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11 UNITED STATES DISTRICT COURT
 12 FOR THE NORTHERN DISTRICT OF CALIFORNIA

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

Plaintiff,

17 v.

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

Defendants.

Case No. 4:10-cv-03084-CW

**FIRST AMENDED COMPLAINT FOR
 DECLARATORY AND EQUITABLE
 RELIEF (UNFAIR BUSINESS
 PRACTICES; VIOLATION OF THE
 NATIONAL ENVIRONMENTAL
 POLICY ACT)**

**(42 U.S.C. §§ 4321 *et seq.*; 28 U.S.C. 2201;
 Cal. Code Civ. Proc. § 1060; Cal. Bus. &
 Prof. Code § 17200 *et seq.*)**

INTRODUCTION

1
2 1. California has pioneered financing for solar power systems, and energy and water
3 efficiency retrofits for homeowners. These programs, called Property Assessed Clean Energy
4 (“PACE”) programs, reduce energy and water use, provide clean power, and are part of
5 California’s efforts to promote clean energy and green jobs. PACE programs do not operate
6 using loans in a traditional sense. Instead, under PACE, local governments finance the upfront
7 installation costs, and homeowners repay those costs over a period of years through assessments
8 on the property tax bill. The California Legislature has declared that “[e]nergy conservation
9 efforts, including the promotion of energy efficiency improvements to residential, commercial,
10 industrial, or other real property are necessary to address the issue of global climate change”;
11 “[t]he upfront cost of making residential, commercial, industrial, or other real property more
12 energy efficient prevents many property owners from making those improvements”; and that,
13 therefore, PACE serves “a public purpose[.]”¹

14 2. Now, by misrepresenting the nature of the PACE programs and municipal financing,
15 in violation of California law, Defendants Federal National Mortgage Association (commonly
16 known as “Fannie Mae”) and the Federal Home Loan Mortgage Corporation (called “Freddie
17 Mac”), are severely hampering California’s efforts to assist thousands of California homeowners
18 to reduce their energy and water use, help drive the state’s green economy, and create significant
19 numbers of skilled, stable and well paying jobs. The actions of these government-sponsored,
20 shareholder-owned private corporations have placed California’s PACE programs – and the
21 hundreds of millions of dollars in federal stimulus money supporting them – at immediate risk
22 while benefitting their own pecuniary interests.

23 3. On May 5, 2010, Fannie Mae and Freddie Mac each issued advice letters to all
24 lending institutions stating that mortgages for residences that also have PACE “loans” with first
25 lien priority (providing PACE funders with priority in recovering unpaid assessments in case of
26 foreclosure) are not allowed under these entities’ standardized mortgage documents. Fannie Mae

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28 ¹ Cal. Streets & Hwy. Code § 5898.14.

1 and Freddie Mac together own or guarantee about half of all residential home mortgages in the
2 United States. Fannie Mae and Freddie Mac purchase home loans from banks and other lenders,
3 in theory freeing up more capital for additional home mortgage lending. Because Fannie Mae
4 and Freddie Mac control the mortgage resale market, lenders will not issue mortgages that do not
5 meet Fannie Mae's and Freddie Mac's requirements. As a result, Fannie Mae's and Freddie
6 Mac's determination – which misrepresents California law – essentially forecloses residential
7 PACE programs.

8 4. On July 6, 2010, the Federal Housing Finance Agency (“FHFA”) affirmed these
9 entities' loan purchase restrictions for residences with PACE funding in the form of a Statement
10 and directive to Fannie Mae, Freddie Mac, and the Federal Home Loan Banks. Fannie Mae,
11 Freddie Mac, and FHFA mischaracterize PACE funding as “loans,” rather than “assessments” as
12 they are unequivocally defined under California law. The FHFA acknowledged that, by affirming
13 Fannie Mae's and Freddie Mac's position, the agency was effectively stopping PACE programs
14 in California – in its words, effecting a “pause” in PACE – with no clear indication of when, if
15 ever, such programs would be allowed to move forward in the future. At this critical juncture,
16 this “pause” will cause permanent, irreparable damage to PACE, threatening tens of millions of
17 dollars of federal stimulus monies currently allocated for California PACE programs. FHFA has
18 effectively precluded PACE programs in California and deprived California and its citizens of the
19 associated residential energy and water efficiency and renewable energy benefits, thereby
20 significantly impacting the human environment, without complying with the Administrative
21 Procedure Act (“APA”) and without completing the required environmental review under the
22 National Environmental Policy Act (“NEPA”).

23 5. Accordingly, California seeks a prompt judicial declaration as against Fannie Mae
24 and Freddie Mac that, under California law: (a) PACE programs operate by assessments, not
25 loans, and such assessments are valid; (b) liens that may result from PACE assessments, like
26 those resulting from other types of assessments, have priority over mortgages; and (c)
27 participation in PACE programs is compatible with, and not in violation of, Fannie Mae's and
28 Freddie Mac's standardized mortgage documents. California also seeks a ruling from this Court

1 that FHFA is required to comply with the APA and conduct the required environmental review
2 under NEPA before taking any action that will limit or foreclose PACE in California.

3 **JURISDICTION AND VENUE**

4 6. This Court has jurisdiction pursuant to 28 U.S.C. § 1331 (action arising under the
5 laws of the United States), 5 U.S.C. §§ 701-706 (Administrative Procedure Act), 12 U.S.C.
6 1452(f) (original jurisdiction in federal district court for actions involving Freddie Mac), and 28
7 U.S.C. § 1367 (supplemental jurisdiction).

8 7. An actual controversy exists between the parties within the meaning of 28 U.S.C. §
9 2201(a). This Court may grant declaratory relief, injunctive relief, and any additional relief
10 pursuant to 28 U.S.C. §§ 2201, 2202 and 5 U.S.C. §§ 705, 706 and under any relevant state laws
11 pursuant to its supplemental jurisdiction.

12 8. The FHFA has made a final administrative determination that is subject to review
13 under the APA. 5 U.S.C. §§ 702, 704.

14 9. Venue lies in this judicial district by virtue of 28 U.S.C. § 1391(e) and Civil Local
15 Rule 3-2(d), because a substantial part of the events or omissions giving rise to the claims
16 occurred in this district.

17 **PARTIES**

18 10. Defendant Fannie Mae is a federally chartered, private corporation, of a type
19 commonly referred to as a government-sponsored enterprise (“GSE”). Fannie Mae facilitates the
20 secondary market in residential mortgages. Together with Freddie Mac, another GSE, Fannie
21 Mae owns or guarantees about half the home loans in the U.S. and California. Fannie Mae is
22 publicly traded, has a Board of Directors, and is required to report to the Securities and Exchange
23 Commission. By statute, Fannie Mae has the power to sue and be sued in both state and federal
24 court. 12 U.S.C. § 1723a(a).

25 11. Defendant Michael J. Williams is the Chief Executive Officer of Fannie Mae and is
26 sued in that capacity.

27 12. Defendant Freddie Mac is a federally chartered, private corporation and also a GSE.
28 Freddie Mac facilitates the secondary market in residential mortgages. Together with Fannie

1 Mae, another GSE, Freddie Mac owns or guarantees about half the home loans in the U.S. and
2 California. Freddie Mac is publicly traded, has a Board of Directors, and is required to report to
3 the Securities and Exchange Commission. By statute, Freddie Mac has the power to sue and be
4 sued. 12 U.S.C., § 1452(c).

5 13. Defendant Charles E. Haldeman, Jr. is the Chief Executive Officer of Freddie Mac
6 and is sued in that capacity.

7 14. Defendant FHFA is a federal government agency created on July 30, 2008, to oversee
8 Fannie Mae, Freddie Mac, and the Federal Home Loan Banks. As of June 2008, the combined
9 debt and obligations of these entities totaled \$6.6 trillion, exceeding the total publicly held debt of
10 the United States by \$1.3 trillion.

11 15. Defendant Edward DeMarco is the Acting Director of the Federal Housing Finance
12 Agency and is sued in that capacity.

13 16. California brings this action by and through Attorney General Edmund G. Brown Jr.
14 Attorney General Brown is the chief law enforcement officer of the state. This complaint is
15 brought pursuant to the Attorney General's independent constitutional, common law, and
16 statutory authority to represent the public interest. Cal. Gov. Code §§ 12600–12612; Cal. Const.,
17 art. V, § 13.

18 MISCHARACTERIZATION OF CALIFORNIA LAW

19 17. The actual controversy at issue in this complaint arises out of Fannie Mae's and
20 Freddie Mac's participation in, and influence over, the residential mortgage market in California
21 and, more specifically, actions taken by Fannie Mae and Freddie Mac on May 5, 2010 and by
22 FHFA on July 6, 2010.

23 18. For well over 100 years, local governments in California have used their assessment
24 powers to finance improvements that serve a public purpose, such as the paving of roads,
25 sidewalk improvements, and the undergrounding of utilities. Under California law, it is well
26 established that in some instances, privately-owned improvements, *e.g.*, seismic and fire-related
27 improvements, can also serve a valid public purpose.

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1 19. Under longstanding California law, assessments create liens that have priority over
2 mortgages.

3 20. By their practices and documents, Fannie Mae and Freddie Mac have for decades
4 accepted and agreed that in California, assessments constitute priority liens.

5 21. Under California law, local governments in California may finance the installation on
6 private property of roof-top solar, other distributed generation renewables, and energy and water
7 efficiency improvements using the same assessment mechanism. Charter cities are authorized to
8 establish PACE programs under the Communities Facilities District Act (commonly known as
9 Mello-Roos Act), which has been in existence since 1982.² With the passage of California
10 Assembly Bill 811 (AB 811) in 2008,³ all other local governments in California are similarly
11 authorized. Under the plain language of California law, any liens that result from PACE
12 assessments have priority over mortgages, operating in the same way as other assessments.

13 22. PACE programs have been multiplying rapidly since the passage of AB 811. One
14 very successful example is Sonoma County's Energy Independence Program. Since March of
15 2009, Sonoma County's program has financed nearly 1,000 projects – including, solar panels,
16 tankless water heaters, reflective roofing, smart irrigation controllers, and attic insulation –
17 totaling over \$30 million.

18 23. In a letter dated June 18, 2009, and addressed to the Conference of Bank Supervisors,
19 the National Association of Credit Union Supervisors, the American Association of Residential
20 Mortgage Regulators, the National Governors Association, and the National Conference of State
21 Legislatures, FHFA asserted in general terms purported risks posed to homeowners and lenders
22 posed by PACE. In making its assertions, the FHFA did not cite any particular state law, or data
23 or evidence gathered from any operating or contemplated PACE program. When FHFA's
24 assertions came to the attention of the California Attorney General, his staff contacted FHFA's
25 General Counsel and offered to discuss the particulars of California PACE programs and why

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27 ² Cal. Gov. Code § 53311 *et seq.*

28 ³ Cal. Streets & Hwy. Code §§ 5898.12, 5898.14, 5898.20, 5898.21, 5898.22, and 5898.30.

1 FHFA's statements concerning risk were unfounded. In response, in a letter dated October 29,
2 2009, Edward DeMarco, FHFA's Acting Director, created the impression that the agency would
3 make a fully informed decision, assuring California that FHFA was "working with other Federal
4 departments and agencies to identify and promote best practices in this area so that the goals of
5 improved energy efficiency, consumer protection, and prudent lending practices may be aligned."

6 24. In September 2009, Fannie Mae issued a "Lender Letter" directed to the home
7 mortgage industry (Exhibit A to this Complaint). The Lender Letter, which contained a link to
8 the FHFA's June 18, 2009 letter, stated that Fannie Mae was "reviewing its underwriting
9 guidelines to determine appropriate requirements in jurisdictions that have enacted legislation
10 establishing [PACE]" and that "[u]ntil such guidelines are issued, lenders should treat [PACE]
11 payments as a special assessment in underwriting a borrower where the security property is
12 subject to an existing [PACE] loan." The Lender Letter further stated that mortgage "[s]ervicers
13 should treat [PACE] as any tax or assessment that may take priority over Fannie Mae's lien."

14 25. Meanwhile, other federal agencies proceeded to support and encourage the
15 development of PACE programs. The White House highlighted PACE in its "Recovery Through
16 Retrofit" initiative in October 2009. In the accompanying report,⁴ the White House noted the
17 benefits of PACE: "Property tax or municipal energy financing allows the costs of retrofits to be
18 added to a homeowner's property tax bill, with monthly payments generally lower than utility bill
19 savings. This arrangement attaches the costs of the energy retrofit to the property, not the
20 individual, eliminating uncertainty about recovering the cost of the improvements if the property
21 is sold." The White House further stated that "Federal Departments and Agencies will work in
22 partnership with state and local governments to establish standardized underwriting criteria and
23 safeguards to protect consumers and minimize financial risks to the homeowners and mortgage
24 lenders." On October 18, 2009, the White House released its "Policy Framework for PACE
25 Financing Programs,"⁵ in which Vice President Joseph Biden announced support "for the use of

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27 ⁴ Available at http://www.whitehouse.gov/assets/documents/Recovery_Through_Retrofit_Final_Report.pdf.

28 ⁵ Available at http://www.whitehouse.gov/assets/documents/PACE_Principles.pdf.

1 federal funds for pilot programs of PACE financing to overcome barriers for families who wish to
2 invest in energy efficiency and renewable energy improvements.”

3 26. The Department of Housing and Urban Development (“HUD”) and Department of
4 Energy (“DOE”) expressly identified PACE as eligible for receipt of hundreds of millions of
5 dollars in federal stimulus funds. Through the American Recovery and Reinvestment Act’s
6 Energy Efficiency and Conservation Block Grant Program, DOE awarded over \$300 million
7 directly to larger California local governments, and an additional \$35 million for disbursement
8 through the California Energy Commission (“CEC”) to smaller local governments. The Recovery
9 Act also funded the State Energy Program, under which California received more than \$226
10 million. Both DOE and the CEC expressly supported the use of these funds for PACE programs,
11 and, accordingly, dozens of counties and cities across California were poised to launch their own
12 PACE programs in part with federal dollars.

13 27. On May 5, 2010, Fannie Mae and Freddie Mac each unexpectedly issued a new
14 “Lender Letter” directed to the home mortgage industry. Fannie Mae’s Lender Letter (Exhibit B
15 to this Complaint) provides in relevant part:

16 Fannie Mae has received a number of questions from seller-servicers regarding
17 government-sponsored energy loans, sometimes referred to as Property Assessed Clean
18 Energy (PACE) loans. PACE loans generally have automatic first lien priority over
19 previously recorded mortgages. *The terms of the Fannie Mae/Freddie Mac Uniform*
20 *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.

21 (Emphasis added.)

22 28. Freddie Mac’s May 5, 2010 Lender Letter (also attached as Exhibit B) provides in
23 relevant part:

24 The purpose of the Industry Letter is to remind Seller/Servicers that an energy-related lien
25 may not be senior to a Mortgage delivered to Freddie Mac. Sellers/Servicers should
26 determine whether a state or locality in which they originate mortgages has an energy loan
27 program and whether a first priority lien is permitted.
28

1 29. On May 7, 2010, DOE, after consultation within the federal government and with
2 other stakeholders, issued its “Guidelines for Pilot PACE Financing Programs”⁶ to “help ensure
3 prudent financing practices during the current pilot PACE programs.”

4 30. On July 6, 2010, FHFA issued a definitive Statement on PACE and directive to
5 Fannie Mae, Freddie Mac, and the Federal Home Loan Banks, together with a cover letter
6 addressed to the California Attorney General. FHFA’s Statement provides that the May 5, 2010
7 Fannie Mae and Freddie Mac “lender letters remain in effect.” Further, both the cover letter and
8 the Statement expressly acknowledge that by affirming Fannie Mae’s and Freddie Mac’s May 5,
9 2010 Lender Letters, the FHFA is effecting a “pause” in California PACE programs. While the
10 Statement holds open the possibility that at some time in the future, the FHFA may allow PACE
11 programs to resume, there is no schedule for the agency to revisit its determination and no
12 guarantee that it will authorize PACE to proceed. In addition, as discussed in the immediately
13 following paragraphs, any pause in PACE at this critical juncture likely is the death knell of
14 widespread, effective PACE programs in California. The FHFA’s Statement and cover letter to
15 the California Attorney General are attached to this Complaint as Exhibit C.

16 31. The summary factual assertions contained in the FHFA’s July 6, 2010 letter are not
17 supported by analysis or citation to authority or evidence. On information and belief, California
18 alleges that the FHFA made its decision without considering data related to successful, operating
19 programs such as Sonoma County’s Energy Independence Program, and thus without considering
20 whether the hypothetical risks it had identified were borne out in practice.

21 32. The May 5, 2010, Lender Letters and the FHFA’s Statement misrepresent the law
22 governing PACE programs in California. California state law is clear: PACE financing is not
23 accomplished through loans, but through assessments.

24 33. Under California law, liens resulting from PACE assessments, like other assessments,
25 have priority over mortgages. Defendants seek to change that priority for their own benefit in
26 violation of California law.

27 ⁶ Available at
28 http://www1.eere.energy.gov/wip/pdfs/arra_guidelines_for_pilot_pace_programs.pdf.

1 now on indefinite hold. Every prospective PACE participant who now cannot participate in the
2 program is being denied economic benefits, including, but not limited to, lower energy and water
3 bills and the opportunity to obtain favorable financing under PACE.

4 36. Defendants' actions are, in addition, endangering the majority of the \$110 million in
5 American Recovery and Reinvestment Act of 2009 State Energy Program funds awarded by the
6 CEC to local governments. After the FHFA's July 6, 2010 Statement, the CEC asked for
7 clarification from DOE on distribution of federal stimulus funds for PACE programs in
8 California. DOE responded that, while it and the Administration continue to support PACE, in
9 light of Defendants' actions, "prudent management of the Recovery Act compels DOE and
10 Recovery Act grantees to consider alternatives to programs in which the PACE assessment is
11 given a senior lien priority." CEC now must consider whether to reallocate federal stimulus
12 funds to avoid the loss of tens of millions of dollars currently allocated for use in California
13 PACE programs. In addition, the CEC reports that Defendants' actions threaten California's
14 ability to obtain an infusion of funding from the Home Star Energy Retrofit Act of 2010 (H.R.
15 5019). Defendants' actions also are interfering with the CEC's ability to complete its duties
16 under California Assembly Bill 758, a state law that requires the CEC to develop a
17 comprehensive energy efficiency program for all existing residential and commercial buildings.

18 37. Fannie Mae's and Freddie Mac's actions are unfair as defined in California Business
19 and Professions Code § 17200, in that they have issued Lender Letters knowing that the effect
20 will be effectively to stop PACE in California, depriving California homeowners of the ability to
21 participate in the program and the State of California of the larger benefits of PACE. Fannie
22 Mae's and Freddie Mac's action are unlawful as defined in California Business and Professions
23 Code § 17200, in that they constitute intentional interference with the prospective economic
24 advantage, including the advantage that otherwise would flow to homeowners, in the form of
25 lower energy and water bills and favorable financing, and to the State of California in the form of
26 federal monies.

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FAILURE TO COMPLY WITH THE ADMINISTRATIVE PROCEDURE ACT

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38. Pursuant to 5 U.S.C. § 706 and controlling case law, an agency must “examine the relevant data and articulate a satisfactory explanation for its action.” *F.C.C. v. Fox Television Stations, Inc.*, ___ U.S. ___, 129 S.Ct. 1800, 1810 (2009) (quoting *Motor Vehicle Mfrs. Assn. of United States, Inc. v. State Farm Mut. Automobile Ins. Co.*, 463 U.S. 29, 43 (1983)). An “agency must show that there are good reasons” for its action. *Fox Television Stations*, 129 S.Ct. at 1811. An agency's failure to supply such reasons renders the agency’s action arbitrary and capricious and, therefore, invalid.

39. In its July 6, 2010, two-page Statement, FHFA made a series of generalized and summary statements about the purported risks posed by PACE programs. For example, the agency asserts that PACE “presents significant risk to lenders and secondary market entities”

40. None of the FHFA’s statements is supported by citations to evidence, lessons learned from operating PACE programs (such as Sonoma County’s successful Energy Independence Program), and/or specific provisions of state PACE law. Moreover, FHFA’s statements cannot reasonably be supported. For example, contrary to the FHFA’s assertion set forth in the previous paragraph, PACE in California presents no significant risk to lenders or secondary markets. PACE programs in California are designed to prevent participation by property owners who have a history of bankruptcy, property tax defaults or mortgage defaults or involuntary liens on their property. Moreover, PACE improvements increase property value and lower homeowners’ energy bills from the first day they are installed. PACE thus reduces the risk of default by making it more likely that that the homeowner will stay current with the mortgage.

41. In addition, contrary to FHFA’s assertion in its July 6, 2010 Statement, the risk to Fannie Mae and Freddie Mac, which hold a portfolio of mortgages, is miniscule, as the following mortgage foreclosure scenario illustrates:

- A local agency levies a \$15,000 PACE assessment on a house valued at \$300,000 with a \$250,000 mortgage; the \$15,000 PACE assessment reflects the costs of a renewable energy system and energy efficiency upgrades, less all

1 available rebates and incentives. (Some large solar projects may cost more;
2 some efficiency-only upgrades will be substantially less.)

3 • Assuming a 7% interest rate (which is on the high side) and a 20-year payback
4 period, the estimated total annual PACE assessment installments would be
5 \$1,470.

6 • If the homeowner stops paying the mortgage and property taxes, including
7 PACE and other assessments, delinquency on the mortgage occurs when the
8 home owner is less than three monthly payments behind in the mortgage, and
9 default occurs when the homeowner is three or more monthly payments behind.
10 Default triggers foreclosure of the mortgage.

11 • At the time the private mortgage is foreclosed, it is likely that at most, one
12 year’s worth of PACE assessment installments totaling ~\$1,500 would be
13 delinquent and subject to foreclosure. (This is because under the laws of most
14 states, including California, there is no acceleration of the entire amount
15 financed for failure to pay an assessment installment, including a PACE
16 assessment; rather, the new owner assumes the continuing obligation to pay the
17 assessment installments as they become due.)

18 • Thus, with a “portfolio” of mortgages that have PACE liens, assuming a high
19 foreclosure rate of 10%, the risk of PACE foreclosures would average \$150 per
20 home (10% x \$1,500).

21 • Using a more reasonable foreclosure rate of 5%, the risk of PACE foreclosures
22 would average a mere \$75 per home.

23 42. In its July 6, 2010 Statement, FHFA also asserts that PACE assessments “do not have
24 the traditional community benefits associated with taxing initiatives.”

25 43. In fact, California already conclusively has determined that PACE provides
26 substantial public benefits. In passing California’s PACE legislation (California Assembly Bill
27 811 (Cal. Stats. 2008, ch. 159)), the California legislature expressly found that:
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- 1 • “Energy conservation efforts, including the promotion of energy efficiency
- 2 improvements to residential, commercial, industrial, or other real property are
- 3 necessary to address the issue of global climate change”
- 4 • “The upfront cost of making residential, commercial, industrial, or other real
- 5 property more energy efficient prevents many property owners from making
- 6 those improvements. To make those improvements more affordable and to
- 7 promote the installation of those improvements, it is necessary to authorize an
- 8 alternative procedure for authorizing assessments to finance the cost of energy
- 9 efficiency improvements.”
- 10 • “[A] public purpose will be served by a contractual assessment program that
- 11 provides the legislative body of any city with the authority to finance the
- 12 installation of distributed generation renewable energy sources and energy
- 13 efficiency improvements that are permanently fixed to residential, commercial,
- 14 industrial, or other real property.”

15 44. For these reasons and others, the FHFA’s July 6, 2010 Statement and directive is
 16 arbitrary and capricious.

17 45. The APA not only requires that an agency provide good reasons for its actions, but
 18 where that action constitutes “a statement of general or particular applicability and future effect
 19 designed to implement, interpret, or prescribe law or policy[,] the agency must follow the APA’s
 20 rule making procedures. 5 U.S.C. §§ 551(4), 551(5), 553. The APA’s rule making requirements
 21 include publication of the proposed rule in the Federal Register and an opportunity for public
 22 comment.

23 46. The FHFA’s July 6, 2010 Statement and directive to Fannie Mae, Freddie Mac
 24 constitutes a rule under the APA. The agency did not publish the proposed rule in the Federal
 25 Register and provided no opportunity for public comment.

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FAILURE TO CARRY OUT ENVIRONMENTAL REVIEW

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2 47. After Fannie Mae and Freddie Mac issued the May 5, 2010, Lender Letters, the
3 California Attorney General’s Office sought clarification from FHFA through letters dated May
4 17, 2010, May 19, 2010, and May 22, 2010. The Attorney General’s letters are attached to this
5 Complaint as Exhibit D.

6 48. On July 6, 2010, the FHFA responded with its final, definitive Statement that ends
7 the effective operation of PACE in California. The Statement, discussed above, is attached to this
8 Complaint as Exhibit C.

9 49. Under the National Environmental Policy Act (“NEPA”), 42 U.S.C. §§ 4321 *et seq.*, a
10 major federal action that may significantly impact the human environment cannot be approved
11 without an Environmental Assessment (“EA”) or Environmental Impact Statement (“EIS”).

12 50. NEPA is the “basic national charter for protection of the environment.” 40 C.F.R.
13 §1500.1. NEPA’s purpose is to ensure “public officials make decisions that are based on
14 understanding of environmental consequences, and to take actions that protect, restore, and
15 enhance the environment” and to “ensure that environmental information is available to public
16 officials and citizens before decisions are made and before actions are taken.” 40 C.F.R. §
17 1500.1(b)-(c). NEPA is designed to “encourage and facilitate public involvement in decisions
18 which affect the quality of the human environment.” 40 C.F.R. § 1500.2(d). “Human
19 environment” is defined “comprehensively to include the natural and physical environment and
20 the relationship of people with that environment.” 40 C.F.R. § 1508.14.

21 51. To achieve these purposes, NEPA requires all federal agencies to prepare a “detailed
22 statement,” the EIS, regarding all “major federal actions significantly affecting the quality of the
23 human environment.” 42 U.S.C. § 4332(c).

24 52. Where an agency does not know whether the effects of its proposed action will be
25 “significant,” it may prepare an EA. 40 C.F.R. § 1501.4(b). An EA consists of an analysis of the
26 need for the proposed action, of alternatives to the proposed action, and of the environmental
27 impacts of both the proposed action and the alternatives. 40 C.F.R. § 1508.9. If the EA indicates
28

1 that the federal action may significantly affect the quality of the human environment, the agency
2 must prepare an EIS. 40 C.F.R. § 1501.4(c).

3 53. Under Ninth Circuit precedent, an agency must prepare an EIS if substantial
4 questions are raised as to whether a project may have significant effects.

5 54. If an agency decides not to prepare an EIS, it must prepare a Finding of No
6 Significant Impact explaining the reasons for the agency's decision. 40 C.F.R. § 1508.13.

7 55. Here, the FHFA's Statement puts an end to the effective operation of PACE in
8 California, wiping out in a single action a state-law sanctioned program designed to assist
9 homeowners and improve and protect the environment. FHFA has taken this action without
10 considering even a single, less drastic alternative or conducting the required environmental
11 review.

12 **FIRST CAUSE OF ACTION**

13 (For Declaratory Relief; Against All Defendants)

14 56. California realleges and incorporates by reference the allegations of the preceding
15 paragraphs.

16 57. Under 28 U.S.C. § 2201 and Cal. Code of Civ. Proc. § 1060, California seeks a
17 declaration of legal rights and duties with respect to Defendants' characterization of PACE
18 programs established under California law as "loans" as opposed to "assessments." More
19 specifically, California seeks a declaration that:

- 20 a. PACE programs operate through assessments, not loans;
- 21 b. Assessments receive lien priority under California law;
- 22 c. Lien priority for assessments does not violate and does not run contrary to Fannie
23 Mae's or Freddie Mac's Uniform Security Instruments;
- 24 d. The GSE's May 5, 2010 Lender Letters, and FHFA's July 6, 2010 Statement
25 mischaracterize California law and the operation of the GSE's own Uniform Security
26 Instruments.

27 58. Without a prompt judicial declaration, PACE programs in California will be
28 substantially reduced or eliminated, to the detriment of current and prospective PACE participants

1 and the many green industries that serve PACE, and the operation of an important state law
2 designed to serve California’s energy conservation, water conservation, and greenhouse gas
3 reduction objectives will be thwarted.

4 **SECOND CAUSE OF ACTION**

5 (For Unfair Business Practices, Cal. Bus. & Prof. Code § 17200; Against Fannie Mae and
6 Freddie Mac)

7 59. California realleges and incorporates by reference the allegations of the preceding
8 paragraphs.

9 60. From May 5, 2010 and continuing to the present, Fannie Mae and Freddie Mac, and
10 each of them, have engaged in and continue to engage in, aided and abetted and continue to aid
11 and abet, and conspired to and continue to conspire to engage in acts or practices that constitute
12 unfair competition as defined in California Business and Professions Code section 17200. In each
13 instance, Fannie Mae’s and Freddie Mac’s acts or practices have interfered and are interfering
14 with homeowners’ ability to participate in PACE and to achieve the economic benefits of the
15 program, and, by effectively stopping PACE, are depriving California and its residents of the
16 economic and environmental benefits of this state law-based program. Fannie Mae’s and Freddie
17 Mac’s act or practices, which were intended to, and/or had the effect of creating lien priority and
18 a more favorable financial position for Fannie Mae and Freddie Mac, include, but are not limited
19 to, the following:

- 20 a. characterization of PACE assessments as loans without support for such
- 21 characterization under California law; and
- 22 b. claims that PACE assessments providing first lien priority are contrary to Fannie
- 23 Mae’s and Freddie Mac’s Uniform Security Instruments.

24 **THIRD CAUSE OF ACTION**

25 (For Violation of and the Administrative Procedure Act, 5 U.S.C. § 706; Against FHFA)

26 61. California realleges and incorporates by reference the allegations of the preceding
27 paragraphs.

1 3. That Defendants Freddie Mac and Fannie Mae and all persons who act in concert
2 with them be permanently enjoined from engaging in unfair competition or in any practice that
3 facilitates unfair competition as defined in California Business and Professions Code section
4 17200, including, but not limited to, the acts and practices alleged in this Complaint, under the
5 authority of California Business and Professions Code section 17203;

6 4. That the Court issue a declaratory judgment that Defendant FHFA violated the APA
7 by acting arbitrarily, capriciously, in an abuse of discretion, not in accordance with law and/or
8 without observance of proper procedures required by law by failing to provide good reasons for
9 its July 6, 2010 Statement, and by failing to follow required rule making procedures, and that the
10 Court set aside FHFA’s July 6, 2010 Statement;

11 5. That the Court issue a declaratory judgment that Defendant FHFA violated NEPA
12 and the APA by acting arbitrarily, capriciously, in an abuse of discretion, not in accordance with
13 law and/or without observance of proper procedures required by law by failing to prepare
14 appropriate environmental review before issuing its July 6, 2010 Statement and that the Court set
15 aside FHFA’s July 6, 2010 Statement;

16 6. That the Court award the costs of suit incurred; and

17 7. That the Court award such other and further relief as it may deem proper.

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19 Dated: September 15, 2010

Respectfully Submitted,
EDMUND G. BROWN JR.
Attorney General of California

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22
23 /s/ Janill L. Richards

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