# HOME BASE

**The Playbook for Cooperative Development**

ncb capital impact™

# ACKNOWLEDGEMENTS

**NCB Capital Impact** would like to thank the following organizations and people for their support and dedication to making this publication possible in order to create more affordable cooperative homeownership opportunities:

**NCB provided funding for this project. About NCB:**
National Cooperative Bank is now simply NCB. While our name and look have changed as of October 1, 2006, our commitment to our customers remains as strong as ever.

NCB is dedicated to strengthening communities nationwide through the delivery of banking and financial services, complemented by a special focus on cooperative expansion and economic development.

Primary markets we serve include the basic ingredients of vibrant communities: housing, education, healthcare, cultural centers, local businesses and social services. In addition, NCB has a growing community banking network in southwestern Ohio.

Since being chartered by Congress in 1978, NCB has answered the financial needs of America's cooperatives and member-owned businesses for more than 25 years. NCB is distinctly qualified to understand first-hand the challenges facing cooperatives, having become one in 1981, and today boasting more than 2,600 customer-owners and more than $6.19 billion in assets under management.

**About NCB Capital Impact**
NCB Capital Impact, the non-profit affiliate of NCB, provides financial services and technical assistance designed to spark systemic change and empower communities to create more affordable cooperative homeownership, assisted living, housing and services for the frail and elderly, and facilities for health care centers and charter schools.

*Also, thanks to:*

**The team of writers:**
Jim Gray
Jon Kelly
Terry Lewis
Jay Marcus
Betsy Newcomer

**The team of reviewers:**
Candace Baldwin
Anne Geggie
Paulette Miller

**Editors:**
Laura Mullane
Betsy Newcomer

**Designer:**
Kimberly Kerin

**Cover and title page photos:**
Shannon Scott

**Printing by:**
HBP Printing, Graphics & Information Services

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# INTRODUCTION:
# Sliding Into Home

IF LIFE WERE A BASEBALL GAME, homeownership would be like sliding into home base. Just as players reach for the plate with their outstretched fingers, aspiring homeowners reach for their "home base"—a place to call their own; a place that gives them a stake in their community; a place that keeps them safe. Unfortunately, home base can be out of reach for many. Skyrocketing real estate prices, building management practices, and other external factors have made owning an apartment, condominium or single-family home difficult at best, and oftentimes impossible.

Cooperatives can change that. Cooperatives are the pinch hitters that can help players round third and slide into home. They offer a homeownership model that allows residents to create wealth through reduced monthly housing costs and by building equity over time. Additionally, cooperatives empower residents by giving them control over building management and operations.

### *The benefits of cooperatives include:*

- Lower costs related to converting cooperatives, as compared to condominiums
- Lower cost of homeownership through reduced per-unit land and construction costs as compared to single-family homeownership
- Preserving affordability of homeownership in order to meet policy goals
- Shared involvement of resident owners in asset and building management
- Avoiding displacement of longtime residents upon expiration of affordable housing subsidies and restrictions (including Low Income Housing Tax Credits)
- Provides an elegant exit strategy for owners of existing rental buildings, for whom the building's residents provide a highly motivated buyer.

So how do you slide into home? This guide is designed to help show you how cooperatives are created. Specifically, it provides resident associations a better understanding of cooperatives, the development process, and how to be smarter consumers. It also provides sponsors and developers with a detailed overview of cooperative creation through both new construction and conversion.

NCB Capital Impact provides technical expertise to cooperative developments nationwide. While there is no substitute for experience in real estate development, this guide draws on the organization's experience to help new players assemble a development team and understand the game plan, including:

- How to convert or construct a housing cooperative
- How to finance the development of a housing cooperative, including sources of funds
- A basic curriculum for training resident owners and their boards of directors

We are excited to share this information to help demystify the development process for housing cooperatives, and thereby increase the supply of this valuable form of affordable housing. Now let's play ball!

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THE GAME PLAN:

# Understanding Co-op Basics

**WHILE SINGLE-FAMILY HOMES** and the land under them can be cooperatively owned, the ownership structure is most often used in multi-family buildings. The close proximity of residences facilitates relationships among the co-op resident/owners. It may encourage community ties based on neighborly interactions.

**THE GAME:** A housing cooperative, like a condominium or a single-family subdivision, is a framework for home ownership. Cooperatives bring people together to own the building in which they live.

**THE PLAYERS:** All types of people at all income levels live in co-ops. Every race, ethnic group, profession, and age group is represented. Famous examples of luxury cooperatives include the Watergate in Washington D.C. Another example is the Dakota in New York City where Leonard Bernstein, Roberta Flack, and John Lennon lived. Some co-ops accommodate senior citizens by offering special activities and services designed with their interests in mind. Some even limit ownership and occupancy solely to seniors. Other co-ops are set up to serve the interests of artists (loft-type structures), college students (even providing meals and study areas as well as a place to live), or people with a variety of disabilities. Other cooperatives are designed specifically to be affordable to low and moderate income people. Most often, co-ops represent a mix of people in many different circumstances.

**THE PLAYING FIELD:** Cooperative ownership can be applied to any type of multiple-unit physical structure or even the division of bare land. Physically, co-ops can be made up of townhouses sharing walls with the homes next to them; single family or duplex structures; garden apartments; walk-ups; mid-rise and high-rise buildings; fraternity-style or dormitory structures for students; individual building sites within a cooperative subdivision; manufactured housing parks; and even marinas.

While single-family homes and the land under them can be cooperatively owned, the ownership structure is most often used in multi-family buildings. The close proximity of residences facilitates relationships among the co-op resident/owners. It may encourage community ties based on neighborly interactions. Usually, all of the residences in a co-op are "under one roof," where the expenses are more likely to impact all owners. Families living in nearby single-family homes could be part of a co-op, but residents with a vested interest in shared property are more likely to be part of a co-op.

**THE RULES:** Owners/residents democratically control the building's management and operation. They come together as a corporation and pay a monthly amount that covers the buildings' costs, including the costs of maintenance, operations, property taxes, insurance, and principal and interest payments on the cooperative's mortgage.

**THE GOAL:** People become homeowners by buying shares in the co-op. Their shares give them the right to occupy a particular apartment, townhouse, or dwelling. The cooperative corporation itself owns the land and buildings. Together, the residents own 100 percent of the cooperative, while the cooperative owns 100 percent of the real estate/property title.

### *How does a housing cooperative work?*

Cooperative owners each own a cooperative interest that is the combination of two things:

1. The co-owner's ownership interest in the cooperative corporation (represented by a certificate of ownership or corporate shares), and
2. An exclusive right to occupy a particular dwelling unit (that is owned by the cooperative corporation), which is represented by an occupancy agreement or proprietary lease.

Each ownership interest gives the co-owner a pro-rata undivided interest in the cooperative's property as a whole and the right to participate in the democratic governance of the cooperative. This pro-rata undivided interest means the owner has a proportionate part of ownership of the corporation that owns the land and buildings. The owner's right to occupy the specific dwelling unit continues as long as the individual is both a co-owner of the cooperative and abides by the occupancy agreement.

## THE VALUE OF SHARED EQUITY

One of the greatest affordable housing challenges is the growing gap between what people can afford to pay for housing and what it costs. This gap between needs and available resources has widened so significantly that many policy makers and developers are questioning the traditional model of dividing all housing into ownership and rental. Under a "shared equity" approach, the appreciating value of the property is controlled and leveraged to promote affordable housing. The models created around the country that capture this "shared" equity approach vary. Limited equity cooperatives, community land trusts, and deed-restricted homes are the most common. In addition to enabling long-term affordability, these models often address rising housing costs, such as insurance, heating fuel, and maintenance by approaching them on a shared basis, providing for economies of scale. As of 2006, over half a million homes have shared equity and the numbers are rapidly growing.

In contrast, when a condominium unit is purchased, the individual is purchasing the title to real estate. That real estate includes everything from the air space to the paint on the back walls of the unit, plus a pro-rata undivided interest in the common elements of the buildings and land. Certain costs involved in developing and purchasing condos are higher than for cooperatives, since in a condo each unit is a separate piece of real estate and each unit sale a separate real estate transaction. Both condos and co-ops offer similar homeownership benefits like financing, tax deductions and equity building.

### *How are cooperatives financed?*

Many advantages of cooperative homeownership come from the flexibility available in cooperative financing. Because the cooperative corporation owns the land and buildings as a whole, the cooperative can mortgage the property as a whole. Co-op corporation ownership is financed with a "blanket" or "underlying" mortgage. The cooperative can use a blanket mortgage to pay for the initial acquisition of its real estate, refinance existing debt, or finance major improvement and rehabilitation projects.

Because each individual cooperative homeowner has an ownership interest, he or she can borrow against that interest in the same way that a single-family or condominium homeowner can borrow against his or her ownership interest. This is known as a "share loan."

Cooperatives can be financed using only blanket debt, only share debt, or a combination of the two. Government funds or even grants can also be applied to financing the blanket or share loan. This allows cooperative developers a great deal of flexibility in matching the financial circumstances of the people likely to buy into a particular co-op.

### *How are cooperatives managed or maintained?*

Cooperatives operate at cost. This means that the cooperative's annual budget reflects its best estimate of the exact cost needed to properly operate and maintain the building(s). These costs can include management, maintenance of the grounds and building structures, funding appropriate reserves, paying property taxes and insurance for the cooperative, and making principal and interest payments on the co-op's blanket mortgage.

Cooperatives can either hire a property management company to manage the building or decide to "self-manage" the property by hiring their own employees to operate and maintain the property. If the property is very small, cooperative owners may even play a role in property operations, depending on the cost and the available time and expertise of cooperative owners.

Homeowners pay monthly charges consisting of their proportionate share of one month's worth or one-twelfth of the cooperative's annual budget. The size and location of the apartment can affect the amount or proportion of the resident's monthly share. These monthly payments are referred to by different co-ops as "occupancy charges," "carrying charges," "housing charges," "assessments," or "maintenance charges." We will refer to them as occupancy charges.

At the end of each fiscal year, any surplus from the occupancy charges is used to benefit all of the member-owners. The funds can become part of the next year's budget, keeping increases in occupancy charges to a minimum. These net savings can also be added to the co-op's reserves for future needs, such as building repairs. Or they can be returned to the homeowners as dividends in proportion to each owner's monthly occupancy charge. This last option is a unique feature of cooperative ownership.

### *What is the difference between "market rate" and "limited equity" cooperatives?*

Developers can choose to create different types of cooperatives. Some cooperatives limit resale prices to keep ownership affordable to succeeding generations of buyers. They are called "limited equity" cooperatives. In most limited equity cooperatives, a formula determines the maximum amount the seller can charge for his/her shares upon leaving the cooperative. The intent of such limitations is to assure continued affordability of the housing to limited income buyers. "Market rate" cooperatives, on the other hand, allow outgoing homeowners to sell their shares at whatever price buyers are willing to pay.

# OWNERSHIP VARIATIONS

## *Different Ways to Play the Game*

This guide focuses on the most basic of cooperative ownership structures: the "fee simple" cooperative. In the fee-simple cooperative, the cooperative corporation owns all of the land and buildings and the individual cooperative members own all of the cooperative interests. But variations of this exist and are used to meet a variety of specific needs – both organizational and financial. The variations include:

***Land Leases/Land Trusts*** –The land on which the cooperative structures are built is owned by a third party (i.e. neither the cooperative corporation nor its members), which grants a long-term lease of the land to the cooperative corporation. The cooperative corporation owns the improvements (buildings, etc.) on the land. Cooperatives generally involve land leases or land trusts for one of two reasons:

1) the land itself is quite valuable and the owner wishes to retain a long-term interest in order to redevelop it after the lease period; or
2) the land lease provides for the enforceability of important restrictions on the use of the land, such as the ongoing affordability of acquisition and occupancy of the housing constructed on it. The lease/land trust provides the landowner/trustee with a compelling means to enforce resale and cost restrictions on both individual cooperative interests and the cooperative improvements as a whole.

***Leasehold Cooperatives*** – A variation on the fee-simple cooperative ownership structure. In leasehold cooperatives, a third-party entity owns the land and buildings in fee simple and rents them as a whole to the cooperative corporation. Cooperative interests become interests in the corporation's leasehold rights (rather than its ownership rights) with coupled governance rights similar to those found in fee-simple cooperatives. Leasehold cooperatives are most often created to allow for the use of Low Income Housing Tax Credits (LIHTCs) in financing cooperative development. Due to the nature of the LIHTC program, the holders of the tax credits must be the actual owners of the housing in order to qualify to use the credits to reduce their federal income tax liabilities. However, the holder of the tax credits may not also be a resident of the building. In many cases, the leasehold cooperative may have the right of first refusal at the end of the LIHTC compliance period.

***Mutual Housing Associations*** – This term has been used to describe a wide variety of situations. It may denote a situation in which a non-profit organization owns one or more sets of land and buildings that are cooperatively operated by their residents or substantially involve residents in asset or building management. In this situation, the non-profit organization may have a governance structure composed solely of representatives of cooperative co-owners; of cooperative co-owners and representatives of the communities in which the cooperatives are situated; or solely of community representatives.

Or it may denote a situation in which one or more fee-simple cooperatives come together to create a non-profit organization that provides professional management or other services to its member-cooperatives on a mutual basis. In this situation, the governance structure of the non-profit is likely to be composed largely or exclusively of representatives of the cooperative co-owners. Mutual housing associations are generally created to provide strength and stability to small cooperatives or as an alternative method of assuring long-term housing affordability.

In other cases, mutual housing associations can be a permutation or combination of the two situations.

***Land-Only Cooperatives*** – These cooperatives involve a situation in which the land itself (and certain common improvements) is owned cooperatively but the dwelling units are owned individually by members of the cooperative. This may include boats in a marina, manufactured housing units on pads in a manufactured housing or "mobile home" park, or even conventionally built single-family structures.

## AT-A-GLANCE: Housing Comparison Chart

| | MARKET RATE CO-OP | LIMITED EQUITY CO-OP | CONDOMINIUM | RENTAL | SINGLE FAMILY |
|---|---|---|---|---|---|
| OWNERSHIP | Owner residents are sole owners through a corporation, which owns the land and buildings. Each owner has exclusive rights to occupy a particular dwelling unit in perpetuity. | Same as a market rate co-op | Unit owners take title to the air space to the back of the paint on the walls of a particular unit plus an undivided interest in the land and buildings. | The landlord owns the land and buildings. Each tenant has the exclusive right to occupy a particular unit during the term of the lease. | Owners take title to the land and building. |
| MONTHLY COSTS | Homeowners pay monthly operating costs to the cooperative—a proportionate share of total operating costs, blanket debt principal and interest, property taxes, insurance, and reserves. Homeowners with share loans make individual principal and interest payments directly to the share lender. | Homeowners pay monthly operating costs to the cooperative—a pro rata share of total operating costs, blanket debt principal and interest, property taxes, insurance, and reserves. Share loans, if any, are small and may be serviced by the cooperative, a credit union, nonprofit, or governmental entity. Homeownerswith share loans make individual principal and interest payments. | Homeowners pay monthly condo fees to the condominium association—a pro-rata share of total operating costs, insurance, and reserves. Homeowners with mortgages make principal and interest payments directly to each lender. Each owner makes his own property tax payments through monthly escrow or directly to the local government. | Tenants pay the rent amount specified in the lease, which may include the landlord's profit margin, typically based on the highest price the market will bear, rather than actual costs. | Homeowners with mortgages make principal and interest payments directly to the lender. Owners make their own property tax and insurance payments through monthly mortgage escrow payments or directly to the insurance company and local government. |
| MAINTENANCE & REPAIRS | Cooperative is responsible for exterior maintenance. Cooperatives can choose how they allocate responsibility for dwelling unit maintenance repairs between individuals and the cooperative. | Cooperative is responsible for exterior maintenance. Cooperatives can choose how they allocate responsibility for dwelling unit maintenance repairs between individuals and the cooperative. Many limited equity cooperatives assume most or all responsibility for dwelling unit maintenance and repair in order to even out and reduce costs to their owners. | Condominium association is responsible for exterior maintenance. Individual unit owner is responsible for all dwelling unit maintenance and repair. | Landlord is responsible for all maintenance and repair. | Owner is responsible for all maintenance and repair. |
| PURCHASE PRICE/ MOVE IN COSTS | Purchaser pays market price for shares/ ownership. Pro-rata share of cooperative's blanket loan remains in place. Purchaser assumes seller's obligations under occupancy agreement. Few or no closing costs. | Purchaser pays low price for shares/ownership. Pro-rata share of cooperative's blanket loan remains in place. Purchaser assumes seller's obligations under occupancy agreement. Few or no closing costs. | Purchaser pays market price for the condo unit. Purchaser becomes obligated to pay monthly condo fees. Closing costs include legal fees, recording costs, and title insurance. | Tenant typically pays first and last month's rent plus a security deposit. | Purchaser pays market price. Closing costs include legal fees, recording costs, and title insurance. |

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## AT-A-GLANCE: Housing Comparison Chart

| | MARKET RATE CO-OP | LIMITED EQUITY CO-OP | CONDOMINIUM | RENTAL | SINGLE FAMILY |
|---|---|---|---|---|---|
| FINANCIAL LIABILITY | Homeowners have no personal liability on cooperative's blanket loan. They are obligated under their occupancy agreement to make monthly operating cost payments to the cooperative. Homeowners with share loans are personally liable to the share lender for the amount of the loan. | Same as a market rate co-op | Homeowners are obligated to pay monthly condo fees to the condominium association. Unit owners with mortgages are personally liable to their lenders for the amount of the loan. | Tenants are obligated under their leases to pay monthly rent until the end of the lease term. | Homeowners with mortgages are personally liable to their lenders for the amount of the loan and are responsible for home maintenance costs. |
| COMMUNITY CONTROL | Cooperative has the right to approve all potential buyers. Cooperative can terminate ownership and evict residents who violate the occupancy agreement, forcing them to sell their shares to new buyers. Homeowners democratically govern the cooperative and elect a board of directors to oversee operations. | Same as market rate co-op. | Condominium association has little to no control over the sale of units or behavior of unit owners. Unit owners democratically govern the condo association and elect a board of directors to oversee operations. | Tenants have no voice in who moves in and no control over the behavior of other residents. | Owners have no control over who moves in nearby and no control over the behavior of neighbors. Owner has the right to sell or rent their home to the buyer or tenant of their choice. |
| FACILITIES IMPROVEMENTS | Three methods are available to finance cooperative rehab, replacements, and improvements: 1) assessment of individual owners for their pro-rata share of the total rehab cost; 2) establishment and funding of replacement reserves; 3) new long-term blanket financing. | Same as market rate co-op | Two methods are available to finance condo rehab, replacements, and improvements of the common elements: 1) assessment of individual owners for their pro-rata share of the total rehab cost; 2) establishment and funding of replacement reserves. | The landlord is responsible for rehab replacements and improvements. | The owner is responsible for rehab replacements and improvements. |
| PROPERTY MANAGEMENT | Cooperative owners democratically elect a board of directors, which hires and oversees property management firm or can self-manage. | Same as market rate co-op. | Unit owners democratically elect a board of directors, which hires and oversees property management firm or can self-manage. | The landlord hires and oversees a property management firm or uses its own management firm. | Owner is individually responsible for property management and all aspects of the property. |

## AT-A-GLANCE: Housing Comparison Chart

| | MARKET RATE CO-OP | LIMITED EQUITY CO-OP | CONDOMINIUM | RENTAL | SINGLE FAMILY |
|---|---|---|---|---|---|
| TAX BENEFITS | Cooperative owners enjoy all of the income tax benefits of homeownership, including deduction of the interest on their share loan, their portion of property tax payments and the interest on the blanket loan. In most states, owners receive whatever property tax benefits are available to other homeowners. | Unless the cooperative has given them up in exchange for tax-exempt financing or nonprofit corporation status, cooperative owners enjoy all of the income tax benefits of homeownership. In most states, owners receive whatever property tax benefits are available to other homeowners. In some states, there are additional property tax benefits or savings due to the limitation of resale prices. | Condominium unit owners enjoy all of the income tax benefits of homeownership. In most states, condominium unit owners receive whatever property tax benefits are available to other homeowners. | Tenants receive no income tax benefits of homeownership. In most states, rental properties incur higher property taxes than owner-occupied housing. The higher taxes are often passed through to tenants as part of their rent. | Owners enjoy all of the income tax benefits of homeownership. In many states, homeowners receive some property tax benefits in the form of lower assessments or lower tax rates. |
| HOME EQUITY | Cooperative owners build equity as the value of their cooperative interest increases and as their share loan debt is paid down. | Growth in equity is limited through a restriction of resale prices. Generally a formula is used to determine the resale price and the portion that the seller will receive of the increased value of their cooperative interest. | Unit owners build equity as the value of their unit increases and as their mortgage is paid down. | Any increase in value belongs to the landlord and typically reflects itself in increased rents. The tenant receives no benefit from the increased value. | Owners build equity as the value of their home increases and as their mortgage principal is paid down. |

# 2

UP TO BAT:

# How to Get a Co-op Started

**SOME CO-OPS GET STARTED,** literally, from the ground up — what is called new construction. Others begin with the acquisition and rehabilitation of vacant buildings. Still other co-ops involve the conversion of an existing, occupied rental property to cooperative ownership — with or without major rehabilitation.

**THE COMPLEX TASK** of creating housing cooperatives or any multifamily residential building requires diverse skills and expertise in real estate development, finance, marketing, law, engineering, architecture, and project management. The cooperative development team must bring those skills together. Because *Home Base* is a manual about co-op development, all of the development steps are focused on co-ops. However, the basic steps outlined are usually required for any well-conceived multifamily residential development, whether co-op, condo, or rental. The complicated real estate development process is by no means unique to the cooperative form of ownership.

## *Devising a Winning Strategy: Planning and Preparation*

Some co-ops get started, literally, from the ground up — what is called new construction. Others begin with the acquisition and rehabilitation of vacant buildings. Still other co-ops involve the conversion of an existing, occupied rental property to cooperative ownership — with or without major rehabilitation. Major differences in the development process will stem from the presence of residents in an existing building. In the case of conversion of a rental building, existing residents are the best and most likely source of owners for the planned cooperative.

The number of units in an existing building or a planned building will greatly impact the complexity of the project and the number of people needed for the development team. It's possible to create a small co-op, but there are a number of costs that do not vary much, regardless of the size of the project. Because of this, it may not be as cost effective to create a small co-op as to a large co-op. A conversion project can be feasible with at least 25 units, though 50 units would be better.

Small co-ops are harder to create and harder to operate once in place. When there are fewer than 25 units, it is difficult to attract and pay for the cost of a professional property manager. It is also difficult for a small co-op to maintain leadership because the responsibilities of serving on the board can't be passed to as many individuals as in a large co-op. These factors are important to consider in planning new construction or conversion of a cooperative.

## WILL THEY BE FANS OR PLAYERS? *Existing Residents*

Where there are existing residents, it is critical to know the degree of resident support for a cooperative, what role they want to play in the development and conversion process, and whether or not there are any prohibitions on resident displacement. Such prohibitions on displacement can come from state or local laws, existing federal or state contracts, or from local governments or governmental agencies. Prohibitions can also be a condition of any social financial investment that will be necessary to make the cooperative affordable to its target market. Any such prohibitions must be a central consideration in planning a cooperative conversion and determining its feasibility. Residents who wish to stay and not purchase into the cooperative may need to remain as rental tenants of the cooperative. The latter case happens when the residents cannot legally be displaced for some reason or if the cooperative does not wish to evict them.

The presence of an existing group of residents will lead to differences in marketing strategies, timing of owner and board training, and the early involvement of prospective owners in the development process. Other aspects of development will be the same, whether or not there are existing residents.

### *Who are the players? The Development Team*

A development team is the group of people that make the cooperative happen. It can comprise members of a single organization or bring together many individuals and organizations.

## The Players:

Sponsor
Coordinator/Project Manager
Financial Packager
Attorney
Architect and Engineer
Marketer
Trainer
Management

*The full team described in this section would most likely be used in a large project, approximately 150 units or more. In smaller co-op development, multiple roles may be played by a single person.*

### *Roles of the Players*

### SPONSOR

For every cooperative, there is a development sponsor: a person or organization who is the final decision-maker, takes responsibility for outcomes, and provides the energy to carry the process through. The sponsor can be an individual or organization, for-profit or non-profit, with real estate development experience. It can also be a church group or charitable organization with little or no development experience, an apartment owner seeking a fair price for the property, or a well-organized group of residents looking to buy their building. Whether the sponsor puts up a substantial investment or obtains most of the necessary start-up funding from other investors or cooperative owners, its effectiveness will come from having a substantial stake in the outcome of the development process whether it is money, ideology, or reputation.

#### *Responsibilities*

During the project concept phase, the sponsor explores options, assesses needs, learns the co-op process, and formulates a plan. By the end of this phase, the sponsor should have the appropriate team and plan prepared to finance and implement the project in a professional manner. The sponsor should also understand state law and procedures as they relate to co-op formation. (Chapter 3 will address details of the project concept and planning phase.)

#### *Skills*

Few sponsors have all of the skills and capacities necessary to carry out every task involved in cooperative development. Therefore, the rest of the development team provides additional skills and capacities. Beyond the members of the development team, the sponsor will generally reach out to lenders, community groups, community leaders, and local, state, and sometimes even offices of federal agencies to provide critical resources to the development process.

### COORDINATOR/PROJECT MANAGER

Next to the role of sponsor, the most critical role that must be filled is the development coordinator or project manager. When the sponsor is a for-profit or non-profit corporation with substantial real estate development experience, a member of its staff typically fills this position. This individual or organization will oversee the entire development process.

#### *Responsibilities*

While various individuals on the team will manage important aspects of the cooperative development, it is the development coordinator who will:

- Oversee the creation of a business plan, timeline, and development plan
- Assemble and contract with the architect, attorney, and other members of the development team
- Ensure that the development team tasks are being completed on schedule
- Coordinate meetings of the team

- Oversee and assist team members with their tasks
- Create and update a financial pro forma and apply for financing, or oversee and work with the financial packager to do this
- Facilitate cooperation and communication among team members
- Ensure all government and other approvals are completed on schedule
- Oversee the creation of the cooperative corporation, consistent with state legal requirements
- Make sure that residents and/or purchasers are fully informed and appropriately involved in the development process. This last step is especially critical when existing residents are in place.

### *Skills*

To be effective, the coordinator must have excellent communication, political, and project management skills. Ideally, the individual or organization that fills the role will also have two sets of critical expertise– in real estate development and finance, and in housing cooperative organizational structure and operations. At a minimum, the development coordinator should have substantial expertise in one of these areas and be ready to work closely and effectively with a team member that has substantial expertise in the other area.

## FINANCIAL PACKAGER

Sometimes this responsibility falls to the development coordinator/project manager. The financial packager obtains the financing, often from a variety of sources, and is a critical component to cooperative development.

### *Responsibilities*

The role of the financial packager involves:

- Analyzing and presenting financing options for the cooperative based on market analysis, incomes of existing or projected residents, construction and/or rehabilitation requirements, and acquisition prices
- Assisting in the preparation of applications for pre-development loans from government programs or private sources to cover fees for architects, attorneys, and other expenses before construction
- Assisting in the preparation of the financial proforma, including the development budget and first-year cooperative estimated operating budget
- Participating in contract negotiations for property acquisition
- Preparing applications for loans, subsidies, and other forms of investment
- Assisting in the selection of and communication with lenders
- Monitoring the construction/rehabilitation program from a financial perspective and updating the pro forma accordingly
- Providing input in drafting cooperative documents, developing marketing programs, establishing cooperative operations, and arranging for owner training that complies with social investment requirements.

A sound development process will require the consideration of several basic financing options and likely many changes to the original option chosen as events and complications unfold.

### *Skills*

The financial packager must be imaginative, able to "make the numbers work" to meet the cooperative's future needs, and have access to funding sources.

## ATTORNEY

To successfully develop a housing cooperative, a number of complex legal hurdles must be cleared. The sponsor or developer needs an attorney who can navigate the many legal issues that arise during the development process.

### *Responsibilities*

The development team attorney plays a number of important roles and is crucial to:

- Negotiating the purchase of land or an existing multi-family building
- Negotiating and drafting contracts between the sponsor and outside members of the development team
- Reviewing and negotiating loan documents
- Drawing up the documents that structure the legal existence of the cooperative corporation and its relationship to individual cooperative owners
- Helping to file the necessary application and plans for the creation of the co-op corporation
- Explaining the legal structure and requirements of the cooperative corporation, if an existing resident group is the sponsor.

### *Skills*

The four primary considerations in selecting an attorney are: expertise, flexibility, capacity, and fee.

- *Expertise* refers to the experience and skill the attorney will bring to the development process. Among the skills that may be needed are negotiation, resident education, and possibly litigation. Areas of knowledge required should include cooperative experience, tenant statutory rights, real estate contracts, partnership and non-profit corporate structure, conversion of ownership form from landlord to cooperative ownership, tax implications, financing, and the structure and management of cooperatives.

- The attorney should have the *flexibility* to work in non-traditional ways. Where an existing group of residents is involved or a deep social investment is sought, the attorney may need to spend time patiently responding to questions at night or weekend meetings. Creativity may be needed to solve financing problems or resolve conflicts among the sponsor, residents, social investors, and community representatives who each have a stake in the development. The attorney must be accessible — willing to return phone calls promptly and available to answer questions and deal with problems as they arise.

- *Capacity* refers to an attorney's time and supporting resources. An attorney may be experienced in all areas but not have the time to commit to a new project. A less experienced attorney on the other hand, may have sufficient time to learn new subjects but will need to consult with other attorneys in order to do a competent job. Supporting resources are especially important when litigation is involved.

- Attorney *fees* can be a significant part of the soft costs of cooperative development. Soft costs are out-of-pocket expenses that are not directly related to property acquisition, construction, or rehabilitation. One way to reduce fees is to have more than one attorney. If the sponsor is a thinly funded community nonprofit or a low-income resident group, it may be necessary to rely to some extent on free legal assistance. Specialized issues involving cooperative structure, tax questions, or

## Hirer Beware

It is not advisable to have a building resident act as an attorney for either the development team or a resident group, particularly for free. No matter how willing a resident/attorney may be to help out, paying clients and other demands often overshadow good intentions. Cooperative development is a unique field and requires specialized expertise. Lastly, there is potential for perceived or real conflict of interest and exploitation.

Neither is it advisable to try to lower legal fees by limiting the attorney's scope of work too tightly. At a minimum, all cooperative documents and contracts should be drafted or reviewed by and discussed with the attorney. The attorney should take the lead in assuring that state corporations and securities requirements are met.

syndication scenarios may arise, requiring the expertise of a specialty attorney. It is important that one specific attorney has the clear responsibility for an end result, no matter how many attorneys or other professionals contribute to the work. Many attorneys will defer payment for a large part of their fees until construction financing.

## ARCHITECT AND ENGINEER

Early in the development process, the need for architectural and engineering reports will arise. In new construction, these professionals will be called upon to analyze prospective sites and make judgments as to what can reasonably be built and whether the location is desirable. Construction plans must meet local zoning restrictions. Utility and sewage lines must be readily available or affordable to install. The stability of the soil, the purchase price, and the number and type of units to be built are crucial early considerations.

### *Responsibilities*

Where existing structures are involved, early reports will provide a preliminary building evaluation of the structures and their environmental hazards. A "Phase 1 Environmental" report from an environmental engineering firm will detail any evidence of concerns -- for example lead paint, asbestos, underground storage tank leakage, etc. The engineer's evaluation (of mechanical systems, structure, roof, etc.) should describe the building, including apartment unit plans, and evaluate the major systems like plumbing and electricity. It should make recommendations for rehabilitation based on code requirements, energy conservation, resident need, and sponsor/cooperative input into amenities and materials required to meet market conditions. The evaluation should include a statement of probable construction costs for a variety of scenarios – from minimal upgrades to optimal improvements. These financial estimates are crucial to the financial packager who will use them to create the development budget, projected annual operating budget, sources and uses, cash flow projections, and other financial pro forma needed for initial loan applications.

### *Skills*

The architect should be familiar with local building codes and approval processes, be creative in design, be able to communicate well with the sponsor/cooperative, and depending on the construction management method chosen, have good construction management experience that ensures the construction timeline is met.

## MARKETER

In order for the cooperative to come into being, individuals must purchase cooperative interests. Some person or organization that is part of the development team needs to identify those people and help them buy into the co-op.

### *Responsibilities*

When already in place, residents represent the most logical marketing prospects. Often, one or two tenant leaders who understand cooperatives and are supportive of the effort can have a major impact in marketing to other tenants. When there are existing residents, the primary marketing task is to organize and train the existing residents. Communication skills, an understanding of cooperative structure and operations, and a profound respect for the needs and capacities of the resident population are required.

When the cooperative needs to identify additional buyers, it is important to educate local real estate brokers on cooperatives and enlist their involvement in advertising and marketing campaigns to identify potential purchasers. It may be necessary for the cooperative to hire a real estate agent to ensure that the cooperative sells out.

When an existing owner of a rental building wishes to convert the building to a cooperative, the property management company will often be the most important player in defining the success of the conversion. Nothing better demonstrates the advantages of ownership than converting to a more effective, resident-responsive management style. An overlap between management and marketing can also reduce development costs.

### *Skills*

The marketing skill sets required will be slightly different depending upon whether the property is new construction or rehabilitation of an existing building. Basic sales techniques should be complemented with an understanding of cooperative structure and operations. In addition, the marketer should have the ability and commitment to retain new owners after the purchase agreement is signed but before the property is ready for occupancy.

## TRAINER

Training is an essential part of the cooperative development process.

### *Responsibilities*

A trainer is responsible for teaching purchasers the basics of homeownership, the cooperative structure and their roles and responsibilities before they become cooperative homeowners. Purchasers must be encouraged to participate actively in the cooperative. Another key aspect of development is board training. A responsible leadership must be developed and nurtured to lead and manage the cooperative. Further, the continuous encouragement of new leadership must be built into the process of cooperative governance, and a commitment to ongoing owner and board training must be built into the cooperative's operating philosophy.

### *Skills*

A good trainer will have solid expertise in cooperative governance and experience in working with cooperative corporations—able to develop rapport with participants.

## PROPERTY MANAGEMENT

Most co-ops will require services from a property management company to take care of operating and maintaining the building. Some co-ops will be able to provide some services internally while others will look for a property management company to act as a consultant and then hire their own employees. All co-ops should have experienced management with good references.

### *Responsibilities*

The co-op will want management that can either provide full services or be willing to develop a plan that includes participation by the cooperative. The management must understand the co-op structure and provide complementary services. This includes meeting with the board at least once a month and providing a full and easily understood accounting of that month's activity.

### *Skills*

Where Federal Housing Administration (FHA) insured financing or Section 8 assistance is anticipated, management should have experience working with

## Timing is Everything:

### *When to develop a management plan*

Ideally, a management plan is put together during development, with management working as part of the development team. This can be especially valuable in conversion of existing occupied properties. Management can be effective in marketing cooperative interests to prospective residents and can have valuable input on cost-saving designs and materials that create savings in property upkeep. However, limited available funds or other factors may make this early involvement impossible. If management cannot get involved early, the financial packager should be able to provide a preliminary annual budget based on research. The management plan is something that can be delayed until the project is further along, if necessary. However, within a month prior to final closing, a management plan ought to be in place for a smooth transition.

## Additional human and organizational resources

In addition to putting together the development team, the sponsor and development coordinator will reach out early to lenders, community groups, community leaders, local governments, and public and private sources of social investment. Gathering support is sometimes formalized by creating an advisory committee whose members make a personal commitment to see the development process through from beginning to end. Advisory committee members should be individuals who can facilitate the mobilization of community resources and/or smooth the process to support development.

Bringing in appropriate government agencies early in the process will help government staff better understand cooperative housing and its financing. Relevant government agencies might include the municipal housing department, county health department, city and state housing authorities, bond agencies, and the local office of the U.S. Department of Housing and Urban Development (HUD).

Housing and Urban Development (HUD)-assisted projects. (See the Terms and Definitions appendix for details on these programs.) The management company might also have familiarity with other subsidy financing that is part of the project. Finally, management must understand that cooperatives are different from rental properties, in that the board makes major decisions and the management works for the board.

### *Money Matters: Fees for Professional Services*

Members of the development team can charge by the hour, a flat fee, or a contingency fee.

*Hourly rates* are most common for attorneys and financial professionals. They will tend to fall within a general range for each profession in its respective geographic location. A more experienced professional, who may charge a higher fee, may consume less time and incur fewer costs in the long run. A retainer or minimum fee may be required in situations where the fee is based on an hourly rate.

*Flat fees* are most common for architectural and engineering firms. Some firms may be willing to do some of the pre-development work without payment, with the understanding that, if development proceeds, they will be hired and paid to do the work.

*Hourly or contingency fees* are most common for financial packagers and development coordinators, especially where roles are combined in a single development consultant organization. Contingency fees are generally an agreed-upon percent of financing or percent of total development costs that are paid after successful completion of the project. Some fees may be deferred until later in the development process, and are paid from a source such as construction or permanent loans, proceeds from the sale of cooperative interests to owners, or from a combination of different sources. Management fees, on the other hand, will be paid on an ongoing basis over the entire life of the cooperative. Sometimes, a management company can be persuaded to become part of the development team in exchange for a contract once the cooperative begins operations.

## Payment for Sponsors

Sponsors, whether non-profit or for-profit, will also be paid for the cooperative development. The sponsor will need to recover its investments both for out-of-pocket costs and for the organization's time and effort. The sponsor will typically receive the bulk of its payment at final closing, when the property is ready for occupancy by owners, permanent financing is put in place, and purchases by cooperative owners are finalized. The sponsor's return can come in cash from the mortgage taken out by the cooperative, the sale of the building to cooperative owners, or a combination of the two. The sponsor can take unsold shares as part of its compensation. Sponsors can also take back mortgages on the cooperative land and buildings and, in this way, receive a return on its investment, its fees or profits, plus interest over time. The sponsor's compensation and the developer's fee are typically between 7.5 and 15 percent of total development costs,including acquisition.

# 3

## RUNNING THE BASES:
# The Cooperative Development Process

**COOPERATIVE DEVELOPMENT** involves two parallel processes: physical and organizational development.

- Physical development is a multi-step process including site/property selection, financial feasibility analysis, design, financing, site/project acquisition, permitting, construction, and operations start-up.

- Organizational development is also a multi-step process: entity creation, owner sales, owner and leadership training, and transfer of control from the developer/sponsor to the cooperative's member-owners.

While many of the steps in physical and organizational development will actually proceed simultaneously and some, like marketing, could be classified as either, each requires its own focus.

## No shortcuts

Different combinations of sponsors and development coordinators will allocate responsibilities differently and other development team roles will be bundled/divided among team members and organizations in different ways. We refer to the center of responsibility for many of the elements of development simply as the "sponsor/developer." Keep in mind the complex reality of development team roles as you work through the outlines of physical and organizational development.

### APPROACHING FIRST BASE: PHYSICAL DEVELOPMENT

There are two types of physical development:

1) Converting an existing building, possibly with moderate renovations.
2) New construction or "gut" renovation of a vacant building. Gut renovation is sometimes used in place of "substantial rehabilitation," a standard term used by lenders for significant restoration or refurbishment of an existing building.

The initial steps in converting an existing property to cooperative ownership are different from those for new construction. The two types converge later in the process and become more similar.

## The 8 Steps

Our description of the physical development process is divided into eight steps. While these steps typically occur in order below, they may vary or be pursued simultaneously depending upon the project.

- STEP 1: Project concept
- STEP 2: Site evaluation and selection using market demand studies and feasibility analysis
- STEP 3: Preliminary financing decisions and preparation
- STEP 4: Finalizing assembly of the development team
- STEP 5: Financial packaging
- STEP 6: Essential commitments
- STEP 7: Property acquisition and construction
- STEP 8: Operations start-up

## STEP 1: Project Concept

The first step is defining what type of project you want to develop. For the conversion of an existing building, as compared with new construction, certain decision points can be abbreviated. The project concept could be detailed in a paper that describes the project for stakeholders.

### Key Elements of Project Concept Plan

EXECUTIVE SUMMARY

- Cooperative Background
- Goals
- Cooperative Management Plan
- Board of Directors Experience & Responsibilities
- Operations/Management Plan
- Training Plan

PRELIMINARY MARKET ANALYSIS

- Market Context
- Market Trends

BUILDING PLAN

- Building Location and Size
- Proposed Design/Renovation
- Anticipated Timeline
- Contingency Plan

THE SPONSOR

- Management Team and Project Management Team
- Experience and Capacity
- Development Partners and Team

PROJECTED FINANCIAL PLAN

- Development Budget
- Operating Budget
- Balance Sheet
- Cash Flow Pro forma

APPENDICES

### *Decision Points*

*New construction or rehabilitation:* One of the first decisions to make is whether to do a new construction or renovation. Renovation projects are appropriate for buildings where residents have expressed interest in purchasing their apartments or there are a substantial number of vacancies in a building. In housing markets with higher vacancy rates, often the cost to acquire and renovate is less than new construction. In low vacancy rate markets, new construction may be preferable. New construction may also be preferable in markets where existing properties are not as adaptable to cooperative housing, for example, when many buildings are small, with fewer than 20 apartments.

*Neighborhood selection:* Define the neighborhood or neighborhoods where you will look for sites. Neighborhood selection research should include discussions with real estate brokers, local government officials, building owners, local neighborhood associations, and community development corporations. (See Step 2 to learn how to select a site.)

*Identifying likely market:* Identifying the likely market for the cooperative units is the next crucial decision to be made. The major things to understand about the market are the household sizes, desired apartment size, community or building amenities, and income. Typically, a better market for cooperative ownership will be individuals or families who are currently renters but are interested in ownership. In markets where cooperatives are less well known, there will often be households who cannot afford homeownership other than under a cooperative structure. In some cases, a cooperative may be for a specific market segment – like artists or seniors– which will require more focused market research.

Identifying the market helps define the type and size of units to be developed, the construction standards, the required local services and amenities, and the prices that will be affordable to that group of households. Affordable purchase prices for owners, as compared to the cost of purchasing and developing a site, also define the amount of subsidy that will be required. If the subsidy required is greater than what is typically available through local government and charitable sources, the project may not be viable or may require extra up-front time to enlist the support of subsidy providers.

Typical sources of information for likely cooperative buyers are census data, city and state community development and housing reports, local homeownership counseling agencies and consumer credit agencies, real estate brokers, and existing cooperative or condominium developers. Some homeownership counseling agencies or non-profit homeownership programs might also be potential sources. Most cities and towns with populations of more than 80,000 typically need to prepare Consolidated Plans to receive certain types of federal funding. These documents, which are publicly available, often have the necessary market information. Home Mortgage Disclosure Act (HMDA) data is also kept by census tract and zip code and can help you determine how many mortgages are applied for and approved in the geographic location and whether the area is experiencing increased or decreased residential investment.

*Concept paper draft:* Based on the above information, the sponsor will write a one-to-two page concept paper that can be given to the board of directors, relevant staff, potential residents, partners, and people who might be helping to identify a site or finance the project. The write-up should include:

- *Description of what a cooperative is and why you are interested in creating one.* Keep in mind that in most markets, your desired audience may not be familiar with cooperative housing.
- *Project type, size, and target neighborhoods.* Describe whether the project will be new construction, acquisition and rehabilitation, or conversion of existing occupied building(s); the number and likely unit sizes; and neighborhoods where you expect to look for property;
- *Target market of resident owners in the cooperative,* including the income ranges of the residents you anticipate will be living in the apartments and any targets for affordability. Also, estimate how fast the units will be filled/shares purchased.
- *Potential funding sources.* If the target market is likely to require subsidies to afford to purchase a unit in the cooperative, then a description of likely funding sources should be included. In addition, the source for pre-development financing (the costs required before construction begins) should also be indicated.
- *Likely timeline.* Determine the number of months to:
  - Find a site (often up to 2 years)
  - Package the financing
  - Complete architectural drawings and other requirements to begin construction or rehabilitation
  - Complete the construction
  - Market and sell the units
  - Seek and receive approval for the creation of the cooperative corporation
- *Potential partners.* Indicate any potential partners including consultants, other non-profit agencies, homeownership or cooperative counseling agencies, and any development team members identified.

### TIME OUT: *Creating a Contingency Plan for the Project Concept*

Planning for potential constraints on the building development process is critical to ensure success. It's important to develop alternatives in case a proposed site becomes unavailable or other problems arise. Lenders typically want to know that development assumptions are conservative, allowing for extra time in the timeline and financial contingencies in the budget, in particular. Lenders also expect the sponsor/developer to understand specific constraints of the process in your area. Summarizing major risks and how to address them is an important part of a solid plan.

- *Time:* The vast majority of developers and cooperatives find that their project took longer than originally expected. Delays are common in several parts of the development process, such as locating an appropriate site, gaining site control, securing financing, addressing environmental issues, obtaining building permits and zoning variances, preparing architectural drawings, completing major construction projects, moving residents if needed, and finishing cosmetic repairs. A project manager can help estimate how long design and construction work will take and ensure the proposed timeline is conservative.
- *Money:* It is critical to know what sources of funds are available before entering the site selection phase. Packaging resources, particularly if subsidy financing is expected, can be time consuming and difficult. Many subsidy sources are highly competitive, have application cycles only once a year, or may require more than one application to be successful. There may be more or fewer resources available than you expect.
- *Rules & Regulations:* Find out the compliance issues for the local jurisdiction of the site, such as building codes or zoning restrictions. Sources of information on local rules and regulations include experienced project managers, other cooperatives, architects, developers, contractors, and local government officials. It is important to note that local officials may interpret zoning rules and building codes differently. Therefore, you may get different answers to the same questions. In addition, buildings that require "special permits" or variances that include public or committee review are always subject to uncertainty. Many times, the final answer may not be available until an inspection or zoning hearing. However, it is important to be aware of the types of concerns that may arise and have a team that is experienced in dealing with them. Sometimes it is necessary to hire an expeditor to move the review and approval process forward.

## Expect the Unexpected

Even in the best of circumstances, situations will arise during the development process that you can't anticipate. Consider these possibilities:

- All three construction bids come in between 3 and 5 percent higher than budgeted.
- There is a shortage of building materials delaying the delivery of selected materials by two months, which in turn extends the project completion by two months and results in increased construction interest costs.
- The contractor discovers asbestos on site that has to be removed. This type of discovery should be avoided if an Environmental Phase I is properly performed.
- An expected funding source falls through, leaving the project $500,000 short.
- The site is vandalized and a portion of the work has to be re-done. While the replacement of materials and the labor cost of the work are covered by the builder's risk insurance, the damage to the project in time delays must be considered.

- *Need for Professional Assistance:* The development process involves a great deal of technical expertise. It is important to contract with knowledgeable professionals to guide you through various aspects of the process. Be aware that using volunteers can be an excellent way to obtain certain services; however, it can also be problematic due to a lack of commitment or time availability.

Contingency planning is a must. Most experts recommend a contingency fund of 5 percent on soft costs, 7 to 10 percent for new construction, and 10 to 15 percent for renovation projects, in addition to the General Contractor's contract. Some subsidy funders restrict contingencies to 10 percent or less; this should be researched in budgeting. A higher contingency for renovation projects is advisable as these often involve older buildings. Renovations can present unforeseen or hidden construction problems that are not discovered until walls are torn down and work is well underway.

While a contingency line item is always required with bank financing, it cannot substitute proper planning, budgeting, and oversight. Projects that go over budget are forced to delay construction while identifying additional funding; reduce the amount of amenities or the quality of materials in the construction/renovation; or eliminate the developer's fee (who may come back to the cooperative to cover that cost).

## STEP 2: Site Evaluation & Selection Using Market Demand Study and Feasibility Analysis

The next step is to identify potential sites, which includes gathering specific information about site location, arranging for site and environmental evaluations, and estimating subsidies available based on potential buyers' incomes. If the project will be rehabilitation or conversion, current residents' actual incomes will be used for estimating subsidies. As information is collected about potential sites, they will need to be evaluated for the feasibility of cooperative development. Banks typically require such an analysis for making financing decisions.

### *Location*

Among the things that need to be considered when choosing a location is which sites are available for new construction? What existing buildings have potential for rehabilitation? How much do the sites cost? A sponsor/developer should also consider:

- accessibility to highways, services, mass transit, and community amenities
- areas targeted by local government for subsidy financing or homebuyer assistance programs
- the homeownership rate in the neighborhood

### Hidden from Plain View

Potential sites can be found in unexpected places. Some leads to investigate include:

- Local realtors
- Foreclosed properties by local or state governments, banks, and Fannie Mae
- Distressed properties with HUD mortgages
- Re-zoning candidates (buildings or vacant lots are typically available in these neighborhoods)

Be sure to talk to your local government's housing and planning departments. Driving around the target neighborhoods is another important first step before beginning a fuller analysis.

If the homeownership rate of the area is falling, marketing any type of homeownership might be difficult. In cases where subsidy financing from the government is required, political support for the project might be important.

Cost should be the first level of investigation for potential sites: identifying building/land owners in the target neighborhoods, assessing their interest in selling, and determining their likely sales price. Information is typically available on-line or at the local building department or finance office. It is important to learn about existing violations on the site, the last purchase date, and the amount of current liens on the property. In addition, pay attention to other cost-influencing factors, such as Brownfield sites or if the building is in an area that might be eligible for an Enterprise Zone, Community Development Block Grants (CDBG), Redevelopment Census Tract, or other sources of funding. Online data from the census, area real estate brokers, and Home Mortgage Disclosure Act (HMDA) are typically useful. This information will help develop a short "back of the envelope" evaluation of likely costs to acquire, rehabilitate, or construct.

### Market Demand Study

Evaluate the housing market for potential demand for cooperative housing. Involve existing residents in gathering information about rehabilitation needs and about whether their fellow residents would be potential purchasers. Most lenders will want a formal market study as part of any financing proposal and will often need to approve the market study contractor. A market study for housing cooperatives has several primary components. It should:

- Demonstrate adequate demand for the property over the long term. Does current market activity suggest there will be an active market of buyers and sellers interested in a cooperative throughout its useful life?
- Demonstrate the price the market would be willing to pay for cooperative interests (shares) in the property. (For more about price, see "The Price is Right" at right.)
- Demonstrate the marketability of the project as a rental. Most lenders, particularly in markets where cooperatives are uncommon, will not provide the financing to construct/rehabilitate a project unless the sponsor can demonstrate that the building could be viable as a rental if it did not sell as a cooperative. In the event that co-ops do not make sense for the market, particularly where multi-family ownership is not well established, evaluating marketability as a rental can be important for assessing alternative operating income and building uses.

*Estimate Costs to Build.* The estimated costs to develop the project, including both "hard" (construction) and "soft" (inspections and reports, architect and attorney fees, taxes and insurance, etc.) costs should be included. These costs should be compared to the amount you expect the units to sell for and the anticipated blanket mortgage including any subsidy funding to ensure the project will be financially viable.

## The Price is Right

Creating housing that is affordable to neighborhood residents is important. In general, total payments for "carrying or common charges" and share loan payments should be similar or less than the typical housing payments for people purchasing properties in the area. In areas where cooperative housing or multi-family homeownership may be a new concept, the share price should be lower, and similar to area rents. Your likely market will be households that are currently renting, unless a specialized market such as a senior cooperative is the project goal. Housing payment amounts in the market can be researched on-line, from local brokers, and from local government housing officials. Determining potential resident incomes from census data or from community surveys or reports is another good strategy. Other research to assess potential for price and demand might include what size apartments are most desired and needed, estimated by household size, recent sales, and rentals in the area.

*Buyer/Seller Negotiation.* Potential sites can typically be narrowed down to one or two. The next step would be to enter into negotiations with the sellers. One challenge is that the time it takes to package subsidy financing is often several months. This can cause problems in hotter markets where owners may be reluctant to wait for the sale to go through. In markets or neighborhoods with higher vacancy rates it is possible to get an "option" to purchase a property that can give you six months or more to purchase it, or a "contract of sale" that provides an extended time (3 to 6 months) needed to close.

*Site and Environmental Testing.* For renovation and construction projects, an environmental review is required, especially if applying for any government funding. This environmental evaluation is different from the engineer's review of the structure and mechanical systems. For an existing building, however, an engineer's report may identify some environmental issues that need to be addressed, including asbestos and lead paint. For new construction projects, tests will include:

- soil borings (soil analysis)
- identification of the location of water, sewer, electric, telephone, and cable lines and the cost to extend them to the property
- a zoning analysis by an architect to see the potential size and number of units that can be in a building
- a review of possible drainage issues

If the environmental analysis identifies any problems, additional testing and a remediation plan may be required to clean up the site before construction or renovation.

The developer will typically test the site to ensure that it can be developed at the given price during the "option" or "contract of sale" period. This contract of sale period should enable the buyer to cancel the sale without penalty if any of the tests come back suggesting significant additional construction costs.

### Early and Often: *Conduct Regular Feasibility Analyses*

Many professionals recommend that feasibility analyses be conducted at six or seven separate times throughout the development process. Early analyses tend to be rough estimates, with each subsequent analysis gaining additional refinement. Throughout the physical development process, it is important that the project manager and/or financial consultant update the financial pro forma as individual line-item cost estimates change or as estimates of market demand or available subsidy require:

1. Predevelopment Phase 1 as the first part of the site evaluation and selection step
2. Predevelopment Phase 2 at the end of the site evaluation and selection step, when the completed market study is available
3. Predevelopment Phase 3 in dialogue with the architect, engineer, and (perhaps) potential contractors as the bid package is being put together
4. Upon completion of any redesign (as required, for example, by funding agencies)
5. Upon feedback from lenders requiring budget adjustments
6. Upon completion of the construction contract documents
7. After the bidding process, to align with the selected bid(s)

*Feasibility Analysis.* The market demand study supplies one side (the income or source side) of a feasibility analysis. The other side builds out the expense or uses of funds. It is one thing to know what the market will pay for cooperative shares at any given location with a particular set of amenities and monthly occupancy costs. It is quite another to balance this market demand with the anticipated project development and operating costs. In order to move forward with a development concept, that is exactly the balance that the developer/sponsor must be able to achieve. While most good developers use a highly sophisticated set of pro forma for their feasibility analysis, the two essential components are:

1. *The Sources and Uses Table* lays out all components of the total development cost, the uses of funds and the sources of funds. Development costs include developer's fees; construction costs; builder's overhead and profit; legal, architectural, financing, and other third-party fees; training and marketing costs; and every other element of the total budget. The uses against all the funds coming into the project include homeowners' share purchase prices, subsidies coming into the project, and long and short-term debt. Appendix C provides a sample sources and uses table.
2. *Operating Budget of the Project* demonstrates that, on an ongoing basis, the potential buyers will be able to pay all of the ongoing project operating and maintenance costs, including debt service on the cooperative's permanent blanket debt, with or without the help of ongoing subsidies. Appendix F provides a sample maintenance and operating budget.

## STEP 3: Preliminary Financing Decisions and Preparation

Much of the research and analysis conducted in the first two steps are essential for step 3. Project development funds come from a combination of three basic sources:

- *Equity* (funds or property provided to pay for construction, purchase or renovation): Contributions come first from the developer/sponsor and, ultimately, from the cooperative purchasers themselves.
- *Debt* (borrowed funds): Comes in the form of construction financing, then permanent blanket debt borrowed by the cooperative and secured by the land and buildings. Individual cooperative purchasers take out share debt that is secured by their cooperative ownership interests. In much the same way as when a company issues its stock, share loans generate debt for the individual but equity or cash for the co-op.
- *Grants, social investment, or "soft debt"* (borrowed or donated funds): Grants or soft debt are frequently provided from governmental or charitable sources for lower income households. Soft debt is borrowed money that need not always be fully repaid. Soft debt may be provided either to the cooperative and applied as a second position mortgage to the blanket debt or provided to individual shareholders as a grant or second position share loan. Often soft debt is forgiven over a period of time that the property is intended to remain affordable. If the co-owner sells and moves before the end of that affordability period, the co-owner may have to repay part or all of the soft debt.

The type of project planned will help define the financing and amounts of the three types of capital required. The sponsor/developer will also need to make preliminary estimates/decisions early on about:

- How much, if any, social investment will be necessary to make the project affordable to the target population;
- What sources of social investment might be available and at what cost. Many sources have substantial timelines for review and approval that can cause delays in a project, as well as requirements that can hurt marketability of the shares, such as resale restrictions or income documentation beyond bank requirements;
- What sources of market rate construction financing and blanket financing are available and at what rates and terms;
- How to balance share prices with blanket debt in structuring permanent financing.

During this early step, it is important to have a good estimate of what it will cost to develop the project and the likely share prices and blanket mortgage amount. Also, meet with potential lenders and subsidy providers to determine their interest in the project and their opinions of its viability. Presenting them with your concept paper, the site cost evaluations and site estimate is important. Potential funders can also provide important information that will help ensure the cost estimates and market assumptions are correct. Be clear with funders that you are still several months away from a firm proposal.

At this point, it is also necessary make a preliminary determination regarding the amount of subsidy needed and whether that amount is likely to be available. If the market prices alone are not enough to enable private financing for the project, social investment financing will be necessary to cover the difference between the price your target market is able to pay and the actual costs. Subsidies can typically be accessed through state and local governments and from the regional Federal Home Loan Bank for developing affordable homeownership or for low-income homebuyer assistance.

This research helps define what income ranges can be targeted because the subsidies can reduce the price to

**TIP:**

It is important to meet with funders before your development team is assembled, since you don't want to spend the time and money to contract with the full development team unless you know the project will be viable and that funders are interested.

the homeowner and enable lower income families to purchase shares. A quick scan and discussion with local and state government housing department staff would be useful. Banks should typically be contacted during the earliest steps and then again when packaging financing. Early contact is especially important in markets where cooperative housing may not be a familiar concept. Prior to applying for government and other social investment financing, a letter of interest outlining terms and conditions of financing will be received. Yet in cases where social investment is necessary, banks will usually not process an application until after commitments of the social investment have been received.

### STEP 4: Finalizing Assembly of the Development Team

At this point, all of the development team players, including the architects, engineers, and attorneys who will assist with the physical and organizational development should be identified. The sponsor/developer should begin to talk with potential contractors. The actual selection of a contractor may not take place until financing is almost or entirely in place.

### STEP 5: Financial Packaging

The first preparation for financial packaging occurs early in the development process during the project concept phase and preliminary financing decisions. It is important to apply for financing once the development team is selected, the more thorough site analysis is completed, construction drawings are prepared, and approval processes are completed or well under way. Government and subsidy funders typically have lengthy applications. Their review process requires extensive staff and, often, reviews by elected officials. These processes tend to take a minimum of six months to complete.

Many state and local governments may be unfamiliar with cooperative housing and uncertain about how to apply their existing subsidy products to the project. Although homebuyer assistance products are usually easy to convert to cooperative housing, some governments may require additional education and some modification to their application. Typically, the lower the income of the target market, the more subsidy financing applications need to be submitted. Often, a developer of affordable cooperative housing will be applying to both state and local governments for financing, and sometimes foundations.

Some may seek funding for pre-development expenses (expenses required before construction begins), if they do not have equity available. Many sponsors/developers first look for outside funding by seeking grants or forgivable loans to pay for engineering and architectural work, option costs to assure property availability, and the costs of putting together the next version of the feasibility analysis. Many nonprofit

## Finding your clean-up batter: *Selecting the contractor*

There can be value to having a contractor involved from the early stages of the development process. However, it can be less costly to wait until architectural drawings and specifications are completed and then find a contractor through a bidding process. If a developer uses a bidding process to select a contractor, an architect will typically prepare the bid package, with developer oversight. Usually around 30 days are permitted for the bidding process, during which time (for a renovation project) a site walk-through for interested contractors will usually be scheduled. Typically the lowest-priced, qualified bidder is selected.

A developer should check a contractor's references, review their bid with the architect to ensure estimates make sense, and ensure they have the capacity to handle your job and other projects scheduled for the same time. After a contractor is selected, negotiations around specific line items help to create a more finalized scope of work. Typically a contractor's bid amount is only committed for 60 to 90 days, so it is important to be ready to begin construction soon after the bidding process. After a contractor has been selected, you will also want to move to construction loan closings with your financiers.

developers, who meet the criteria for being "Community Housing Development Organizations" from their local or state government, are eligible for forgivable loans from the Federal HOME program for these costs. More detailed proposals are required to seek large amounts of social investment along with construction and permanent financing (including FHA-insured loans) from conventional lenders.

The feasibility analysis will be the centerpiece of these proposals. The level of detail and certainty involved will increase as one moves from proposals for small amounts of predevelopment funding, through additional seed money, and on to larger commitments for permanent social investment and construction and permanent debt financing.

## More About Pre-sales and Documentation

Many lenders will require pre-sold units as documentation of cooperative interest. These sales will be secured with down payments held in escrow from purchasers who can afford the balance of the ownership price and whose income can support the cooperative's projected monthly occupancy charges. The required percentage of pre-sales will vary among lenders and development scenarios. Higher blanket loan-to-value ratios may, for example, call for higher percentages of pre-sales. Markets where cooperative housing is less common will also typically require higher pre-sales.

### STEP 6: Essential Commitments

The sponsor/developer will need to put certain commitments in place in order to complete financing and move to construction. A firm purchase price must be finalized with the property owner and a realistic construction/rehabilitation cost with firm drawings established to be able to approach lenders with a loan request. Often, commitments and proposals will proceed through several iterations as costs and funding sources become more certain. For example:

- Loan commitments are generally made contingent on

## The Paper Trail: *Construction Documents*

A complete set of construction documents typically consists of:

1) **Working drawings.** These are the large floor plans, elevations, sections, and details that cover each and every aspect of the building. They provide dimensions, materials, layouts, and in some cases, construction phasing. The working drawings include architectural, structural, mechanical, electrical, plumbing, civil, landscape, interior design, and other specialty area drawings approved by the appropriate local government agency.
2) **Construction specifications** (or the "project manual"). These "specs" outline the materials and methods to be used and provide the contractor with everything from manufacturer and model numbers for equipment, to color numbers and finishes for paint. The drawings and specifications jointly form the "contract documents" to which the contractor will refer when preparing his or her bid. Since the specifications define the quality of the materials that will be used, it is important for the sponsor and/or developer to go over the specifications carefully with the architect to review the materials that will be used. Understanding the durability and aesthetic nature of the materials, their ease of maintenance, and their desirability in the local market are all important in reviewing the specifications.
3) **Bidding requirements.** These are instructions for those who wish to bid on the construction contract. Bidding requirements vary by funding source. Most funding sources require that the invitation to bid be sent to a list of approved contractors, though many also require advertising and outreach to minority and/or small contractors.
4) **Addenda (or additions)**. Addenda are additions to any of these documents issued by the architect during or after the bidding and/or negotiation process.

commitments for specific kinds and amounts of social investment.

- Social investment is often contingent on loan commitments.
- Construction and acquisition financing are generally contingent on a commitment for permanent underlying financing as well as some share pre-sales or documentation of the marketability of the shares.

### STEP 7: Property Acquisition/Construction or Rehabilitation

Once financing commitments have been secured, it will be time to complete whatever steps remain to acquire the property and begin construction/rehabilitation. The following elements must be in place to begin construction:

- Complete set of construction documents including final drawings, construction specifications, and bidding requirements.
- The executed general contractor's contract including conditions, contract modification forms (such as change orders) and the form of lien waivers to be used
- Site control evidenced by an executed sales contract, a signed lease, or some other legally binding agreement
- Firm commitment for permanent financing.
- All necessary third-party approvals required by the local jurisdiction to begin construction.

#### *Construction/Renovation Process Monitoring*

In preparing for work to begin, it is important to have the construction monitoring process in place. The architect will typically have either weekly or biweekly meetings on-site that the project manager or a representative of the developer/sponsor should attend. A representative, such as an inspector, from the lenders also attends. The architect's minutes from these meetings are an important log of the progress of the construction/rehabilitation and ensure the timeline created by the contractor is being followed. The contractor will typically request payment once a month or every couple of months and typically require payment within 30 days thereafter. An internal process enables the expedited review, sign off, and payment of invoices, including drawing down the funds from the funders. Most contractors, particularly the smaller firms, rely on those disbursements to pay their sub-contractors. Most contractors will also have interest or penalty clauses in their contract if they are not paid on time. In both instances, payment delays can lead to work slow-downs and increased costs.

#### *Constitution Changes*

Creating an expeditious process for review and approval of "change orders" is essential. Unfortunately during most construction and rehabilitation projects, changes are requested from the contractor. The reasons for this can vary: a certain material listed in the specifications is not available and the contractor suggests an alternate, or the contractor discovers different conditions in a building being renovated once the existing walls are torn down – and everything in between. Each change order request will require rapid review and decisions from the developer and architect. Most development budgets have a contingency line item to cover the cost of change orders. Since each change order reflects a cost increase, or very rarely, a decrease, it needs to be reviewed. If contingencies

### The Construction Process

Construction is initiated by the bidding process and selection of a general contractor. It is completed when the building is finished and the government issues a certificate of occupancy that permits individuals to move into the building. During this period, these activities occur:

1) A contractor is selected.
2) The contract and construction timeline are negotiated.
3) Mortgage financing is closed.
4) Construction is initiated.
5) The construction process is managed.
6) Change orders are monitored.
7) The certificate of substantial completion is negotiated.
8) The certificate of occupancy is obtained.

are used rapidly in the early part of the project, it can be sign of trouble later in the project and should be monitored carefully. To the degree that a change order may decrease the developer's fee/profit when exceeding contingencies, it will often require approval of the developer's staff/board in addition to the project manager and bank. A process should be in place to ensure rapid discussions and decision-making.

### STEP 8: Operations Startup

If the cooperative corporation has not already assumed ownership of the property, it usually will soon after the certificate of occupancy is issued. Once ownership and certificate of occupancy prerequisites are met, the cooperative can set up closings with the initial purchasers. At closing, the purchasers buy their shares from the cooperative and enter into occupancy agreements with the cooperative. After the closing, the new cooperative homeowners may occupy their units. Where 100 percent of the cooperative interests have not yet been sold, the sponsor/developer will remain financially responsible for the occupancy charges of the unsold units. The development budget will typically have a "working capital" line item to cover these costs. The financial health of the sponsor/developer and the cooperative corporation will depend on quickly selling the remaining cooperative interests or leasing units temporarily until all interests are sold. Typically, permanent lenders will not close on the underlying mortgage until binding purchase agreements/ subscriptions for a minimum number of apartments are in place.

By the time the certificate of occupancy is issued, the co-op will need management that can either provide full services or properly outsource the work to manage the property. Management also needs to develop a plan of participation by the cooperative's board and all of its members. The management must understand the co-op ownership structure and provide services that will complement it. This includes meeting with the board at least once a month and providing a full and easy-to-understand accounting of each month's activity.

#### *To self-manage or not to self-manage?*

One of the first decisions a cooperative board of directors will need to make is whether to self-manage, hire a management consultant, or hire a management company.

## The Ins and Outs of Cooperative Property Management

Effective cooperative property management protects the value of the building, the co-ops' principal asset, and keeps members satisfied by maintaining basic services and responding to co-owner requests and complaints in a timely and professional manner. Good management will:

- Prepare an annual management plan and operating budget for review and approval by the board of directors
- Prepare and submit all reports required by lender(s) and/or regulatory agencies
- Supervise all aspects of project operation and maintenance, including the purchase of necessary maintenance supplies and equipment, reporting major physical problems to the board, and providing expertise in the planning of major rehabilitation projects
- Collect amounts due and maintain accurate records on the daily operations of the property
- Serve as liaison with lender(s), various government agencies, professionals, vendors, and the co-op
- Hire, train, and terminate employees as necessary, with the board's approval
- Attend at least one board meeting each month to present the monthly financial statements (including actual versus budget amounts for expenditures and revenue, and assets and liabilities) and discuss any problems that may arise
- Assist the board in planning for required capital replacements and improvements that may be required over time
- Institute a well-defined and easy-to-follow work order, request, and complaint process.

Self-management is usually not recommended because few co-ops, even small co-ops, are able to adequately perform the multitude of important management tasks and establish sufficient internal control systems. Often the financing sources for the cooperative may require the co-op, at least initially, to hire a property management company to manage operations. What is right for a particular co-op will depend on its size, population, financing and regulatory requirements, and (in the long run) the experience, needs, and wishes of the cooperators themselves.

## TYPES OF MANAGEMENT

*Self-Management:* There are two types of self-management. In the first kind, the cooperative directly hires maintenance and administrative employees to manage daily operations. This usually includes a senior employee (property manager) who reports directly to the board and supervises all other employees and operations. In the second scenario, cooperative members perform the functions of maintenance and administrative personnel. No outside people are employed.

*Management Consultant:* The cooperative can hire a management consultant to administer some of the management responsibilities (such as collections and accounting) and handle other responsibilities itself (such as maintenance). Management consultants are often used in combination with one of the two forms of self-management.

*Management Company:* The cooperative hires a management company to administer all of the management functions, including collections, disbursements, and financial management, as well as supervising employees and maintenance.

### *How to Determine Which Management Form Best Suits Your Cooperative*

The style of management which best suits a particular cooperative is dependent on several factors:

- *Size* — A 10-unit cooperative may be financially unable to hire a full-time management agent. Much of the work may have to be handled by members.
- *Experience* — A board composed of relatively new members with little cooperative experience and no prior management experience may find self-management too much of a challenge and not cost-effective.
- *Time* — Self-management of the second sort (i.e. without employees) will only work if board members have ongoing, consistent time to devote to cooperative operations.
- *Legal or Contractual Requirements* — By agreement, the cooperative's lender or a regulatory agency such as HUD may require that the cooperative retain professional management. Legislation creating government social investment programs may also impose some sort of management requirement.

## ROUNDING SECOND BASE: *ORGANIZATIONAL DEVELOPMENT*

The organizational process is broken down into seven steps:

**STEP 1:** Creating the cooperative corporation
**STEP 2:** Preparing an owner handbook
**STEP 3:** Marketing the cooperative
**STEP 4:** Owner education
**STEP 5:** Purchasers become owners
**STEP 6:** Transition to owner control
**STEP 7:** Board of directors' training

The process will be profoundly influenced by the degree to which residents initiate or take an active role in cooperative development. Nevertheless, the steps described will help in understanding the process itself.

### STEP 1: Creating the Cooperative Corporation

The first step in organizational development is the formation of the cooperative corporation. Once it is formed, proposals can be written and financing inquiries can be made on behalf of a viable corporation. The articles of incorporation and bylaws must deal with both the development period and the ongoing operations of a mature cooperative.

In cases of conversion or where residents have been involved in establishing the cooperative, it is important to have them as involved as possible during the development phase, even before the cooperative corporation has been formed. In conversions, the sponsor/developer appoints an initial cooperative corporation board to represent the resident perspective throughout the development process, but which will allow the sponsor/developer to control the development process.

Care must be taken to comply with both federal and state laws when writing cooperative document provisions and setting up long-term contracts in the name of the cooperative during the development period.

Control of the board by the sponsor/developer does not mean that existing residents and/or subscribers (individuals who have signed agreements to purchase cooperative interests prior to the completion of the construction or conversion process) are to be left out of the decision-making process. In a resident-initiated conversion, the initial board may even contain one or more representatives of the residents. Appropriate resident involvement will heighten commitment to purchase, generate, and maintain interest through a sometimes lengthy period of physical development, improve design choices, and greatly strengthen the effectiveness of post-development cooperative governance.

### STEP 2: Preparing the Owner Handbook

The purpose of the owner handbook, often called Offering Statement or Prospectus, is to inform prospective purchasers of cooperative interests of just what it is that they will be purchasing. Solid legal advice is of critical importance here, as state and federal corporate, securities, tax, and consumer protections laws all come into play and the legal requirements vary somewhat from state to state. In several states, a cooperative corporation cannot sell shares until these plans are filed, reviewed and approved by the state.

At a minimum, the owner handbook will contain the cooperative documents (such as articles of incorporation, bylaws, purchase agreement, occupancy agreement, and rules) along with a narrative description of ownership, governance, and operations. The nature of cooperative homeownership, its income, and property tax will typically be addressed, as will the financial details of operations, possibly including a detailed first-year's budget. The narrative will also typically address issues of financing and management, and a summary of the building's condition. In the case of a renovation, the age of the major systems is also usually included.

If the cooperative is subject to regulation by a third party, (HUD, for example, where FHA-insured financing is used), then the documents related to the regulatory authority and the respective rights and obligations of the cooperative will also be included. The narrative in these cases will include a discussion of the regulatory design and its impact on individual cooperative owners.

## Save the Sales Pitch

The owner handbook is not a marketing brochure. It should carefully avoid making promises or predictions that are less than certain. On the other hand, both the narrative and the legal documents should be written in understandable language. A reasonable resident-owner of the target market should be able to get a clear and substantial understanding of cooperative ownership in general and of their particular cooperative by reading the handbook. A well-designed owner handbook will also become a useful text for much of the ownership training to come.

## An Inside Job: *Resident-Initiated Conversions*

A resident-initiated conversion can happen in several ways. For example:

- An owner may have abandoned the building, forcing the residents to assume the responsibilities of paying the bills to maintain services. Those residents may eventually contact a sponsor/developer to help them explore purchasing the property.
- An owner may want to sell the property and will either approach the residents voluntarily or be legally obligated to do so.
- A sponsor/developer may approach an active resident organization to suggest that they jointly explore the group's purchase of the building.

A resident-initiated conversion can differ significantly from one initiated by the sponsor/developer in that the residents may sometimes choose to take a more active role in the entire development process. An active resident group can greatly benefit the project down the road, both when it comes to marketing the cooperative interests and when the responsibility for cooperative operations is transferred completely to the membership. Involved residents tend to be very savvy. They will want the process to be theirs, and rightly so. The development process is about their homes and a home represents a significant emotional investment. A strong sponsor/developer recognizes the emotional component of the development process for existing residents. However, even an engaged resident group needs the expertise of the development team. The relationship between residents and the development team must be a trusting one, if the co-op is to succeed.

### Structured Communications

An active resident organization generally has a core of a few concerned residents. Others will be reluctant to join until enough substantive information is available to allow them to evaluate and make choices in their own best interest. Therefore, it is critical that the dissemination of information be consistent, comprehensive, and fully available to all residents. An organized system of communication with the residents can be set up through a combination of newsletters and floor, area, or court captains. This dual mode of communication ensures not only that everyone receives the same information (newsletters), but also that everyone has access to someone who can respond to questions. By involving committed residents more deeply, the resident organization becomes stronger.

### Balancing Opposing Values in a Cooperative Conversion

An existing building will usually require some degree of rehabilitation. The goal is to turn over a physical structure to the newly formed cooperative that is sound and unlikely to need major repairs in the near term. The cooperative will then need to accumulate funds in a replacement reserve to pay for future repair and replacement costs. At the same time, existing residents will generally place a high value on ensuring that all residents who want to stay can afford the new monthly occupancy charge, as well as the purchase price of their ownership share. This priority will be especially acute in resident-initiated conversions.

A well-planned rehabilitation will certainly produce long-term savings (e.g. in the form of reduced utility and maintenance costs). Nevertheless, where buildings are in need of substantial rehabilitation, the net result will inevitably be an increase in cost. This, in turn, will be reflected either in the amount of the membership price or the principal amount of the cooperative's blanket loan and its attendant monthly debt service, increasing monthly occupancy charges.

Accumulating reserves will inevitably raise monthly occupancy charges, even as it provides assurance of the cooperative's future viability. Social investment can certainly help fill the gap. But it is rare to be able to find enough social investment to pay for all the rehab needed. The process of finding a workable compromise can be especially arduous in resident-initiated conversions. Effective communications, especially providing a structured opportunity for inquiry and dialogue, will be critical in moving the development process forward. Fortunately, the structure of cooperative financing allows the maximum flexibility in balancing the need for rehab with the need for affordability.

## STEP 3: Marketing the Cooperative

Projects will vary depending on when the cooperative owners will be involved in development and the form of the cooperative corporation. In new construction projects the corporation won't be formed until after the building is built and achieves occupancy. Yet pre-sales will often be critical to the sponsor/developer's ability to obtain the necessary construction financing for new construction and vacant property development. A well-designed marketing program will target the population segments identified as prospective owners in the market study. Particularly in markets where cooperative housing is a newer concept, it is important to begin marketing early and to articulate both the homeownership quality of cooperatives and their unique aspects.

The developer should consider, based on the market trend data, whether the primary market is the immediate neighborhood, or if it extends to the city or region. If intending to apply for subsidy financing, these funders may have certain marketing requirements, such as a waiting list process and lottery system.

*Some marketing methods that can be used to reach out to new owners include:*

- community meetings
- newspaper articles
- Web lists (like www.craigslist.org or online newspaper ads)
- radio/TV appearances
- bulletin boards in laundromats, churches, schools, coffee shops, libraries and community centers
- waiting lists of qualified low-income buyers available through homeownership counseling agencies and nonprofit community development corporations

A key component to most marketing campaigns will be reaching out to area real estate brokers. Most local brokers have networks that meet monthly or quarterly. Calling them and arranging for a presentation on cooperative housing could be an effective first step. Contacting brokers in the neighborhood where your project is located would be the next step.

An effective marketing campaign will include enough orientation to ensure that prospective owners understand what a cooperative is and what their responsibilities will be. One of the purposes of orientation is to allow people who will not want to be a part of a cooperative community to self-select out. Early orientation and self-selection will both reduce dropouts during construction and enhance the long-term success of the cooperative.

One of the biggest mistakes a sponsor/developer can make is to adopt a landlord's approach to filling up units, particularly for limited equity cooperatives, where the share prices are low. While it is important to fill the units before closing, it is more important to fill them with educated owners. The ultimate measure of success of a sponsor/developer lies in the continued success of the co-op, not just in how quickly or with what financial results the sponsor/developer completes and disengages from the project. Co-ops are more prone to fall into financial difficulties without careful owner-selection and proper education. This is specifically true of co-ops targeting low-income groups and/or first time homebuyers – both of which tend to have few financial resources to cushion economic shocks.

## STEP 4: Owner Education

Training is an essential part of a successful housing cooperative, before, during, and after the development process – but it shouldn't require excessive time or burden on the resident-owners. In fact, training helps unmask the benefits at the heart of cooperative ownership and reveals that effective management can save residents time over the long-term compared to other forms of home ownership. Before becoming homeowners, prospective purchasers need to learn about the cooperative structure and what their roles and responsibilities will be. Training serves this purpose. Each purchaser should also be encouraged to participate actively in management to assure cooperative benefits are realized.

Special training is strongly encouraged for co-op board members so that their leadership remains easy, democratic and transparent. The cooperative will thrive as long as residents develop and nurture responsible leadership. By fostering a culture where new people circulate into the leadership periodically, the overall management burden becomes lighter, shared by everyone. Effective training should continue after closing, through the transition of control period, and, in fact, become a permanent part of cooperative living. Ongoing owner and board training built into the co-op's operating philosophy can help residents to achieve these benefits.

In addition, a trainer with no financial stake in the development will often be heard far more clearly than someone who is perceived to have interests adverse to the owner's own — even when all of the parties are saying the same things.

## Help Wanted

The best sources of training for cooperative board members are co-op associations like the National Association of Housing Cooperatives (NAHC). NAHC offers comprehensive, low-cost training at its annual meetings. Participating in NAHC's meetings is a great way for co-op board members to get quality training, and simultaneously reward leadership for their work. NAHC also has a network of regional cooperative associations that often provide more locally focused training and technical assistance. For lower income cooperative purchasers, there are housing counseling agencies in most areas that can assist in homeownership and financial planning training and preparation.

### *Training Curriculum*

An effective training program for owner education will inform the owners about their collective responsibilities to maintain the property from legal, financial, structural, and social perspectives. A basic, initial, training curriculum should look something like the following. (Note: This is only an outline of topics to be covered in an initial training. Ongoing training is essential for a healthy co-op.)

#### Ownership Basics (for owners)

- What is co-op/mutual ownership?
- Financing fundamentals
- Rights and obligations as residents
- Rights and obligations as owners
- Regulatory structure
- Property transfers – who can sell what to whom and for how much?
- Budget basics

#### Governance – Democracy in Action (for owners)

- Role of owners
- Role of board
- Bylaws – the structure of governance
- The annual meeting – eligibility, quorum, proxies, agenda
- Elections
- Changes to structure
- Regulatory program impact

#### Board Basics (for the board/leadership)

- Acting on behalf – delegation of authority
- Accountability and standard of care
- Property operations – roles of owners, board of directors, management, vendors, lender(s), regulator(s)
- Officers' roles and duties
- Committees

#### Financial Management (for the board/leadership)

- Review – financing fundamentals and budget basics
- Budget process
    - The annual cycle
    - Estimating fixed and variable costs
    - Reserves
    - Debt service coverage ratio
- Rehabilitation and improvements
    - Planning (estimated useful life)
    - Financing options
- Management
    - Oversight – asking the right questions and understanding the answers

- Accounting principles – cash v. accrual
- Monthly reports
- Payables & receivables

### Owner Screening and Training (for ownership committee/leadership)

- Making ownership policy
  - Fair housing issues
  - Financial accountability
  - Effective policymaking
- Designing a screening process
  - Role of the board
  - Delegation of responsibility
  - Role of management
  - Role of ownership committee
  - Appeals
- Owner training (training for trainers)
  - Review of owner training curricula
  - Effective training techniques

## What happens at closing?

- Purchasers pay any balance of the ownership price beyond their original deposits. Sometimes, this involves closing on a share loan or signing documents that enable subsidy dollars to be paid to the cooperative by a third party on behalf of the purchaser.
- Purchasers sign the occupancy agreement and become subject to its obligations. This includes monthly payments, the first of which is generally made at closing.
- Cooperative ownership certificates or shares are issued, as are proprietary leases, evidencing the ownership interest and occupancy rights of the new owner.
- Once complete, the new owners will be entitled to occupy their dwelling units for the first time as cooperative owners.

A large amount of training information is available for free from the Urban Homesteading Assistance Board. In addition, the North Country Cooperative Development Fund has several free, downloadable cooperative housing toolboxes available online that contain information for boards, owners, and committees. Finally, NCB Capital Impact is a source of training materials and provides technical assistance to housing cooperatives. Please continue to check our website for the latest information at www.ncbcapitalimpact.org.

### STEP 5: Purchasers Become Owners

There comes a point in the physical development process when the building is complete and operations begin. Typically, this coincides with the point in organizational development when purchasers become owners. After reading owner handbooks, signing purchase agreements, putting down deposits, participating in at least some training, and, possibly, participating in some part of the development decision-making, the buyers are now ready to purchase the cooperative interests and become owners. The importance of this transition is both legal and financial.

### STEP 6: Transition to Owner Control

Board control by the sponsor/developer will end at the first annual meeting of cooperative owners when they elect a new board. At this meeting, the original sponsor/developer-controlled board of directors will be replaced by a board elected by the cooperative owners. This should take place after the property is ready for occupancy and a given percentage of the cooperative interests have been sold. This does not mean that residents can have no part in the governance of the cooperative corporation prior to the first annual meeting nor does it mean that the sponsor/developer will necessarily have no part thereafter. It does mean, however, that the balance of power and responsibility in cooperative governance will shift considerably.

After this transition, sponsors/developers can continue to have a role in governance in one of two ways. First, they may hold a number of unsold ownership shares during the first annual meeting of the cooperative. This means that under the cooperative bylaws the sponsors/developers can vote in the election of directors. They may be able to appoint owners to the cooperative board until most or all of the remaining co-op shares have been sold.

The second way in which sponsors/developers may have a role depends on the bylaws. They may be able to reserve one or more seats on the cooperative board, whether or not they hold any unsold shares. It could be temporary to allow the cooperative to access the sponsors/developers' expertise during a limited transition period, or permanent to provide the sponsors/developers with a continuing stake in the cooperative's success. The latter would be most likely if the cooperative were part of a mutual housing association.

## The Power of Training

With the transfer of cooperative governance and control to the owners, the importance of the owner-training program will become strikingly evident. According to most cooperative bylaws, the first annual meeting of owners is triggered by the achievement of a threshold level of closing of ownership shares (for example within 90 days after closing 60 percent of all available memberships), or within a specified period after closing on the first membership sale (within two years), whichever comes first. An effective training program will have prepared both the ownership at large and the new board for their new roles and responsibilities. The continuation of some form of training, especially for the board and leadership, through the first year of owner governance is highly recommended as well.

### STEP 7: Continued Board Training

The role of the board of directors in understanding and overseeing financial and building/physical planning reports is an expertise few board members will intrinsically have and requires training to understand. As the board membership changes over time, new directors will be required to receive training. The board should plan to participate in at least one annual training on "board basics," understanding financial statements, and building operations.

In addition, it will be important for board members to seek outside training, as well as communicate with other cooperatives and owners. Often ideas for cost savings in insurance, energy, and various contractors arise by communicating with other cooperatives or property owners. The local chamber of commerce or building owner associations usually have annual meetings or conferences and may also sponsor trainings. The Consortium for Housing and Asset Management has training and materials online to assist in this effort.

# 4

KEEPING SCORE:

# Financing Cooperatives

**IN CHAPTER 1,** we outlined the main concepts of financing a cooperative: blanket and share loans. In chapter 3, the Cooperative Development Process, we summarized preliminary financing decisions related to debt, equity, and social investment, along with some financial planning processes. This chapter will address potential financing sources and the loan process in more detail.

## *The ABCs of Blanket and Share Loans*

Co-op corporations are financed with a combination of "blanket" debt and equity. Equity is typically derived from the sale of shares or ownerships. Ultimately, the total of the initial debt and equity is what finances the development of the cooperative.

### *What's a Blanket Loan?*

A blanket, or "underlying" loan, is the financing used by the cooperative corporation to purchase the land and/or building. Cooperatives also can use a blanket mortgage to refinance existing blanket debt or finance major improvement and rehabilitation projects. The cooperative corporation is liable for the blanket mortgage. The individual owners of the cooperative are not liable to the blanket lender, nor do they need to individually qualify for the blanket loan. The owner occupancy agreement obligates cooperative owners to pay their proportionate share of the monthly blanket loan payment. The cooperative can and will enforce this obligation, but the blanket loan lender cannot. However, should the cooperative be unable to make payments on the blanket loan, the lender may have certain rights in order to be paid.

### *What's a Share Loan?*

The cooperative share of each owner can be financed with a share loan, or an agreement between the co-op owner and the share loan lender. The share loan enables the owner to pay for the purchase of a share in the co-op corporation that owns the real estate. The corporation does not participate in the share loan, though it will need to legally agree to the share lender's ability to foreclose on a shareholder who is unable to pay his/her share loan debt. If an owner has obtained a share loan, only the owner is individually liable to the share lender. The cooperative incurs no financial obligation to the share lender.

### *Why Is A Blanket Loan so Useful?*

The ability of the cooperative to secure long-term blanket debt can be especially advantageous when financing major improvements or rehabilitation. Only cooperatives have the option of using new, long-term blanket debt financing to spread costs over time in affordable monthly payments for which their owners do not need to individually qualify. Like condominiums and homeowners' associations, cooperatives can choose to accumulate reserves at a high enough annual rate to cover anticipated rehab and improvement costs. Additionally, co-ops can assess individual owners for their share of the total cost of a rehab or improvement project when needed. Blanket lending is more equitable because it casts the financial obligation of improvements over a period of time in the future. Therefore, the individuals who benefit from the improvements pay for them at the time they are needed. In contrast, when improvements are paid through building assessments, the costs are paid by owners who may not remain in the building long enough to enjoy the full benefits of the improvements they paid for.

*Share Loan Default and Foreclosure*

In the event of foreclosure by the share lender, the co-op board terminates the individual's ownership and evicts the owner, based on a "recognition agreement" with the individual share lender *(see the sidebar "What is a Recognition Agreement?")*. The lender becomes the legal owner of the share, and then sells it as outlined in the recognition agreement, subject to a new owner gaining approval by the co-op board.

## What is a Recognition Agreement?

A recognition agreement "recognizes" that the cooperative and the share lender have potentially competing interests. In the event of default by a share owner, the collateral is his/her ownership share in the cooperative. Share lenders require a recognition agreement as a condition of each share loan. The recognition agreement establishes the rights and obligations among the share lender, the cooperative corporation and the share owner. Recognition agreements vary according to the share lender. But a typical agreement states that:

- the cooperative corporation guarantees that it is the owner of the real estate and that the share owner (borrower) is a member-owner of the cooperative in good standing.
- the cooperative corporation consents to the share owner's pledge of his/her cooperative share as security for the share loan. This can also protect the share owner from predatory lending.
- the cooperative corporation agrees to notify the share lender of any default by the share owner in his occupancy charges or the cooperative corporation's own default on the blanket mortgage or taxes.
- the share lender is given a right to end/repair certain defaults by the share owner or cooperative.
- the cooperative agrees to terminate ownership if the share owner defaults on his/her share loan obligations.
- priorities related to who gets paid first are established between the cooperative, the share lender, and the share owner upon foreclosure and resale of the share owner's cooperative share.

## What is an Aztec Agreement?

The Aztec Agreement is an industry standard recognition agreement. It generally creates a favorable situation for the co-op corporation through the share lender in the event of default by a share owner. Other recognition agreements spell out some of the subjects/issues that are implied by the Aztec Agreement, but may favor the share lender (such as a bank) over the cooperative in certain default or foreclosure matters. A best practice for cooperatives is to negotiate with share lenders for a recognition agreement as close to the Aztec Agreement standard as possible.

*Blanket Loan Default and Foreclosure*

In the unlikely event of a foreclosure by the blanket lender on the mortgage of the building, the lender could potentially sell the entire building. If there are any proceeds in excess of the sale price following foreclosure on a blanket mortgage loan, this money goes to the cooperative shareholders. However, the termination of the cooperative corporation's ownership of the building would also terminate the share owners' shares in the building and their occupancy rights.

### *The 1-2-3s of the Development Budget*

A development budget is required to build a new co-op or pay for a major rehabilitation project. Developing a preliminary budget for the cost of establishing the cooperative building (through either renovation or construction) is important for the following reasons:

- Sets the project's financial boundaries
- Supports educated decisions about financing options
- Convinces lenders and funders to support the project
- Reduces risk of unwelcome "surprises" during the development process

A development budget is typically divided into three phases: pre-development, construction financing, and permanent financing:

- *Pre-development financing* is used before construction or renovation begins. Predevelopment expenses typically include architectural, legal and filing fees, environmental testing, soil borings (soil analysis), up-front construction financing fees (such as appraisals and bank legal costs), building or engineering reports, and other consultants. Some costs can be deferred until the closing of construction financing, while others will require immediate payment. Most often predevelopment costs are paid for by the developer or from its own cash or credit. In the case of conversions of an occupied building, the residents may agree to fund some of these costs to enable the co-op conversion to occur.

## Where to Find Predevelopment Financing

Nonprofit agencies may have access to pre-development financing from local or national nonprofit intermediaries such as NCB Capital Impact, Enterprise Communities, or Local Initiatives Support Corporation (LISC) and others. In addition, most state and local governments have pre-development funding available for community-based nonprofit organizations through the Federal HOME program.

- *Construction financing* is required for a new development or the renovation of a building. The amount of financing a bank will provide during construction varies, but is usually based on the building's value upon completion. This is typically between 75 and 90 percent of the after-built value – called the "loan to value" ratio. Banks will often request that the building be valued both as a cooperative and as a rental building to determine the "loan to value" ratio. This assures the lender that it can be repaid by selling the property, if for some reason the cooperative does not get formed. Banks may also require that the developer or sponsor provide cash equity during construction, even if the loan-to-value requirements are met otherwise. This assures the bank that the developer or sponsor has a real stake in the project completion. Banks need a substantial review time and often require their own building or engineer's report, environmental report, and appraisal. Banks will also review the drawings and specifications, as well as the financial statements of the developer. Bank review and approval usually takes at least 90 days.

## Who's on First? *Order of Lender Repayment*

In affordable housing development, bank financing is the first loan to be repaid, called "first position," ensuring repayment to the lender even if the project is not completed. Government and social investment financing for projects typically take second position during construction or third, if there are more than two lenders. Because government or social investment lenders are paid after the bank lender, this funding can help ensure that the bank financing meets loan-to-value requirements. If the funding goes to the developer/sponsor, government and social investment financing may also meet the developer/sponsor's equity requirements. Some social investors are willing to have their funding disbursed in advance of the construction loans. If a social investor lends at a reduced interest rate, this can save in construction loan interest costs, making the project less expensive and potentially more affordable. Some social investors require that their investment be made in tandem with bank financing.

- *Permanent Financing* includes two components: blanket loans and share/ownership purchase loans. Individuals usually obtain a share loan to purchase their cooperative share. The share/ownership purchases are considered "equity" to the cooperative corporation, since the purchase provides cash to the corporation. Social investment funding can take the

## Piece by Piece: *Components of a Development Project Budget*

The following twelve categories are a part of most development project budgets. Each item may not apply to your specific project, but they have been included to demonstrate the possible scope of project costs:

**(1) Land or Building Acquisition**

- Surveys and Site Assessments
- Appraisals
- Engineering Studies
- Environmental Testing
- Purchase Price (of land)
- Soil Borings
- Legal Fees
- Demolition Costs of Existing Structure(s) (if appropriate)
- Title and Recording Fees

**(2) Professional Fees**

- Architects and Engineers
- Legal Counsel
- Project Management
- Space Programming
- Construction Manager
- Cost Estimator
- Interior Designer
- Technology Consultants (Information Technology, Security)
- Equipment Planner
- Environmental Consulting Firm (if environment testing indicates remediation is required)
- Financial Consultant
- Other Professional Consultants

**(3) Construction**

- General Contractor Contract or separate contracts for various specialties (used only if required by funders or if the developer has substantial construction management experience/skills)

**(4) Site Preparation**

*(Most should be in the General Contractor contract)*

- Utilities (water, sewage, gas, etc.)
- Site Drainage
- Landscaping
- Parking Lot
- Surfacing and Fencing
- Outside Lighting
- Environmental Remediation
- Demolition
- Appendix D provides a sample development project budget
- Temporary or Permanent Relocation (if renovations make an apartment uninhabitable. For projects receiving federal funds, federal relocation assistance requirements must also be followed)

**(5) Furniture, Fixtures & Equipment (FFE)**

- All Movable Furnishings
- Computers, Telephones, Data Lines
- Security Systems
- Signage/Artwork
- Installation Fees

**(6) Inspection**

- Inspector to supervise work on owner's and/or lender's behalf

**(7) Administrative & Permitting Costs**

- Postage & Shipping
- Permits, Filing, and License Fees
- Moving/Storage Costs

**(8) Financing Costs**

- Commitment Fees
- Mortgage Recording Costs
- Interest during pre-development and construction
- Lender's inspection during construction
- Lender's Legal Costs
- Letter of Credit Fees
- Mortgage Insurance Fees
- Interest Reserves

**(9) Insurance**

- Builder's Risk
- Errors & Omissions (Architect)
- Property and Liability
- Worker's Compensation Insurance
- Fire & Theft
- Sponsor/Developer Directors and Officers Liability Insurance

**(10) Contingencies for emergencies and unforeseen events and change orders during construction**

- Soft costs – 5 percent
- Hard costs – 7.5 to 15 percent

**(11) Developer's Fee (Typically 7.5 to 15 percent of total development costs, minus acquisition)**

**(12) Up-front Replacement and Operating Reserves**

form of grants that reduce the permanent debt or equity financing requirements or may be "soft debt" at the investor's discretion, applied to either the underlying or the share loan, typically as a second position lien.

## *Other Budget Nuts and Bolts*

### WHAT IS A FINANCIAL PRO FORMA?

A financial "pro forma" is an educated projection before the project is built about income and expenses a cooperative will generate after construction is complete. Pro formas are important tools for understanding how cooperative financing works and how the three development budget phases described above are integrated. The pro forma typically includes three interdependent budgets:

- *The development budget* includes acquisition and construction/rehabilitation costs and soft costs, such as legal, training, and development fees, as well as reserves for covering unanticipated construction costs and anticipated vacancy losses during the post-construction sell-out period. *(See Appendix D.)*
- *Sources and uses of development funds* showing where the money is coming from and how it will be spent, including equity, conventional debt, and social investment. This is sometimes broken out into three sections reflecting the three phases: pre-development, construction, and permanent financing. *(See Appendix C.)*
- *Detailed operating statement* showing where the money comes from and how it will be spent to run the co-op once it has been built. The operating statement expenses typically include utilities, maintenance, property tax, insurance, and administrative costs, along with prudent operating, replacement reserve funding, and debt service payment (this refers to the amount of money required to make the payments on the co-op's blanket mortgage loan). Income sources include occupancy charges or, in the case of apartments, rental income. The pro forma typically shows estimates for the operating statement for 10 years or the underlying mortgage loan term. *(See Appendix F.)*

## More about the Operating Statement

An operating statement (or budget) shows the annual revenues and expenses of the building with any resulting surplus or deficit. It also shows that sufficient Net Operating Income (NOI) exists to pay the underlying mortgage payments. A "debt coverage ratio" in the budget is used to demonstrate to lenders that there will be enough cash flow after all expenses to cover the mortgage payment. If estimates are used for any items, sources should be clearly noted. For example, an insurance broker could be used for estimating insurance costs, or a property management company can be useful in deriving estimates for many of the items. A ten-year budget projection should also be included; an inflation factor is usually applied to the occupancy charges for future year projections. An accountant or management company can help prepare the operating statement.

## Purchase Prices and the Pro Forma
## *In addition...*

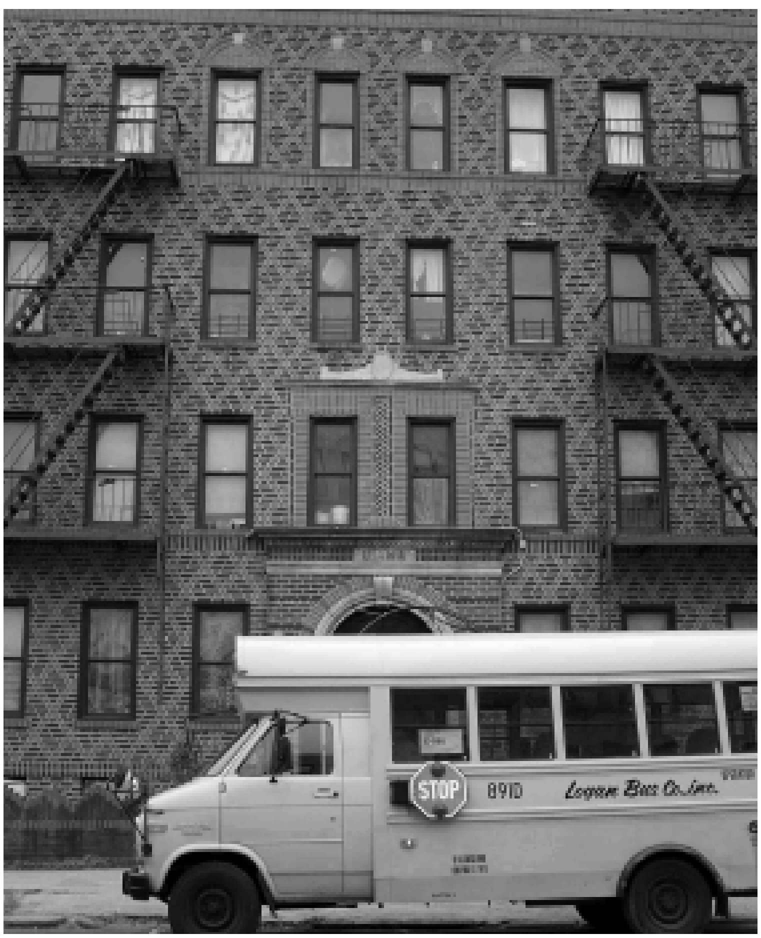
When dealing in affordable housing, most subsidy funders will want a chart added to the pro forma indicating that the share/ownership purchases are affordable to the target population. Subsidy funders will require that no more than 30 to 33 percent of the purchaser's income goes to pay for the residents' housing costs, including the common charges and the share loan.

The pro forma summarizes the conclusions of the market study, as well as the construction and operating cost analyses, to determine whether the cooperative is financially viable. A proper pro forma ensures that the share/ownership prices for units are realistic given the local market, and also factors in that purchasers will need to pay the budgeted "occupancy charges" each month. The pro forma also assists in estimating the amount of subsidy financing required to establish purchase prices and occupancy charges that are affordable to low and moderate-income households.

### *Cash Flow Pro-Forma*

Separate from the financial pro forma and operating budget, the cooperative will want to have a month-by-month cash flow pro forma. The cash flow pro forma usually covers the fiscal year and is broken down by month so the cooperative can monitor its cash flow and cash needs. This report is important because the timing of funds received may or may not coincide with the time when funds are needed. Many expenses are billed annually or quarterly, while revenue tends to be fairly consistent by month, except for vacancies. Therefore, a cooperative may have an operating surplus when revenues exceed expenses for the year, but a cash flow deficit when cash cannot cover expenses for a specific month. To ensure there is sufficient cash in the bank to meet operating expenses, a monthly report can be useful.

Monthly budgets are also useful as a quick-warning system for the board of directors if costs are changing or if cash management is becoming lax. It enables the board to detect and address changing circumstances, such as rapidly rising insurance costs or increased energy prices. Often, based on the monthly reports, a cooperative may make a "budget modification" after six months.




### *Finding Funds: Loan Types*

The loan type chart *(on the next page)* highlights the primary differences between various loans used in a typical development project. When the construction and rehabilitation project is completed, all short-term loans are repaid by the cooperative's blanket and share loans. The loan types are listed in the order they are needed. Pre-development loans are required first and are typically the smallest loans. These loans carry the highest risk since they are usually needed before a project is fully defined or financed and often before there is a property to provide collateral. Loan types decrease in risk as the process progresses.

Construction lenders have a short-term focus and a unique set of skills that enable them to closely monitor the construction/rehabilitation process. Although a short period (6 to 24 months), it carries substantial risk because of potential scheduling delays, cost overruns, subcontractor nonperformance, or a slower market delaying sales of units. Since the amount of the "construction loan" interest and other costs increase the longer the project takes, unpredictable time delays can threaten a project's viability, thus increasing loan risk. The decision to lend on a particular project is normally based primarily on having permanent "take-out" financing to repay the loan at project completion, even if the construction lender and permanent lender are one and the same.

| LOAN TYPE | USE OF LOAN FUNDS | TYPICAL LOAN TERMS | COMMENTS |
|---|---|---|---|
| Pre-Development Loan | Covers initial costs such as down payments and architect, engineer, legal, appraisal, site & environmental testing fees. Also applications for grants and other funding sources. | Term is typically 12-24 months at a fixed interest rate that can be relatively low given the short-term. Often underwritten more as a line of credit based on the developer/ sponsors financial assets. Loan can typically be repaid early without penalty. | Usually smaller loan amounts (under $100,000). Interest may be payable quarterly or deferred until repayment. |
| Bridge Loan | Covers time gap between end of construction loan term and closing of permanent loan, or to "bridge" other funding that has long processing time. | Higher rates due to the risk that the permanent or government/subsidy loan will not close. Terms range from 3 to 36 months. | More complicated loan structure that involves more sophisticated lenders who command higher fees. |
| Construction Loan | Covers the costs to acquire land and construct a building or to acquire and renovate an existing building. | Variable interest rate with only interest paid during construction (some government lenders may defer interest payments until permanent closing). Full principal repayment is usually required at permanent loan closing (which also typically requires a certain percentage of units sold). Terms range from 6 to 24 months. Lender will control disbursements, based on inspections, to ensure construction is proceeding as agreed. | Lender will not usually close until a commitment has been issued for a permanent loan to repay the construction loan. Collateralized by property. |
| Blanket/ Underlying Loan Permanent Loan or Commercial Mortgage Loan | Purchase land or buildings and/or finance a project at the end of the construction period. | Cooperatives may have to provide up to 25 percent equity (in other words, the loan may be limited to 75 percent of the value of the property plus any improvements). May also require a certain number of units be sold or rented before closing.<br>Payments of principal and interest are made monthly based on an amortization of 15+ years. | In conversion of existing cooperative improvement projects, the construction and permanent loan may be the same loan. The loan term is often shorter than the amortization period – requiring a balloon payment or refinancing at maturity. Repayment depends on ability of the cooperative to fill units, collect occupancy charges, & make payments. Collateralized by real estate. |
| Share Loan | Covers cost of a co-op share purchase. Finances the borrower's interest in the co-op corporation. | Depending on the share price, these loans can mirror condo loan terms: 75 to 95 percent loan-to-value, fixed and variable interest rates based on 30-year amortization schedule. | Collateralized by co-op owner's shares. |

### *Making Sense of Debt, Equity, and Social Investment*

Funds for cooperative development can come in three basic forms: *equity, debt,* and *social investment*. Generally, it takes a combination of funding from all three to make affordable housing development happen.

*Equity:* At the beginning of the development process, equity comes from the sponsor. The initial amount may be small to cover the salaries and other costs of pre-development analysis. Most construction lenders will require equity, including actual cash equity during construction. A portion of the (non-cash) equity may be in the form of the value of the land or building to-be-developed, if they are owned by the sponsor/developer. Social investors may provide funding directly to the sponsor, thus providing a portion of the equity. After the cooperative is formed, some of the equity will come from sale of the shares.

*Debt:* At the beginning of the process, debt can take the form of a pre-development loan. Further along, that loan may be refinanced as part of an acquisition or construction loan. Ultimately, most cooperatives will have some form of permanent blanket loan in place. The blanket loan can consist of loans that were used to acquire land and/or construct or rehabilitate a building.

*Social Investment:* Making housing affordable to low- and moderate-income individuals and families often requires some form of social investment. Social investment comes from government or charitable sources and can take many forms:

- *Direct grants* from governmental or charitable sources to the cooperative itself or to individual owners to pay part of the purchase price of individual memberships
- *In-kind contributions* such as free or reduced cost (below market) property and/or free development or legal services
- *"Soft second loans"* to either the cooperative or individual owners that do not need to be repaid until resale (some of these loans may be forgivable over time or remain in place as long as the cooperative or the unit remains affordable)
- *Reduced-interest-rate blanket or share loans* from government or charitable sources
- *Payment in lieu of taxes (PILOT) programs,* or other state and local programs to reduce property taxes
- *Individual Development Accounts (IDAs)* are programs, typically administered by banks or nonprofit agencies, that provide matching funds to low- or moderate-income households for home purchases or education
- *Ongoing payment assistance* to owners in the form of Housing Choice Vouchers (if the local housing authority has a HUD-approved homeownership program) or similar government subsidies

## Counting on Foundations

Foundations can be a useful source of social investment, particularly when requesting funding for specific small pieces of the total need, such as pre-development or bridge loans. Foundations provide funds as:

- Grants that do not need to be repaid
- Reduced-rate program-related investments that require repayment within a specified time frame
- Forgivable loans whose repayment can be waived upon certain conditions

The size, focus, and priorities of foundations range widely, as does their awareness of cooperative ownership. It is often useful to present the housing development or rehabilitation as a means to advance specific foundation priorities rather than presenting cooperative development as an end in itself. Such priorities might include: community and affordable housing development within a given locale; wealth creation or asset building through accumulated home equity for low-income families; community stabilization; and high-quality senior living.

### *Debt Financing*

Both developers/sponsors and existing cooperatives require debt financing. While no one likes to take on additional debt, there are times when it can be beneficial:

- When calculating the balance between an underlying mortgage and share loan, the developer/sponsor might find that raising the underlying mortgage and lowering share prices may make homeownership accessible to residents who might not have the down payment or financing for a larger share loan
- As compared to paying for repair/replacement costs up-front, borrowing can free up the cooperative's cash for other operating needs
- Bridging a long-term capital campaign with borrowed funds allows the capital project to be completed more quickly
- Repaying a loan encourages financial discipline and improves cash flow management
- Establishing a positive lending relationship may lead to additional resources, including access to working capital lines of credit for short-term cash flow needs or more flexible loan requirements for future capital improvement projects.

## Do You Have the Right Stuff? What Lenders Look For

When assessing a loan application, lenders typically review the following: credit, cash flow, capacity, collateral, and competition. These are used in one form or another to measure risk of default by the cooperative for any potential loan, the risk the loan will not be repaid, or the risk that the agreement will be breeched. Different organizations and people will interpret them in different ways, but all lenders will likely have similar questions about the developer/sponsor or cooperative and any future plans. This chart can help you look at your proposed cooperative and be prepared to discuss your strengths and weaknesses as a borrower.

### Credit

- What are the developer and cooperative's track records, if any, with other creditors such as banks, credit unions, and vendors?
- Do the financial statements of the borrower and developer indicate positive net assets? Do they have an audit without any comments?
- What is the borrower's previous experience or proposed plan for managing debt?

### Cash Flow/Operating Income

- What will be the primary source of repayment, such as the proposed division between blanket and share loans?
- Based on the proposed common charges, budget and financial projections, will there be adequate cash flow available for debt repayment?
- How much debt can the cooperative repay, given its projected common charges and expenses?
- If the building does not become a cooperative or if the cooperative corporation defaults, what would be the operating income of the building as a rental property?

### Capacity

- Does the sponsor/developer have experience in developing other affordable housing projects, and in particularly affordable homeownership projects?
- What type of oversight or technical assistance is currently being provided to help the cooperative? Are there new or additional plans for the future?
- Who will be the developer/sponsor's key managers or board members? What real life experience do they bring to their roles? What is their commitment to the success of the cooperative?
- What other projects will the developer/sponsor be undertaking in the next couple of years? Does the developer/sponsor have the staffing/financial capacity to take on these projects?
- What is the cooperative's proposed governance structure, such as the board of directors and shareholder/tenant involvement?
- What is the developer/sponsor's plan for managing the proposed development project?
- Does the developer/sponsor have the capacity to manage the development process? If not, who will be hired and what is their previous experience?

### Collateral

- In the event of a loan default, is there adequate security or guarantee in the real estate to repay the loan? What is the fair market value of the property now? What will the value be upon completion of the development? What would the value be as a rental property should the market become less favorable for ownership?
- Are there any obstacles to properly perfecting the lender's security interest?

### Competition

- What competing housing options are there in the geographic area?
- Has the developer/sponsor shown that there is a local market for cooperative housing, with the blend of share loan/occupancy charges they project?
- What is the fair market value of other units in the building's location?
- Has the cooperative undertaken an evaluation or market analysis to assure it can fill the units within a reasonable period of time?

## The Fear Factor: The Role of Risk in Receiving Loans

When approaching an organization for a loan, remember that lenders are risk averse. Every lender's primary objective is to make sure that the loan will be repaid as agreed. Depending upon the type of financing sought by the developer/sponsor or cooperative, risk will be evaluated differently. Below are some risks that lenders consider.

| RISK | INDICATORS | WAYS TO MITIGATE RISK |
|---|---|---|
| Organizational Risk | Limited development track record.In the case of conversion, limited experience of residents in building management. | • Partner with experienced developer or hire consultants<br>• Active tenant association formed to prepare for co-op conversion<br>• Contract for professional management |
| Construction Risk | The developer/sponsor or cooperative board lacks real estate development experience. | • Hire an experienced project manager and/or architect<br>• Provide a detailed project budget with well-researched cost estimates and ample contingency |
| Repayment Risk<br>*(ability to repay the loan from cash flow without considering collateral)* | Cash flow at the early stages of loan repayment may be inadequate to cover payments. This may be caused by unit sales not matching projections, resulting in decreased revenues and initial operating losses. | • Demonstrate waiting lists for residents wanting units or pre-sell units<br>• Show detailed cash flow projections under multiple scenarios (worst case, best case) sometimes called: "Debt Service Coverage Ratio"<br>• Show adequate reserves to offset any cash flow shortfall until enough units are filled to generate sufficient cash flow. |
| Collateral Risk | In the case of a payment default, can the property be sold for enough money to repay the loan in full? | • Demonstrate the value of the property through an appraisal by a certified appraiser, approved by the lender.<br>• Make an equity contribution to the project, if possible, to reduce the loan balance versus the value of the property (sometimes called "loan to value ratio").<br>• Design the construction / renovation so the property could be converted to a different use should the cooperative fail.<br>• Provide information about how the property could be used for other purposes, including rental housing. Include a pro forma indicating viability as a rental building.<br>• Describe a property management plan and reserve funds to be set aside for maintenance and repairs to maintain the property's value. |

## Loan Fees Demystified

Be prepared to pay several types of loan fees and remember to budget for these costs associated with the loan process. Because one lender's fees might be substantially higher than another's, it is best to check with more than one potential lender. A list of common costs follow:

- **Application or Underwriting Fee –** Lenders may charge a fee that must accompany the original loan application package and covers the upfront work lending institutions complete before a loan is funded. This normally ranges from $500 to $5,000 and may be credited toward the commitment fee if the loan is approved.
- **Commitment Fee –** Sometimes called an "origination fee," it covers the cost of the lender reviewing and approving the loan request. The fee is typically 1 to 2 percent of the loan amount. For example a 1 percent commitment fee on a $500,000 loan would be $5,000. This may be negotiable based on the overall strength of the credit application. Normally this fee is non-refundable even if the loan never closes.
- **Appraisal Fee –** The lender will require an appraisal to obtain the fair market value of the real estate offered as collateral. The appraisal is usually ordered once a commitment has been issued. The cost can range from $2,000 to over $10,000 based on the complexity of the project. The applicant pays for the appraisal when it is ordered and the fee is non-refundable, even if the loan never closes.
- **Environmental Assessment Fee –** The lender will order an environmental assessment to ensure there are no outstanding issues either with contaminants in the land or in any structures on the property. The cost can be as little as $1,000 for a basic assessment when there is no concern or apparent issues. This can increase to a range of $5,000 to well over $20,000 for Phase 1 and Phase 2 studies when issues are uncovered. These costs are paid by the borrower prior to closing and are not refundable even if the loan does not close.
- **Legal Fees and Closing Costs –** Lenders charge for the preparation of legal documents and other costs of executing the loan. Be sure to ask about them at the beginning of the application process. These fees will vary depending on the complexity of the deal (multiple properties or property owners, for example) and the time spent negotiating loan terms and the related legal documents. Borrowers normally pay for their legal costs and for those of the lender. A deposit for these fees is usually collected at the time of commitment and is typically not refundable, even if the loan never closes.
- **Interest Reserve –** During the construction period, an account is established to pay the estimated interest costs during the construction of the building. Since the borrower is only charged interest on the amount of funds disbursed, an estimate of the average disbursed amount is made.
- **Bank Engineer –** The borrower normally pays the bank's costs to hire an engineer to review the drawings and specifications, and to have an engineer or construction supervisor review invoices and work completed during construction.

### *Loan Application Process*

All loans have four elements that may be used when comparing terms from lenders: interest rate, fees, term, and amortization. Lenders suggest beginning the loan process once a site is under consideration and the developer knows what resources can be committed. The process that begins during the site selection phase will continue through development and throughout the life of the loan.

The following steps will guide you through the loan application process:

1. *Be prepared.* Compile details about your project before you call the lender:
    - Summary of experience of the developer/sponsor and business plan detailing the current state of the cooperative and any future plans.
    - Details of the real estate development project including purchase and sale agreements, realtor listings, real estate appraisals, and environmental studies (although lenders may order their own appraisals or studies instead of accepting those already done). Indicate whether the project meets current zoning and, if not, the process for obtaining zoning.
    - Preliminary plans for the site, schematic drawings, and capital improvement plans
    - Proposed prices for share/ownership and evidence that there is a market for these units.
    - Preliminary sources and uses of funds to complete the project.
    - Audited financial statements or federal income tax returns for the past three years (if applicable).
    - An interim financial statement, if possible.
    - Minimum three years of monthly and annual budget projections, including any impact from the construction/renovation project.

2. *Schedule an appointment* to meet with the lender to discuss the project. A lending institution's internal process will involve an initial review of your detailed information. There are three possible responses at this point: not interested, need more information, or interested.

3. An interested lender will usually issue a *term sheet or letter of intent.* This document is non-binding, meaning the institution is expressing an interest but not a legal commitment to lend money. This document will outline loan terms and conditions similar to those listed below:
    - Loan amount;
    - Use of loan proceeds (usually limited to specific items);
    - Length of loan and amortization;
    - Interest rate that may be fixed or variable (based on some type of index); sometimes the lender will offer a choice;
    - Fees for underwriting, application, commitment, and legal;
    - Loan pre-payment penalties, if any;
    - Collateral for the proposed loan and how it will be secured;
    - Maximum loan-to-value (LTV) ratio allowed, which is usually based on the current or as-completed appraised value (both as cooperative housing and often as rental fallback);
    - Reporting requirements for the submission of financial statements, rent rolls, etc.;
    - Financial covenants (i.e., promises that the borrower will meet certain financial benchmarks in its operations) for indicators of financial condition such as debt service coverage ratio and liquidity ratio;
    - Conditions to be met prior to closing, such as revised project costs, unit occupation benchmarks, and letters of commitment from additional sources of funds (i.e. grants);

- Specific date for accepting the offer to proceed with the underwriting process (this is acknowledged by returning a signed copy of the letter of intent to the lender).

It is important to read the letter carefully as it contains details of what the lender expects. Approach your lender with questions and be aware that some items, like fees, may be negotiable.

4. Some lenders will require a *completed loan application form* that they will provide you. Submit this form along with any additional information requested. This will all be used in the underwriting or "due diligence" performed by the lender.

5. Maintain regular communication with the lender during this process. It is important to promptly provide additional information as it becomes available, such as the following items:
   - Finalized project budget
   - Purchase, lease, or other official site contracts
   - Final architectural drawings
   - Contract with developer/general contractor
   - Zoning variances or approvals
   - Letters of commitment from other funders
   - Permits

Upon completion of due diligence, the lender will write a loan approval memo that remains an internal document not released to the applicant. The loan approval memo includes an overview of the proposed development project, the cooperative, management structure, financial analysis, and credit risks.

6. Once the approval process is successfully completed, your lender should issue a *commitment letter*. All of a loan's costs – indeed all of its terms – are potentially negotiable with the lender. This is especially true if you have more than one lender interested in providing financing. Use a financing worksheet to compare sources of financing, their terms, and conditions.

## What the commitment letter means...

The receipt of a commitment letter will allow you to officially commit to your development project and finalize the contract to purchase and with your contractor. This letter is more specific than the letter of intent, and is a legal commitment by the lender to make a loan under the conditions specified. A signed copy of this letter will be returned to the bank along with a check for any required commitment fee and upfront expenses for appraisals, environmental studies and preliminary legal work related to the loan closing. As these fees are generally not refundable, it is important to be relatively confident that the project will proceed before signing the commitment letter and paying the fees.

A worksheet for comparing sources of financing can be found in the Appendix G.

7. Once you've signed the commitment letter the actual *loan closing* is typically 30 to 90 days away. Lenders will now begin work on legal documents and complete their due diligence process on the appraisal, environmental report, title, and lien searches. Your project may have other specific items to be completed before closing, such as building permits or enrollment targets.

Prior to closing you should request draft legal documents to review, which usually include a promissory note, mortgage or deed of trust, loan agreement, and a security agreement. The lender will hire a lawyer to represent it and coordinate the loan closing. The cooperative should also hire an attorney to represent the corporation through the closing process. The closing date is typically scheduled about a week ahead of time. At closing, the lender and borrowers will sign the legal documents and transfer funds for all fees and equity contributions.

## The Paper Trail

*Summary of Support Documents Required for Construction Lending*

This list is provided for illustration purposes only and pertains only to the construction-specific aspect of the transaction. Information about the property might include:

LENDER-PROCURED DUE DILIGENCE (LENDER MUST APPROVE SOURCE):

- Phase I Environmental Report
- Appraisal Report - "as is" and "as built"
- Building Evaluation regarding existing structure(s) if any property condition assessment
- Building Inspection Report

OWNER SUBMITS:

- Market Study
- Complete Sources and Uses Schedule that outlines each source and use of funds
- Scope of Work Summary
- Development Budget, with subtotals for hard and soft cost items, and a separate line item for contingency, with an industry standard around 10 percent contingent reserve for the hard costs and 5 percent contingent reserve for soft costs
- Overall project timeline, including at least the following project benchmarks:
    - 50 percent construction completion
    - certificate of occupancy
    - marketing start
    - homeownership counseling
    - cooperative training start
    - timeline for sales
- Summary description of ownership and history of ownership
- Summary of the development team with resumes, describing the relevant experience of the borrower, architect, attorney, general contractor, and project manager, with additional details:
    - **Architect** - qualification statements, list of current and completed projects, evidence of insurance (professional liability), and financial statements for the past three years
    - **General Contractor** - qualification statements, list of projects, evidence of insurance (general liability and worker's compensation), financial statements for the past three years, and type of lien waivers used
- Construction Schedule - illustrating stages of construction, prepared by general contractor or architect
- Draw Schedule - amounts to be funded with dates and type of work to be done
- Title Insurance
- Final plans and specifications
- Executed agreement between owner and general contractor
- Performance bond of general contractor
- Lists of subcontractors
- Insurance:
    - Flood (if applicable)
    - Builder's risk
    - General liability – third party
    - Worker's compensation insurance
- Executed Agreement between owner and architect
- Soil report (if applicable) – In new construction, the soil must adequately support the proposed improvements.
- Utility available letter
- Permits
- If other funding is not closing at the same time, letters of commitment from other funders

## LOAN SOURCES

### *Traditional Banks/Conventional Lenders*

Most cooperatives are financed using some degree of blanket debt obtained from or through a conventional lender. Blanket loans for the co-op corporation are often bigger than individual share loans taken out by the resident owners. Share loans, when compared to blanket loans, may need a different funding source due to their relative size. Where share ownership prices are reasonably substantial (for example $20,000 or more), share lending – like blanket lending – usually starts with conventional banks. Where share ownership prices are very low, for example below $20,000, share financing can be harder. Conventional lenders typically cannot afford, or choose not to make, very small loans. The cost of processing a small share loan is generally the same as the cost of processing a large loan, while the interest and fees generated by the small loan are rarely substantial enough to cover its processing cost. Therefore, some other sources of funding for small-sized share loans can include:

- Co-op corporation makes loans from its own reserve funds
- Co-op corporation pools the reserve funds of several local cooperatives
- Sponsor loans
- Local community loan funds
- Credit unions
- Owner savings programs created by sponsors and developers (these programs have been used effectively during lengthy development periods to allow subscribers time to put money aside to accumulate some or the entire purchase price)
- Individual Development Accounts (IDA) available through banks, employers, nonprofit homeownership counseling agencies, and other sources can provide matching funds. In Atlanta, the local United Way launched a successful IDA to encourage savings for home purchases. Programs that write down purchase prices and/or closing costs (for example, FHLBank Affordable Housing Program and HomeFirst programs, HOME, and Community Development Block Grant pass-through programs) can be used to lower or eliminate share costs to incoming cooperative owners.

### Three Reasons to Look to Community Development Lenders

Community development lenders are an excellent resource for debt financing for cooperatives:

1. Many community development lenders have knowledge of the market and a dedicated interest in affordable housing that is backed by committed loan pools for this purpose.
2. Community development lenders can be considered "flexible" sources of financing. They can structure a loan with a longer amortization schedule, higher loan-to-value ratio, or an interest-only period. They also frequently accept non-traditional forms of collateral and real estate located in economically distressed areas. CDLs are typically structured to take higher risk loans than conventional banks.
3. Some CDLs may offer lower interest rates and simply make available financing that would otherwise not exist.

Beyond these differences, borrowing from a community development lender is much like borrowing from a conventional bank, including the loan closing documentation and process.

### *Community Development Lenders (CDLs)*

CDLs are specialized financial institutions that provide a wide range of services and technical assistance, usually targeted to low-income households and businesses located in distressed communities. Some CDLs are called Community Development Financial Institutions (CDFIs) or Community Development Credit Unions (CDCUs). Generally, government or foundation seed money is invested in the CDFI/CDCU/loan fund to support its mission and to generate additional private investment. Such lenders usually work in market niches that are underserved by traditional financial institutions. Community development lenders have successfully broken down credit barriers, and demonstrated the creditworthiness of community-based businesses to investors.

### *Government-Related Public Investment*

Local, state, and federal programs can provide financing in the form of loans, mortgage subsidies, soft second loans, tax credits, and other funding to ease the cost of developing a cooperative. Many government programs, mortgage subsidies, and other financing support are funneled through the cooperative's lender. Although such funds are usually accessed through community development lenders, some are available directly through government agencies or in the form of tax credits.

While cooperative share lending is eligible under many federal programs, awareness of cooperative ownership varies greatly. It may take some work by local cooperatives and their lenders to move local programs from legal/theoretical eligibility to actuality. Programs that write down purchase prices and/or closing costs (for example, some FHLBank Affordable Housing Programs and HOME or Community Development Block Grant pass-through programs) can reduce or even virtually eliminate small share costs to incoming cooperative owners.

As a preview, the chart below outlines federal programs available to co-ops.

## Summary of Federal Housing Programs

| PROGRAM | AGENCY | DESCRIPTION |
|---|---|---|
| Section 515 | USDA | Rural rental housing program that can be used to finance co-op housing. |
| Housing Choice Vouchers (formerly Section 8) | HUD | Supplements the amount that households pay towards total monthly housing costs. While considered a rental subsidy, it can be used to cover monthly carrying charges. Housing Choice Vouchers funds may be used for homeownership if the local Housing Authority creates such a program. |
| Section 202 | HUD | Subsidies for elderly housing. Can be used for co-ops. |
| Section 811 | HUD | Subsidies for supportive housing for persons with disabilities. Can be used for co-ops. |
| CDBG | HUD | Provides Federal funds to local governments. Local governments determine how to best use the funds to create affordable housing. |
| HOME Funds | HUD | Same as CDBG. |
| FHA Section 213 | HUD | If used, could provide 40-year fixed-rate, federally insured co-op blanket loans. |
| Rural Housing and Economic Development | HUD | Grant for improving distressed rural areas. Can be used to build affordable cooperatives or to create revolving loan fund for underlying or share loans. |
| Brownfield Economic Development Initiative (BEDI) | HUD, though City or State must be the applicant | Grant to make a Section 108 loan (a loan guaranteed by CDBG funding) viable, when used in conjunction with cleaning a Brownfield site, including for affordable housing. |

Many of these programs – HOME, CDBG, Housing Choice Vouchers – are administered by state housing finance agencies, local public housing authorities, and/or city/county community development departments. These agencies have substantial discretion in administering these programs and typically have lengthy application and review processes. Most have specific request for proposal (RFP) processes (often with annual deadlines when proposals can be submitted) that can be found on their websites. When the funding can be used differs from program to program, with some city and state agencies funding projects as early as at-risk pre-development costs, and others not funding until the low-income household purchases the unit.

That's why it is important to learn how these funds are administered in your locality and state during the Project Concept stage, and to contact the agencies to begin discussion. Most of these governmental entities are interested in ideas that promote affordable housing and typically have extensive experience in affordable housing (if not cooperative housing) development that can be useful. Contact your local community development agency, state housing finance agency, local housing authority, and/or local HUD (or USDA in rural areas) to ask them about their financing programs and get their ideas and perspective on your project.

### *Affordable Housing Trust Funds*

These are agencies of state and local governments that provide money to developers and affordable housing programs. A majority of states and large cities have housing trust funds. Most trust fund money is disbursed through requests for proposals and can take the form of no-interest loans, forgivable loans, below-market loans, and grants. Policies and objectives vary considerably from fund to fund. The trust funds target low-income households, typically those who earn less than 80 percent of the area median income in a given area. The units can be either single or multifamily and either for purchase or rent, depending upon the policies and objectives of the particular fund. Awareness of cooperative ownership can vary greatly from fund to fund. While policies will vary by location, in most cities funding will not be provided directly to the homebuyer or cooperative share purchaser.

### *United States Department of Housing and Urban Development (HUD) and the United States Department of Agriculture (USDA)*

Both HUD and USDA administer a number of programs, including the Federal Housing Administration's (FHA's) mortgage insurance programs. The programs can be used to enhance the affordability of cooperative housing.

### *Housing Choice Vouchers Assistance Program*

HUD specifically administers the Housing Choice Vouchers (HCV) Program, formerly Section 8 Assistance Program, that supplements the amount an individual household can afford to pay to cover their monthly housing costs. HUD administers contract renewals and a limited number of new project-based housing contracts. These contracts are tied to dwelling units within specific affordable housing projects. Through local public housing authorities, HUD distributes HCVs to individuals and families to use in housing of their own choice. While HCV is considered a rental subsidy, it can also be used very effectively in a cooperative to cover monthly occupancy charges. HCV funds may be used for homeownership more broadly through down-payment assistance and mortgage assistance. Section 202 provides subsidies for elderly housing and section 811 provides supportive housing for persons with disabilities.

### *Equity through Federal Tax Credits*

There are several federal tax credit programs that can provide a source for equity in very specific circumstances. All of the tax credit programs are quite complicated and require a developer/sponsor to consult a tax credit specialist in order to pursue these funding opportunities. The Low Income Housing Tax Credit (LIHTC) program is the primary federal program for producing low-income housing. Investors who provide equity for affordable housing can get credits to diminish their income tax obligations. Tax credits are allocated by state housing finance agencies (HFAs) within certain parameters. To access this benefit, a for-profit partnership or limited liability company must own the property. The LIHTC program can be used to create leasehold cooperatives in which the owner leases the property to a cooperative corporation. The compliance requirements of the LIHTC program severely limit the degree of control a cooperative can exercise during the minimum 15-year compliance period, but can create an effective opportunity for the cooperative to purchase the property at the period's end.

*Reduced Interest Through Tax-exempt Bonds*

In addition to allocating LIHTCs, state HFAs allocate tax-exempt mortgage revenue bonds to finance affordable housing. Blanket mortgages to cooperatives meeting the definition of "limited-equity" are eligible for funding under the tax-exempt bond rental program. Share loans to individuals and families are eligible for share-loans funded under the single-family program. However, many HFAs are completely unfamiliar with cooperatives and with their eligibility under these programs. Additional discussion with the HFA may be required in many states.

In addition to governmental issuance of tax-exempt bonds, certain charitable organizations that meet the requirements for a tax-exempt non-profit organization may issue them. While a few traditional cooperatives have qualified for 501(c)(3) status, generally that status is available only to variants of the basic cooperative ownership structure, such as mutual housing associations and resident-managed non-profit housing.

Both sources of tax-exempt bond funding allow for lower interest rates than are available from conventional lenders. However, tax-exempt bond financing is complex. It involves higher fees and closing costs to cover the higher transaction costs of bond issuance. The higher costs of conventional financing may outweigh the advantages of the lower interest rate of tax-exempt financing unless the amount to be financed is substantial. Because of the complexity, if you wish to pursue tax-exempt bond financing, you should add a specialist in tax-exempt bond financing to your development team.

## Conclusion: The Bottom of the Ninth

With increasing housing costs and other price pressures, the need for affordable housing is more critical than ever. The challenge remains for policymakers, lenders, developers, and consumers to build a road to homeownership together, applying creative and effective measures. Developers and tenants' groups can play an especially important role in increasing the supply of affordable units and avoiding displacement by considering cooperative housing as an option. In doing this, perhaps everyone can reach home base.

The following appendices include examples of templates, such as loan documents, bylaws, and financing worksheets. In addition, a bibliography and supplemental resources list provide sources for further research on particular subject areas. We invite you to return to our website at www.ncbcapitalimpact.org as we periodically post additional information that will supplement this manual.

# Appendices

A: AN OVERVIEW OF COOPERATIVE DOCUMENTS

B: AZTEC AGREEMENT EXAMPLE

C: STATEMENT OF SOURCES AND USES

D: SAMPLE DEVELOPMENT BUDGET

E: SAMPLE SALES PRICES ANALYSIS

F: SAMPLE MAINTENANCE & OPERATING BUDGET

G: FINANCING COMPARISION WORKSHEET

H: REFERENCES AND INFORMATION RESOURCES

# APPENDIX A: AN OVERVIEW OF COOPERATIVE DOCUMENTS

***This appendix gives an overview of several legal documents used to help establish the cooperative.***

NOTE: *Items in italics are applicable only to limited equity and/or government-related cooperatives.*

| DOCUMENT | PURPOSE | EFFECTS |
|---|---|---|
| Articles of Incorporation | Establishes the existence of the cooperative. | 1. Makes the organization (not the individual members) the operating entity.<br>2. Limits the purpose for which the organization can act.<br>3. Defines the basic structure of the cooperative. |
| Bylaws | Regulates the internal workings of the cooperative. | 1. Defines membership in terms of eligibility, rights, terminations, and transfers.<br>2. Defines powers, operations, and officers of the Board of Directors.<br>3. Provides for annual meeting of owners and elections of directors.<br>4. Establishes maximum transfer value.<br>5. *All of the above are made secondary to the Regulatory Agreement.* |
| Subscription Agreement (designed to operate during start-up period) | Creates a conditional agreement to purchase and sell a membership. | Gives prospective members a limited right to buy a co-ownership from the cooperative in exchange for a down payment that secures the cooperative against default. |
| *Regulatory Agreement* | *Controls the operations of the cooperative so that they meet the purposes of the government program under which the cooperative was financed/ insured/subsidized.* | *1. Restricts the (initial) membership of the cooperative to members of the target population.*<br>*2. Regulates the price of membership resales, as well as requiring resale to the target population.*<br>*3. Regulates the financial operations of the cooperative (occupancy charges, reserves, contracts, borrowing, investments).*<br>*4. Regulates the maintenance and repair of the structures and grounds.*<br>*5. Provides for any waiting list procedures for future residents.*<br>*6. Provides a way for enforcement of rules.* |
| Recognition Agreement | Sets forth obligations of share lender, blanket lender, and cooperative. | 1. Cooperative guarantees the truth of certain statements regarding the status of the cooperative as owner of the real estate, and the borrower as a member of the cooperative.<br>2. Cooperative consents to co-owner's pledge of cooperative interest (co-ownership certificate plus occupancy agreement) as security for loan.<br>3. Cooperative agrees to notify lender of any threat to the borrower's status as a co-owner in good standing of the cooperative or of any impairment in the cooperative's financial status.<br>4. Gives lender rights to cure or 'forgive' certain defaults by a co-owner or by cooperative.<br>5. Requires cooperative to terminate co-ownership if borrower defaults on share loan obligations.<br>6. Sets out priorities between cooperative, lender, and borrower upon foreclosure and resale of borrower's cooperative interest. |

# APPENDIX B: AZTEC AGREEMENT EXAMPLE

*This is an example of a type of recognition agreement, called an Aztec Agreement, between a share lender and the cooperative. It recognizes that the cooperative and the share lender have potentially competing interests if the share owner defaults on the loan, because the defaulting share owner has responsibilities to both the cooperative and the share lender. Note: This form is not intended for use if the Proprietary Lease already has financing provisions or "requirements" which duplicate much of this agreement or differ significantly with this agreement.*

Premises:___________________

Apartment:__________________

Gentlemen:

We have been asked by_________________ ("Lessee") for a loan of $____________to be secured by a pledge, security interest, mortgage and/or assignment (hereinafter sometimes collectively referred to as "the Security") of shares of your Corporation allocated to the above Apartment and of the Proprietary Lease (the "Lease") appurtenant thereto (the shares and Lease collectively referred to as "the Apartment").

1. (a) You are a ______________corporation formed for the purpose of cooperative ownership and (owner
in fee / ground tenant) of the above premises.

(b) Your records show that the Lessee is the owner of the Apartment.

(c) You have duly approved or consented to the creation by the Lessee of the Security, if and to the extent such approval is required by the Lease.

2. (a) You will not consent to any further encumbrances, subletting, termination, cancellation, surrender or modification of the Apartment by the Lessee without our approval, which we will not unreasonably withhold but this provision shall not apply to any modification or termination which, by the terms of the Lease, may be effective against a Lessee when approved by a fixed percentage of other holders of your shares, or which may be effective in the event of condemnation or casualty.

(b) The Lessee has agreed that, without our written approval, the Lessee will not exercise any right that he may have under the lease to terminate the lease so long as the loan is outstanding.

(c) You will notify us of any notice of intention to terminate the Lease, and

(1) If the Lessee's default can be cured by the payment of money, you will also notify us promptly of any default involving an amount equal to or exceeding three months maintenance payments and will take no action to terminate the Lease or cancel the shares if the default be cured either by us for the account of the Lessee or by the Lessee within 15 days after such notice of default or intention to terminate; or

(2) If the default cannot be so cured, you will institute no action to terminate the Lease or cancel the shares until we have had reasonable notice and opportunity, by action or otherwise, to induce the Lessee to cure the default, such opportunity to be no less than the time provided in the Lease for the Lessee to cure.

(3) If you shall terminate the Lease and cancel the shares for a default not curable by the payment of money, then, provided we pay you the amounts which are due to you under the Lease (including its deficiency clause) when due, you shall not sell or sublet the apartment without our approval, unless the net proceeds of such sale or subletting shall equal or exceed the amount owning to us by Lessee.

(d) You will accept payment from us on behalf of Lessee of any sums due under the Lease (including its deficiency clause), any payments made by us under the terms of this agreement will be deemed so paid, and no payments made in accordance herewith shall be deemed to limit our rights against the Lessee pursuant to law.

(e) You shall recognize our right as lienor against the Apartment pursuant to the Security, and, if the Lease be terminated and/or shares cancelled, against the net proceeds of any sale or subletting of the apartment, after reimbursement to you of all sums due you under the Lease.

3. (a) Before delivery of this letter by you to us, we will have authority from the Lessee to give, and will, on request, give you a copy of the financial and credit information provided by him, but shall be under no duty to advise you of the results of any credit check we may make.

(b) Notwithstanding any apparent authority granted to us under agreements with the Lessee, WE SHALL HAVE NO RIGHT OR POWER TO TRANSFER THE APARTMENT UPON FORECLOSURE OR OTHERWISE EITHER TO US OR ANYONE ELSE WITHOUT YOUR APPROVAL AS REQUIRED BY THE LEASE provided, however, that nothing contained herein shall limit any rights we may have to dispossess the Lessee pursuant to law or realize upon our security in accordance herewith.

(c) If through oversight or negligence you or your agents or employees shall fail to notify us of Lessee's default prior to termination of the Lease, we will not seek to hold you or your agents or employees liable for breach of this agreement, provided that:

(1) you advise us promptly after discovering your failure, and

(2) if you have already sold or contracted to sell the Apartment, that you pay us the net proceeds of such sale (after reimbursing yourselves for all sums due you), or such lesser sum as shall equal the amount owing to us by the Lessee (the balance being payable to the Lessee) , or

(3) if you have not contracted to sell the Apartment, that the provisions of paragraphs 2(c)(3) and 2(e) hereof shall apply.

(d) We will indemnify you and your agent against loss, liability or expense incurred in connection with any claim by the Lessee, his successors or assigns against either of you arising out of our representations pursuant hereto or your agreements herein (except as stated in paragraph 3(a) hereof), provided you give us prompt notice of any such claim.

We may contest such claim in your name and on your behalf, but at our sole cost and expense, and you will execute such documents and do such things as are reasonably necessary to assist us in such contest.

4. While we have the right but no obligation to cure the Lessee's defaults under the Lease, if we do not do so within the time provided for herein, you shall have no obligation to us, except that in the event of sale or subletting the Apartment, you shall recognize our rights as lienor against the net proceeds of any sale or subletting (after reimbursement to you of all sums which are due to you under the Lease).
Any notice of approval provided for herein shall be deemed valid only if in writing and sent you registered or certified mail, as follows: to you, in care of your Managing Agent, with a copy by regular mail addressed
to________________________________________
at________________________________________;
to us at______________________________________.

Either of us may change the address to which notices or approval shall be mailed by notice given as herein
provided. This letter and the representations and agreements contained herein shall be deemed made as of the date of the making of the loan.

__________________________ Bank

By:__________________________

Agreed to:

__________________________
Lessor

By:__________________________

Approved:

__________________________
Lessee

__________________________
Lessee

# APPENDIX C: STATEMENT OF SOURCES AND USES

*Example Project*

| | Per unit | Entire Project | Percentage |
|---|---|---|---|
| **CONSTRUCTION SOURCES** | | | |
| Construction Loan | $175,519 | $5,967,634 | 64.64% |
| Second Mortgage | $47,059 | $1,600,000 | 17.33% |
| Third Mortgage | $11,765 | $400,000 | 4.33% |
| Developer Equity | $13,576 | $461,577 | 5.00% |
| Deferred Developer's Fee | $23,598 | $802,321 | 8.69% |
| TOTAL SOURCES | $271,516 | $9,231,531 | 100.00% |
| **PERMANENT SOURCES** | | | |
| Gross Sale Proceeds | $196,596 | $6,684,260 | 72.41% |
| Bank Blanket/Underlying Mortgage | $16,096 | $547,272 | 5.93% |
| Second Mortgage | $47,059 | $1,600,000 | 17.33% |
| Third Mortgage | $11,765 | $400,000 | 4.33% |
| Surplus | $0 | $0 | 0.00% |
| TOTAL SOURCES | $271,516 | $9,231,531 | 100.00% |
| **USES** | | | |
| Acquisition Costs | $11,941 | $406,000 | 4.40% |
| Construction Costs | $185,294 | $6,300,000 | 68.24% |
| Soft Costs | $13,300 | $452,200 | 4.90% |
| Financing Fees | $6,418 | $218,203 | 2.36% |
| Carrying Costs | $30,965 | $1,052,807 | 11.40% |
| Developer's Fee | $23,598 | $802,321 | 8.69% |
| TOTAL USES | $271,516 | $9,231,531 | 100.00% |

Please note that Total Sources should always equal Total Uses

# APPENDIX D: SAMPLE DEVELOPMENT BUDGET

| | | | | | Square Feet: | 40,000 |
|---|---|---|---|---|---|---|
| **PROJECT NAME:** | **EXAMPLE PROJECT** | | | | $ per sq ft: | $150.00 |
| | | | | | Units: | 40 |
| Predevelopment Costs | | | | | | |
| Predevelopment Loan Interest | | | | | | |
| **LAND & BUILDING ACQUISITION COSTS:** | | | $400,000 | | | |
| City Transfer Tax | 1.00% | of acquisition | $4,000 | | | |
| State Transfer Tax | 0.50% | of acquisition | $2,000 | | | |
| **SUBTOTAL:** | | | **$406,000** | | | |
| | $10,150 | /dwelling unit (du) | | | | |
| **CONSTRUCTION COSTS:** | | | | | | |
| Contractor Price | $150,000 | /du | $6,000,000 | | | |
| General Conditions | | | $0 | | | |
| Contingency | 5% | of Contractor Price | $300,000 | | | |
| Other | | | $0 | | | |
| Other | | | $0 | | | |
| **SUBTOTAL:** | **$157,500** | **/DU** | **$6,300,000** | | | |
| **PROFESSIONAL FEES:** | | | | | | |
| Borrower Legal | | | $40,000 | | | |
| Co-op Plan Filing Fees | | | $20,000 | | | |
| Architect/Engineering Fees | 5% | of construction cost | $315,000 | | | |
| Accounting/Audit | | | $8,000 | | | |
| Property Tax Exemption Fee | | | $200 | | | |
| | | | $0 | | | |
| Environmental Phase I/Phase II | | | $8,000 | | | |
| Survey | | | $2,000 | | | |
| Borings | | | $4,000 | | | |
| Consultant | | | $10,000 | | | |
| Construction Manager | | | $20,000 | | | |
| Expeditor | | | $5,000 | | | |
| Homebuyer Preparation | $500 | /buyer | $20,000 | | | |
| **SUBTOTAL** | | | **$452,200** | | | |
| **FINANCING FEES:** | | | | | | |
| Construction loan fee | 1.00% | of construction loan | $59,676 | | | |
| Construction | | lender's | | | engineer | |
| & inspection fee | | | $25,000 | | | |
| Construction lender's legal fee | | | $20,000 | | | |
| Appraisal | | | $5,000 | | | |
| Market study | | | $5,000 | | | |
| Fee on soft loans/grants | 1.00% | of soft loans/grants | $20,000 | | | |
| Permanent loan fee | 1.00% | of permanent loan | $66,843 | | | |
| Permanent loan mortgage insurance | 0.10% | of permanent loan | $6,684 | | | |
| Financial advisor fee | | | $10,000 | | | |
| **SUBTOTAL** | | | **$218,203** | | | |

## APPENDIX D: SAMPLE DEVELOPMENT BUDGET *(continued)*

| PROJECT NAME: | EXAMPLE PROJECT | | | | |
|---|---|---|---|---|---|
| | | | | Square Feet: | 40,000 |
| | | | | $ per sq ft: | $150.00 |
| | | | | Units: | 40 |
| **CARRYING COSTS:** | | | | Months | Av. Balance |
| Construction Interest | 7.50% | (int. rate on loan) | $451,983 | 18 | 65% |
| Water & Sewer Tax | | | $10,000 | | |
| Real Estate Taxes | | | $10,000 | | |
| Utilities | | | $5,000 | | |
| Transfer Tax (developer to Coop) | 0.50% | combin. mortgage | $12,736 | | |
| Co-op Maintenance for Unsold Shares | $1,000 | /du | $40,000 | | |
| Insurance (Fire and Extended) | | | $90,000 | | |
| Marketing | $500 | /du | $20,000 | | |
| Sales Office Fee | 4.0% | sales | $267,370 | | |
| Capitalized Reserves | 1.0% | sales | $66,843 | | |
| Soft Cost Contingency | 5.0% | of soft costs | $78,875 | | |
| **SUBTOTAL** | | | **$1,052,807** | | |
| **TOTAL SOFT COSTS** | | | **$1,723,210** | | |
| Developer's Fee | 10.00% | | $802,321 | | |
| **TOTAL DEVELOPMENT COST:** | | | **$9,231,531** | | |
| **CONSTRUCTION SOURCES** | | | | Source | Interest Rate |
| Construction Loan | | | $5,967,634 | Bank | 7.50% |
| Second Mortgage | $40,000 | /du | $1,600,000 | HOME funds | 1.00% |
| Third Mortgage | $10,000 | /du | $400,000 | FHLB AHP* | 0.00% |
| Developer Equity | 5.0% | of total dev. cost | $461,577 | | |
| Deferred Developer's Fee | | | $802,321 | | |
| **TOTAL** | | | **$9,231,531** | | |
| **PERMANENT SOURCES** | | | | Source | Interest Rate |
| Gross Sale Proceeds | | | $6,684,260 | | |
| Bank Blanket/Underlying Mortgage | | | $547,272 | Bank | 7.50% |
| Second Mortgage | $40,000 | /du | $1,600,000 | HOME funds | 2.80% |
| Third Mortgage | $10,000 | /du | $400,000 | FHLB AHP* | 0.00% |
| ***Surplus*** | | | | | |
| **TOTAL** | | | **$9,231,531** | | |

**FHLB AHP = Federal Home Loan Bank Affordable Housing Program*

## APPENDIX E: SAMPLE SALES PRICE ANALYSIS

*Example Project*

| | |
|---|---|
| Area Median Income (AMI) | $70,900 |
| Interest Rate | 7.50% |
| Down Payment | 10% |
| Discount Factor* | 95% |

| | % Area Median Income Target | # of Units | Average Total Monthly Payment | Average Monthly Maintenance | Estimated Mortgage Payment | Estimated Mortgage Amount |
|---|---|---|---|---|---|---|
| Efficiency | 130% | 2 | $1,686 | $575.00 | $1,111 | $158,829 |
| Efficiency | 100% | 0 | $1,297 | $575.00 | $722 | $103,199 |
| Efficiency | 80% | 2 | $1,037 | $575.00 | $462 | $66,112 |
| One Bedroom | 130% | 7 | $1,806 | $650.00 | $1,156 | $165,322 |
| One Bedroom | 100% | 0 | $1,389 | $650.00 | $739 | $105,718 |
| One Bedroom | 80% | 3 | $1,111 | $650.00 | $461 | $65,982 |
| Two Bedroom | 165% | 0 | $2,751 | $800.00 | $1,951 | $278,972 |
| Two Bedroom | 130% | 20 | $2,167 | $800.00 | $1,367 | $195,526 |
| Two Bedroom | 100% | 0 | $1,667 | $800.00 | $867 | $124,001 |
| Two Bedroom | 80% | 4 | $1,334 | $800.00 | $534 | $76,318 |
| Three Bedroom | 130% | 2 | $2,480 | $925.00 | $1,555 | $222,418 |
| Three Bedroom | 100% | 0 | $1,908 | $925.00 | $983 | $140,562 |
| Three Bedroom | 80% | 0 | $1,526 | $925.00 | $601 | $85,991 |
| Total Residential Sales | | 40 | | | | |
| Parking Spaces | | | | | | |
| **TOTAL SALES** | | | | | | |
| Efficiency Rooms | 1.0 | 4 | | | | |
| One Bedroom Rooms | 3.0 | 30 | | | | |
| Two Bedroom Rooms | 4.0 | 96 | | | | |
| Three Bedroom Rooms | 5.0 | 10 | | | | |

| Down Payment Assistance | Cash Down Payment | Estimated Sales Price | Total Sales Price | Actual Income @ 33% | Actual Income's % of AMI | Common Charge |
|---|---|---|---|---|---|---|
| $0 | $17,648 | $176,477 | $352,954 | $61,293 | 124% | $1,150 |
| $0 | $11,467 | $114,666 | $0 | $47,149 | 95% | $0 |
| $0 | $7,346 | $73,458 | $146,916 | $37,719 | 76% | $1,150 |
| $0 | $18,369 | $183,691 | $1,285,838 | $65,671 | 124% | $4,550 |
| $0 | $11,746 | $117,465 | $0 | $50,516 | 95% | $0 |
| $0 | $7,331 | $73,314 | $219,941 | $40,413 | 76% | $1,950 |
| $0 | $30,997 | $309,968 | $0 | $100,022 | 157% | $0 |
| $0 | $21,725 | $217,251 | $4,345,025 | $78,805 | 124% | $16,000 |
| $0 | $13,778 | $137,779 | $0 | $60,620 | 95% | $0 |
| $0 | $8,480 | $84,798 | $339,193 | $48,496 | 76% | $3,200 |
| $0 | $24,713 | $247,131 | $494,262 | $90,188 | 124% | $1,850 |
| $0 | $15,618 | $156,180 | $0 | $69,376 | 95% | $0 |
| $0 | $9,555 | $95,546 | $0 | $55,501 | 76% | $0 |
| | | | $6,684,260 | | | $29,850 |
| | | | $0 | | | |
| | | | **$6,684,260** | | | |

*What is the discount factor? Funders often require that incomes of purchasers do not exceed a certain amount. As an example, assume the limit is 80% of area median income (AMI). Most applicants will not have incomes exactly at 80%, however, if they have incomes slightly above, then they are not eligible. When the maximum income is set at 80%, quaified applicants will have incomes between 70% and 80% of median - an average of about 95% of 80% of AMI. This is why a discount factor of 95% is used to calculate average monthly payment.

# APPENDIX F: SAMPLE MAINTENANCE & OPERATING BUDGET

***Example Project*** Rooms: 140

| | | |
|---|---|---|
| Residential Income | | $358,200 |
| Vacancy Rate | 5.0% | $17,910 |
| Net Rental Income | | $340,290 |

| EXPENSES | | ANNUAL BUDGET | PER rm/du | |
|---|---|---|---|---|
| Supplies/Cleaning/Exterminating | | $7,000 | $50 | /du |
| Heating | | $33,600 | $240 | /rm |
| Gas & Electricity | | $8,000 | $57 | /rm |
| Cooking Gas | | $0 | $0 | /du |
| Repairs/Replacement | | $16,000 | $400 | /du |
| Legal | | $2,500 | $63 | /du |
| Accounting | | $4,000 | $100 | /du |
| Painting | | $5,600 | $40 | /rm |
| Staff Fringe & Overhead | 25% | $13,000 | $325 | /du |
| Superintendent salaries | | $31,000 | $775 | /du |
| Porter salaries | | $21,000 | $150 | /du |
| Elevator Maintenance & Repairs | | $4,500 | $4,500 | /elev. |
| Management Fee | | $26,865 | 8% | of GI |
| Water & Sewer | | $17,500 | $125 | /rm |
| Fire and Liability Insurance | | $21,800 | $545 | /du |
| Other Expenses (Specify): | | $0 | $0 | /du |
| Marketing | | $1,000 | $25 | /du |
| Security | | $8,000 | $200 | /du |
| Landscaping | | $1,500 | $38 | /du |
| Franchise Taxes | | $2,000 | $50 | /du |
| **M & O Before Taxes and Debt Service** | | **$224,865** | **$5,622** | /du |
| Operating Reserve | 1.0% | $ 3,582 | $90 | /du |
| Bldg Reserve | | $10,000 | $250 | /du |
| Real estate taxes | | $1,200 | $30 | /du |
| **Total Expenses** | | **$239,647** | **$5,991** | /du |
| | | | $1,712 | /rm |

| | |
|---|---|
| Net Operating Income | $ 100,643 |
| First Mortgage | $48,531 |
| Second Mortgage | $44,800 |
| Third Mortgage | $0 |
| | |
| Cash Flow | $ 7,312 |
| Debt Service Coverage Ratio (1st) | 2.07 |
| Debt Service Coverage Ratio (TOTAL) | 1.08 |

# APPENDIX G: FINANCING COMPARISION WORKSHEET

*The following worksheet can be adapted to your cooperative's financing needs. Use it to compare sources of financing, as well as their terms and conditions.*

| | Financial Institution #1 | Financial Institution #2 | Financial Institution #3 |
|---|---|---|---|
| Name | ___________ | ___________ | ___________ |
| Loan Amount<br>*Equity required?* | ___________ | ___________ | ___________ |
| Term (in months or years) | ___________ | ___________ | ___________ |
| Amortization (in months or years) | ___________ | ___________ | ___________ |
| Balloon Payment | ___________ | ___________ | ___________ |
| Interest Rate<br>*Fixed or variable?* | ___________ | ___________ | ___________ |
| Collateral Required<br>*Mortgage/Assignment of Contracts/Leasehold* | ___________ | ___________ | ___________ |
| Application Deadline | ___________ | ___________ | ___________ |
| Application Fee | ___________ | ___________ | ___________ |
| Estimated time to approval/rejection | ___________ | ___________ | ___________ |
| Estimated time from approval to closing | ___________ | ___________ | ___________ |
| Origination Fees | ___________ | ___________ | ___________ |
| Legal Fees | ___________ | ___________ | ___________ |
| Other Closing Costs | ___________ | ___________ | ___________ |
| Prepayment Penalties (if any) | ___________ | ___________ | ___________ |
| Loan Disbursement Schedule<br>*When and how will you get the loan proceeds?* | ___________ | ___________ | ___________ |
| Billing Schedule<br>*How often will you be billed for loan payments?* | ___________ | ___________ | ___________ |
| Other Loan Conditions | ___________ | ___________ | ___________ |

## APPENDIX H: REFERENCES AND INFORMATION RESOURCES

| LOOKING FOR INFORMATION ABOUT… | HERE'S A RESOURCE… | HERE'S WHERE TO FIND IT… |
|---|---|---|
| ALTA surveys | Flatirons Surveying, Inc. | http://www.flatsurv.com/alta.htm |
| Architecture and design savings | Affordable Housing Design Advisor | http://www.designadvisor.org |
| Banking and financial services for economic development, focused on cooperatives and similar organizations | NCB | www.ncb.coop |
| CDFI program overview/explanation | Community Development Financing Institutions Fund | http://www.cdfifund.gov/overview/index.asp |
| CDFIs information and locator | Opportunity Finance Network (formerly National Community Capital) | http://www.communitycapital.org/financing/investing_in_cdfis.html |
| Charter schools | *The Answer Key Charter School Guide* (2005). Published by NCB Capital Impact. | http://www.ncbcapitalimpact.org/ |
| Community development finance | *Effective Strategies for Community Development Finance.* Published by the Office of the Comptroller of the Currency (OCC). | http://www.occ.treas.gov/cdd/strategy.pdf |
| Cooperative housing toolbox | *Cooperative Housing Toolbox: A Practical Guide for Cooperative Success* (2003). Published by the Northcountry Cooperative Development Fund. | http://ncdf.coop/Toolboxes.html |
| Cooperative membership organizations | National Association of Housing Cooperatives<br>National Cooperative Business Association | http://www.coophousing.org<br>http://www.ncba.coop/ |
| Enterprise Community Partners, Local Initiatives Support Group, NeighborWorks America | Consortium for Housing and Asset Management | www.cham.org |
| Federal Home Loan Bank region in which you live and the specific programs available from that FHLBank | Your local Federal Home Loan Bank | http://www.fhlbanks.com |
| Financing sustainable communities | Smart Communities Network | http://www.sustainable.doe.gov/financing/community.shtml |
| Grants | Foundation Center provides a searchable online directory of more than 70,000 grant makers and 150,000 grants for limited monthly fees. | http://fdncenter.org/ and http://fconline.fdncenter.org/ |
| Grants, loans, loan guarantees, services, information, scholarships, training, insurance | Catalog of Federal Domestic Assistance Programs (CFDA) – a government-wide compendium of 1,499 federal programs, projects, services, and activities that provide assistance or benefits to the American public | http://aspe.os.dhhs.gov/cfda/ (searchable index) |

## APPENDIX H: REFERENCES AND INFORMATION RESOURCES *(continued)*

| LOOKING FOR INFORMATION ABOUT… | HERE'S A RESOURCE… | HERE'S WHERE TO FIND IT… |
|---|---|---|
| Guide to building cooperative communities | *People Building Communities Guide* by Terry Lewis (2000). Published by the Cooperative Housing Information Center, Cooperative Housing | Coalition. www.housinginfo.coop |
| Guide to cooperative housing | *Cooperative Housing Guide* by Terry Lewis (2006). Published by the Cooperative Housing Information Center, Cooperative Housing Coalition. | http://www.housinginfo.coop/chc/chcinfo.nsf/guideoutline.htm |
| Home mortgage lending (HMDA) data | United States Federal Reserve | www.federalreserve.gov |
| Homeownership assistance resources and tools | Urban Homesteading Assistance Board | www.uhab.coop and www.uhab.org |
| Housing finance, development, and housing trust funds | Policy Link | http://www.policylink.org/EDTK/HTF/How.html |
| Limited equity condominiums and limited equity housing | We Own.net | http://www.weown.net |
| Manufactured housing cooperatives | *Management Guide for Manufactured Housing Cooperatives* (2003). Published by the New Hampshire Community Loan Fund. | www.nhclf.org |
| Mortgage insurance for cooperative housing (Section 213) | Federal Housing Administration Program Section 213 | http://www.hud.gov/offices/hsg/mfh/progdesc/coop213.cfm |
| One-stop resource for multi-family housing development | Department of Housing and Urban Development | multi-family home page http://www.hud.gov/groups/multifamily.cfm |
| On-line model documents and "best practices" in affordable housing development | Enterprise Community<br>Local Initiative Support Corporation (LISC) | www.enterprisecommunity.org<br>www.liscnet.org |
| Recognition agreements | Jon B. Felice & Associates Attorneys at Law | http://www.jbfelice.com/legal.html |
| Rural community technical assistance and financing for housing, community development, and infrastructure improvement | Rural Community Assistance Program (six regional affiliates) | http://www.rcap.org/ |
| Rural development technical assistance and financial programs | US Department of Agriculture Rural Development | http://www.rurdev.usda.gov/rd/index.html |
| Rural housing development | United States Department of Agriculture Rural Development | www.usda.gov |
| Terms and definitions | Wikipedia | http://en.wikipedia.org |
| Training | National Association of Housing Cooperatives | www.coophousing.org |

# Glossary

# A

**Affordable Housing Trust Funds** provide developers, local units of government, housing authorities, and other service providers the funds to address the needs of low-income households. Most housing trust funds derive their revenue from local real estate transfer taxes, document recordation fees, or developer fees. There are over 275 local housing trust funds nationwide that provide more than $750 million annually to create tens of thousands of affordable housing units.

**ALTA Survey** is a boundary survey prepared to a set of standards that have been prepared and adopted by the American Land Title Association and the American Congress on Surveying and Mapping. The ALTA Survey shows improvements, easements (which are defined rights to use the property in a particular way), and other elements impacting the ownership of land.

**Amortization** is the payment of an obligation in a series of equal installments. The amortization period is the length of time it would take for a loan to be paid off in equal periodic (usually monthly) payments. For any given loan amount, the longer the amortization period, the smaller the monthly payment. When the amortization period of a loan is longer than its loan term (the time within which the loan must be paid off), the loan will have a balloon payment. This is usually a single, substantial payment of the remaining principal balance due at the end of the loan term.

**Appraisal** is a professional judgment or assessment of a property's price or value.

**Area Median Income** is a measure of the middle-income level within a geographic region. The measure divides households into two equal segments, the first half of households earning less than the median household income and the other half earning more. It is often used to determine which households in a particular area are eligible for government subsidies to help them access rental or home ownership opportunities.

**Assessment** is a review of the rehabilitation needs and costs of a building. The physical needs assessment is done in order to determine how much money each resident must contribute toward the renovations.

**Aztec Agreement** is an industry standard type of recognition agreement, between a share lender and the cooperative. Share lenders require a recognition agreement as a condition of each share loan. The recognition agreement establishes the rights and obligations of the share lender, the cooperative corporation, and the share owner. It "recognizes" that the cooperative and the share lender have potentially competing interests in the event of a default by a share owner because the defaulting share owner's collateral is an ownership interest in the cooperative. A best practice for cooperatives is to negotiate with share lenders for a recognition agreement as close to the Aztec Agreement standard as possible.

# B

**Balloon Payment** is a single substantial payment of the remaining principal balance of the loan due at the end of the loan term. (See Amortization)

**Blanket Loan (Blanket Debt/Mortgage)** is usually the loan that finances the co-op corporation's ownership of its land and building(s). This can be used to pay for initial acquisition of the real estate, to refinance existing blanket debt, or to pay for major improvement and rehabilitation projects. Cooperative members are not individually liable to the blanket lender, nor do they need to individually qualify for the blanket loan. The cooperative's occupancy agreement obligates members to pay their proportionate share of the monthly blanket loan payment to the cooperative.

**Brownfield Sites** are locations where environmental cleanup is necessary to make the site safe for reuse.

# C

**Carrying Charges, Common Charges, or Occupancy Charges** are monthly payments made by members to the cooperative corporation for common expenses such as operating costs, blanket debt service, insurance, property taxes, and capital reserves. Carrying charges include the same sorts of expenses covered by condominium association fees plus the expenses individual condominium members pay directly, rather than through their association. In this manual, the term Occupancy Charges is used.

**Certificate of Occupancy** is a document issued by the government that gives individuals written authorization to move in to a newly completed or substantially completed building.

**Closing Costs** are expenses incurred by the purchaser or seller of a property in addition to the purchase price paid. These costs typically include fees and points paid to the buyer's lender, proration of prepaid expenses (e.g. taxes), funding of escrow accounts for property taxes and insurance, title insurance costs, transfer taxes, and recording fees. Many closing costs that usually accompany single-family home or condominium purchases are avoided when purchasing a cooperative membership.

**Closing** is the meeting at which the legal documents are signed to consummate a transaction and cause a property to change hands from buyer to seller.

**Collateral** is a form of security to the lender in case the borrower fails to pay back the loan.

**Community Development Block Grants (CDBG)** provide federal funds to local governments to enable them to craft affordable housing programs (within wide program parameters) to meet local needs. Federal HOME funds fuel first-time homebuyer programs.

**Community Development Finance Institutions (CDFIs)** are organizations that work to provide credit, capital, and financial services to underserved populations and communities in the United States.

## D

**Debt Service Coverage Ratio** is calculated by dividing net operating income by the total debt service (such as the loans or mortgages on the property). This ratio is used by lenders to verify that there will be enough operating income to cover annual payments due on debt, without having to liquidate the collateral.

**Due Diligence** is a process of checking carefully the accuracy of information gathered. For example, a bank's review of a loan application requires due diligence to assure they are lending to a borrower that will be able to repay the loan.

## E

**Enterprise Foundation** is a national non-profit intermediary that works with non-profit groups in a variety of locales to facilitate affordable housing development. Through its subsidiaries, Enterprise is an active syndicator of Low-income Housing tax credits (LIHTC).

**Enterprise Zone or Community** is an area where the federal government, aided by local government, attempts to stimulate economic development.

**Environmental Phase I** is a written report issued by an engineering firm describing certain environmental conditions of the property being inspected – such as lead paint, asbestos, underground storage tank leakage, etc. – that might influence construction costs. Lenders require this report to help evaluate whether costs might be incurred that are not yet factored into a construction budget.

**Equity** is the value of a property that is beyond the total amount owed on mortgages, liens, or other borrowed funds. It can also be used to describe the funds or property provided to pay for the new construction, purchase, or renovation of a building.

## F

**Fair Market Value** is the price a typical buyer would pay to a typical seller for a property in a transaction on the open market. The fair market value of housing will change with time, fluctuations in the desireability of a given location, the supply of and demand for similar housing, and changes in the overall economy.

**Fannie Mae and Freddie Mac** are the major secondary market conduits for non-luxury housing financing. These agencies purchase residential loans originated by banks, package them with other loans, and sell the loan packages to groups of investors. This provides liquidity to the banks so that the banks can make more housing loans. The terms that Fannie and Freddie set for buying both multi-family (e.g. blanket) and single-family (e.g. share) loans greatly influence the terms that banks are willing to offer to borrowers.

**Federal Home Loan Banks (FHLBanks)** are 12 regional wholesale banks operating as a system that are each owned by their lender-member banks. The system works to enhance the financial strength of member-banks by providing them with liquidity to meet the needs of the member-banks' borrowers. Every year since 1989, the 12 FHLBanks have each used 10 percent of their net income to fund their own Community Investment (CIP) and Affordable Housing Programs (AHP). Each FHLBank shapes its own CIP and AHP priorities within certain guidelines and the overall program goal of making housing affordable for low- and moderate-income families.

**Federal Housing Administration (FHA) 213 Program** insures mortgage loans to facilitate the construction, substantial rehabilitation, and/or purchase of cooperative housing projects. Cooperative Housing (Section 213) insures lenders against loss on mortgage defaults, enabling non-profit cooperative housing corporations or trusts to develop or sponsor the development of housing projects to be operated as cooperatives.

**Federal Housing Administration (FHA)** is a federal government entity within the U.S. Department of Housing and Urban Development that administers a variety of multi-family mortgage insurance programs that can be accessed by qualified multi-family lenders. FHA-insured mortgages are backed by the U.S. Government. Federal mortgage insurance enables lenders to make long-term, fixed-rate, high loan-to-value loans to borrowers, including housing cooperatives. Borrowers pay a mortgage premium to their lender, which is then passed through to FHA, which uses the premium to cover losses from FHA's pools of insured loans.

**Fiscal Year** is the financial year, usually 12 months, which marks the time when accounts are settled. It typically matches the calendar year, but can sometimes begin and end on a different month. For example, the federal government's fiscal year ends on September 30.

**Foreclosure** is a legal procedure that may occur when a borrower defaults, or stops making payments on their loan to the lender. During foreclosure the lender usually gets their claim against a property satisfied, often by getting the proceeds from the sale of the property.

**Forgivable Loans** have no repayment obligation if program requirements are met for a specified period of time. In other words, the loan may be "forgiven" or absolved instead of being fully repaid to the lender.

# G

**General Contractor** commits to construct a building or project, rather than for a portion of the work. The general contractor hires subcontractors, such as plumbing or electrical contractors, and coordinates all work. They are responsible for paying the subcontractors.

# H

**Hard Cost** is the cost of actual land acquisition, renovation, or construction of a building. In contrast, soft costs are the portion other than the cost of the improvements themselves. Examples of soft costs are professional fees such as those charged by architects and engineers.

**Home Mortgage Disclosure Act Data (HMDA)** is information collected by lenders about their lending activity for the government to make public reports on various demographic characteristics of home mortgage borrowers. HMDA data collected includes home purchase and home improvement loans, refinancing, and denied, incomplete, and withdrawn applications.

**Housing Cooperative** is a legal entity, usually a corporation that owns real estate. Each shareholder of the legal entity is granted the right to occupy one housing unit.

**Housing Finance Agencies (HFAs)** are sources of low-interest financing from tax-exempt mortgage revenue bonds for single- and multi-family housing. State and local HFAs are active in shaping a variety of programs to disburse federal funds for affordable homeownership.

# I

**Interest** in the co-op is used to describe the value or share that the co-owners have in the cooperative corporation. This is different from interest rates, which are a portion of cost charged by a lender for borrowing their money.

**Interest Rate** is a means of expressing the cost charged for borrowing money as a percentage of the amount borrowed. Interest rates are usually quoted as annual percentage rates. For example, to borrow $100 at an annual interest rate of 8 percent would cost $8 in interest for one year. Interest rates can be fixed or variable. Fixed interest rates will not vary over the life of the loan. Variable interest rates will change weekly, monthly, annually, or at the end of multi-year intervals, depending on the terms of a given variable interest loan. Variable rate loans may have interest rate caps, upper and lower limits on rate changes over the life of the loan.

# L

**Liability Insurance for Directors and Officers** offers the cooperative Board of Directors protection they need from personal liability and financial loss arising out of decisions or acts committed in their leadership capacity.

**Liens** are created when, in addition to promising to repay a loan, a borrower agrees that, if timely payments on the loan are not made, the lender can sell a pledged item (often whatever is bought with the loan proceeds) and credit the proceeds of the sale against the balance due on the loan. The lender is said to have a lien on (or a "security interest" in) the pledged item. A specific item can be pledged as security for more than one obligation, which can have equal or different priorities. When obligations have equal priorities, the proceeds of the sale of property are distributed to the equal lien holders. When obligations have different priorities, the proceeds of the sale are distributed in order – the first lien must be fully satisfied before any amount is distributed to pay for the second lien, and so on.

**Loan Term** is simply the length of the loan. A five-year loan term means the loan must be fully repaid by the end of five years.

**Low Income Housing Tax Credit (LIHTC)** was created in 1986 by the federal government as its primary means of producing affordable low-income housing. Investors provide equity in exchange for credits against their federal income tax obligations. Tax credits are allocated by state Housing Finance Agencies (HFAs).

# M

**Mortgage Escrow** is a dedicated account that collects money monthly, often as part of the mortgage payment, and is held by mortgage lenders to pay the borrower's property taxes, fire hazard insurance premiums, and mortgage insurance premiums throughout the year. The account is set up during the financing process and may be a lender requirement.

**Mutual Housing Associations** is a term used to describe a wide variety of situations. It may denote a situation in which a non-profit organization owns one or more sets of lands and buildings that are operated by their residents on a cooperative basis. It may denote a situation in which one or more fee-simple cooperatives come together to create a non-profit organization that provides professional management or other services to its member-cooperatives on a mutual basis. It may denote some permutation or combination of the two situations. In the first situation, the non-profit organization may have a governance structure composed solely of representatives of cooperative residents; composed of a mixture of cooperative residents and representatives of the communities in which the cooperatives are situated; or composed solely of community representatives. In the second situation, the governance structure of the non-profit is likely to be composed largely or exclusively of representatives of the cooperative residents. Mutual housing associations are generally created to provide strength and stability to small cooperatives or as an alternative method of assuring long-term housing affordability.

# N

**NCB Capital Impact** is a non-profit affiliate of NCB that empowers America's underserved communities by creating access to capital and expert technical assistance otherwise unavailable to low- and moderate-income communities, often dealing with higher risk while maintaining financial strength.

**NCB** is an acronym for National Cooperative Bank, a corporation chartered by the federal government under the National Consumer Cooperative Bank Act in 1978 and privatized in 1981 as a cooperative financial services company. NCB is dedicated to strengthening communities nationwide through the delivery of banking and financial services, complemented by a special focus on cooperative expansion and economic development. Today, NCB is owned by more than 2,600 customer-owners with more than $6 billion in assets under management.

# O

**Occupancy Agreement/Proprietary Lease** is the agreement between a cooperative and each of its individual members setting forth the terms whereby a member may have exclusive occupancy of a specific dwelling unit owned by the cooperative corporation until he/she sells.

**Operating Costs** are expenses incurred by the owner (e.g. a cooperative corporation or the landlord of a rental building) to operate the property. Operating costs include the cost of management, building maintenance, grounds maintenance, common utilities, etc.

**Origination** is the term used to describe the process of creating a loan. Through this process, the terms of the mortgage agreement (such as the amount of loan, interest rate, compounding frequency, etc.) are established and the parties involved agree to the transaction.

# P

**Perfection (Perfection of a Security Interest)** is the establishment of a particular creditor's lien position, giving the creditor priority access to the collateral over other claimants in case of default. In a cooperative, a creditor with a perfected security interest may have certain priority rights to the building. This may help repay the loan if the cooperative corporation can't repay the loan according to the agreed terms. (See Lien for more information.)

**Performance Bond** is a written "promise" issued by an insurance company to guarantee satisfactory completion of a project by a contractor.

**Position (First, Second, or Third)** is used to describe the order in which creditors or lenders get paid back in the event that a borrower is not paying as expected. For example, the courts or a contractual agreement may determine that the bank (in first position) must be paid back before the cooperative is paid back (in second position), in a case where the borrower owes money to both the bank and the cooperative.

**Pre-Payment Penalty** is a charge the lender makes when a mortgage is repaid early, before a certain period of time elapses. In effect, the borrower is penalized for paying off the mortgage early.

**Principal** is the amount borrowed, exclusive of interest or any other costs of borrowing.

**Pro forma** is a detailed breakdown of financial assumptions or projections.

**Public Housing Authority (PHA)** is a local governmental body that administers either public housing or Section 8 vouchers, or both, for the federal government.

## R

**Recognition Agreement** "recognizes" that the cooperative and the share lender have potentially competing interests in the event of a default by a share owner because the defaulting share owner's collateral is an ownership interest in the cooperative. Share lenders require a recognition agreement as a condition of each share loan. The recognition agreement establishes the rights and obligations among the share lender, the cooperative corporation and the share owner.

**Remediation Plan** created to resolve environmental issues related to site construction or rehabilitation.

**Rent Roll** is a list of lease fees, which includes the names of tenants and the amount of rent they pay.

**Reserves** are funds set aside by a cooperative or a condo association to cover unanticipated expenses. This type of reserve is usually called operating reserves. Rehabilitation/improvement or replacement reserves are collected and saved to cover future, anticipated costs of building repairs.

## S

**Scope of Work** is a term used to describe the job to be accomplished by a hired professional.

**Secondary Market** is made up of a variety of conduits that link lenders to investors and provide liquidity for banks to make loans. Fannie Mae and Freddie Mac are examples of such conduits. They attract investment capital into mortgage lending by annually buying billions of dollars worth of mortgages from lenders, bundling the mortgages, and re-selling the mortgages to investors. Secondary market criteria for loan purchases shape the type of loan products banks can offer their borrowers.

**Security Interest** (see Lien)

**Share Loan** is a loan made to a cooperative co-owner that is secured by a pledge of the co-owner's ownership interest in the cooperative (his/her "shares"). If a cooperative co-owner has obtained a share loan, only that person is individually liable to the share lender. The cooperative itself incurs no financial obligation to the share lender.

**Soft Debt** is debt that is not always expected to be fully repaid. The term includes debt that is forgiven over time or that is due usually if certain terms and conditions are not met by the borrower. Soft debt is frequently extended by a government to achieve a policy objective.

## T

**Title Insurance** is protection against loss arising from problems connected to the title to the property owned. The cooperative corporation usually takes out title insurance on the building whereas that share owners do not need title insurance on their shares.

## U

**United States Department of Agriculture (USDA)** Rural Development Program includes the Rural Housing Service (RHS). RHS provides loan guarantees for multi-family mortgages in rural areas under the Section 515 program, among its other affordable housing programs.

# Index

# INDEX

*This index is intended for manual users to look up unfamiliar terms. While we have referenced a page that best describes the word, we have not listed every place in the manual where all of these terms appear. "G" signifies that the term is defined in our glossary.*

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