

2004

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Recommended Citation

Bernhardt, Roger, "Enforceability of affordable housing restrictions: Dieckmeyer v Redevelopment Agency, 2004" (2004).

Publications. Paper 281.

<http://digitalcommons.law.ggu.edu/pubs/281>

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**Enforceability of affordable housing restrictions:
Dieckmeyer v Redevelopment Agency, 2004
Roger Bernhardt**

Although condominium owner who purchased unit under affordable housing program was entitled to prepay loan, she was not entitled to reconveyance of trust deed that also secured her compliance with affordable housing restrictions.

Dieckmeyer v Redevelopment Agency (2004) 118 CA4th 1136, 13 CR3d 624

In 1994, Dieckmeyer purchased a condominium unit under an affordable housing program. The unit was subject to recorded CC&Rs that, among other things, restricted transfer for 30 years and required subsequent buyers to qualify as lower or moderate income. The CC&Rs also contained an increased-income exception, which provided that “owner-occupants who were qualified buyers on the date of sale but are no longer qualified by virtue of an elevation of household income since the date of sale will not be subject to this affordability covenant.” In connection with the purchase, Dieckmeyer executed a promissory note for \$23,000 in favor of the City for a loan to finance the purchase. A deed of trust secured repayment of the note and Dieckmeyer’s compliance with the CC&Rs. In 2001, Dieckmeyer decided to prepay the loan. In exchange for accepting her prepayment, the City wanted Dieckmeyer to execute a new deed of trust to secure performance of the affordable housing restrictions. Dieckmeyer successfully petitioned for a peremptory writ of mandate that compelled the City to provide a payoff amount, accept payment, cancel the note, and reconvey the deed of trust.

The court of appeal reversed, holding that although Dieckmeyer was entitled to prepay the loan, she was not entitled to reconveyance of the trust deed. The court explained that the trust deed secured both the loan and the affordable housing restrictions. The court stated that Dieckmeyer’s partial performance, *i.e.*, paying off the loan, did not extinguish the lien to the extent it secured the restrictions. Therefore, Dieckmeyer was not entitled to reconveyance and the City had no need of a second deed of trust because the existing deed of trust would remain as security for Dieckmeyer’s obligations under the CC&Rs.

The court also rejected Dieckmeyer’s argument that she was released from the obligations of the CC&Rs under the increased-income exception. The court explained that the only reasonable interpretation of the exception was that it freed an owner from the restriction limiting occupancy to low- or moderate-income households, but nothing more. The court refused to interpret the exception in a manner that would allow a unit to be sold at market price when the owner’s income increased, as this would completely undercut the reason for the 30-year transfer restriction.

THE EDITOR’S TAKE: Ironically, the City lost because it drafted good documents some years earlier. The court held that the City did not need to get a new deed of trust precisely because the original one it had required the owner to sign when she first purchased the property remained in effect to secure the surviving obligations, even after the underlying debt was paid off. While licking its wounds over the fact that it has to pay Ms. Dieckmeyer her attorney fees, the City should nevertheless appreciate that it may have gained an

important holding regarding the validity of the documents it previously invented. At least as far as all other transactions are concerned, the City has been the prevailing party.

A housing accommodation is made affordable not by virtue of cheap construction, but because a government subsidy enables it to be purchased for less than market value. Because the subsidizer is usually interested in keeping the accommodation “affordable” and occupied only by those who need it most (qualified, low- and moderate-income purchasers), the original purchaser cannot be allowed to capture the value of the subsidy by turning around and reselling the unit “at market” to someone wealthy enough to pay that much.

A covenant in the deed that requires the grantee only to sell to a similarly qualified purchaser, or that gives the government a right to approve any future resale (here both approaches were taken), ensures the proper qualifications of the next owner. If the covenant is made to run with the land, it will also apply to future owners as well. Under these circumstances, it is unlikely that any court would conclude that a covenant restricting purchases to low- or middle-income buyers would constitute an invalid restraint on alienation.

However, a covenant like that does nothing to keep the price down (except somewhat indirectly by confining the pool of eligible purchasers to poor people). More must be done. Could Ms. Dieckmeyer have been made to further covenant that she would not resell her property at a price in excess of some specified formula? Had she done so, could the covenant have been enforced by way of injunction or invalidation of the sale, or by liability in damages for the overage collected? Those would be difficult questions to answer under an affordability covenant.

The City of Huntington Beach, however, went in a different direction. Because it was also making her a down payment loan that would ultimately have to be repaid, it demanded a share of the profits as well. Had this participation arrangement appeared in the promissory note (as a contingent interest), it would certainly have worked, but it probably would have disappeared once the note was paid off. Since the deed of trust secured the CC&Rs as well as the note, it would survive the payoff of the note, but the profit participation feature would still be gone, due to satisfaction of the note. If all of that is what the City was originally worrying about, it was much smarter to put the profit provision in the loan agreement rather than the note, and to have the deed of trust secure the entire loan agreement and not just the note.

I think it would have been even smarter to also have included the profit participation provision in the CC&Rs. Although this opinion did not cover the point, it seems to me an argument could have been made that the loan agreement itself came to an end once the loan was paid off, which would again take profit participation out of the picture. Did the loan agreement really provide that paying an equity share was a part of the loan such as to survive after the principal balance of the loan was paid? Even if it did say so, was that valid or did it constitute some kind of clog on the equity of redemption? The CC&Rs were designed to have a longer potential life than the loan, and since the deed of trust secured them as well, it would outlast both the note and the loan agreement.

Indeed, I would have included a provision in the CC&Rs themselves saying that any resale profits were to be shared between covenantor and covenantee for so long as the covenants endured, whether or not the original loan still existed. That way, even if the deed of trust was cancelled, intentionally or inadvertently, the CC&Rs would continue and would bind successive owners by their own force; securing the CC&Rs by the deed of trust improved remedies for their breach, but did not enhance their duration or “running” features. (For more observations on running covenants, see comment to *Greenbriar Homes Communities, Inc. v Superior Court* (2004) 117 CA4th 337, 11 CR3d 371).

Proper construction of the transaction should depend to some degree on what social purpose was being served by this particular arrangement. That prompts me to ask, just how does a profit split keep an accommodation affordable? Its main effect seems to be to ensure that a poor property owner is less likely to climb out of poverty. Is that what the City intended, or was it tempering its altruism with a bit of predatory banking fever? —*Roger Bernhardt*