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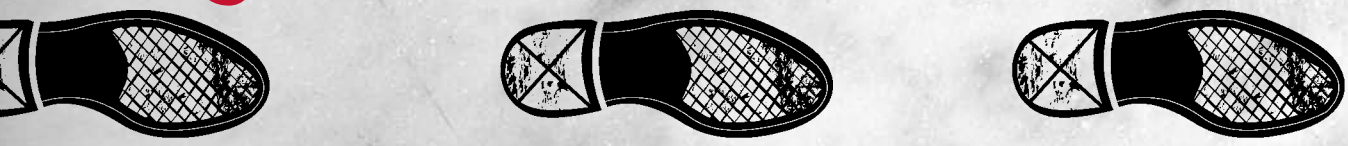
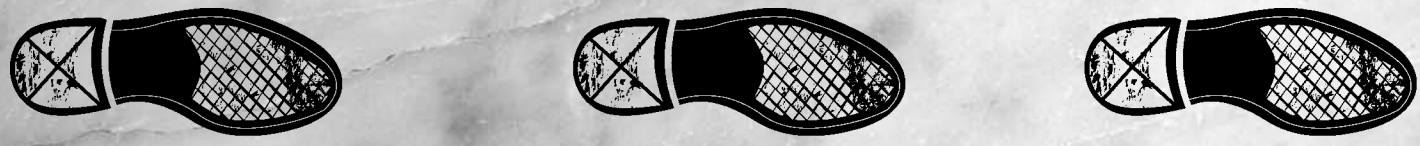
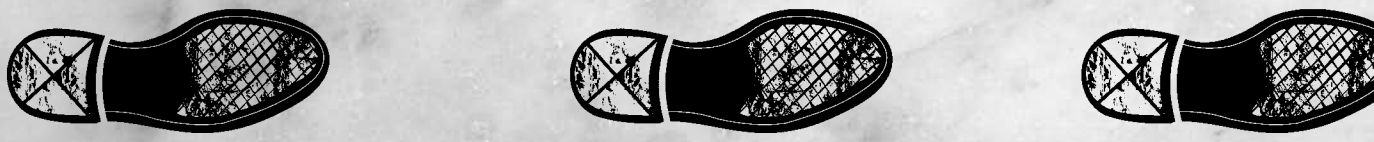


THE SUPREME COURT CONTINUES ITS MARCH TO THE RIGHT





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SHRIVER CENTER
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Case Notes

Seventh Circuit Decision Jeopardizes Federally Assisted Housing Preservation Programs

In what appears to be the first case of its kind in the country, a local municipality has been given the initial green light to take by eminent domain a federally subsidized housing development, in spite of strong opposition from the property owners, the tenants, and the U.S. Department of Housing and Urban Development (HUD). The City of Joliet, Illinois, recently won a significant court decision in the Seventh Circuit in its ongoing attempt to condemn Evergreen Terrace, a local low-income housing development. The Seventh Circuit's ruling could have potential harmful consequences for federally assisted housing programs, particularly those initiatives aimed at preservation.

Evergreen Terrace I and II are HUD-insured, project-based Section 8 multifamily housing properties in Joliet; they bank the river across from the city's thriving downtown. The Evergreen Terrace properties are owned by New West and New Bluff, Illinois, limited partnerships. A total of 356 families live in the developments, and most residents are low-income African Americans. For the past ten years, the city has pressured HUD, the property owners, and the Illinois congressional delegation to condemn or otherwise eliminate the Evergreen Terrace low-income housing.

Property Owners Restructure Their HUD Financing

In 2001 the property owners informed HUD that they would like to restructure their mortgages for Evergreen Terrace under the Multifamily Assisted Housing Reform and Affordability Act of 1997 (MAHRA).[1] Creating the Mark-to-Market program, MAHRA reduces subsidized Section 8 rents for multifamily housing to comparable market rents; HUD-insured and HUD-held financing is correspondingly restructured so that the mortgagor can make its monthly payments from the reduced rental income.[2] Congress intended MAHRA to finance the rehabilitation of HUD-insured, project-based Section 8 housing such as Evergreen Terrace.[3] Congress also intended "to preserve low-income rental housing affordability and availability while reducing the long-term costs of project-based [Section 8] assistance."[4]

As part of the property owners' restructuring of their Evergreen Terrace mortgages, the Illinois Housing Development Authority submitted to HUD a report that found a critical need to preserve the Evergreen Terrace properties. When Joliet challenged these findings, HUD hired a private company to conduct a second analysis of the local housing market (among other actions). This company likewise found that the need to preserve Evergreen Terrace's low-income housing was compelling in part because identifying affordable, viable replacement housing in the community would otherwise be nearly impossible for Evergreen Terrace's current residents. In spite of Joliet's vocal opposition and political maneuvering, HUD approved the final mortgage restructuring under MAHRA in September 2006.

HUD paid off, also as part of the restructuring, the original mortgages that it had insured and became the new mortgagee. MAHRA required thirty-year use agreements, recorded against both properties in November 2006.[5] The agreements required that the property be used solely as rental housing with no reduction in the number of residential units unless approved by HUD and that a specified number of units remain as project-based Section 8 housing.[6]

Property Owners File Civil Rights Suit Against Joliet

In March 2005, before the completion of the MAHRA mortgage restructuring, the property owners filed a civil rights action against Joliet and several individual defendants under 42 U.S.C. §§ 1982 and 1983 and the Fair Housing Act.[7] The property owners alleged that the city and certain public officials were engaged in a campaign to force low-income African American residents out of Evergreen Terrace and that to achieve their goal the city sought to stop the MAHRA restruc-

[1]Multifamily Assisted Housing Reform and Affordability Act of 1997 (MAHRA), Pub. L. No. 105-65, tit. V, 111 Stat. 1384 (codified in 42 U.S.C. § 1437f note).

[2]MAHRA § 511(b)(1), 42 U.S.C. § 1437f note.

[3]See MAHRA Interim Rule, 63 Fed. Reg. 48,926, 48,926 (Sept. 11, 1998).

[4]MAHRA § 511(b)(1), 42 U.S.C. § 1437f note.

[5]*Id.* § 514(e)(6)(A), (B).

[6]*Id.*

[7]*New West Limited Partnership v. City of Joliet*, No. 05-C-1743, 2006 WL 2632752 (N.D. Ill. Sept. 8, 2006), reversed and remanded, 491 F.3d 717 (7th Cir. 2007) (Clearinghouse No. 56,142).

turing and the related project-based Section 8 contract renewal.[8] The district court dismissed this suit, but the Seventh Circuit reversed the lower court and upheld the owner's right to file a civil rights suit on behalf of the low-income tenants of Evergreen Terrace.[9]

Joliet Begins Eminent-Domain Action

After the property owners filed their civil rights suit but before the district court and Seventh Circuit decisions in that case, Joliet in August 2005 declared Evergreen Terrace a public nuisance and a blighted area, notwithstanding that Joliet, as administrator of the annual contributions contract for Evergreen Terrace II, was receiving from HUD monthly payments based on the city's certification that this portion of the development was maintained in a decent, safe, and sanitary condition.[10] After its declaration of public nuisance—required by state law in order to initiate an eminent-domain action—Joliet enacted in October 2005 Ordinance No. 15298, authorizing the commencement of eminent-domain proceedings to acquire fee simple title to Evergreen Terrace.[11] The city then filed a condemnation suit in order to proceed with the eminent-domain action.[12]

On behalf of HUD the United States removed the case to federal district court pursuant to 28 U.S.C. §§ 1442 and 1444, and Joliet eventually named HUD as a defendant along with the property owners. Although the city failed to name the tenants as defendants to the condemnation action, the court subsequently granted them intervention.[13]

HUD and the property owners' answer cited several defenses to the condemnation, including federal preemption of the city's action under the supremacy clause of the U.S. Constitution, violation of the Constitution's contracts clause and property clause, and violation of the doctrine of intergovernmental immunity.[14] HUD and the property owners argued that Section 221 of the National Housing Act of 1954 (as amended in 1961 and 1966) (the provision providing mortgage insurance for the Evergreen Terrace properties) and MAHRA preempted Joliet's intended condemnation of Evergreen Terrace. The city's condemnation ordinance, they argued, presented a clear obstacle (commonly referred to as conflict preemption) to the accomplishment of Congress' stated purposes to provide and preserve federally insured low-income housing developments through MAHRA and Section 221 of the National Housing Act.

District Court Decisions Reject Preemption Defenses

Following the Seventh Circuit's opinion in the property owners' civil rights suit, Joliet moved for judgment on the pleadings with respect to the preemption defenses raised by HUD and the property owners in the condemnation suit. In August 2007 the district court granted the city's motion. Relying on *dictum* from the Seventh Circuit's *New West* decision, the district court concluded, we believe incorrectly, that because Evergreen Terrace was privately owned and the property owners' initial participation in HUD housing programs was voluntary, there could be no finding of preemption.[15] The regulations implementing the project-based Section 8 program and MAHRA itself, the district court also found, do not forbid the condemnation of the property or otherwise preempt the city's actions.[16]

Shortly after this decision, HUD and the property owners filed separate motions for summary judgment, again arguing that the city's intended taking was barred by the supremacy, property, and contracts clauses of the U.S. Constitution and the doctrine of intergovernmental immunity. The district court rejected these motions in March 2008.[17] HUD and the property owners then petitioned the district court to certify its orders for interlocutory appeal pursuant to 28 U.S.C. § 1292(b). The district court and the Seventh Circuit granted both petitions and accepted the appeals.

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[8]*Id.* at *2.

[9]*New West Limited Partnership*, 491 F.3d 717. This case is stayed; see *infra* note 16.

[10]See 24 C.F.R. § 5.703 (2009) (standard of decent, safe, and sanitary conditions for U.S. Department of Housing and Urban Development (HUD) and HUD-assisted housing). The annual contributions contract provided the terms under which HUD would give Joliet the money required to fund and administer the housing assistance payments contract.

[11]See 735 Ill. Comp. Stat. 30/1-1-1 *et seq.* (2009) (Eminent Domain Act).

[12]*City of Joliet v. Mid-City National Bank*, No. 05 C 6746, 2007 U.S. Dist. LEXIS 57397 (N.D. Ill. Aug. 3, 2007), summary judgment denied, 2008 U.S. Dist. LEXIS 24924 (N.D. Ill. March 27, 2008), affirmed, *City of Joliet v. New West Limited Partnership*, 562 F.3d 830 (7th Cir. 2009) (Clearinghouse No. 56,128).

[13]The Sargent Shriver National Center on Poverty Law, representing the Evergreen Terrace tenants, argued that they were necessary parties for purposes of Federal Rules of Civil Procedure 19(a) and 71(a) (see *infra* note 18 and accompanying text).

[14]U.S Const. art. VI, cl. 2 (supremacy clause), art. I, § 10, cl. 1 (contracts clause), art. IV, § 3, cl. 2 (property clause).

[15]*City of Joliet v. Mid-City National Bank,* 2007 U.S. Dist. LEXIS 57397, at *13–14.

[16]*Id.* at *14–15. *In dictum* in its 2007 decision, the Seventh Circuit noted its view that the civil rights suit could not bar the condemnation from proceeding and that it was "hard to see any obstacle [to Joliet's condemnation action] in federal law" (*New West Limited Partnership*, 491 F.3d at 721). The Seventh Circuit relied on its reading of the National Housing Act, the Fair Housing Act, and several inapplicable federal housing regulations to come to this decision, which we believe to be erroneous. The Seventh Circuit directed the district court to handle the condemnation case before moving on to the civil rights case. Thus, since remand of the civil rights suit, the district court has stayed that case.

[17]*City of Joliet v. Mid-City National Bank*, 2008 U.S. Dist. LEXIS 24924.

Tenants Intervene in Condemnation Suit and File Fair Housing Act Suit

After HUD and the property owners had filed for summary judgment but before the district court rejected both motions, a group of Evergreen Terrace residents, represented by the Sargent Shriver National Center on Poverty Law, filed in December 2007 a motion to intervene as defendants in Joliet's condemnation case.[18] The Evergreen Terrace tenants also filed a separate Fair Housing Act case, *Davis v. City of Joliet,* against Joliet; they argued that the city's efforts to remove Evergreen Terrace and the majority of African American residents who live there amounted to intentional race discrimination and had a disparate impact on African Americans.[19]

In January 2008 the district court granted the Evergreen Terrace tenants' motion to intervene in the condemnation case.

Seventh Circuit April 2009 Decision Rejects Preemption Defense

In accepting the appeals, the Seventh Circuit asked the parties to address also the question "whether a contract between a private developer and a federal agency can curtail a government's power of condemnation." The parties presented oral arguments in January 2009.

In April 2009 the Seventh Circuit affirmed the district court's decision rejecting HUD's and the property owners' summary judgment motions.[20] The panel rejected the supremacy-clause affirmative defenses raised by HUD, the property owners, and the Evergreen Terrace tenants in addition to the property clause, contracts clause, and doctrine of intergovernmental immunity defenses raised by the property owners and the tenants.[21] Relying on *Wyeth v. Levine*, the panel held that, short of a federal "preemptive regulation with the force of law," a federal statute would not be found to have impliedly preempted a state or local law, regardless of the interference it may have on the methods by which a federal statute is designed to reach its goals.[22] Relying on what we believe to be its mistaken view of *Wyeth*, the panel never addressed HUD's, the property owners', and the tenants' argument that Joliet's intended condemnation of Evergreen Terrace without HUD's approval would directly frustrate the purposes of Section 221 of the National Housing Act and MAHRA to preserve certain federally subsidized low-income housing developments. The panel also held that no conflict could exist between the federal and state laws because neither the National Housing Act nor MAHRA makes compulsory an owner's initial participation in federal housing programs.[23] The panel placed considerable weight on its factual and legal misapprehension that "[p]rivate owners are entitled to withdraw their properties from the program at any time despite their 20-year and 30-year promises" by paying off the federally insured loan.[24]

The opinion had one bright spot for HUD, the property owners, and the Evergreen Terrace tenants. The Seventh Circuit recognized that if a municipality sought to use its eminent-domain powers in furtherance of race discrimination, this discriminatory purpose could serve as a bar to the eminent-domain action.[25] Both the property owners and the tenants asserted that Joliet's taking was motivated by race discrimination and pled those allegations as an affirmative defense in the condemnation case.

In May 2009 the three defendants—HUD, the property owners, and the Evergreen Terrace tenants—filed petitions for a rehearing or a rehearing *en banc*. The defendants argued that the Seventh Circuit had a mistaken view of *Wyeth* and that the U.S. Supreme Court still recognized its long-standing belief that implied conflict preemption would be found when the state or local law posed an "obstacle to the accomplishment and execution of the full purposes and objectives of Congress."[26] Thus, the defendants argued, a preemptive regulation with the force of law was not necessary to find conflict preemption. The defendants corrected the Seventh Circuit's perception that they were relying only on the purposes and findings sections of the National Housing Act and MAHRA as a basis for their conflict-preemption arguments. The defendants noted their repeated reference to MAHRA's Section 514(e)(6), which mandates use restrictions on the property: the Restructuring Plan "shall … require the owner or purchaser of the project to maintain affordability and use restrictions in accordance with regulations promulgated by [HUD], for a term of not less than 30 years." The Seventh Circuit's view that preemption does not exist where the initial program participation is voluntary conflicts with the Supreme Court and other U.S. courts of appeal (including the Fifth, Eighth, and Ninth Circuits) jurisprudence recognizing that the voluntary or mandatory nature of a federal program is irrelevant to the question of preemption, the defendants argued.[27] The defendants corrected the Seventh Circuit's misapprehen-

[18]The briefs are available on the Shriver Center's www.povertylaw.org/poverty-law-library/case/56100/56128.

[19]*Davis v. City of Joliet*, No. 07 C 7214 (N. D. Ill. filed Dec. 21, 2007) (Clearinghouse No. 56,127). Joliet's motion to stay this Fair Housing Act case is pending, and the case is effectively stayed until the court rules on that motion.

[20]*City of Joliet v. New West Limited Partnership,* 562 F.3d 830.

[21]See *id.*

[22]*Id.* at 835 (relying on *Wyeth v. Levine,* 129 S. Ct. 1187 (2009)).

[23]*Id.* at 835–36.

[24]*Id.*

[25]*Id.* at 837–38.

[26]*Wyeth*, 129 S. Ct. at 1201 (quoting *Hines v. Davidowitz*, 312 U.S. 52, 67 (1941)); see also *Geier v. American Honda Motor Company*, 529 U.S. 861, 883 (2000).

[27]*City of Morgan City v. South Louisiana Electric Cooperative Association*, 31 F.3d 319 (5th Cir. 1994); *Forest Park II v. Hadley*, 336 F.3d 724 (8th Cir. 2003) (Clearinghouse No. 55,465); *Public Utility District No. 1 of Pend Oreille County v. United States*, 417 F.2d 200 (9th Cir. 1969).

sion that the property owners could voluntary exit the housing programs at any time. Because the property owners may not unilaterally withdraw from the program and are bound by a legally enforceable use agreement that is required by Section 514(e)(6) of MAHRA and that commits them to provide this low-income housing for the next thirty years, the conflict between the National Housing Act and MAHRA and Joliet's condemnation law becomes much more apparent, the defendants also argued.

In July 2009 the Seventh Circuit denied the defendants' petitions for a rehearing or a rehearing *en banc*. HUD determined that it would not seek certiorari to the U.S. Supreme Court. On October 13, 2009, the property owners and the Evergreen Terrace tenants filed separate petitions for certiorari to the U.S. Supreme Court. A decision on the motions is not expected until January 2010 at the earliest. On October 2, 2009, one of the Evergreen Terrace tenants also filed a land-use Fair Housing Act complaint with the HUD Office of Fair Housing and Equal Opportunity. That complaint is under review by the U.S. attorney general.

Seventh Circuit Decision Has National Significance

The Seventh Circuit decision in Joliet's condemnation suit could have potentially damaging implications for federal housing programs, such as MAHRA endeavors, that are aimed at long-term preservation of federally supported low-income housing.

The Decision Could Undermine Federally Assisted Housing Preservation Efforts. Though not mentioned in the opinion, the 2005 controversial and far-reaching eminent-domain decision of the U.S. Supreme Court, *Kelo v. City of New London*, might have led the Seventh Circuit to believe that a local government's power of eminent domain should not be halted even when in direct conflict with federal laws and federal programs.[28] The Seventh Circuit's view could deter private owners from participating in federally assisted housing programs or entering preservation programs such as MAHRA or, worse still, embolden other municipalities opposed to affordable housing to eliminate publicly assisted low-income housing by eminent domain. *Kelo* upholds the state's use of its eminent-domain power to take private property as long as there is a "legitimate public purpose" to the taking.[29] However, *Kelo* never addresses federal preemption, and thus *Kelo* should not apply to Joliet's condemnation suit against Evergreen Terrace or in other cases in which a property successfully participates in a federal housing preservation program. In Joliet's condemnation case and in other cases involving MAHRA-preserved developments, forcing the property owners to comply with both laws—the ordinance condemning the property and the federal law obligating its extended preservation and rehabilitation—is impossible.

The Decision Questions the MAHRA Use Restrictions, Thereby Risking Other Federal Housing Programs that Rely on the Same Preservation Mechanism. The Seventh Circuit's legal and factual misapprehension that private owners subject to the MAHRA thirty-year use restrictions can simply "withdraw their properties from the program at any time despite their 20-year and 30-year promises [and] [a]ll they have to do is pay off the federally insured loan …" could have damaging consequences for several housing programs, not just MAHRA.[30] Most of the housing preserved by congressionally created federally funded housing programs has similar restrictions limiting their use to affordable rental housing in order to ensure long-term affordability and occupancy by low-income households. For example, the Low-Income Housing Tax Credit program requires a thirty-year agreement to provide low-income housing as do the projects assisted under the Low-Income Housing Preservation Act, projects foreclosed by HUD, and projects with HUD-held mortgages pursuant to 12 U.S.C. §§ 1701z-11(e)(3), (k)(1)–(2).[31] In spite of the court's ruling, even if the property owners in Evergreen Terrace did prepay their restructured mortgages, prepayment would not extinguish the MAHRA-mandated thirty-year use restriction, which is also incorporated into a separate agreement as a restrictive covenant that runs with the land. Certain private owners nonetheless may rely on the Seventh Circuit's erroneous decision to attempt to extinguish their use restrictions.

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[28]*Kelo v. City of New London*, 545 U.S. 469 (2005) (Clearinghouse No. 55,821).

[29]*Id.* at 477, 480–83.

[30]*New West Limited Partnership,* 562 F. 3d at 835–36.

[31]Low-Income Housing Tax Credit Program, 26 U.S.C. § 42 (h)(6); Low-Income Housing Preservation Act, 12 U.S.C. § 4112(a)(2).

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