PACE  
 13 first-lien mortgages in California would undermine the Enterprises’ ability to operate under uniform  
 14 and consistent standards. A lack of uniformity can itself be a threat to safety and soundness. As  
 15 courts have observed in the national bank context:

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16  
 17 <sup>48</sup> See 12 U.S.C. § 4511(b)(2) (“The Director shall have general regulatory authority over each  
 18 regulated entity and the Office of Finance, and shall exercise such general regulatory authority,  
 19 including such duties and authorities set forth under section 4513 of this title, to ensure that the  
 20 purposes of this Act, the authorizing statutes, and any other applicable law are carried out.”).

21 <sup>49</sup> See *Fidelity Fed. Sav. & Loan Ass’n v. de la Cuesta*, 458 U.S. 141, 153-54 (1982) (“Where  
 22 Congress has directed an administrator to exercise his discretion, his judgments are subject to  
 23 judicial review only to determine whether he has exceeded his statutory authority or acted  
 24 arbitrarily.”); *Franklin Savs. Ass’n v. Director, Office of Thrift Supervision*, 934 F.2d 1127, 1145-46  
 25 (10th Cir. 1991) (“Whether a financial institution is in an unsafe or unsound condition is largely a  
 26 predictive judgment (i.e., what may happen if this practice continues), and reviewing courts should  
 27 be particularly deferential when they are reviewing an agency’s predictive judgments, especially  
 28 those within the agency’s field of discretion and expertise.”).

<sup>50</sup> FHFA may exercise its authority through orders or guidelines rather than notice-and-comment  
 regulations. HERA distinguishes between “regulations” and “guidelines,” and makes clear that  
 FHFA may fulfill its duties through either mechanism. See, e.g., 12 U.S.C. § 4526 (“The Director  
 shall issue any regulations, *guidelines*, or orders necessary to carry out the duties of the Director  
 under this chapter or the authorizing statutes . . . . Any *regulations* issued by the Director under this  
 section shall be issued after notice and opportunity for public comment . . . .” (emphases added));  
 § 4513b(a) (“The Director shall establish standards, by regulation or guideline . . . .”);  
 § 4513b(1)(A) (explaining consequences of failing to meet standards, which differ according to  
 whether standards were established via regulation or guideline).

1 When national banks are unable to operate under uniform, consistent,  
2 and predictable standards, their business suffers, which negatively  
3 affects their safety and soundness. The application of multiple, often  
4 unpredictable, different state or local restrictions and requirements  
5 prevents them from operating in the manner authorized under Federal  
6 law, is costly and burdensome, interferes with their ability to plan their  
7 business and manage their risks, and subjects them to uncertain  
8 liabilities and potential exposure.<sup>51</sup>

9 Thus, a finding of liability would “stand[] as an obstacle to the accomplishment and  
10 execution” of Congress’s objective that FHFA be the supervisory financial regulator and  
11 Conservator of the Enterprises. *See* 12 U.S.C. § 4617(a)(7) (Conservator is not subject to the  
12 direction or supervision of any State in the exercise of its rights, powers, and privileges); § 4617(f)  
13 (“no court may take any action to restrain or affect the exercise of powers or functions of” FHFA as  
14 a Conservator). Accordingly, Plaintiffs’ state law claims against the Enterprises must be dismissed  
15 as preempted by HERA.

16 **B. Plaintiffs’ State Law Claims Are Expressly Preempted Because They Would**  
17 **Subject the Conservator to the Direction and Supervision of a State**

18 Not only are Plaintiffs’ state-law claims pre-empted by virtue of the inherent conflict  
19 between (a) subjecting the Enterprises to state-law claims of the sort Plaintiffs assert, and (b)  
20 Congress’s delegation to FHFA of exclusive authority to regulate the safety and soundness of the  
21 Enterprises, but Congress has also expressly preempted the assertion of such claims to the extent  
22 that they would affect the Conservator. In HERA, Congress decreed that “When acting as  
23 conservator . . . , the Agency shall not be subject to the direction or supervision of any other Agency  
24 of the United States or any State in the exercise of the rights, powers, and privileges of the Agency.”  
25 12 U.S.C. § 4617(a)(7). *See also Waterview Mgmt. Co. v. FDIC*, 105 F.3d 696, 700-01 (D.C. Cir.  
26 1997) (describing operation of analogous banking-agency provision as “express preemption”).  
27 Here, with both Enterprises in conservatorship, Plaintiffs’ state-law claims would interpose the

28 <sup>51</sup> *Nat’l City Bank of Indiana v. Turnbaugh*, 463 F.3d 325, 332-33 (4th Cir. 2006) (quoting OCC, Bank Activities and Operations: Real Estate Lending and Appraisals, 69 Fed. Reg. 1904 (Jan. 13, 2004)). Further, PACE programs vary not only by counties within a state but as well among states; for example, California permits loans of up to 10% of a property’s assessed value, while New Mexico sets a 40% maximum. N.M. Stat. Ann. § 4-55C-4(D)(2) (West 2010); Cal. Pub. Res. Code § 26123.

1 environmental policies of the State of California and its attorney general directly between the  
 2 Conservator and its mission to “preserve and conserve [the Enterprises’] assets and property.”  
 3 Hence, Plaintiffs’ state-law claims are expressly and entirely preempted by § 4617(a)(7).

4 **V. PLAINTIFFS’ STATE CLAIMS FAIL AS A MATTER OF LAW**

5 **A. California’s Unfair Competition Law Claim Fails As A Matter of Law**

6 California’s UCL claim fails because the Complaint does not and cannot allege the  
 7 necessary prerequisite that the Enterprises have “violated another law” or engaged in any “unfair  
 8 business practice.”<sup>52</sup>

9 *First*, no underlying violation of “another law” has occurred. California alleges that under  
 10 “California law, liens resulting from PACE assessments, like other assessments, have priority over  
 11 mortgages,” and that the Enterprises “seek to change that priority for [their] own benefit *in violation*  
 12 *of California law*,” Cal. Am. Compl. ¶ 33 (emphasis added), but that is wrong. No facts are alleged  
 13 to suggest that the Enterprises are ignoring or “changing” any lien priority. To the contrary, the  
 14 facts alleged make clear that by considering and applying the terms of the USIs in response to the  
 15 financial risks posed by PACE programs, the Enterprises (under the conservatorship of the FHFA)  
 16 have acted in acknowledgement, not contravention, of the lien-priming feature of such programs.  
 17 And nothing about the Enterprises’ decisions in that regard violates any term of any California law.  
 18 Neither the statewide PACE legislation nor any local government PACE program purports to (a)  
 19 impose any duty on the Enterprises to purchase loans secured by a property subject to a senior  
 20 PACE lien or (b) address the legal effect of a lien arising from a PACE program on compliance  
 21 with the terms of the Enterprises’ USIs. To the contrary, numerous PACE programs explicitly  
 22 highlight for homeowners that they must carefully review their mortgage documents to confirm  
 23 whether PACE financing may violate the loan documents’ terms.<sup>53</sup> The decision not to purchase

24 \_\_\_\_\_  
 25 <sup>52</sup> See Cal. Bus. & Prof. Code § 17200; *Ingels v. Westwood One Broad. Servs., Inc.*, 129 Cal.  
 26 App. 4th 1050, 1060 (2005) (a defendant does not violate the unlawful prong of the UCL without  
 27 violating some other law); see also *Newson v. Countrywide Home Loans, Inc.*, --- F. Supp. 2d ---,  
 28 2010 WL 2034769, \*8 (N.D. Cal. May 19, 2010) (same).

<sup>53</sup> Yucaipa Loan Application at 7, [http://www.yucaipa.org/cityPrograms/EIP/PDF\\_Files/  
 Application.pdf](http://www.yucaipa.org/cityPrograms/EIP/PDF_Files/Application.pdf) (last visited Oct. 14, 2010); Sonoma County Loan Application at 9,  
<http://www.drivecms.com/uploads/sonomacountyenergy.org/application.pdf> (last visited Oct. 14,

(Footnote Continued on Following Page)

1 and hold loans that are subject to a PACE lien simply does not violate any law.<sup>54</sup> Indeed, FHFA has  
 2 recognized the priority accorded PACE loans under California law, has made this clear in its public  
 3 statements and has noted the safety and soundness threat posed by this alteration to the credit risk  
 4 profile of the Enterprises.

5 *Second*, California law imposes no liability for either “unlawful” or “unfair” business  
 6 practices against a defendant where the challenged conduct has been expressly sanctioned or  
 7 approved by the governing authority, as occurred here. Thus, for example, the Ninth Circuit  
 8 affirmed dismissal of a claim in *Webb v. Smart Document Solutions, LLC*, noting that a practice  
 9 cannot violate the UCL if the responsible federal agency intended to permit the conduct.<sup>55</sup> FHFA’s  
 10 July 6, 2010 Statement affirms the May 5 Advisories and concludes that, because the first liens  
 11 created by PACE financing create significant safety and soundness issues, prudential actions must  
 12 be taken with respect to loans with senior PACE liens. *See* Cal. Compl. ¶ 4.

13 *Third*, California does not allege conduct by the Enterprises that is otherwise “unfair” under  
 14 the UCL. In construing a claim under the unfairness prong of the UCL, “[c]ourts may not simply  
 15 impose their own notions of the day as to what is fair or unfair.” *Cel-Tech Comm’c’ns, Inc. v. Los*  
 16 *Angeles Cellular Tel. Co.*, 20 Cal. 4th 163, 182, 186-87 (scope of unfair practices under the UCL in  
 17

18 (Footnote Cont’d From Previous Page)

19 2010). *See* [Yucaipa Disclosure Regarding Assessment Financing; Sonoma Disclosure Regarding  
 20 Assessment Financing; Sonoma Consent Agreement at 4].

21 <sup>54</sup> California also contends that the Enterprises violate the UCL when they “intentionally  
 22 mischaracterize” California law relating to PACE “to support their unfounded contention that  
 23 participating in PACE is contrary to” their own Security Instrument. *See, e.g.*, Cal. Am. Compl.,  
 24 ¶¶ 32, 34, 60. As discussed *supra*, (i) the fact that the PACE legislation uses the term “assessment”  
 25 rather than “loan” to describe PACE financing does not make it so and (ii) the Enterprises’  
 26 interpretation of PACE obligations is consistent with the USI, a document they created and enforce  
 27 under the supervision of their Conservator.

28 <sup>55</sup> 499 F.3d 1078, 1087-88 (9th Cir. 2007) (affirming dismissal of UCL claim based on alleged  
 overcharging for medical records because the complaint “failed to sufficiently allege a violation of  
 HIPAA,” and the governing federal agency had indicated the charge at issue was permissible). *See*  
 also, *e.g.*, *Cal Med. Ass’n v. Aetna Healthcare of Cal.*, 94 Cal. App. 4th 151, 169 (2002) (if the  
 Legislature has permitted certain conduct, the courts cannot override that by making it actionable  
 under the UCL); *People v. Duz-Mor Diagnostic Lab., Inc.*, 68 Cal. App. 4th 654, 662, 672 (1998)  
 (conduct not unfair under the UCL because it was “known to and accepted as appropriate by the  
 federal and state regulatory agencies”).

1 competitor actions to include only “conduct that threatens an incipient violation of an antitrust law,  
2 or violates the policy or spirit of one of those laws because its effects are comparable to or the same  
3 as a violation of the law, or otherwise significantly threatens or harms competition”). Though  
4 California courts have not yet provided definitive guidance as to which test now applies in non-  
5 competitor actions such as this one, this District has cautioned that if the “unfairness” under the  
6 UCL is not “tethered to some legislative policy,” courts would be invited to “roam across the  
7 landscape of consumer transactions picking and choosing which they like and which they dislike.”  
8 *Van Slyke v. Capital One Bank*, No. C 07-00671 WHA, 2007 WL 3343943, \*11 (N.D. Cal. Nov. 7,  
9 2007).

10 Here, the Advisories have not had “effects [that] are comparable to or the same as a  
11 violation of the law.” See *Cel-Tech*, 20 Cal. 4th at 187. California’s PACE legislation does not  
12 declare as its purpose that the Enterprises should be obligated to accept loans that are subject to  
13 senior PACE liens. Rather, California’s purpose in implementing PACE was to encourage real  
14 property energy efficient improvements to “reduce energy and water use, provide clean power” and  
15 “promote clean energy and green jobs,” Cal. Am. Compl. ¶ 1.<sup>56</sup>

16 California’s claim also fails under the pre-*Cel-Tech* balancing test because the benefit of  
17 guarding against unsafe and unsound lending practices far outweighs the speculative harm to  
18 Californians in the form of reduced utility costs.<sup>57</sup> While California alleges that the Enterprises’  
19

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20 <sup>56</sup> See *Wolfe v. State Farm Fire & Casualty Ins. Co.*, 46 Cal. App. 4th 554, 564 (noting that  
21 cessation of sales of insurance policies underlying UCL claim was not “unfair” in light of policy of  
22 insurance law to “ensure that insurance is fair, available, and affordable for all Californians,” since  
23 the supposed evil sought to be remedied was unavailability due to high insurance costs, not  
24 unavailability due to a cessation of sales).

25 <sup>57</sup> This Court has previously adopted the pre-*Cel-Tech* balancing test, at least in the context of a  
26 consumer action. See *Morgan v. AT & T Wireless Svcs., Inc.*, 177 Cal. App. 4th 1235, 1254-55  
27 (2009) (to allege an unfair practice under the UCL, a plaintiff must plead that “(1) the consumer  
28 injury is substantial, (2) the injury is not outweighed by any countervailing benefits to consumers or  
29 competition, and (3) the injury is one that consumers themselves could not reasonably have  
30 avoided.”) (internal citations omitted). The Ninth Circuit has indicated that district courts have  
31 discretion in applying either the *Cel-Tech* test or the balancing test in non-competitor actions  
32 brought under the unfair prong of the UCL. *Lozano v. AT&T Wireless Servs., Inc.*, 504 F.3d 718,  
33 736 (9th Cir. 2007) (district court did not err by using balancing test, and adopting either the *Cel-  
34 Tech* or the balancing standard “does not necessitate rejection of the other”).

1 actions are “depriving California and its residents of the economic and environmental benefits” of  
 2 PACE, it overlooks that *all taxpayers* are placed at risk by unsafe and unsound lending practices,  
 3 based in part on risk transfer, absence of consumer underwriting protections, and an absence of  
 4 energy retrofit standards. *See* Cal. Am. Compl. ¶ 60. Conclusory assertions of harm to California,  
 5 without consideration of the countervailing interests in maintaining the health of the fragile U.S.  
 6 mortgage market and the economy as a whole, are insufficient to state a claim for unfair business  
 7 practices. *See Twombly*, 550 U.S. at 555 (plaintiff must plead more than labels and conclusions; a  
 8 formulaic recitation of the elements of a cause of action will not withstand a motion to dismiss).

9 **B. Sonoma’s Intentional Interference with Prospective Economic Advantage Claim**  
 10 **Fails as a Matter of Law**

11 To establish its claim, Sonoma must plead and prove (1) an economic relationship between  
 12 Sonoma and some third party, with the probability of future economic benefit to Sonoma; (2) the  
 13 Enterprises’ knowledge of the relationship between Sonoma and the third party; (3) intentional and  
 14 independently wrongful acts on the part of the Enterprises designed to disrupt the relationship;  
 15 (4) actual disruption of the relationship; and (5) economic harm to Sonoma proximately caused by  
 16 the acts of the Enterprises.<sup>58</sup> Sonoma fails to allege either an existing economic relationship or that  
 17 the Enterprises engaged in any independently wrongful conduct.

18 **1. Sonoma Does Not Allege an Existing Economic Relationship, Much Less**  
 19 **One with a Reasonable Probability of Future Economic Benefit**

20 Sonoma alleges that “through its [PACE] program [it] has prospective economic relations  
 21 with its residents that would result in economic benefit to [Sonoma] in the form of a healthy local  
 22 economy, a reduction in greenhouse gas emissions, and greater water conservation.” *See* Sonoma  
 23 Compl. ¶ 65. This allegation does not satisfy the first element of a claim for interference with  
 24 prospective economic advantage because even if there were such a relationship, the complaint does  
 25 not adequately allege a probability of economic benefit to Sonoma.

26  
 27 <sup>58</sup> *Edwards v. Arthur Andersen LLP*, 44 Cal. 4th 937, 944 (2008); *Reeves v. Hanlon*, 33 Cal. 4th  
 28 1140, 1152 n.6 (2004) (citation omitted); *Korea Supply Co. v. Lockheed Martin Corp.*, 29 Cal. 4th  
 1134, 1153 (2003) (citations omitted); *Della Penna v. Toyota Motor Sales U.S.A., Inc.*, 11 Cal. 4th  
 376, 393 (1995); *Buckaloo v. Johnson*, 14 Cal.3d 815, 827 (1975).

1           The tort of intentional interference with prospective economic advantage protects only the  
 2 expectation that an *existing* economic relationship will produce the desired benefit, not “the more  
 3 speculative expectation that a potentially beneficial relationship will arise.” *Korea Supply Co. v.*  
 4 *Lockheed Martin Corp.*, 29 Cal. 4th at 1164 (internal quotations omitted). Sonoma’s claim— to the  
 5 extent based on a broad class of all possible, yet to be unidentified SCEIP applicants— fails as a  
 6 matter of law.<sup>59</sup> See Sonoma Compl. ¶ 46 (“Defendants’ actions create substantial uncertainty for  
 7 SCEIP participants going forward and are likely to prevent future participation in the program by  
 8 many county property owners.”). Allying this hypothetical class of homeowners does not satisfy  
 9 Sonoma’s burden to plead an existing economic relationship, much less one with the probability of  
 10 future economic benefit. See *Westside Center Assocs. v. Safeway Stores 23, Inc.*, 42 Cal. App. 4th  
 11 507, 523 (1996). California courts have refused to extend liability for interference with a  
 12 prospective advantage to a relationship that is purely conjectural.<sup>60</sup> In the face of this authority,  
 13 Sonoma asserts simply that it has “prospective contractual relationships with its residents that would  
 14 result in economic benefit to the County in the form of a healthy local economy, a reduction in  
 15 greenhouse gas emissions, and greater water conservation.” Sonoma Compl. ¶ 65; see also Sonoma  
 16 Compl. ¶ 46. Such a speculative and conclusory allegation is inadequate to survive a motion to  
 17 dismiss.

18 \_\_\_\_\_  
 19 <sup>59</sup> The particular subsets of current and former PACE participants described by Sonoma do not  
 20 satisfy the “existing relationship” requirement either. See Sonoma Compl., ¶ 46 (since issuance of  
 21 the Advisories, “several property owners . . . have been unable to refinance or transfer their property  
 22 without paying off the amount financed in full . . . . Since FHFA’s issuance of its July 6, 2010  
 23 Statement, 21 applicants have withdrawn their applications from [PACE]”). Any harm allegedly  
 24 caused by a property owner’s inability to refinance (if true) flows to the property owner, not the  
 25 County.

26 <sup>60</sup> See, e.g., *Youst v. Longo*, 43 Cal.3d 64, 71 n.6 (1987) (no claim for interference where the  
 27 requisite relationship involved as yet unknown or nonexistent third persons); *Blank v. Kirwan*, 39  
 28 Cal.3d 311, 331 (1985) (plaintiff had no protectable expectancy of a relation with a class of  
 potential poker club patrons “but at most a hope for an economic relationship and a desire for future  
 benefit.”); *Salma v. Capon*, 161 Cal. App. 4th 1275, 1291 (2008) (reversing in part and directing  
 dismissal of interference claim because there was no allegation of an existing relationship with  
 potential lenders or purchasers for property); *Westside Center*, 42 Cal. App. 4th at 528  
 (“interference with the market theory” insufficient as a matter of law to show company had an  
 economic relationship with prospective buyer that was reasonably likely to produce future  
 economic benefits).

2. Sonoma Fails to Allege an Independently Wrongful Act

Sonoma also fails to specific allege facts demonstrating that the Enterprises engaged in any independently wrongful act beyond the supposed interference. *Reeves v. Hanlon*, 33 Cal. 4th 1140, 1152 (2004); *see also Della Penna*, 11 Cal. 4th at 392-93. “[A]n act is independently wrongful if it is unlawful, that is, if it is proscribed by some constitutional, statutory, regulatory, common law, or other determinable legal standard.” *Korea Supply Co.*, 29 Cal. 4th at 1159; *see Reeves*, 33 Cal. 4th at 1152. “[A]n act must be wrongful by some legal measure, rather than merely a product of an improper, but lawful, purpose or motive.” *Korea Supply Co.*, 29 Cal. 4th at 1159 n.11.

As discussed with respect to California’s UCL claim *supra*, Sonoma has not (and cannot) allege that the Enterprises violated PACE or any other law. Indeed, “[w]ith rare exceptions, a business entity has no duty to prevent financial loss to others with whom it deals directly. A fortiori, it has no greater duty to prevent financial losses to third parties who may be affected by its operations.” *Quelimane Co., Inc. v. Stewart Title Guaranty Co.*, 19 Cal. 4th 26, 59 (1998). *Id.* Accordingly, the California Supreme Court in a related context has held that, “[w]hile title insurers cannot discriminate among purchasers on the basis of the purchasers’ race, ethnicity, religion, gender or other personal characteristics . . . they may opt to limit their potential liability by declining certain risks without violating any statutory or common-law obligation.” *Id.* (title insurers had no duty to issue policies for properties that had been sold at tax sales) (citation omitted). *See also Wolfe*, 46 Cal. App. 4th 554 (with certain exceptions, nothing in the Insurance Code prohibits an insurer from deciding to halt or curtail its sale of new policies). That is so here as well. Nothing in PACE or in California law dictates how the Enterprises as directed by FHFA must conduct their business. Put another way, nothing prohibits the Enterprises from declining, based on reasonable financial judgment, to accept mortgages subject to PACE liens.

**VI. PLAINTIFFS’ DECLARATORY JUDGMENT CLAIMS THAT PACE PROGRAMS DO NOT OFFER LOANS FAIL TO STATE A CLAIM AND MUST BE DISMISSED.**

The premise of Plaintiffs’ non-NEPA claims is that Defendants have incorrectly characterized the funding available from PACE programs as “loans” rather than “assessments.” California and Sonoma both move for a declaration that (1) PACE programs operate through assessments, not loans; (2) assessments receive lien priority under California law; (3) lien priority

1 for assessments does not violate and does not run contrary to Fannie Mae and Freddie Mac’s USIs;  
 2 and (4) the Enterprises’ May 5, 2010 Advisories and FHFA’s July 6, 2010 Statement  
 3 mischaracterize California law and the operation of the Enterprises’ own USIs.<sup>61</sup>

4 Plaintiffs’ claims fail for a number of reasons. *First*, Plaintiffs’ claims are an attempt to  
 5 elevate semantics into justiciable claims by turning differences of opinion over the economic effect  
 6 of the PACE program on the Enterprises into a declaratory judgment action over the meaning of  
 7 “assessments” versus “loans” in a California statute. The parties agree that PACE funds are repaid  
 8 using the local tax assessment system and that PACE obligations have first-lien priority — exactly  
 9 what the California legislation provides. As FHFA’s Statement makes clear, FHFA’s concerns  
 10 about first-lien PACE programs have to do with the risks they create for the Enterprises and,  
 11 consequently, the economic effects they have on mortgages owned or guaranteed by the Enterprises  
 12 — not the label that California or any state has placed on the mechanism by which PACE funds are  
 13 repaid. Regardless of label, PACE obligations make the Enterprises’ mortgage-related assets riskier  
 14 and less valuable. Defendants have determined that the safer and sounder course is for the  
 15 Enterprises not to buy mortgages encumbered with PACE obligations. These determinations are  
 16 not actionable because Plaintiffs do not have a right to require that the Enterprises do business with  
 17 them, or (as to the governmental plaintiffs) their residents or (as to Sierra Club) members. *See*  
 18 *Groos Nat’l Bank*, 573 F.2d at 897 (plaintiffs “cannot claim a constitutionally protected right to do  
 19 business with a particular bank”).<sup>62</sup>

20 *Second*, California has repeatedly and authoritatively stated that PACE programs offer  
 21 “loans.” Specifically, the statute under which the state provides assistance to local governments  
 22 implementing PACE programs mandates that the state must consider whether:

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24 <sup>61</sup> Cal. Am. Compl. ¶ 57; Sonoma Compl. ¶ 62. In addition, Sonoma alleges that FHFA’s  
 25 description of a PACE obligation as a “loan” is “arbitrary, capricious, an abuse of discretion, and  
 26 otherwise not in accordance with law,” in violation of the APA. Sonoma Compl. ¶ 53 (citing 5  
 U.S.C. § 706(2)(A)).

27 <sup>62</sup> Neither the California PACE legislation nor any local government PACE program purports to  
 28 (a) impose any duty on the Enterprises to purchase loans secured by property subject to senior  
 PACE obligations, or (b) addresses the legal effect of such programs under the Security  
 Instruments.

- 1 • “Loan recipients are legal owners of underlying property;”
- 2 • “Loan recipients are current on mortgage and property tax payments;”
- 3 • “Loan recipients are not in default or in bankruptcy proceedings;” and
- 4 • “Loans are for less than 10 percent of the value of the property.”

5 Cal. Pub. Res. Code § 26123(a)(1)-(a)(4) (West 2010) (emphases added). A related statute  
6 mandates that, in order to qualify for assistance, a PACE program must reflect a “[m]inimum legal  
7 loan structure and credit underwriting criteria as determined by the authority are met.” Cal. Pub.  
8 Res. Code § 26121(b) (West 2010) (emphasis added). Similarly, the sponsor of California’s PACE  
9 legislation stated that :

- 10 • PACE programs “provide low interest loans to property owners with  
11 long-term repayments added to their annual property tax[] bills;”
- 12 • “The loans for the upfront costs are repaid through a *voluntary* fee on  
13 the borrower’s property tax bill”; and,
- 14 • “Individual property owners who take the loan then contract directly  
with qualified private solar installers or contractors for energy  
efficiency and solar projects on their buildings.”

15 Legislative History & Intent, Government Code § 53340(c), vol. 4, at 280, 281 (emphasis added)  
16 (Border Decl. Ex. 24). Indeed, the California Attorney General has described PACE financing as a  
17 loan. In a letter to the then-Director of FHFA, James B. Lockhart, dated October 12, 2009,  
18 California Deputy Attorney General Janill L. Richards asserted that:

- 19 • “[FHFA] expressed concern about energy efficiency and renewable  
20 energy loan tax assessment programs, also referred to as Property  
Assessed Clean Energy (PACE) programs”;
- 21 • “property owners pay back the loans through special assessments or  
22 taxes that appear on their property tax bills”; and,
- 23 • “The obligation to repay the loan runs with the land and is assumed by  
the new property owner on sale.”

24 Letter from Janill L. Richards, Deputy Attorney General, California, to James B. Lockhart,  
25 Director, FHFA (Oct. 12, 2009) (emphases added), *available at* <http://ag.ca.gov/globalwarming/pdf/>

1 FHFA\_Letter\_re\_PACE\_programs.pdf (Border Decl. Ex. 25). Sonoma County even provides a  
2 form of “truth in *lending*” disclosure to PACE borrowers.<sup>63</sup>

3 *Third*, Plaintiffs’ assertion that PACE obligations are not loans is wrong as a matter of law.  
4 PACE transactions have all the indicia of home improvement loans, notwithstanding Plaintiffs’  
5 efforts to characterize them as tax assessments. Just like other loans, PACE obligations must be  
6 repaid pursuant to a contract, with interest, over a set period of time. The “settled meaning under  
7 common law” of a loan is a transaction “where, pursuant to a contractual relationship, one party  
8 transfers a defined quantity of money, goods, and services to another and the receiving party agrees  
9 to pay for the sum or items transferred at a later date.” *In re Hawkins*, 317 B.R. 104, 109 (9th Cir.  
10 B.A.P. 2004) (citing *In re Renshaw*, 222 F.3d 82, 88 (2d Cir. 2000)). Just like other loans, PACE  
11 obligations are voluntarily accepted. Tax assessments are just the opposite — compulsorily  
12 imposed within a defined geographic area. *See, e.g., City of Marina v. Bd. of Trustees of the*  
13 *California State University*, 138 P.3d 692, 703 (Cal. 2006) (“An assessment connotes, at the very  
14 least, a compulsory charge imposed by the government on real property. . . . [The payment in this  
15 case] can properly be described neither as compulsory nor, for that reason, as an assessment.”).  
16 And just like other loans, PACE financing funds property-specific improvements that inure to the  
17 benefit of either the individual homeowner or the public at large, but not a particular taxing  
18 district.<sup>64</sup> By contrast, purportedly comparable assessments — such as for sewer or water hook-up  
19 — fund collective, governmentally controlled and maintained improvements for the general use of  
20

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21 <sup>63</sup> *See* Sonoma County Energy Independence Program, Truth in Lending Disclosure Statement,  
22 *available at*  
23 [http://www.drivecms.com/uploads/sonomacountyenergy.org/1678785227truth\\_in\\_lending\\_disclosure\\_agreement.pdf](http://www.drivecms.com/uploads/sonomacountyenergy.org/1678785227truth_in_lending_disclosure_agreement.pdf) (Border Decl. Ex. 26).

24 <sup>64</sup> Black’s Law Dictionary in defining “assessment” notes that “[t]here is a distinction between  
25 public improvements, which benefit the entire community, and local improvements, which benefit  
26 particular real estate or limited areas of land. The latter improvements are usually financed by  
27 means of special, or local, assessments. These assessments are, in a certain sense, taxes. But an  
28 assessment differs from a general tax in that an assessment is levied only on property in the  
immediate vicinity of some local municipal improvement and is valid only where the property  
assessed receives some special benefit differing from the benefit that the general public enjoys.”  
BLACK’S LAW DICTIONARY 125 (8th ed. 2004) (quoting Robert Kratovil, *Real Estate Law* 465 (6th  
ed. 1974)).

1 the municipality. *Silicon Valley Taxpayers Ass’n, Inc. v. Santa Clara County Open Space Auth.*,  
 2 187 P.3d 37, 51 (explaining that “assessments may not be levied for purposes of conferring purely  
 3 general benefits”).<sup>65</sup>

4 *Fourth*, the Enterprises’ interpretation of PACE obligations is also consistent with the USIs.  
 5 California’s PACE legislation specifically provides that PACE financing constitutes a first priority  
 6 lien against the affected real property, and that PACE liens secure the full amount of the  
 7 assessment. *See* Streets and Highways Code § 5898.30. Pursuant to Section 4 of the USI Deed of  
 8 Trust, any lien “which has priority over [the] Security Instrument” must be discharged. *See* USI,  
 9 § 4.<sup>66</sup> Regardless of whether PACE financing is characterized as a “loan” instead of “assessment,”  
 10 and regardless of the “historical treatment” of “other assessments,” the unique risk-shifting  
 11 characteristics of PACE support the Enterprises’ determinations that PACE liens are disallowed  
 12 under the Security Instrument.

13 *Finally*, Plaintiffs are incorrect in asserting that the Defendants’ Advisories and Statement  
 14 “mischaracterize” California law. Nothing in the Advisories or the Statement characterizes  
 15 California law or how the California Code labels its PACE loans in order to provide first-lien  
 16 priority. In fact, the Advisories explain that a first-lien PACE program in *any* state raises safety and  
 17 soundness concerns and is prohibited by the USI.

18 Therefore, Plaintiffs’ declaratory judgment and APA claims based on the premise that  
 19 Defendants’ use of the term “loan” is a mischaracterization fail as a matter of law. Defendants’  
 20 Advisories and Statement acknowledge that the PACE programs operate through assessments. But  
 21 in common parlance, even Plaintiffs state that the PACE programs are providing loans to  
 22

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23  
 24 <sup>65</sup> The California Legislature’s declaration that the PACE program will serve a “public purpose”  
 25 neither identifies any benefit that would primarily affect the municipality nor, to the extent such  
 26 assertion might be implied, provides any substantiation. *See* Cal. Am. Compl. ¶ 43 (quoting Cal.  
 27 Streets & Highways Code § 5898.14). Rather, the legislature identifies global benefits. Cal. Streets  
 28 & Highways Code §§ 5898.14(a)(1) (“Energy conservation efforts . . . are necessary to address the  
 issue of global climate change.”).

<sup>66</sup> That the full amount of the lien is not accelerated upon default under PACE does not change  
 the facts that PACE liens still take priority under California law and that under the express terms of  
 the Security Instrument, they must be discharged.

1 homeowners for energy retrofits. In addition, Plaintiffs' requests for a declaration that Defendants  
 2 "mischaracterize California law" should be denied because the Advisories and the Statement did not  
 3 purport to characterize, adopt, or reject California's chosen terminology of "assessment." See Cal.  
 4 Am Compl. ¶ 57(d); Sonoma Compl. ¶ 62(d). Similarly, given the common understanding of the  
 5 PACE programs as offering loans, Sonoma's claim that FHFA's *description* is "arbitrary,  
 6 capricious, an abuse of discretion, and otherwise not in accordance with law" also fails.<sup>67</sup>

## 7 **VII. PLAINTIFFS' APA CLAIMS FAIL AS A MATTER OF LAW**

### 8 **A. Plaintiffs Lack Prudential Standing for Their APA Claims**

9 To meet the statutory requirements for prudential standing under the APA, a plaintiff must  
 10 establish that "its injury falls within the 'zone of interests' of the statutory provision the plaintiff  
 11 claims was violated." *Nuclear Information and Resource Service v. Nuclear Regulatory Comm'n*,  
 12 457 F.3d 941, 950 (9th Cir. 2006) (quoting *Churchill County v. Babbitt*, 150 F.3d 1072, 1078 (9th  
 13 Cir. 1998)). In determining whether a plaintiff satisfies the "zone of interests" requirement, the  
 14 court must consider the "substantive statute whose duties the plaintiff [is] seeking to enforce." See  
 15 *Cetacean Community v. Bush*, 386 F.3d 1169, 1177 (9th Cir. 2004).<sup>68</sup>

16 Here, Plaintiffs allege that FHFA's safety and soundness determination with respect to first-  
 17 lien PACE programs was arbitrary and capricious, *i.e.*, that FHFA purportedly misapplied HERA.  
 18 See, *e.g.*, Cal. Am. Compl. ¶ 63; Sonoma Compl. ¶ 53; Sierra Club Compl. ¶ 50. But HERA was  
 19 not enacted to protect Plaintiffs' environmental or economic interests. The purpose of HERA was  
 20 to "ensure that the government sponsored Enterprises supporting the mortgage markets operate in a  
 21 safe and sound manner and *fulfill the missions assigned under their charters*, both through  
 22

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23  
 24 <sup>67</sup> "The scope of review under the 'arbitrary and capricious' standard is narrow and a court is not  
 25 to substitute its judgment for that of the agency." *Motor Vehicle Mfrs. Ass'n of U.S. v. State Farm*  
 26 *Mut. Auto. Ins. Co.*, 463 U.S. 29, 43 (1983). This standard is "highly deferential, presuming the  
 27 agency action to be valid and affirming the agency action if a reasonable basis exists for its  
 28 decision." *Indep. Acceptance Co. v. California*, 204 F.3d 1247, 1251 (9th Cir. 2000).

<sup>68</sup> See also *Bennett v. Spear*, 520 U.S. 154, 175 (1997) ("In determining whether the petitioners  
 have standing under the zone-of-interests test to bring their [APA] claims, we look . . . to the  
 substantive provisions of the [statute], the alleged violations of which serve as the gravamen of the  
 complaint.").

1 establishment of a strong, independent regulator and through enhancements to their mission  
 2 responsibilities.”<sup>69</sup> The Fannie Mae and Freddie Mac charters — congressionally enacted federal  
 3 statutes — establish missions relating to housing finance, not environmentalism. *See* 12 U.S.C.  
 4 § 1716 *et seq.* (Fannie Mae charter); 12 U.S.C. § 1451 *et seq.* (Freddie Mac charter).

5 Sierra Club gamely but erroneously attempts to come within the zone of interests of HERA  
 6 by pointing to the provision that states that the Director must ensure that “each regulated entity and  
 7 the manner in which such regulated entity is operated are consistent with the public interest.” Sierra  
 8 Club Compl. ¶ 50 (citing 12 U.S.C. § 4513(a)(1)(b)(iv)). However, the “public interest” referred to  
 9 in HERA does not encompass every conceivable interest or public good such as environmental  
 10 impact or economic effects on Sierra Club members. Rather, Congress defined the relevant public  
 11 interest in the missions of the two Enterprises as set forth in their charters. As defined in their  
 12 charters, the mission of the Enterprises is to provide stability and ongoing assistance to the  
 13 secondary market for residential mortgages and to promote access to mortgage credit throughout the  
 14 nation (including underserved areas) by increasing the liquidity of mortgage investments and  
 15 improving the distribution of investment capital available for residential mortgage financing. 12  
 16 U.S.C. § 1716; 12 U.S.C. § 1451 note. The relevant “public interest” is met by ensuring that the  
 17 Enterprises operate in a safe and sound manner in fulfilling that mission.

18 **B. FHFA’s July 6 Statement Falls Within the Interpretative Rule**  
 19 **Exception to the Notice-and-Comment Requirements of the APA.**

20 Plaintiffs also allege that FHFA violated the APA by failing to provide notice and an  
 21 opportunity for comment before issuing the July 6 Statement.<sup>70</sup> Contrary to Plaintiffs’ contentions,  
 22 the APA does not require federal agencies to follow notice and comment procedures for all  
 23 pronouncements of the agency’s views. Specifically exempt from the notice and comment  
 24

25 \_\_\_\_\_  
 26 <sup>69</sup> H.R. Rep. No. 110-142, at 122 (2007) (House Report on the Federal Housing Finance Reform  
 Act of 2007) (emphasis added).

27 <sup>70</sup> Count 4 of California Am. Compl. ¶¶ 64-67; Count 2 of Sonoma Compl. ¶¶ 56-60; Count 2 of  
 28 Sierra Club Compl. ¶¶ 52-57. FHFA did spend over one year discussing the issues with  
 stakeholders before issuing the Statement.

1 requirement are “interpretative rules, general statements of policy, or rules of agency organization,  
2 procedure, or practice.” 5 U.S.C. § 553(b)(3)(A).

3 The APA distinguishes between interpretative and legislative rules. Legislative rules —  
4 those subject to notice-and-comment rulemaking — “create rights, impose obligations, or effect a  
5 change in existing law pursuant to authority delegated by Congress.” *Hemp Indus. Ass’n v. DEA*,  
6 333 F.3d 1082, 1087 (9th Cir. 2003); *see also National Latino Media Coalition v. F.C.C.*, 816 F.2d  
7 785, 787-88 (D.C. Cir. 1987) (a substantive rule “is intended to have and does have the force of  
8 law”). An interpretative rule, by contrast, “merely explain[s], but do[es] not add to, the substantive  
9 law that already exists in the form of a statute or legislative rule.” *Hemp Indus.*, 333 F.3d at 1087.  
10 The mere fact that an interpretative rule has a substantial impact does not, without more, mean that  
11 it is subject to notice and comment. *Alcaraz v. Block*, 746 F.2d 593, 614 (9th Cir. 1984). The  
12 “‘interpretative rule’ exception was designed to provide agencies with a degree of flexibility . . . and  
13 to allow administrative officers the freedom to explain what they think a regulation or statute means  
14 without undertaking cumbersome proceedings.” *Sentara-Hampton Gen. Hosp. v. Sullivan*, 980 F.2d  
15 749, 759 (D.C. Cir. 1992). To distinguish interpretative rules from legislative rules, the Ninth  
16 Circuit applies a three-part test: (1) whether, in the absence of the rule, there would not be an  
17 adequate legislative basis for an enforcement action; (2) whether the agency explicitly invoked its  
18 general legislative authority; or (3) whether the rule effectively amends a prior legislative rule.  
19 *Hemp Indus.*, 333 F.3d at 1088. FHFA’s issuance of the July 6 Statement fails to satisfy each part  
20 of the test; FHFA properly exercised its statutory authority, as other financial regulators do as a  
21 matter of course, by providing guidance outside the notice-and-comment process to address a matter  
22 of safety and soundness concern.

23 *First*, because there is an adequate legislative basis for FHFA to act regarding PACE  
24 programs even absent the Statement, the Statement cannot be a legislative rule. “If there is no  
25 legislative basis for enforcement action on third parties without the rule, then the rule necessarily  
26 creates new rights and imposes new obligations. This makes it [a] legislative” rule. *Erringer v.*  
27 *Thompson*, 371 F.3d 625, 630-31 (9th Cir. 2004) (citations omitted). In *Erringer*, the Ninth Circuit  
28 held that rules issued by the Secretary of Health and Human Services giving criteria to Medicare  
contractors for the creation of Local Coverage Determinations (“LCDs”) were interpretative and not

1 legislative rules. The court concluded that because the Medicare Act required contractors to deny  
2 claims for services that were not “reasonable and necessary,” even in the absence of the LCDs at  
3 issue, there was an adequate legislative basis for the agency to bring an enforcement action.

4 *Erringer*, 625 F.3d at 631 (quoting 42 U.S.C. § 1395y(a)(1)(A)). Accordingly, the court held the  
5 LCD rules to be interpretative, explaining that they “simply interpret the reasonable and necessary  
6 standard contained in the” Medicare Act and were “not a case of pure delegation of authority to the  
7 agency to determine a standard.”<sup>71</sup> *Erringer*, 625 F.3d at 631.

8 Here, the Statement does not create new rights; it directs the Enterprises to assert their pre-  
9 existing rights so as to fulfill their pre-existing obligation to operate safety and soundly. Providing  
10 supervisory guidance on safety and soundness issues is an exercise of FHFA’s manifest regulatory  
11 authority under HERA, which the Statement did not purport to alter or expand. *See* 12 U.S.C.  
12 § 4513(a)(1)(A) & (a)(1)(B)(i). Accordingly, this is not “a case of pure delegation of authority to  
13 the agency to determine a standard.” *Erringer*, 371 F.3d at 631.

14 *Second*, the Statement does not invoke FHFA’s legislative authority. The second prong of  
15 the Ninth Circuit’s analysis requires the court “to look at the agency’s own treatment of the rule.”  
16 *Erringer*, 371 F.3d at 631. For example, “if Congress had specifically delegated legislative power to  
17 the agency and the agency made it clear that it intended to use that power in promulgating the rule  
18 in question, that would militate toward the rule having the force of law and hence being legislative.”  
19 *Erringer*, 371 F.3d at 631. Nothing in the Statement invokes the rule-making — that is, legislative  
20 — authority conferred by HERA on FHFA. The Statement provides FHFA’s interpretation of the  
21 statutorily imposed safety and soundness parameters under which the Enterprises must operate and  
22 FHFA must regulate.

23 \_\_\_\_\_  
24 <sup>71</sup> The court in *Erringer* contrasted the LCD provisions with the rules at issue in *American Min.*  
25 *Congress v. Mine Safety & Health Admin.*, 995 F.2d 1106 (D.C. Cir. 1993). *Erringer*, 625 F.3d at  
26 630. In *American Min.*, proxy rules promulgated by the SEC were challenged for failure to follow  
27 notice and comment rulemaking. The Securities Exchange Act provision governing proxies  
28 proscribed no specific conduct, only prohibiting proxies “in contravention of such rules and  
regulations as the Commission may prescribe.” *Id.* (citing *American Min.*, 995 F.3d at 1109  
(quoting 15 U.S.C. § 78n(b)). Thus, the proxy rules were found to be legislative because in their  
absence, the Securities Exchange Act provision “provide[d] no legislative basis for the enforcement  
of anything.” 995 F.3d at 1109.

1            *Third*, the Statement also does not effectively amend a prior legislative rule. Plaintiffs make  
 2 no allegation that the Statement amends a prior FHFA regulation, and nothing suggests that the  
 3 Statement is inconsistent with another rule having the force of law. Accordingly, under the third  
 4 prong of the Ninth Circuit test, the FHFA Statement is not a legislative rule.

## 5 **VIII. PLAINTIFFS' NEPA CLAIMS MUST BE DISMISSED**

### 6 **A. The Absence of APA Jurisdiction Requires Dismissal of the NEPA Claims**

7            All three Plaintiffs allege that FHFA violated NEPA, 42 U.S.C. § 4321 *et seq.*, by failing to  
 8 prepare an Environmental Impact Statement (“EIS”) before issuing the Statement.<sup>72</sup> NEPA does  
 9 not contain a private right of action, and therefore Plaintiffs’ NEPA claims are reviewable only if  
 10 jurisdiction exists under the APA. *Ka Makani ‘O Kohala Ohana Inc. v. Water Supply*, 295 F.3d  
 11 955, 959 (9th Cir. 2002). As described *supra*, however, this Court does not have jurisdiction under  
 12 the APA to review FHFA’s actions with respect to PACE programs. *See supra* and 5 U.S.C. § 702  
 13 (no APA jurisdiction if another statute withdraws jurisdiction). Consequently, Plaintiffs’ NEPA  
 14 claims must also be dismissed under Rule 12(b)(1). *See Nat’l Coalition to Save Our Mall v.*  
 15 *Norton*, 161 F. Supp. 2d 14, 19-20 (D.D.C. 2001) (“Given that the court does not have jurisdiction  
 16 under the APA to entertain plaintiffs’ claims, the court also does not have jurisdiction under NEPA  
 17 to review plaintiffs’ specific NEPA arguments.”). Although the Court need look no further than the  
 18 lack of APA jurisdiction, several other grounds support dismissal of Plaintiffs’ NEPA claims.

### 19 **B. FHFA’s July 6 Statement Was Not a Major Federal Action for** 20 **Purposes of NEPA**

21            Only a “major federal action” can trigger NEPA’s procedural requirements. 42 U.S.C.  
 22 § 4332(2)(c). The dual requirements that the action be “major” and “federal” operate  
 23 independently. *Northcoast Environmental Center v. Glickman*, 136 F.3d 660, 668 (9th Cir. 1998).

24            The requirement of “federal” action means that a NEPA plaintiff’s alleged environmental  
 25 injury must be “fairly traceable to the challenged [federal action] and not the result of the  
 26 independent action of some third party . . . .” *Lujan v. Defenders of Wildlife*, 504 U.S. 555, 561

27  
 28 <sup>72</sup> Cal. Am. Compl. ¶¶ 49-55, 68-75; Sonoma Compl. ¶¶ 68-74; Sierra Club Compl. ¶¶ 58-61.

1 (1992) (internal citations and quotations omitted). Here, Plaintiffs cannot “fairly trac[e]” any  
 2 purported environmental consequence to any action of FHFA. The only apparently federal action  
 3 alleged in Plaintiffs’ complaint is FHFA’s issuance of the Statement.<sup>73</sup> But the Statement addresses  
 4 *purely financial* matters; it has *no* direct impact on the environment. *See generally Lujan*, 504 U.S.  
 5 at 561. Indeed, FHFA has indicated that it would favorably consider other programs to support  
 6 energy retrofits that did not create the risks the PACE programs pose to homeowners, lenders, and  
 7 mortgage investors.<sup>74</sup> To the extent Plaintiffs assert that the Statement’s issuance could cause  
 8 significant *indirect* environmental impact, their assertions are impermissibly “speculative or  
 9 hypothetical” and therefore not plausible. *See Northcoast*, 136 F.3d at 668.

10 FHFA has no regulatory authority over the terms of home-improvement financing. Hence,  
 11 the Statement could not and does not require that municipalities shut down their PACE programs  
 12 (indeed, Sonoma has not done so)<sup>75</sup> or that PACE programs take (or not take) any particular form.  
 13 Moreover, although FHFA can and does supervise the criteria mortgage loans must meet in order to  
 14 be eligible for purchase by the Enterprises, there is an active secondary market for mortgage loans  
 15 that do not meet the Enterprises’ portfolio criteria. Defendants’ willingness to purchase mortgage  
 16 with any particular set of attributes and risks simply is not a prerequisite for market acceptance.  
 17 Rather, third parties (such a mortgage lenders seeking to market their loans) exercise their own  
 18 independent judgment in determining whether, given the Enterprises’ lack of appetite for the risks  
 19

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20 <sup>73</sup> For purposes of NEPA, it is irrelevant that the Enterprises are in conservatorship. Being in  
 21 conservatorship does not make the Enterprises federal agencies. *See In re Fed. Home Loan Mortg.*  
 22 *Corp. Derivative Litig.*, 643 F. Supp. 2d 790, 795 (E.D. Va. 2009). As the Supreme Court has  
 23 stated in the analogous national banking context, “the FDIC [receiver] is not the United States.”  
 24 *O’Melveny & Myers v. F.D.I.C.*, 512 U.S. 79, 85 (1994). *See also United States v. Ely*, 142 F.3d  
 1113, 1121 (9th Cir. 1998) (“This earnest argument does not succeed because the FDIC did not sue  
 the defendants as the United States. The FDIC was acting only as the receiver of a failed  
 institution. The United States was not a party.”) (internal quotations omitted).

25 <sup>74</sup> FHFA Statement on Certain Energy Retrofit Loan Programs (July 6, 2010), *available at*  
 26 <http://www.fhfa.gov/webfiles/15884/PACESTMT7610.pdf> (attached as exhibit C to the California  
 27 amended complaint) (“FHFA remains committed to working with federal, state, and local  
 government agencies to develop and implement energy retrofit lending programs with appropriate  
 underwriting guidelines and consumer protection standards. FHFA will also continue to encourage  
 the establishment of energy efficiency standards to support such programs.”)

28 <sup>75</sup> *See* Sonoma Compl ¶ 46 (indicating that Sonoma continues to operate its PACE program).

1 inherent in mortgages subject to PACE obligations, to do business with the Enterprises, and it is the  
2 broader secondary market for residential mortgages that will ultimately determine whether first-lien  
3 PACE programs are or are not viable in light of the risks they pose to holders of mortgage-related  
4 assets. (Indeed, if Plaintiffs are correct that the risks first-lien PACE programs pose to mortgage  
5 assets are “miniscule,” then other secondary market participants will profit from investing in PACE-  
6 encumbered mortgages and ultimately take market share from the Enterprises.) Plaintiffs’ alleged  
7 injury is not “fairly traceable” to FHFA’s issuance of the Statement or any other “federal” action.

8         The separate requirement of “major” federal action is lacking here as well. *Nat’l Wildlife*  
9 *Federation v. Espy*, 45 F.3d 1337 (9th Cir. 1995), is instructive. There, the Farmers Home  
10 Administration (“FmHA”) took title to a wetlands parcel, which it then transferred to a private  
11 party. *Id.* Plaintiffs claimed that NEPA required FmHA to prepare an EIS concerning the transfer,  
12 because the transferee permitted an environmentally harmful activity — grazing — on the parcel.  
13 The court, however, held that the transfer did not constitute “major federal action,” because the  
14 grazing predated FmHA’s acquisition of the parcel. *Id.* at 1343-44. As the court explained,  
15 “[d]iscretionary agency action that *does not alter the status quo* does not require an EIS.” *Id.* at  
16 1344 (emphasis added). The Court reasoned that “[t]he complaint alleges FmHA’s [transfer] of the  
17 [parcel] will result in but one injury — continued degradation of the wetlands from grazing. [But]  
18 [i]t is not alleged that the [transfer] will add to that harm.” *Id.* Hence, under *Nat’l Wildlife*  
19 *Federation*, even federal action that permits “continued degradation” of the environment is not  
20 “major federal action” for NEPA purposes unless it “alter[s] the status quo” in such a way as to  
21 “add to that harm.” *Id.* Here, there can be no plausible allegation that FHFA has altered the status  
22 quo or added to any alleged environmental harm. Rather, the most that can be said is that FHFA’s  
23 action *did not facilitate environmental change* that Plaintiffs seek to foster (the reduction in  
24 emissions that Plaintiffs claim would result from the energy-efficiency projects Plaintiffs claim  
25 PACE programs would spawn), not that FHFA *altered the environmental status quo*. But under  
26 *Nat’l Wildlife Federation*, even if the “status quo” involves “continued degradation” of the  
27 environment — a circumstance FHFA would abhor and that FHFA actively seeks (within the  
28 bounds of its authority) to prevent — “[d]iscretionary agency action that does not alter the status  
quo does not require an EIS.” *Id.*

1 Applying both requirements, a federal agency's mere affirmation or confirmation of non-  
 2 federal action, which merely preserves the status quo, is not major federal action. *See Burbank v.*  
 3 *Goldschmidt*, 623 F.2d 115, 116-17 (9th Cir. 1980) (holding that an EIS is not required when "[t]he  
 4 only aim here is the preservation of the status quo."). But that is exactly what Plaintiffs' contend  
 5 here. Plaintiffs themselves assert that their alleged injury flows primarily from the Enterprises'  
 6 Advisories.<sup>76</sup> Plaintiffs have not alleged, nor could they credibly allege, that the Statement was  
 7 necessary to effectuate the Advisories.<sup>77</sup> As Plaintiffs acknowledge, instead, the Statement provides  
 8 that the Advisories "remain in effect"; that is, the Statement "affirms" or "confirms" the Advisories'  
 9 views on the safety and soundness risks posed by first-lien PACE programs. Cal. Am. Compl. ¶ 4;  
 10 Sonoma Compl. ¶ 45; *see also* Sierra Club Compl. ¶¶ 12, 14 (FHFA "condones and encourages"  
 11 Enterprises' actions). There is no "major federal action" here, and Plaintiffs' NEPA claims  
 12 therefore fail.

13 **C. FHFA Is Statutorily Precluded from Altering Its Safety and Soundness**  
 14 **Determinations Based on Environmental Considerations**

15 Consistent with the maxim that "the law does not require a useless act, particularly where, as  
 16 here, it would only enhance the actor's loss,"<sup>78</sup> a "rule of reason . . . inherent in NEPA and its  
 17 implementing regulations" exempts an agency's decision-making process from NEPA's procedural  
 18 requirements in circumstances where the agency cannot base its decision on environmental  
 19 considerations. *Dep't of Transp. v. Pub. Citizen*, 541 U.S. 752, 786 (where preparation of an EIS  
 20 would serve no purpose, "no rule of reason worthy of that title would require an agency to prepare  
 21 an EIS."). Accordingly, where an agency has no discretion to take environmental considerations  
 22 into account when taking particular actions, NEPA does not require the agency to prepare an EIS.

23  
 24  
 25 <sup>76</sup> Cal. Am. Compl. ¶ 3; Sonoma Compl. ¶ 46; Sierra Club Compl. ¶ 10.

26 <sup>77</sup> The May 5 Freddie Mac Advisory states that "[t]he purpose of this Industry Letter is to remind  
 27 Seller/Serviceers that an energy-related lien may not be senior to any Mortgage delivered to Freddie  
 28 Mac." The May 5 Fannie Mae Advisory states "[t]he terms of the Fannie Mae/Freddie Mac  
 Uniform Security Instruments prohibit loans that have senior lien status to a mortgage."

<sup>78</sup> *U.S. v. Buffalo Coal Min. Co.*, 343 F.2d 561, 565 (9th Cir. 1965). *Buffalo Coal* is neither a  
 NEPA case nor an administrative law decision; we cite it as a concise expression of the maxim.

1 For example, in *Grand Council of the Crees v. FERC*, plaintiffs sued the Federal Energy  
2 Regulatory Commission for, *inter alia*, failing to conduct an environmental assessment under  
3 NEPA when determining “just and reasonable rates” for the sale of electric power by a new entrant.  
4 198 F.3d 950, 953-54, 956 (D.C. Cir. 2000). The court agreed with plaintiffs that the setting of  
5 rates had environmental consequences, but held that when fulfilling its statutory mandate to set “just  
6 and reasonable” rates, FERC “properly d[id] not consider environmental concerns” and, therefore,  
7 the court upheld that agency’s decision not to conduct an EIS or an environmental assessment. *Id.*  
8 at 957, 959.<sup>79</sup>

9 Here, the compromise of safety and soundness that would necessarily result if fiscal  
10 imperatives were to be balanced against purported environmental considerations would be directly  
11 contrary to HERA.<sup>80</sup> FHFA was created amid a national housing crisis following the Congressional  
12 determination that “the continued ability of [Fannie Mae and Freddie Mac] to accomplish their  
13 public mission is important to providing housing in the United States and the health of the nation’s  
14 economy” and therefore “more effective regulation is needed to reduce the risk of the failure of the  
15 Enterprises.” 12 U.S.C. § 4501(2).<sup>81</sup> The Congressional mandate of FHFA is “to ensure that [the  
16 Enterprises] operate[] in a safe and sound manner . . . .” 12 U.S.C. § 4513(a)(1)(B)(i). All other  
17 considerations, including attenuated environmental impact, are subordinate, for if the Enterprises  
18 are to “effectively [] perform their public purposes, they must be financially sound and liquid.” 12

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19  
20 <sup>79</sup> See also *City of New York v. Minetta*, 262 F.3d 169, 177-178 (2d Cir. 2001) (“[W]here the  
21 agency’s decision does not ‘entail the exercise of . . . discretion,’ an EIS is not required.”);  
22 *Sugarloaf Citizens Ass’n v. F.E.R.C.*, 959 F.2d 508, 513 (D.C. Cir. 1992); (“[W]hen an agency has  
23 no discretion to consider environmental values implementing a statutory requirement, its actions are  
24 ministerial and not subject to NEPA.”).

25 <sup>80</sup> The Enterprises abide by applicable state and federal environmental laws, and continue to  
26 support energy-efficiency lending with the appropriate safeguards. Further, the Enterprises require  
27 their seller-servicers to comply with all federal and state laws or they may put back loans made in  
28 violation of such laws.

29 <sup>81</sup> The Enterprises’ financial infirmity at the time of HERA’s passage imperiled not only their  
30 public missions but, as then-Secretary of the Treasury Hank Paulson described when they were put  
31 into conservatorship, threatened “great turmoil in our financial markets here at home and around the  
32 globe.” See Statement by Secretary Henry M. Paulson Jr. on Treasury and Federal Housing Finance  
33 Agency Action to Protect Financial Markets and Taxpayers (Sept. 7, 2008), available at  
34 <http://www.ustreas.gov/press/releases/hp1129.htm> (Border Decl. Ex. 27).

1 C.F.R. Pt. 1720, App. B (2002).<sup>82</sup> As the D.C. Circuit has held in the analogous national banking  
 2 context, a federal regulator exceeds its statutory powers whenever “it undermines the safety and  
 3 soundness of the [regulated entity].” *Indep. Cmty. Bankers Ass’n of S. Dak. v. Bd. of Governors of*  
 4 *the Fed. Reserve Sys.*, 820 F.2d 428, 440 (D.C. Cir. 1987).

5 In short, while HERA’s broad grant of discretion to FHFA “gives deference to the  
 6 [Agency’s] judgment, knowledge, and expertise,” that discretion is limited to actions taken in the  
 7 interests of the Enterprises fiscal health and stability. *See Franklin Sav. Ass’n*, 934 F.2d at 1137  
 8 (discussing the powers granted under the Financial Institutions Reform, Recovery and Enforcement  
 9 Act of 1989, upon which HERA is directly based).<sup>83</sup> Hence, FHFA (as regulator or Conservator)  
 10 cannot, consistent with its statutory mandate, elevate the purported environmental benefits Plaintiffs  
 11 claim that PACE programs might achieve over the financial risk Plaintiffs admit that PACE  
 12 programs would inflict upon the Enterprises mortgage portfolios.<sup>84</sup> As Congress has not authorized  
 13 FHFA to consider environmental effects in supervising the Enterprises’ asset portfolio management  
 14 in light of the financial risks posed by PACE programs, NEPA’s procedural requirements did not  
 15 attach and Plaintiffs’ NEPA claims must be dismissed.

### 16 CONCLUSION

17 For the reasons presented, FHFA respectfully requests that this Court dismiss with prejudice  
 18 each of the Plaintiffs’ complaints against each of the Defendants.

22 <sup>82</sup> Congressional intent is also reflected by the provisions that preclude judicial review of the  
 23 agency’s compliance with ancillary obligations, such as environmental review under NEPA. *See*  
 24 *supra*, discussions of § 4635(b), § 4617(f).

25 <sup>83</sup> Plaintiff Sierra Club’s citation to 12 U.S.C. § 4513(a)(1)(b)(iv), which states that FHFA shall  
 26 ensure that “the activities of each regulated entity . . . are consistent with the public interest,” does  
 27 nothing to alter the analysis here. *Sierra Club Compl.* ¶ 30. Any action that undermines the safety  
 28 and soundness of the Enterprises and increases their risk of failure is, by definition, contrary to the  
 public interest and harmful to the Enterprises’ public interest missions. *See* 12 U.S.C. § 4501(1)-  
 (7). The “public interest” the Director must consider cannot be read to include every conceivable  
 public good. *See supra*.

<sup>84</sup> *See supra* fn. 37.

