Public Housing
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PUBLIC HOUSING HOMEOWNERSHIP DEMONSTRATION

BALTIMORE CASE STUDY

Introduction

Row houses in many Baltimore, MD neighborhoods are affordable to moderate-income families. When subsidized financing is available to buy these modest-priced units or when they are discounted below their market value, they become affordable to lower-income families. These two facts, coupled with an extraordinary amount of effort to qualify home buyers for financing, explain the high success that Baltimore has achieved in its public housing homeownership demonstration. Although the PHA has fallen two short of meeting its goal of selling 30 scattered-site, single-family units, it appears that the 28 families who have closed on their loans are achieving their dream of homeownership. By pricing the units using a 25 percent housing cost to income ratio and excluding temporary income and the income of minors from consideration, Baltimore's program planners have done their best to ensure that families would not be assuming an unmanageable financial burden soon after they took title to their homes.

There is no doubt that in Baltimore the elimination of ceiling rents in public housing and the requirement that tenants pay 30 percent of their income for rent means that many families in scattered-site units can afford to acquire their houses with minimal assistance from the PHA. In some cases, too, with HUD paying the outstanding debt on the units under Section 5(h), ownership costs under the PHHD are even lower than public housing rents.

Managing the Demonstration

Baltimore has 18,147 public housing units under its Annual Contributions Contract including 2,600 scattered-site single-family units, most of which were acquired with HUD public housing development funds during the 1960s. Baltimore also has approximately 4,000 Section 8 certificates and 500 vouchers. The PHA has also financed several Section 8 new and substantial rehab projects under its Section 11(b) bond authority. These projects, however, are not owned by the PHA. Sensitivity about replacement housing is high in Baltimore because the public housing waiting list contains about 36,000 families.

Baltimore sold nine scattered-site public housing units under Section 5(h) several years ago. These units were sold at their appraised value and were financed under the FHA Section 203(b) program. But given the incomes of public housing tenants vary, few could afford to buy their homes without subsidies. The PHA has also demolished a few public housing units where an isolated
scattered-site unit was the sole remaining unit on a block or parcel to be redeveloped.

The PHHD was an initiative of former Mayor Donald Shaefer. He believed that the city had a high proportion of renters to owners and that anything that could be done to increase homeownership would benefit the city.

The specific goals of the program were to give people with incomes of $10,000 or more who live in public housing the ability to become homeowners. The program was also designed to match homeownership with rent payments. Ownership should keep families together and give families something to pass on to their children. The goal was to sell 30 scattered-site units to their current occupants. A total of 352 families living in the 2600 scattered site units had incomes of $10,000 or more. There would be no relocation because families who do not qualify would not be part of the demonstration. The goals of the program were not changed although the problem of qualifying families for financing was more difficult than anticipated. So far the city has fallen two short of its goal, having sold 28 of the 30 units earmarked for the demonstration program.

Replacement housing has been a concern of agency staff. The only way that the city would consider expanding its program would be to receive replacement housing or Section 8 certificates on a one for one basis. The deputy commissioner of the Neighborhood Progress Administration (NPA) indicated that he would expand the program by 30 units per year if HUD would assign the unexpired portion of the ACCs associated with the for sale housing to the city so that he could use it with city-acquired housing as replacement low income units.

The policies for the PHHD were made by a task force appointed by the commissioner of the NPA and by the chairman of the housing authority. The task force included a PHA commissioner, PHA staff, a representative of the mayor's office and a member of the tenants' residence advisory board.

Baltimore's PHHD was administered by the NPA. NPA is a combination of the old Department of Housing and Community Development (HCD) which has always included the housing authority, and the city's employment and manpower development programs. Historically, the commissioner of HCD was also the executive director of the PHA. Now, the commissioner of the NPA is head of all housing and employment programs. The NPA was the creation of Mayor Donald Shaefer who is now Governor of Maryland. The NPA's office of homeownership services designed and administered the PHHD.

Subsequent to the commencement of the PHHD, the city created a Homeownership Institute within NPA which provides a variety of services to first-time home buyers. Among these are homeownership counseling sessions to assist first-time home
buyers in preparing to buy a home, including a review of credit, debts, income and property selection. The institute also provides conversion counseling to tenants receiving notice under the city's Tenant's Right of First Refusal Ordinance, by helping them evaluate their purchase options.

The PHHD was labor intensive. There was one full-time counselor, a part-time cost estimator and a half-time clerical worker assigned to the program. In addition, two PHA maintenance workers repair the sale units.

Baltimore received a $46,000 technical assistance grant from HUD which it used for preparation of legal documents, payment of fee appraisals on the properties, and funding of a counseling staff position. If additional technical assistance funds were available, they would have been used for additional counseling staff to help families get through the process, and for assistance in preparing loan packages for state processing.

Selecting and Rehabilitating Properties

The 28 units that had been sold as of September 1989 were selected based on the ability and the desire of existing tenants to buy. Units occupied by families with incomes over $10,000 who indicated an interest in buying their scattered-site units were selected. Interested families completed applications and if they were approved under the PHA/state or conventional lending programs, their units became one of the 28 sold.

Each of the sale units was acquired and rehabilitated by the housing authority in the 1960s at an average cost of nearly $26,000 per house. Thus, their pre-sale condition was good. Only modest repairs averaging around $2,600 per unit were needed to make them sales-ready. All units received new storm doors and screens; some electrical systems were upgraded. No major systems were replaced. All units were painted. The state Minimum Property Standards were used as the applicable rehab standard. Since financing for most of the units came from the state it was essential to meet MPS requirements. The repair work was carried out by PHA personnel and was financed by the PHA. Modernization funds are not being used because scattered site units are too new to be a high priority for renovation under HUD's comprehensive modernization program.

No relocation has been necessary in any phase of the program. Since the PHHD is a scattered-site program, neighborhoods vary a great deal.

Attracting and Selecting Owners

The homeownership program office set seven household eligibility criteria:

1. Must have an income of at least $10,000 per year;
2. Must have lived in their present house for at least three years;

3. Must have worked or had another steady source of income for the last 3 years;

4. Must have at least $500 cash for down payment;

5. Must have a good rental history with the PHA;

6. Must be able to plan, budget and save; and

7. Must be able to assume all responsibility for maintenance and upkeep of the house and yard.

First, the PHA identified all families living in scattered-site housing having incomes of $10,000 or more. A total of 352 families were identified. This is about 14 percent of all scattered-site occupants. A letter was sent to all 352 families inquiring about their interest in the PHHD. Two hundred-sixteen families responded that they would like to have more information on the program (61 percent). A full application was sent to each of these families spelling out eligibility criteria and program requirements. Seventy-nine families completed the application (37 percent). Of those, only 28 qualified for financing and actually became home owners under the PHHD.

Fifteen of the buyers (53.3 percent) are husband-wife households; 10 (35.7 percent) are female-headed families with young children; and three (10.7 percent) consist of a non-elderly adult, a daughter and her young children. As implied in the eligibility criteria, all home buying-households contained at least one full-time wage earner. Slightly more than half (15) of those employed worked in the private sector and the remainder worked for either state (6), local (6) or federal (1) government. According to the PHA, the average buyer had an income of $19,449 at the time of closing.

The average buyer in Baltimore has lived in the same unit for 12 years. Under the city's resale restrictions, the houses will remain available to low or moderate income people for the better part of 10 years after closing. In short, these scattered-site units have not experienced turnover in many years, have housed families whose incomes have risen over the years, and will continue to house the same families for many years to come.

Property Conveyance

The PHHD sales units were sold fee simple at their appraised value which averaged $23,534, and ranged from $20,700 to $33,800. Financing for all but three sales was provided by the state Department of Economic and Community Development (DECD). The remaining three sales were conventionally financed by a private
lender under a below market rate mortgage program. The average first mortgage for all buyers was $18,259.

Final closing costs are not known, but the State of Maryland has high settlement charges. Staff estimate that closing costs averaged around nine percent of the sales price, or $2,250 on a $25,000 house. All but $500 of these costs were paid by the city.

Financing

It was very important to the homeownership program office that the PHA not finance the sales. The feeling was that families must end their dependence on the PHA and could no longer pay rent a little late if they had a problem. Families had to understand from the beginning that the mortgage had to be paid each month on time.

The city tried unsuccessfully to interest private lenders in the program. Loans were too small and too costly to originate and service. Eventually, the city was able to arrange financing through the state's housing finance agency in the Department of Economic and Community Development. For underwriting purposes, the city initially defined housing affordability in terms of a 35 percent housing expense to income ratio, but decided that such a high ratio would leave a $10,000 income household too little leeway to meet financial emergencies. Therefore, the PHA elected to establish a first mortgage at a principal amount and interest rate needed to hold housing expenses to 25 percent of the adjusted income used by the housing authority in setting rent. A silent-second mortgage to be held by the PHA would be used to bridge the difference between the first mortgage and the appraised value of the property. This silent-second mortgage will be reduced at ten percent per year over a 10 year period.

The financing and reduction of the liability for the silent-second mortgage works as follows. The first mortgage comes from the state DECD with an interest rate and term that varies with the home buyer's income. If income is above $20,000 for a one to four person family, above $20,463 for a five person family or above $21,667 for a six person family the interest rate is 7.75 percent and the term 25 years. These families met the criteria of a standard state single-family bond program that is insured by the Maryland Housing Fund. If family income is between $18,000-$20,000 the interest rate is five percent with a 30 year term. If family income falls below $18,000, the interest rate is four percent. The source of funds for the lower two income groups is repayment from previous bonds. These are uninsured mortgages. The size of the first mortgage loan is based on affordability defined as 25 percent of gross family income for PITI plus utilities.

The sales prices of the units were based on independent fee appraisals and ranged between $20,700 and $33,800. A down
payment of $500 was required of all purchasers. The silent second, which will cover the difference between the first mortgage and the sale price, accrues interest at the rate of one percent simple interest per year.

Since the PHA is not the first mortgage holder, a foreclosure would not directly involve the agency. Loans would be foreclosed by the state. Nevertheless, the PHA will monitor loan payments very carefully. The feeling is that the PHA cannot afford to let the program fail.

Based on 28 sales, the average sales price was $23,534 and the average first mortgage was $18,259, or around 78 percent of sales price. Silent-second mortgages averaged $5,285, although the incomes of 12 buyers were high enough to afford to pay the full appraised value of their house without the PHA having to take back a second mortgage.

Three families who purchased their scattered-site units had incomes that exceeded the state's maximum income limits and had to secure conventional financing. The PHA helped these families acquire favorable first mortgage financing from Maryland National Bank under a Community Reinvestment Act-inspired below market rate lending program. These FHA insured mortgages were at a nine percent interest rate.

Monthly mortgage payments for all buyers, including property taxes and insurance (PITI), averages just $185, which is 54 percent less than the average $397 they were paying to the housing authority for rent and utilities. We should note, however, that these homeowner costs do not include allowances for utilities and maintenance. While PHHD officials are concerned about the ability of the home buyers to keep up with rising homeownership costs, especially local real estate taxes, PHHD participants in Baltimore may be better able to withstand future cost increases than buyers in other cities because their first mortgages are based on 25 percent rather than 30 percent of their income.

Overall, Baltimore's financing programs have worked exceptionally well. All income-eligible buyers were eventually qualified to receive state-subsidized mortgage loans and the few whose incomes exceeded the state's limits secured favorable FHA insured loans. This kind of success, however, comes neither cheaply nor without a great deal of effort. The program staff had a difficult time qualifying public housing tenants for loans, even for state-sponsored mortgages. Not only were many potential buyers disqualified for mortgages because of poor credit histories, but many who received loans were approved only because of the extraordinary efforts of the PHHD coordinators. Some buyers had outstanding judgments, late payments and overdue bills at the local hospital for emergency room treatment. Every one of these credit problems had to be either cleared up, explained away or rationalized to the satisfaction of the loan underwriters.
Without the dedication of the PHHD staff, financing for PHHD buyers would not have been available.

Counseling

All home buyers were required to attend a one-hour credit counseling seminar given by the Consumer Credit Counseling Service of Maryland, a non-profit organization sponsored by major department stores and other extenders of commercial credit. The session emphasized the responsible use of credit and personal budgeting.

In addition to this mandatory session, Ms. Carol Curtis, a member of the PHA staff who is a HUD certified counselor, worked with the home buyers. She assisted them, made applications, reviewed appraisals and repair schedules on their house, explained what mortgages are, how the program's financing worked, what soft seconds are and how the sales limitations apply. She also accompanied each buyer to the closing.

There are no plans for any formal post-purchase counseling. There are, however, plans to convene all home buyers in mid 1990 to assess homeowner needs. The post-purchase assistance would probably stress home repair skills and be staffed by a PHA weatherization and maintenance crew.

Windfall Profits and Retention Provisions

The city has placed a 10 year resale restriction on PHHD units by requiring the silent second mortgage to be repaid in declining percentages the longer the unit is owned.

The second mortgage note plus accrued interest at one percent per year shall be forgiven at a specified rate over a 10 year period as follows:

- 100% is due and payable if resale is within 1 year of settlement;
- 90% between 1 and 2 years;
- 80% between 2 and 3 years;
- 70% between 3 and 4 years;
- 60% between 4 and 5 years;
- 50% between 5 and 6 years;
- 40% between 6 and 7 years;
- 30% between 7 and 8 years;
- 20% between 8 and 9 years;
- 10% between 9 and 10 years; and,
- 0% 10 years and after.

Also, if a sale is made within the first 10 years, the city has right of first refusal at the market price. The house does not have to be resold to a low income family. If the city buys the
house, however, and rolls over the second, it can keep the unit affordable to low income families for a modest cost.

Provision for Maintenance After Sale

The PHA warrants all major systems for two years after sale. Thus far, one roof and two hot water heaters have been replaced under the warranty, funds for which were secured from net sales proceeds and placed into a reserve account. Plans also call for the PHA to assist homeowners with major repair needs beyond two years through creation of a subsidized loan program. This loan program, which was also to be capitalized from a portion of net sales proceeds, has not yet been put in place.

Handling Non-participants

As a scattered-site project there was no relocation. Those who failed to qualify for loans will continue living in their single-family units as public housing tenants.

Amount and Use of Sales Income

Since financing is being provided by outside lenders, the PHA has received several hundred thousand dollars in sales proceeds as follows:

<table>
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<th>Description</th>
<th>Amount</th>
</tr>
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<tbody>
<tr>
<td>From down payments (28 @ $500)</td>
<td>$14,000</td>
</tr>
<tr>
<td>From first mortgage loans</td>
<td>$511,252</td>
</tr>
<tr>
<td>Total Sales Proceeds</td>
<td>$525,252</td>
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This, however, is not the accounting method that the housing authority uses to determine net sales proceeds. To arrive at net sales proceeds, the PHA deducts from gross sales revenues all rehab costs, warranty reserves, housing authority-paid closing costs, and original property acquisition and initial rehabilitation costs. The latter costs averaged nearly $26,000 a unit, which means that, from an accounting standpoint, net sales proceeds are negative.

While all net revenues from the PHHD will be used for low income housing activities, the negative balance in the PHHD "account" allows the PHA to use the net sales revenues for other activities and programs.

Impact of Sales Program

With an inventory exceeding 18,000 units, and a public housing homeownership demonstration under which just one percent of the PHA's scattered-site stock was sold, it is reasonable to conclude that the PHHD has had an imperceptible effect on housing authority operations.
Conclusions

Though of modest size, Baltimore's scattered-site homeownership demonstration is large enough to have learned several important things about public housing homeownership. First, a sales program is very labor intensive, especially if the housing authority is not providing the permanent loans. In Baltimore's case, financing is coming from the state's Department of Economic and Community Development. Publicizing the program, identifying potential buyers, preparing loan packages for submission to the state, and counseling families takes a great deal of time. It is unclear whether there are economies of scale in this kind of program, but it may well be that as much effort is involved in structuring a program to sell 30 scattered-site units as would be required to sell a much larger number of units.

Second, the PHA is not interested in expanding its sales program unless the replacement housing issue can be satisfactorily resolved. Baltimore's experience of converting long term residents into buyers of their units deflates the argument that a public housing sales program takes scarce low cost units off the market. The combination of long-term occupancy and an extended set of resale restrictions means that the sales units are likely to continue to meet the same long term need they would have in the absence of the program.

Finally, Baltimore's difficulty in qualifying buyers under the state's subsidized financing programs suggests the need for a program of permanent financing tailored to low-income buyers with marginal credit histories. Alternatively, the city's experience raises the question of pricing policies. There is no a priori basis for pricing units according to appraised value. To maximize affordability, prices can be discounted as much as the housing authority cares to discount them.
Introduction

The demonstration program in Chicago, Ill. was designed to sell 31 single family and duplex units to public housing tenants. The units sold are scattered throughout Wentworth Gardens, a 98 unit development consisting of single family, duplex, and townhouse units on the south side of Chicago. Financing for the sales was originally provided by a city sponsored bond program, and once that program expired, by a variety of private mortgage companies offering FHA insured loans. The sale prices were set between $17,000 and $25,000 depending on the type and size of the units. These prices are approximately one-half of the estimated market values. Upon completion of the sale, sales proceeds were lent back to buyers in the form of a silent-second mortgage to rehabilitate and improve their units. This silent-second will be forgiven after five years. As of July 1989, 14 units had been transferred to former public housing tenants. The major problems encountered in meeting the sales goals include great difficulty in obtaining private financing and lack of staff assigned to manage the program.

Managing the Demonstration

The demonstration in Chicago is being managed by the Chicago Housing Authority (CHA) which manages approximately 49,000 housing units for low- and moderate-income people. The authority has approximately 30,555 units of conventional public housing for families and 9,974 units of elderly housing. CHA also administers approximately 8,951 Section 8 certificates and a small number of housing vouchers. There are 43,000 people on the waiting list for public housing, although not all of these have been income certified.

Two reasons were given by local officials for participating in the demonstration. First, the authority's executive director at the time of the initial application was interested in improving relations with HUD and saw participation in the program as a means of doing that. Second, they wanted to fulfill a promise that was made to the residents of Wentworth Gardens that they would be able to buy their units. In anticipation of this, residents were screened very carefully when they were first moved into this development.

The initial idea for participating in the demonstration came from the CHA's executive director who along with the head of the planning research and development division, took a lead role in developing the proposal. In the early phase of the program the city's department of housing offered financing for the sales through the CHAMP II program, which was a city sponsored bond program that offers low interest loans to qualified applicants.
The Root Street Tenant's Organization, which represents the tenants of Wentworth Gardens, supported the application, as did then Mayor Harold Washington. In developing the proposal, staff raised three major concerns: the lack of replacement units, the effect of the sales on the authority's operating subsidies, and the potential for buyers to reap windfall profits. The first two concerns were not strong enough, given the number of units to be sold, to discourage participation and the concern over windfall profits was handled by placing restrictions on the resale of units for the first five years of ownership.

For the purposes of description two phases of the program can be distinguished: an early phase when the planning, research and development division managed the demonstration and loans were available through the city bond program, and a later phase when the legal department managed the program and buyers had to find their own financing with little or no assistance from the housing authority. Each phase lasted approximately two years.

During the initial phase the authority's planning research and development division handled program publicity, helped to arrange financing, and had overall program management responsibilities. The legal department was involved in drafting sales and repair contracts, setting up escrow accounts for the rehabilitation work to be done, and preparing the closing documents. A local consultant was also hired to provide counseling to the prospective buyers. Several banks and mortgage companies participating in the CHAMP program were involved in reviewing and processing loan applications.

In the latter stage of the demonstration one of three attorneys from the legal office had full responsibility for the program. During this time they handled the legal aspects of sales and provided informal advice to prospective participants on how to obtain private financing. No one was responsible for the other aspects of the program, however, including recruitment of program participants, counseling of tenants, and overall program management.

Program staffing during the initial phase involved approximately the equivalent of one full time position with an estimated cost of $30,000 per year. This breaks down into half of the demonstration manager's time and half of an attorney's time. An additional $1,000 was said to have been spent on printing flyers and brochures. In the latter stage, the lawyers spent approximately 15 percent of their time on the demonstration, costing the authority approximately $6,000 per year. The overall cost of administering the demonstration over the four year period was approximately $72,000.

Chicago received a technical assistance grant of $40,193. The grant was used during the initial phase of the program to hold seminars and training sessions for PHA staff, and to pay for an outside contractor who provided counseling to prospective buyers.
The technical assistance grant, however, was exhausted during the first half of the demonstration period. If more technical assistance funds had been available, they would have been used for publicity aimed at selling the program to tenants and would have provided more counseling services to buyers. The CHA also could have used more help in arranging financing for prospective buyers. Moreover, more technical assistance funds would have been used to fund additional CHA staff to manage the program during its latter phase.

The demonstration in Chicago experienced several management problems. First, there was considerable staff turnover in the housing authority throughout the period of the demonstration. It had three executive directors during the course of the demonstration. This slowed the early progress of the demonstration considerably. Furthermore, the planning research and development division experienced major staff reductions making it difficult for the remaining staff to find time to work on the demonstration. The head of that office then left CHA and the program was assigned to the first of the lawyers who were to assume responsibility for it. Clearly this staff turnover and the lack of attention paid to the demonstration was a major factor in its falling well short of its sales goals. Moreover, given the other problems the authority was facing during this period, it is not surprising that less than full attention was paid to this rather small demonstration program.

Selecting and Rehabilitating Properties

Although Wentworth Gardens consists of 98 single family and duplex units, the CHA only requested permission to sell 31 of those units; the remainder would continue to be occupied by CHA tenants. Wentworth Gardens was originally selected for sales because residents had been promised the opportunity to buy and because the program designers thought the single family, duplex, and townhouse units in this development could be easily sold. By July 1989, 14 units had been transferred to tenants.

Wentworth Gardens is a four square block subdivision consisting of relatively new (circa 1968) single family, duplex, and townhouse units. The units sold are scattered throughout the development since they are selling any unit for which there is an interested and qualified buyer or which becomes vacant. These units have estimated market values in the $35,000 to $40,000 range.

Wentworth Gardens is bordered on one side by a well kept apartment building for the elderly, on a second side by a railroad trestle, on a third side by an industrial building, and on a fourth side by older single-family and duplex units in fair condition. The surrounding neighborhood was described as low income with residents making $15,000 to $25,000 a year. It is almost 100 percent black and there is a high proportion of rental housing. It is a stable area, however, with little abandonment
and housing conditions that were described as fair. There are no major public improvement programs on-going in the neighborhood.

Before the sales these units were in fair to poor condition. In the early phase of the program an architectural firm inspected each unit for city and state code violations and recommended improvements. In the latter phase tenants had contractors perform similar inspections. In both phases tenants were given an opportunity to suggest improvements and, if the budget allowed, these improvements were incorporated into repair specifications. The cost of repairs could not exceed $17,500 per unit. Improvements typically included repairing or replacing roofs, siding, bathroom tile, and plumbing. Fencing and back yard patios were also added to many units. The final repair work cost approximately $16,000 per unit. Repairs were performed by independent contractors selected by the buyers and were paid for by sales proceeds that were lent by the CHA to the buyers upon closing. An escrow account was established for these funds which, with the approval of the CHA, were used to pay for repairs and improvements. Tenants did not need to be relocated to carry out the repairs and there does not seem to be any major problem with the repair work completed.

**Attracting and Selecting Owners**

Priority for participating in the demonstration was given to families in the Wentworth Gardens development who could meet the financial qualifications for a loan. Other CHA residents were eligible, however, for units that became vacant during the demonstration.

Tenants of Wentworth Gardens were originally notified of the program by meetings and brochures sponsored by the CHA. The program was also brought to the attention of other public housing residents through a monthly newsletter published by the CHA. Screening of prospective buyers during the initial phase was handled by the mortgage companies participating in the CHAMP II program. Interested buyers went to one of the participating mortgage companies to see if they could qualify for a loan. Those mortgage companies applied standard underwriting criteria since the loans had to be approved by a private mortgage insurance company. One mortgage banker interviewed described this as unfortunate since many of those that applied could not qualify and the program was not helping those for whom it was originally intended.

During the latter phase of the program, screening was essentially handled by any number of mortgage companies. Those interested in buying often heard about the program through word of mouth and had to arrange their own financing. No special assistance was provided to prospective buyers in obtaining the needed financing and many were rejected because of poor credit histories.
Property Conveyance

Properties were conveyed to buyers fee simple. The purchase prices were based on the estimated market value minus the costs of rehabilitation. If the unit was single family, a two bedroom unit sold for $20,000, a three bedroom for $22,500 and a four bedroom sold for $25,000. If the unit was part of a duplex, a two bedroom unit sold for $17,000, a three bedroom for $20,000 and a four bedroom sold for $22,000. A typical deal would be as follows. The purchase price of a three-bedroom, single-family house was set at $22,500. Upon closing, the CHA lent up to $17,000 of the sales proceeds back to the buyers in the form of silent-second mortgages to pay for the rehabilitation. This silent-second mortgage accrues market rate interest but buyers do not have to make payments on either the principal or interest unless the unit is sold within five years after the original sale. Moreover, the silent-second and the accrued interest will be forgiven after this five year period. Closing costs were paid for out of the sale proceeds and averaged approximately $4,000 per sale.

Financing

During the initial phase of the demonstration, sales were financed through a city bond program called CHAMP II (the Chicago Affordable Mortgage Program). This program provided 30-year fixed rate mortgages at 9.68 percent from the sale of approximately $131 million in single family revenue bonds. A minimum downpayment of five percent was required and a service charge of 1.5 percent of the mortgage amount was charged for a home in this area of Chicago. Twelve mortgage companies participated in this program but only two actually made loans to those buying PHHD properties. A total of seven sales were financed under this bond program.

Underwriting criteria for the CHAMP II loans were described as conventional secondary market criteria. The mortgage companies were responsible for screening buyers, making preliminary decisions, and forwarding applications to both the city and private mortgage insurers (PMIs) working with the program. In order for a loan to close, both the city and the private mortgage insurer had to accept the application. During this period a local technical assistance provider helped tenants clear credit problems and complete the necessary forms to apply for loans. During the latter phase of the program the CHAMP II program was no longer available; thus, those interested in buying a home were told to arrange their own financing. Those that were successful obtained FHA insured loans from a variety of mortgage companies doing business in the city. The FHA was said to be cooperative in allowing the rehabilitation work to be done after, rather than before, the sale. A total of seven units were sold during the second phase of the program.
Arranging financing for the sales has been the major obstacle to the success of the Chicago demonstration. The program staff began by trying to arrange private financing. At least five financial institutions were contacted but all refused to accept applications from CHA tenants, in part, because the properties which they wanted to buy were part of a public housing development. For this reason program staff turned to the CHAMP II program. Long delays in loan processing and the rejection of many of the tenants applying for loans severely restricted progress. Rejections of many otherwise acceptable applications were based on late rent payment histories, sometimes dating back several years. The long delays in loan processing were the result of two factors. First, staff turnover at one of the principle mortgage companies handling the loans slowed progress. Each change in the bank's personnel meant that the bank's review process began anew. Second, reluctance of PMIs to insure these loans contributed to the long delays. After many meetings and phone calls, however, one mortgage insurance company finally agreed to insure the first seven loans.

These delays led to a new problem. In March of 1987, the CHAMP II program ran out of funds and was no longer available to finance sales. At this point the technical assistance funds had been exhausted and the CHA seemed to have given up on the program. Nonetheless, lawyers did continue to sell units to those who could arrange their own financing. Many of those interviewed felt that to be successful a special mortgage program would have to be established to provide accessible and affordable financing for buyers.

Among those who did buy there is no evidence of defaults or foreclosures. The Declaration of Covenants Conditions and Restriction requires the lenders to provide the CHA notice within 15 days of an owner becoming two months in arrears in their mortgage payments. The CHA has not been notified of any such delinquencies.

Counseling

In the early phase of the demonstration program counseling of program participants was the responsibility of Erwin France Associates, a local consulting firm with approximately 15 years of experience in the housing field. Their responsibilities included group orientation sessions, one-on-one counseling, training of CHA staff and development of a homeownership handbook for prospective buyers. Funding for these services came from the HUD technical assistance grant.

Two orientation sessions were held to discuss the homeownership program, the responsibilities of homeownership, and the process of buying a home. The consultants also developed a five page handbook on homeownership. It covered topics including the process of buying a home and the costs and responsibilities of homeownership and home maintenance. CHA had also planned to hold
several more group sessions on home maintenance and other topics but funds ran out before these were offered.

Most of their work, according to Mr. France, involved individualized counseling with tenants trying to buy their units. His basic philosophy is that technical assistance is best when people are actually going through the process, not in abstract group sessions. In individualized counseling particular emphasis is put on the need for tenants to take responsibility for various aspects of homeownership including maintenance and the prompt payment of mortgage, utility and other housing related bills. They also acted as an intermediary between the tenants interested in purchasing their units and the CHA.

During the latter phase of the demonstration program no formal counseling was available to buyers. The lawyers handling the closings would often recommend possible sources of home financing but that was the extent of counseling. Clearly, the lack of counseling in the latter part of the program contributed to the low number of sales. It is too early to tell if it also will lead to higher rates of default.

Windfall Profits and Retention Provisions

To guard against windfall profits the CHA holds a silent-second mortgage on the funds that were provided to make repairs and improvements. If the unit is sold within the first five years, the second mortgage, both principal and interest, has to be paid in full. After five years, the units can be sold at market value and any profit is kept by the owner.

The CHA has also retained a first right of refusal if the unit is offered for sale. The Declaration of Covenants, Conditions and Restrictions requires the owner to notify the CHA if the property is offered for sale and it has 30 days to notify the owner of its intention to repurchase the property. There appears to be no time limitation on this provision. The purchase price in the event of a sale is to be determined by independent appraisals at the time of sale. If within the first five years, however, sale of the unit to a third party results in proceeds in excess of both the original sale price and the rehabilitation cost, CHA and the owner will share equally in such excess. No resales had taken place at the time of our last site visit.

Provision for Maintenance After Sale

The approved program summary indicates that a revolving loan fund was to be established with part of the sales proceeds to provide for major repairs after sale. This fund, however, has not been established—the buyers appear to be on their own. This appears to be a consequence of the lack of overall program management.
Handling Non-Participants

Only units with interested and eligible occupants and vacant units are being sold. Existing tenants who cannot or do not wish to participate will remain in their current units. When units become vacant through tenant initiated moves, however, these units are being offered for sale. Because of the difficulties potential buyers have had in obtaining financing, however, some units have remained vacant for a long period of time (more than one year) and some vandalism has occurred.

Amount and Use of Sales Income

Most of the sales proceeds are being lent back to the buyers in a silent second mortgage to make repairs on their units and will be forgiven after five years. The closing costs are also being paid out of sales proceeds. The remaining funds, several thousand dollars per unit, have gone into the CHA general fund.

Impact Sales Program

The demonstration has had very little financial impact on the CHA. The sale of 14 units represents an extremely small fraction of the housing stock and will have a negligible influence on the operating subsidy and the maintenance and operating costs. The demonstration has caused some management problems, however, as the management office responsible for the site was not made aware that some of the units had been sold. Moreover, some units have remained vacant waiting for sale and have been vandalized. Finally, the CHA has been receiving complaints from the buyers about the poor condition of some adjacent properties. One CHA staff person interviewed felt that this was a positive outcome in that the buyers represented "extra eyes for the authority." He felt that they watched over the development and were more likely to call the police or the CHA to report problems.

The demonstration program in Chicago has benefited the local government in that the 14 buyers now pay city taxes. Given that the CHA pays no taxes to the city, this is a net increase in the city's tax revenue. It is impossible to tell if the program has had any effect on the surrounding neighborhoods but the houses which have been sold are clearly in better condition than the surrounding units.

Those who have been able to buy their units are generally satisfied with the program. Based on an interview with the president of the tenant council, however, there are many people who want to buy, but have not been able to because of their inability to obtain private financing. These people are not very happy with the program.
Conclusions

Clearly, the program in Chicago has been less than successful. In almost four years the CHA has only succeeded in selling 14 of 31 units. The biggest problems were difficulty in obtaining financing and the failure to commit sufficient staff to the program during its latter phase. These two problems were not unrelated. In the early phase of the program, sufficient staff was assigned to manage it and technical assistance was being provided by a local contractor. Problems in arranging financing, however, greatly slowed progress and during this time the technical assistance funds provided by HUD were expended. During the latter phase of the program, the CHA was not willing to commit enough of its own staff and funds to effectively manage the demonstration.

The most interesting aspect of the demonstration program in Chicago is the method of financing repairs to the units. In all other demonstration programs the repairs were made before the units were transferred. In Chicago sales proceeds were used to fund repairs that were made after the units were transferred. The establishment of an escrow account for the funds ensured that the needed improvements were made. This method of handling repairs meant that the CHA did not have to use other resources to fund the needed repairs.

There is no desire among the CHA officials interviewed to sell any more scattered-site public housing beyond that which has already been approved for sale. The lack of financing, public outcry, and a court order to integrate their housing stock were given as reasons. The scattered-site units are more likely to be in integrated neighborhoods, and selling these would increase the percentage of CHA units in minority neighborhoods. The CHA is, however, considering the sale of at least one of its non-scattered site developments.
Introduction

Denver's public housing homeownership demonstration is unique in several respects. First, it consists of two separate 44 unit cooperatives that are part of the same 448 unit Curtis Park housing project that was built in 1954. Second, Curtis Park is the most physically distressed project in the Denver Housing Authority (DHA) inventory and homeownership is being viewed as an integral part of a management strategy to revitalize the project and its surrounding neighborhood. Third, Denver's financing of both co-ops is very innovative. DHA provided construction financing for both Upper Lawrence, the first co-op, as well as for Arapahoe, the second co-op. The National Cooperative Bank and the Colorado Housing Finance Agency provided permanent financing for Upper Lawrence, while Arapahoe's permanent financing came through sale of Federal Low Income Housing Tax Credits, with the housing authority acting as the developer/syndicator, and from a housing authority direct loan. The second co-op took advantage of the Federal Low Income Housing Tax Credit with the housing authority acting as the developer/syndicator of the project. To access the tax credit, the project must remain in rental use for a minimum of 15 years. Thus, Arapahoe is a rental co-op with the tenant cooperative owning the land and serving as the general partner in a limited partnership that owns the improvements. A corporate limited partner investor purchased the tax credit for an upfront cash payment to the housing authority of $1,350,000. DHA plans to use the net syndication proceeds to acquire additional permanent low-income housing.

As discussed fully in the text of the case study, both of Denver's public housing co-ops, but especially Upper Lawrence, are suffering from a variety of management deficiencies. In Upper Lawrence's case, this has led to substantial turnover in the months following closing, a high vacancy rate, and serious financial deficiencies. The housing authority is currently working hard to improve management services, stabilize finances and revitalize the co-op. Whether it will be successful remains to be seen.

Managing the Demonstration

The Denver Housing Authority operates a wide range of housing programs, including conventional public housing (4,264 units), Section 8 (568 new construction, 442 moderate rehab and 1,233 certificates) and Section 23 leased housing (69 units). DHA also participates in HUD's rental rehab and housing voucher programs.
One hundred-fifty vouchers are tied to the rental rehab program, and 200 are free-standing.

DHA has also acquired and rents 82 housing units at market rents. Its ability to do acquisitions and rehab, and to finance the renovation of its public housing sales project comes from a $10 million revolving fund. The fund was granted from a $10 million bond issue that was originally intended to finance housing for athletes in the 1976 Olympics, which the city was planning to host until the citizens of Denver rejected the proposal. The plan was to turn the housing over to the PHA after the Olympics, but when the Olympics were not approved, DHA ended up with a $10 million dollar revolving fund to support its programs.

DHA's waiting list totals 800 families. Five hundred of the total are waiting for Section 8 certificates or vouchers while 300 are on the public housing waiting list.

DHA's program involves the redevelopment of two segments of the Curtis Park project. Phase I of the demonstration converted 44 row-type family units of public housing located at 33rd and Lawrence Streets into a limited equity cooperative named the Upper Lawrence Co-op. In the process, four buildings were demolished from the center of the block, thereby significantly reducing the family density, and allowing for the development of on-site parking and open green space areas for the purchasers. Phase II of the homeownership demonstration converted another 44 units in the same project located at Arapahoe and 26th Streets into a rental cooperative named the Arapahoe Co-op. As the name implies shareowners in the Arapahoe co-op do not have the same ownership rights as their counterparts in Upper Lawrence. The significant differences between these two types of cooperative ownership are more fully discussed later in this case study. Similar to Phase I, DHA demolished four interior buildings from the center of the Arapahoe project to reduce density, create on-site parking and open space for the residents. Unlike Upper Lawrence, however, the Arapahoe conversion includes virtually no one- or two-bedroom units which proved difficult to market, and many more three- and four-bedroom units for which there was a very strong demand. Merging small apartments into larger ones and adding additional amenities that were lacking at Upper Lawrence made it easier to market Arapahoe units. However, it also significantly increased rehabilitation costs, which is what motivated DHA to finance the Arapahoe conversion using the low-income housing rental tax credit.

The concept of the homeownership demonstration was endorsed by the Curtis Park Resident Council which reinforced DHA's position that homeownership opportunities would act as a catalyst to a broader improvement in the immediate environment and community. In a 1985 letter of endorsement, the Curtis Park tenant leaders
explained the basis of their support as well as their reservations about the proposed homeownership demonstration:

For several years the residents of Curtis Park have been interested in seeing their development improved. The possibility of a modernization program is important to us--it will improve our facilities, our living conditions, and provide the means to participate as full citizens in Curtis Park and surrounding neighborhoods.

It is our position that a homeownership component should be part of the modernization program. Some of us have lived in this development for many years. This is our home and this is where we want to live. To become actual home owners is a goal we have long sought.

A number of residents pay more than $250 each month for rent. If it is true that financing can be arranged so that payments will not exceed $250 per month, then you will have the support of Curtis Park residents... At the same time, it must be noted that the majority of residents will not qualify for homeownership. For them, the main concern is whether the ownership component will take away from the other aspects of modernization which we know will benefit all Curtis Park residents.

When the Denver Housing Authority was first awarded a HUD grant for this homeownership demonstration project, it hoped that a major impact could be made--not only in the existing neighborhood, but in the future of public housing as well. Staff, residents, city planners, community residents, and leaders embarked upon the arduous task of working together to obtain a common goal--the betterment of the neighborhood and an opportunity for ownership for current public housing residents.

The site selected was unique because it was in one of the older neighborhoods of Denver. It is adjacent to the urban sprawl of downtown; sections of the neighborhood had been designated as an historic district; and with the migration of young urban professionals to the community, the public housing project was viewed as an eyesore and a threat to neighborhood safety.

Although the city was not heavily involved with the PHA, the Denver Leadership Forum played a major role in supporting the PHHD. The forum, consisting of business leaders, city officials, and foundation representatives, committed itself to making an impact on housing and honed in on converting Curtis Park to homeownership. The forum proposed and legitimized the concept of public housing sales as a city objective. The PHHD proposal, however, was prepared by DHA staff. Motivation for preparing the proposal was to use homeownership as an incentive to help turn
around a difficult project as part of an areawide redevelopment program.

DHA had never sold any public housing units prior to the demonstration, although it demolished 252 units in 1979-80. The 40 demolished units for the two PHHD demonstration sites raised the total to 292, and this number will increase as the redevelopment of the remainder of the Curtis Park project proceeds. In fact, DHA officials believe the homeownership demonstration "significantly affected HUD approval for the demolition of buildings from the adjacent blocks of public housing, and the availability of Comprehensive Improvement Assistance Program (CIAP) monies to modernize the remaining housing stock."

Tenants were consulted in terms of the redesign of the units through a tenant survey. Some PHA commissioners were concerned about the replacement housing issue and some tenants worried about where they would end up. Most of the opposition, however, quickly faded. Tenants were given the choice of staying in other parts of Curtis Park (few chose this option) or being relocated to scattered-site housing. Some housing in this desirable inventory became available because DHA froze the vacancies in scattered-site housing 60 days prior to beginning relocation from Curtis Park. Another option was the use of Section 8 certificates or housing vouchers for relocation in private housing. Virtually all the alternatives were seen as more desirable than remaining in Curtis Park.

In addition to high-level executives, professional staff from several divisions of the housing authority and many individuals were involved in managing the homeownership demonstration. Unlike most other multi-family sites, the rehabilitation of all buildings involved in the demonstration was carried out by housing authority employees. According to DHA, "utilizing the Force Account to complete construction allowed the project to be as cost effective as possible." A large number of DHA employees helped relocate families to other housing so that rehabilitation of the homeownership units could take place. The operations department was responsible for marketing the units and for providing homeownership counseling. Site managers were individually responsible for evaluating the potential of individual families to assume the responsibilities of homeownership.

A sizeable number of DHA staff were involved in managing the demonstration. One staff member served as chief liaison with the co-op and was virtually full time on the PHHD. He was also the principal trainer and counselor. The PHA had a third party counseling contract with two counseling organizations.

Brothers Redevelopment, Inc. and Northeast Denver Housing, two experienced counseling groups were chiefly responsible for doing the initial eligibility or intake screening and loan
underwriting-type assessments. They were assisted by consultant Onka Dekka, from the National Foundation of Housing Counsellors in Washington, D.C. The counseling contract was negotiated as a result of a Request For Proposals (RFP) that DHA issued.

The $46,000 counseling contract was paid for with technical assistance funds received from HUD in the amount of $50,000. The remaining $4,000 was applied toward the legal fees incurred in creating the Upper Lawrence Cooperative. Total legal fees exceeded $40,000. The much more extensive legal, accounting, financing and related fees associated with the creation of the Arapahoe rental co-op were paid for out of the syndication proceeds that DHA received from the equity investor who purchased the low income housing tax credit that was generated by the rehabilitation of the project.

DHA estimates that between 1.5 and two staff FTEs were devoted to the demonstration. With the completion of the Arapahoe Cooperative, and the need to remarket several Upper Lawrence units that were vacated by the original purchasers, DHA created a new staff position to take charge of what were generally referred to as asset management responsibilities. With a background in community-based housing, the individual hired to fill this new position is spending a substantial amount of time on PHHD matters, thus increasing the DHA staff time associated with the homeownership program.

From almost the very beginning, the homeownership demonstration has suffered from serious communications problems between the home buyers and the housing authority. This is due partly to the fact that cooperatives are an entirely new form of homeownership in the Denver area and few families understood the implications of this kind of interdependent living. Also, since virtually none of the families who moved out of the units prior to renovation came back as home owners, the housing authority had to create an environment of mutual trust and a sense of community among families who did not know each other. Additional management problems with the demonstration will be discussed in other sections of the case study.

Selecting and Rehabilitating Properties

Phase one of the demonstration involved the sale of 44 units from a block originally containing 64 units. After demolishing 20 units, the co-op was formed and 44 families acquired shares in the co-op. The sale was closed in May 1987.

As indicated earlier, each of the cooperatives contain 44 row house-type units that are configured in a single square block with interior parking and open space. The co-ops, part of the larger Curtis Park development, are located on the edge of the Denver central business district next to a historic neighborhood and a gentrifying area. Nevertheless, the area still suffers from extensive housing problems, high crime rates, and an
assortment of social ills. A variety of revitalization activities are taking place in the immediate vicinity of the co-ops: some new construction on vacant lots, CDBG-financed public improvements, economic development projects sponsored by EDA, and private reinvestment in housing and retail strip development that DHA attributes to the PHHD. Also, the city has revitalized Curtis Park, for which the nearby housing project is named. According to DHA, Curtis Park was selected for inclusion in the homeownership demonstration because it was one of the housing authority's most troubled projects and the source of severe management problems. The concept was to use homeownership as part of a broad-based strategy to reverse the cycle of decay and distress.

Curtis Park was completed in 1954 at a cost of $4,596,911. The project is a row-type development located within the area bounded by 25th and 34th, Arapahoe and Lawrence Streets. The project consists of 74 separate buildings which contain a total of 448 housing units. The interior of the buildings are configured to provide 68-one bedroom units, 224-two bedroom units, 103-three bedroom units, 44-four bedroom units and 9-five bedroom units.

Two separate HUD-funded rehabilitation projects had been undertaken at Curtis Park before part of the development was selected for sale. The first was a $1,550,000 modernization project in 1977-78. The work included the following items:

1. New kitchen cabinets and fixtures;
2. Installation of forced air furnaces, water heaters and new electrical service; and
3. Replacement of unit water supply lines.

The second project was accomplished with CDBG funds in 1980. With these funds smoke detectors were installed and work was done on window security.

The part of the project to be sold in Phase One of the demonstration received extensive additional renovation. This rehabilitation process involved significant input from prospective buyers. The authority's architect and a privately contracted architectural firm interviewed individuals in the neighborhood and examined existing units. The condition of the blocks showed dense building coverage that provided no security and no green space.

Potential home buyers were very specific about the needs they wanted addressed:

1. They wanted a distinct definition of ownership;
2. They wanted the project to provide safety and security features;
3. They wanted a place for their children and families to play; and

4. They wanted secure off street parking.

The architects decided they must start from the interior of the site. They demolished four of the center buildings (20 units) which provided open space. This area is now cut into four small parking lots and seven small green space areas. Playgrounds created in the center of the existing buildings are easily seen from the units.

In addition, small fences have been erected in the front and back yards to help foster a sense of ownership and territoriality. Fences along the outside of the development further enhance this scheme. Further security is provided by the courtyard lighting and all units are equipped with alarm systems.

The townhomes duplicate the entry of the single family homes in the neighborhood as they go from the sidewalk, to a fenced yard, to the front porch, to the door. All existing power and phone lines were buried underground to add to the aesthetic beauty of the development.

The architects and the Denver Housing Authority staff felt if they could establish a situation where residents could feel a sense of pride and could believe their unit and yard was really theirs, then they would be more likely to accept the responsibility of upkeep. The design was aimed toward creating a sense of ownership.

Renovations cost a total of $983,364, or $22,349 per unit. These are hard costs only and do not include soft costs such as architectural design and supervision fees; financing costs; demolition; appraisals; relocation costs; legal costs for closing loans and establishing the co-op; and co-op training (including costs of PHA staff allocated to training).

The Upper Lawrence renovations included:

- all new plumbing and electrical systems;
- new furnaces and ductwork;
- new hot water tanks;
- kitchen cabinets disposals, sinks, faucets and ranges;
- new thermopane anodized windows;
- patching and texturing walls;
- reglazing old bathtubs, installing new tub and shower valves;
- new lavatories and vanities, lights and toilets;
- jambs and doors on all closets, metal insulated doors on back and front;
- new carpeting and vinyl floor covering;
-Replacing old tar and gravel roof with 3/4 inch plywood and new roof dormers fabricated from metal;
-Installing R-30 insulation in attic;
-Installing all new playground equipment in the common area; and,
-Installing gutters on the front of roofs and security systems in each unit.

The renovation costs for Arapahoe averaged a much higher $35,000 a unit due to the need to reconfigure the project and the addition of more amenities that DHA believed were necessary for marketing. Each Arapahoe unit was equipped with new kitchen cabinets and range, refrigerator, furnace, hot water heater, garbage disposal, security system, thermal windows, fenced front and rear yards, and a sprinkler system in the common area. Neither co-op was equipped with washers and dryers which was a big disappointment to home buyers.

The redesign of the Curtis Park units included in the homeownership demonstration was prepared jointly by a consulting architect and the DHA's own architect. All renovation was carried out by Denver Housing Authority crews which is very unusual for a project of this magnitude.

The PHHD units are being renovated to a higher standard than are other units in Curtis Park that are being renovated using HUD modernization funds. CIAP units receive the same plumbing and electrical treatment, but a lower grade of kitchen cabinets. The facades in units repaired using modernization funds are not as detailed nor is there any carpeting, or texturing of walls. Units repaired with modernization funds do receive, however, the same energy-efficient windows.

Attracting and Selecting Owners

The PHA staff determined that $12,000 income should be the minimum threshold based on an average rent of $250 per month plus utilities, and a housing expense to gross income ratio of around 30 percent.

All households in Curtis Park and other public housing projects with incomes of at least $12,000 were sent letters informing them of the demonstration. The PHA's newsletter was used to publicize the program and PHA staff attended tenant council meetings to discuss the program.

Demand for units varied with bedroom count. Demand was very strong for three- and four-bedroom units and much weaker for one- and two-bedroom units. The DHA eventually had to use a lottery to select tenants for larger units and do intensive marketing to fill smaller ones.
Priority criteria for filling large units included income at or above $12,000; one full-time employed household member; residency in Curtis Park; and an $800 down payment.

Because of higher rehab costs, a different financing method and serious marketing, operating, and turnover problems at Upper Lawrence, which will be discussed later, the housing authority tightened qualifications for admission into the Arapahoe co-op. While maintaining a maximum 30 percent housing expense ratio, higher projected monthly carrying costs that ranged between $295 and $350, caused DHA to raise minimum income requirements to $12,500 for a one-bedroom unit, $13,360 for a three-bedroom unit, and $14,000 for a four-bedroom unit. Second, past payment records of applicants were scrutinized more carefully and housekeeping practices were assessed through an in-home visit. Finally, in order to be considered for admission into the Arapahoe homeownership project, public housing tenants had to be recommended in writing by the manager of the project where they currently resided. The latter requirement placed on-site managers, who have more frequent contact with residents than any other housing authority employees, in pivotal positions.

Upper Lawrence owners have an average income of $14,140 per year. Seventeen of 44 owners (38.6 percent) are married couples, 22 (50 percent) are single females and five (11.4 percent) are single males. The average owner has 1.5 children under 16 years of age. Twenty-two (50 percent) of all owners are black, 18 (40.9 percent) are Hispanic and four (9.1 percent) are white. The average age of the owners is 38.6 years, and ranges between 20 and 67 years.

The incomes of Arapahoe cooperators average around $17,000 a year. While this is only about $3,000 more than in Upper Lawrence, there is a general consensus among those most closely associated with the demonstration that Arapahoe owners not only have more stable incomes than their Upper Lawrence counterparts, but incomes that are much more likely to increase over time. This is because more Arapahoe wage earners hold technical and managerial positions, and are less likely to be laid off. They are also more likely to have fringe benefits that include health insurance which means that, in times of sickness, they are also less likely to forego making their co-op mortgage payment in order to pay medical bills. The higher income also means that if Arapahoe buyers do fall behind, they have more resources to make-up the deficiency reasonably quickly. However, once an Upper Lawrence family falls behind, delinquency problems are more likely to increase, with the family falling further and further in debt.

The qualitative and quantitative differences in the incomes of the two co-ops is reaffirmed by interviews with the co-op's managing agent. As of August 1989, approximately one-third of all Upper Lawrence home buyers were behind in their housing payments, compared to a fifth of Arapahoe households. Moreover,
turnover is much greater in Upper Lawrence than in Arapahoe. According to DHA officials, between September 1988 and August 1989, at least 12 of Upper Lawrence's 44 units had vacancies, which translates to an annual turnover rate of 27 percent. Five units (10 percent) were vacant and unsold in August 1989.

According to the director of the demonstration, 50 percent of median is too low a threshold for an ownership program. Reflecting on the income differences between the two co-ops, he indicated that Upper Lawrence cooperators are just too close to the economic margin to deal with the obligations of homeownership. They have no family or relatives to rely on in case of a layoff or other emergency and they are more likely to walk away from their obligations in times of stress and financial need.

Members of the Arapahoe board of directors indicated that three of their units turned over during the first year of operations. They attribute this to the fact that DHA was under pressure to fill all the units by October 1, 1988, so that the project would generate its full complement of tax credits for the calendar year. (The tax credit issue is fully discussed in the financing section). The board believes that DHA accepted several buyers into the co-op for financial reasons who were not "homeownership material," and that additional turnovers will occur during the next six months as the "weeding out process" continues.

Under both co-ops' regulatory agreements, DHA pays all carrying charges and accumulated delinquencies on vacant units once they are turned over to the housing authority for remarketing. If the co-op chooses to remarket a vacant unit, it is responsible for all past-due payments and all carrying charges that accumulate during the marketing period. Because it no longer has confidence in DHA to represent the co-op's best interests, the Arapahoe board plans to take responsibility for marketing all vacancies despite the unaffordable financial burden associated with this course of action.

The board of directors screens all potential buyers. Applicants are also interviewed by the co-op's managing agent. Then, DHA runs a credit check, and if that turns out all right, the membership committee conducts an in depth interview to "determine whether the individual has the right attitude to be a co-op member."

**Property Conveyance**

**Upper Lawrence**

The decision to create a co-op at Upper Lawrence rather than a condo was based largely on DHAs feeling that individual tenants would never be able to qualify for $18,000 mortgage loans. Also, they felt that the interdependencies built into cooperatives, the
joint decisionmaking, was important in bringing families together to fight neighborhood decline.

It must be kept in mind that cooperatives are very rare in Colorado and a great deal of education about co-ops was necessary to sell the program.

From an individual buyer's perspective, the financial requirements for an Upper Lawrence unit are as follows:

<table>
<thead>
<tr>
<th>Amount</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>$800</td>
<td>down payment</td>
</tr>
<tr>
<td>18,000</td>
<td>pro rata share of co-op's $800,000 blanket first mortgage loan</td>
</tr>
<tr>
<td>8,500</td>
<td>second mortgage from the DHA payments start at $10/month and increase to $32/month in 5 years for remainder of 25 year term.</td>
</tr>
<tr>
<td>2,273</td>
<td>pro rata share of $100,000 grant from the Colorado Division of Housing</td>
</tr>
</tbody>
</table>

$29,573 Total price of unit

Because the PHA's second mortgage will be paid off so slowly and will be kept in force as co-op shares are sold to income-eligible buyers in the future, and because the pro rata share of the state grant does not have to be repaid, DHA advertises the sale price as being $18,800, rather than $29,573.

For buyers who do not have the $800 in cash for the down payment, the Denver Families Housing Corporation, a local non-profit, will finance from $100 to $600 of it, to be repaid over five years.

The DHA has agreed to indemnify the co-op against defaults on individual co-op shares as a condition for securing the permanent financing from the Colorado Housing Finance Agency and National Consumer Co-op Bank. This means that the DHA will acquire co-op shares of individual share holders who fail to meet their carrying charge obligations. Also, the co-op's Articles of Incorporation provide for the DHA taking control over the board if emergency conditions should warrant such extreme action. Therefore, neither of the partners in the co-op's permanent financing are exposed to any substantial risk of loss.

It is important to note that the $200,000 loan from the Colorado HFA came from the agency's reserve funds rather than from any of its multi-family financing programs. This is because the co-op could not qualify for these programs because of mortgage insurance requirements as well as for cost reasons. With respect
to the latter, for example, DHA officials indicated that separate surveys of each of the 44 units in the co-op would have been necessary if the financing were to come from CHFA's regular multifamily programs. Because co-op units are in 2-story buildings containing six-eight units per building, with larger units overlapping the second floor of smaller units on the first floor, individual surveys would have cost $5,000 per unit.

Although DHA's target was $250, initial co-op charges at Upper Lawrence averaged a substantially higher $329 a month. Moreover, because of DHA's failure to properly account for property taxes in the co-op's initial budget an unanticipated increase in water charges and fire and liability insurance, and because DHA's second mortgage had a built-in annual increase, within about a year of closing the co-op's carrying charges had to be raised by $10 a month. The breakdown of the projected pro forma costs is as follows:

<table>
<thead>
<tr>
<th>Cost</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>$160.00</td>
<td>pro rata share of co-op's first mortgage</td>
</tr>
<tr>
<td>10.00</td>
<td>DHA second mortgage</td>
</tr>
<tr>
<td>85.00</td>
<td>co-op carrying charge</td>
</tr>
<tr>
<td>55.00</td>
<td>utilities</td>
</tr>
<tr>
<td><strong>$310.00</strong></td>
<td><strong>Total</strong></td>
</tr>
</tbody>
</table>

The carrying charge varies from $80-$95 per unit depending on the number of bedrooms.

Closing costs for all 44 Upper Lawrence units totaled $112,500, or $2,557 per unit, excluding prepaid taxes. Individual components of the closing costs are:

- Points on permanent loan: $24,000
- Attorney's fees: $50,000
- Title insurance: $10,000
- Appraisal fee: $4,500
- Prepaid insurance: $16,000
- Surveyor's fee: $8,000
- (Excludes prepaid taxes)
- **Total**: $112,500

There are three legal documents that had to be prepared in order to create the Upper Lawrence Co-op as an independent entity from the rest of the Curtis Park project. All legal papers were drawn up by a Denver law firm. The three documents are the occupancy agreement, the subscription agreement, and the co-op bylaws. No tenants were involved in the preparation of the bylaws. A summary of each of the legal documents follows.
The occupancy agreement between the Upper Lawrence Cooperative Corporation and the buyer provides for the stockholder's (buyer) ownership of a certificate of one share of stock of the corporation and proprietary rights to occupancy of a designated housing unit within the project.

The occupancy agreement spells out the owner's responsibilities to pay carrying charges of the co-op which the board of directors shall set at least annually, or at more frequent intervals should circumstances so require. The agreement provides for payment of late charges after the tenth day of the month.

Stockholders may not sublease their unit without prior written consent of the corporation, except for one period of not more than 90 days per calendar year, if stockholder's permanent residence remains at the unit and the stockholder is temporarily gone from Denver for the period.

In the event of death of stockholders, heirs to the stock can occupy the unit for 60 days as long as they pay carrying charges. If eligible to become an owner, the corporation will enter into a replacement agreement for occupancy of the unit as long as all back charges are made current.

Stockholder may not make any structural alterations in the unit without written consent of the corporation.

One long article (XIII) deals with the definition of default by the stockholder and its effects. The article details definitions of default, which include ceasing ownership of the stock for any reason, failure to make payments required by this agreement, a wrongful assignment of the agreement, sublet, or a material default in the performance of a material obligation of the agreement. This article details hearing and eviction procedures.

This agreement also provides for membership in the Upper Lawrence cooperative at a specified price and terms:

\[
\begin{align*}
$800 & \quad \text{Downpayment} \\
18,000 & \quad \text{Pro-rated amount financed by Blanket Mortgage} \\
18,800 & \quad \text{Total purchase price}
\end{align*}
\]

The agreement also identifies the stockholder's dwelling unit.

All owners are subject to the regulations contained in the bylaws. The bylaws contain the following eligibility requirements:

1. Members must have an income \leq 50\% of median under HUD guidelines, subject to approval of lender or guarantor or indemnitor
of mortgage loan, solely to evaluate applicant's credit worthiness. A guarantor or indemnitee of blanket mortgage debt owed by the corporation is eligible to own stock in the Corporation if it acquires stock as a result of guarantee or indemnification.

2. Board of Directors must approve all members. Applications may be rejected for any reason except race, color, religion, creed, national origin, sex, or age.

Each stock certificate has one vote. Majority vote of a quorum of membership is necessary for action to be taken by the corporation. Twenty-nine votes are necessary for a quorum.

Denver Housing Authority has special non-stock membership in the corporation. DHA members may attend and participate in meetings but can only vote if it takes ownership of share(s) through warranty or indemnification, or if it takes control of the corporation under its extraordinary powers specified in the co-ops articles of incorporation.

The bylaws call for the corporation to have a president, one or more vice presidents, a secretary and a treasurer. All officers will be elected by the board and hold office at its pleasure. All officers must be stockholders of the co-op or employees or authorized agents of the DHA members.

The co-op's articles of incorporation also provide for residual interest of DHA in the cooperative corporation (the corporate member). The corporation may not, without prior written approval of the corporate member, take any action that results in a default under terms of any mortgage to which the corporation is a party. If the board fails to meet for two calendar months, fails to meet at two consecutive special meetings, or if the board fails to perform any of its obligations under the bylaws, the DHA corporate member may exercise its "extraordinary powers as follows: Effective immediately upon giving written notice, the stockholder members right to vote, including the right to elect or remove directors, shall be suspended and such right to

1 These same emergency powers, which were also included in Arapahoe's bylaws, have become an area of disagreement between HUD and DHA over the concept of homeownership. Simply put, are the rights and entitlements generally associated with homeownership consistent with a legal arrangement that gives the public housing authority extraordinary powers to take over management and financial control of the co-op in the event of a major crisis? Although HUD did not formally raise an objection to DHA's continuing presence on the co-op's board of directors in Upper Lawrence, it did in the case of Arapahoe. This is because of the unique way that the Arapahoe co-op was financed, which is discussed in the following section.
vote shall be vested in the corporate member. The cooperate member may exercise extraordinary powers as long as it deems necessary." The initial board of directors has three DHA members: the PHA director; the PHA general manager; and the PHA director of planning.

Arapahoe

As will be fully discussed in the financing section, DHA's second conversion under the homeownership demonstration was structured as a rental co-op to take advantage of the federal low income housing rental tax credit. Consequently, the legal and institutional structure of the Arapahoe Co-op is quite different from those of Upper Lawrence. The most important difference is that the co-op does not own the public housing units its members occupy, at least not during the first 15 years of the co-op's existence. Among the legal documents unique to Arapahoe are a limited partnership agreement that defines the structure of the project's ownership and financing and details the rights and obligations of the partners, including the co-op, DHA and the limited partner investor. The agreement also spells out the means by which the co-op will be able to acquire the buildings its members occupy at the end of 15 years. Additional legal documents pertain to the tax credit, including an application for registration of the project as a tax shelter, and legal opinions attesting to the project's eligibility to receive rental tax credits.

DHA maintains non-voting membership on the Upper Lawrence board of directors to protect its long-term financial interests in the co-op as an indemnitor of its permanent mortgage lenders. Similarly, as a special limited partner in the Arapahoe conversion, DHA maintains certain extraordinary management controls over the co-op's operations to protect its own financial interests as well as those of the limited partner who acquires the project's tax credits. Among DHA's powers that are unique to the Arapahoe conversion are those pertaining to the prior approval of every new co-op member. This is because of the federal penalties for admitting an income-ineligible tenant in a rental tax credit project and the fact that DHA is indemnifying the limited partner against loss of tax credits. Also, under the partnership agreement, the co-op may not amend its bylaws without the written approval of DHA. These and other DHA controls over the co-op have become the subject of serious disagreement with HUD, which has not yet certified that Arapahoe meets the legal requirements of a Section 5(h) conversion.

Financing

Upper Lawrence

Because the Denver Housing Authority has a $10 million revolving source of capital to support development and other programs, its
financing program for the PHHD demonstration is unique among participating PHAs.

For one thing, extensive rehabilitation totaling $983,364 in hard costs ($22,349 per unit) were entirely financed from DHA's own funds. That is, no HUD modernization or other federal funds were used for the renovations. This allowed DHA to reserve CTAP funds to modernize the remaining units in the Curtis Park project, of which the PHHD Upper Lawrence co-op was a part. This also meant, however, that if DHA did not obtain outside financing for the co-op's permanent blanket mortgage loan, it would be out a lot of money for an extended period of time.

DHA was successful in securing outside financing for the co-op. Financing arrangements were as follows:

- $100,000 (non repayable) grant from the Colorado Housing Finance Agency (not to be used for administrative expenses)
- $200,000 9.5% 25 year loan (not to exceed 12.5%, over the life of loan) from CHFA reviewable after three years
- $600,000 loan 9.5% (same terms as above) from the National Consumer Co-op Bank
- 35,200 equity pay-in from 44 buyers

$935,200 Total

The $200,000 loan from the Colorado HFA did not come from its normal homeownership financing program. Rather, it came from CHFA's reserve funds. The co-op did not qualify under any of the agency's mortgage programs. The loan posed few risks to CHFA since DHA committed to indemnify the co-op the amount of money owed by defaulting shareholders to maintain the co-op's ability to keep its blanket mortgage current.

The Denver Housing Authority provided interim financing for the rehabilitation of the Upper Lawrence Co-op. The construction loan was largely retired from the proceeds of the permanent loans from the Co-op Bank and Colorado Housing Finance Agency (CHFA) and the CHFA grant. Although the Upper Lawrence Cooperative is heavily encumbered by mortgage debt and some of the shareholders are even more burdened because they needed additional loans to finance their down payments, the co-op holds title to all 44 Upper Lawrence units and the land associated with them. With each cooperator owning a pro rata undivided share of the co-op's property and having a proprietary right to occupy a given unit indefinitely into the future, and to sell that right to others, the conversion meets all of the commonly accepted conditions of homeownership as well as the technical requirements for Section
5(h) public housing sales. Despite its extraordinary degree of creativity, this is not the case with respect to the Arapahoe conversion.

Arapahoe

In contrast to Upper Lawrence, the financing for the Arapahoe conversion was structured to take advantage of the low income housing tax credits that were created in the 1986 Tax Reform Act. Since the tax credits were created to stimulate the construction or rehabilitation of low income rental housing by equity investors, rather than sales housing by owner-occupants, DHA structured the Arapahoe conversion as a rental co-op rather than as a conventional homeownership project. This means that rather than title to the housing being initially vested in the cooperative corporation itself, it is vested in a third party which then leases the housing to the co-op. As a member of the co-op, each shareholder owns one share of stock or 1/44th of the corporation. Because ownership of a stock share entitles the bearer the exclusive right to lease and occupy a specific unit from the corporation, the right to sell that share for a profit, and gives the Arapahoe Cooperative Corporation the exclusive right to purchase the buildings at the end of 15 years, DHA believes that there is little practical distinction between the rights and entitlements of Upper Lawrence and Arapahoe buyers. However, this is not the view of either HUD or several members of Arapahoe's board of directors who believe that the Arapahoe conversion is inconsistent with both the spirit and intent of Section 5(h), and fails to provide shareowners the independence and security that is commonly associated with homeownership. Details of the financing are presented below.

The centerpiece of the Arapahoe conversion is the Arapahoe Redevelopment Partnership, Ltd., a limited partnership consisting of three partners. The general partner is the Arapahoe Cooperative Corporation, whose shareholders are the 44 former public housing tenants who want to become homeowners. The two limited partners in the partnership are a private investor (a local corporation) which has acquired the low income tax credit that has been generated by the substantial rehab of the project, and the Denver Housing Authority. For reasons to be discussed below, DHA's legal status is as a special limited partner.

As the general partner, the co-op owns the land under the buildings and controls the partnership's daily activities through the Management Services Agreement and the Limited Partnership Agreement. As the special limited partner, DHA monitors the property's operation. Both the limited partner and DHA have the power to vote on certain important partnership decisions and to remove the cooperative as the general partner if the cooperative does not properly manage the affairs of the partnership. According to DHA, this extraordinary degree of potential control over co-op affairs is necessary for three reasons: to protect the co-op by providing a safety net in the event it gets into
serious financial and other operating problems that could jeopardize its long term viability; to ensure that the co-op does not violate any of the provisions of the tax laws that would trigger a recapture of the tax credit acquired by the limited partner; and to protect DHA's own long-term financial interests. The latter requirement is due the fact that, unlike the Upper Lawrence conversion where the housing authority's financial exposure was for only a short time because its construction loan was taken out by permanent mortgages provided by others, DHA is the permanent lender for the Arapahoe conversion.

After the cooperative and the limited partnership were formed in late August, DHA sold the buildings and other facilities to the partnership in exchange for cash from the limited partner and a promissory note from the partnership in the amount of $1,650,000, which was the approximate amount of the cost of redeveloping the Arapahoe project. The note has a fixed interest rate of 5.25 percent and carries a 25 year term. The substantial rehabilitation of the Arapahoe project is projected to generate nearly five million dollars in federal income tax benefits through the low income housing tax credit provisions of the 1986 Tax Reform Act. Acting as its own syndicator, DHA sold those tax benefits to a local corporate investor for a one-time payment of $1,350,000. Thus, DHA received a substantial amount of cash up-front from syndication proceeds plus it receives monthly debt service payments on the permanent mortgage.

As indicated earlier, DHA transferred title to the project's land to the co-op at a price of one dollar, but made the transfer subject to a 25-year ground lease. The partnership will pay a ground rent of one dollar per year for the first 15 years of the lease. If the partnership continues to lease the grounds for the last 10 years of the lease, it will have to pay the grounds full rental value for each of the last 10 years. Increasing the ground rent to market value after 15 years, which is when the holding period for the tax credits expires, is intended to force the partnership to sell the buildings to the cooperative. At this point, the cooperative would own the land and buildings subject to DHA's outstanding first mortgage. In this way, the buildings will remain low income housing for an indefinite period. Simply put, since the use restrictions on the buildings require low income occupancy, once the ground lease payments rise to market levels, the partnership will not be able to earn sufficient income from the property to maintain an economic investment and will sell it to the cooperative. Another factor favoring this option is that even without a sale, title to the improvements would revert to the cooperative upon expiration of the ground lease.

Sale of the buildings to the partnership was also subject to a long term lease with the co-op. The monthly lease payments of $9,888 are equal to the debt service on DHA's permanent mortgage loan. With 44 co-op units, the pro rata rent payment for debt service averages $225 a month. This level of debt service, which
was determined by DHA to be affordable to co-op members, was arrived at by reducing the interest rate all the way down to 5.25 percent. Under terms of the lease, in addition to the rent (debt service), the co-op is also responsible for meeting all other fixed and variable costs of operating the project, including property taxes, insurance and all maintenance, management reserve and related expenses, which are estimated to average around $110 a month per unit. A breakdown of Arapahoe's first year carrying charges, excluding debt service follow:

<table>
<thead>
<tr>
<th></th>
<th>Annual</th>
<th>Per Unit/month</th>
</tr>
</thead>
<tbody>
<tr>
<td>Property insurance</td>
<td>$4,248</td>
<td>$8.05</td>
</tr>
<tr>
<td>Real Estate Taxes</td>
<td>13,360</td>
<td>25.30</td>
</tr>
<tr>
<td>Replacement Reserve</td>
<td>10,000</td>
<td>18.94</td>
</tr>
<tr>
<td>Water/Sewer/Wastewater</td>
<td>13,000</td>
<td>24.62</td>
</tr>
<tr>
<td>Area Electrical</td>
<td>1,100</td>
<td>2.08</td>
</tr>
<tr>
<td>Management (4.5%)</td>
<td>7,700</td>
<td>14.58</td>
</tr>
<tr>
<td>Maintenance</td>
<td>8,640</td>
<td>16.36</td>
</tr>
<tr>
<td></td>
<td><strong>$58,048</strong></td>
<td><strong>$109.93</strong></td>
</tr>
<tr>
<td>Plus Debt Service</td>
<td><strong>$118,800</strong></td>
<td><strong>$225.00</strong></td>
</tr>
<tr>
<td>TOTAL CARRYING CHARGES</td>
<td><strong>$176,848</strong></td>
<td><strong>$334.93</strong></td>
</tr>
</tbody>
</table>

Arapahoe has not been in occupancy long enough to judge the accuracy of these estimated carrying charges.

The cooperative has an option to purchase the buildings from the partnership after 15 years at the greater of the market value of the property or the outstanding balance of DHA's mortgage, which will be $922,000. Since the combined effects of the ground lease restrictions and the continuing low income use restrictions of the buildings will depress market value, the co-op is virtually guaranteed the right to acquire the buildings at the price that will require debt service payments that are the same as the co-op's rent.

Because it has become an item of major concern to HUD, one final element of Arapahoe's financing must be discussed. As part of its efforts to maximize the equity investment, and to provide the limited partner with a competitive rate of return, DHA felt it had to give the limited partner an absolute assurance that it could sell its interests in the partnership at the end of 15 years at a price that was known at the time of the initial closing. Moreover, that price would have to be sufficient to pay the limited partner's tax liability on the sale to DHA. This was accomplished by giving the limited partner a "put" option, exercisable at the end of 15 years, to transfer its partnership interest to DHA at a known price. The price was negotiated to be approximately $691,000.
Agreeing on a price and assuring the limited partner that the DHA will have the necessary $691,000 available to satisfy the put option 15 years into the future are two different things. The creative way that this problem was resolved was for DHA to acquire a sufficient quantity of deep discount zero coupon U.S. treasury bonds having 15 year maturities to accumulate to a value of $691,000 in the 2003. Since current T-bill interest rates, which were around nine percent, were known at the time of closing, it was a simple matter for DHA to determine the face value of the bonds that had to be acquired in order to accumulate $691,000 in 15 years. The amount was approximately $167,500. DHA used a portion of the limited partner's $1.35 million in equity contributions to pay for the bonds, as well as to underwrite all other costs of syndicating the tax credits.

Under DHA's resale scenario, the limited partner is certain to exercise its put option at the end of 15 years, at which time DHA will transfer ownership to the buildings to the co-op at a price equal to the outstanding value of the mortgage. With just 10 years remaining on DHA's note, this means that the co-op will own all land and buildings associated with the Arapahoe Cooperative free and clear, at the end of 25 years.

**HUD's Objections to the Financing**

At the time of this writing, HUD and DHA have been unable to resolve their differences in opinion as to whether the conversion of Arapahoe meet the requirements of Section 5(h). According to HUD, such "a sale must vest the tenants with rights incident to ownership, such as possession and control of the project (both land and improvements) upon conveyance [and] we cannot see such evidence of ownership in the Phase II sale." HUD specifically objected to four aspects of the Arapahoe conversion. HUD's first concern is whether tenants participated in the design of the co-op. Because of the complexity of the co-op's financing, HUD is worried that if tenants were not involved in the formative stages of the conversion, they could have been misled into thinking that they were buying into a limited equity co-op when, in fact, they would be renters for a minimum of 15 years.

HUD's second concern relates to the substantial control that DHA and the limited partner can exercise over the co-op:

The control over the co-op by the DHA should be modified to eliminate or significantly limit its authority over the co-op's operations regarding approvals and decision-making. If sufficient justification exists for the DHA to retain these extraordinary powers, safeguards must be provided to protect the rights of the tenants, the intended beneficiaries under Section 5(h). Safeguards should include stringent procedures for the exercise of the DHA's extraordinary powers, an independent determination that the exercise of such power is
justified by the facts, and, when exercised, provisions included for the immediate return of the control to the tenants upon correction of the cause. Lastly, the DHA control over the co-op should be terminated at some point.

The authority of the special and limited partners to remove the co-op (tenants) as general partner of the partnership should be eliminated or substantially modified to limit removal to instances of serious cause, in compliance with specific procedures protecting the rights of the tenants, and upon correction of the cause for removal, the co-op should be reinstated as general partner.

Third, although conveyance of the project to the co-op at the end of the lease term must occur in order to satisfy the requirements of Section 5(h), HUD believes that the current 'option to purchase' clause in the lease agreement is too conditional to assure conveyance at the end of the 15-year lease term.

Finally, HUD raises concerns about whether the co-op will be able to afford to acquire the project at the end of the lease term. It will be recalled that DHA structured the transaction so that the sale would occur at the greater of the market value of the improvements or the outstanding balance of the mortgage note, which will be approximately $922,000 15 years into the future. Since continued low income use restrictions on the buildings and an increase in ground rent to full value should depress market value to a level below DHA's note balance, the co-op's acquisition price should be equal the note's balance, with debt service payments no different from the rent the co-op paid the partnership for the preceding 15 years. Despite this fact, HUD questions DHA's rationale for suggesting that the co-op will be able to pay market value for the buildings in 15 years if they cannot now, and then further complicates the issue by choosing to interpret the value of the limited partner's put option as the equivalent of a sales price rather than as a negotiated component of the investor's internal rate of return. This leads HUD to conclude that DHA is operating on a two-track pricing system that discriminates against the co-op. According to HUD, by acquiring the limited partnership interest for $691,000 and then immediately selling the improvements to the co-op at a price equal to the outstanding mortgage balance ($922,000), DHA is not being fair to the tenant buyers.

HUD's recommendation on the pricing matter is to replace the current lease agreement with an option to buy with a formal lease/purchase agreement. HUD believes that if DHA were willing to give the co-op some credit from the rents paid at the end of the lease term it would be able to sell the buildings to the co-op for the same $691,000 price of the limited partner's put option. If DHA were to agree to HUD's proposal, it would have to
write down its mortgage note because the sale price would be lower than the outstanding loan balance.

DHA's response distinguishes between "tax" and "real" ownership and control of the project. It argued that the former is vested in the limited partner and the latter in the co-op. With respect to the co-op's financial stake in the partnership over time, DHA argues that "effectively by structuring the transaction to cause the buildings to be purchased through an assumption of the DHA note, the cooperative is being given equity in the project created by (a) capital contributions of the limited partner which were used to redevelop the property, and (b) principal payments on the DHA note throughout the initial 15-year period." Finally, on the matter of the dual pricing system, DHA argues

(a) this is a method to provide a return to the limited partner investor without requiring the cooperative to provide such return through its purchase option; (b) the put option between DHA and the limited partner has no effect on the option price when the cooperative acquires the improvements pursuant to its purchase option; and (c) by having DHA and the cooperative as partners in the Partnership, the cooperative will be able to exercise its purchase option through assumption of the DHA note. DHA, as the then-limited partner, will not be looking for any return on investment and will desire an assumption of its note only. Thus, the put option is one of the methods used to ensure that the cooperative will be able to exercise its purchase option merely through an assumption of the note payable to DHA.

Finally, because most of DHA's out-of-pocket costs of rehabilitating the Arapahoe units will be recovered through repayments on the $1,650,000 permanent loan it extended to the partnership, HUD has taken the position that the $1,350,000 DHA raised from sale of the tax credits represents an undeserved profit. DHA netted approximately one million dollars from the sale of the tax credits after deducting all syndication costs, including the purchase of the 15 year deep discount treasury bonds that will enable the housing authority to acquire the limited partner's partnership interest when it exercises its put option 15 years into the future. DHA plans to use the million dollars to acquire 34 privately-owned condominium units for use as permanent, low-income housing. Rather than being condemned by HUD for profiteering, DHA believes that it should be praised for creating a financing mechanism that not only accomplishes the homeownership goals of the demonstration, but generates additional revenues it can use to expand its permanently affordable inventory that will not require federal public housing operating subsidies.
Counseling

Recognizing the importance of training and that such skills were not available in-house, the housing authority had two choices: either to enter into a third-party contract that would provide all the educational and training needs required by the co-op or to bring in an outside firm to train a core group of PHA staff who would then train the home buyers. The housing authority chose the latter option. In response to an RFP it issued in the spring of 1987, DHA executed a $46,000 short-term counseling contract with a consortium of organizations consisting of two local entities (the Northeast Denver Housing Center, a black organization, and Brothers Redevelopment, Inc., a Hispanic agency serving the western part of the city) and an organization from Washington, D.C. (the National Federation of Housing Counselors). These organizations were to help with preliminary marketing, screening, and credit counseling tasks, and to train housing authority staff in the nuts and bolts of a cooperative conversion.

DHA staff indicated that a substantial amount of time and effort had gone into training the Upper Lawrence co-op board. Board members indicated that everyone was learning together, including the DHA trainers and that they, the board, needed more training before they would feel confident running a co-op.

Although at the time of the closing of the Upper Lawrence Co-op, DHA had no plans for instituting a formal post-purchase counseling program by a third party, Northeast Denver Housing was preparing a proposal for submission to the housing authority that would continue home buyer training. That proposal was never approved by DHA. However, because of the co-op board's lack of confidence in its own governing ability and deteriorating relationship with DHA, it hired an attorney to represent the co-op's interests. While the attorney was probably helpful in convincing DHA to make certain building repairs that were due to construction defects, he proved to be a costly and divisive figure in the co-op's initial year of operation and was eventually fired by the board.

Additional training for Upper Lawrence board members and the initial training of the Arapahoe board was provided by a local management company named WHERE, Inc. WHERE, which currently owns and manages three low-income mobile home co-op parks in the Denver area, is now under contract to manage both public housing co-ops at a flat fee of $6,000 for the first year. The two main principals of the management firm advise both boards on a wide range of matters, represent their interests before DHA, and devote substantial amounts of time to helping both boards seek sources of outside funding for a variety of much-needed services and improvements.

Finally, it is important to note that the very disappointing experience with Upper Lawrence's initial efforts to be a self-
managing co-op led to the decision to have Arapahoe professionally managed from the very beginning.

The conversion model adopted by the Denver Housing Authority differs from all other demonstration participants. The buildings that were converted to the Upper Lawrence Housing Co-op under the PHHD required extensive rehabilitation that necessitated the relocation of all tenants. Under the demonstration design, only qualified buyers would be permitted to move into the renovated units. We found, however, evidence of a substantial amount of anxiety, unhappiness, and confusion among the initial 44 families who moved into the redesigned, rehabilitated units of the Upper Lawrence Housing Cooperative.

To a large degree, this problem seemed to have been caused by a lack of adequate preparation of the low-income, tenant buyers. Whereas, for example, in both Nashville and Paterson, the bylaws and regulatory agreements were prepared with the full participation of the co-op membership, the drafting of these and related rules and regulations in Denver were treated as technical tasks that were handled by the housing authority's legal counsel. All of the documents in their final form, including such complicated and controversial provisions that provide for PHA emergency takeover powers in the event the co-op suffers extreme financial distress, were waiting for the cooperators when they arrived in their newly innovated units. This coupled with the fact that there is little experience in the Denver area with housing cooperatives, made it even more important that DHA put together a comprehensive counseling/training program to prepare Upper Lawrence home buyers for their new lives.

There appear to be several reasons why Denver's training program was not successful. First, the accelerated project time schedule was not in keeping with the complexity of the conversion process. The other PHHD programs that involve cooperatives have taken substantially longer and provided more training to future cooperators. Another problem seems to be that the "train the trainer" model simply did not work. When it came to such basics as being able to satisfactorily explain financing arrangements, how co-op sales prices were determined, the nature of individual cooperators' responsibilities, the continuing obligations of the housing authority, the nature of construction warranties, or why the co-op's reserve funds shrank during the transition to buyer control, the housing authority personnel did not always have the necessary information and expertise to do an effective job. All participants in the demonstration, including home buyers, housing authority officials, and staff seemed to be learning together.

Thus, for example, despite the fact that one-on-one counseling and group training sessions were ostensibly held on topics including resolving credit problems, homeownership costs, co-op living, administrative policies, managing the business of a co-op, communications skills and team building, co-op board members felt unprepared to assume their responsibilities. The minutes of
the ORA's meeting of April 20th, 1988 contain the comments of the co-op president, Ms. Doris Dinweeed:

Although Doris stated that she attended all the training seminars provided by the Authority, she feels totally unprepared for the task of managing a co-op, being a board member or president.

Despite counseling sessions on buying a co-op, the same minutes indicate that, more than a year after closing, the buyers still do not understand the role that mortgage interest played in home financing:

One of the attractive aspects of the membership was the asking price of the townhome, approximately $28,000. In the minds of co-op members, the $28,000 was the total amount they would have to pay for the townhome. However, after Richaline [Treasurer] investigated the mortgage situation, she learned that the purchase price quoted to the Co-op members did not include the interest payments (during the negotiations process the interest payments were never mentioned). When the interest for both mortgages is added to the purchase price, the cost of the townhome will be approximately $60,000. Richaline stated that this is a cause of concern for the Co-op members. The members feel that getting a single detached home (for the same $60,000) would have been a better investment.

Another problem in Denver and, perhaps, in other sites as well, is that not every buyer received training. According to the Upper Lawrence Cooperative's first Annual Report, co-op members arrived in two groups. The first consisted of 20 to 26 members who moved in on or about October 1986 while the second group moved in later over a period of time.

While the first group was made aware, through training, of the responsibilities awaiting them, the second group enjoyed no such training. And the lack of training bore a relation to subsequent delinquencies and ultimately evictions.

(Upper Lawrence Cooperative Annual Report)

Three original members of the co-op were evicted by the board during its first full year of operation. According to the co-op's annual report, all three members were part of the second group that received no formal training or counseling.

Upon receiving the co-op's report and learning of the members' unhappiness with their preparation to assume leadership of the Upper Lawrence Housing Co-op, DHA issued a strong defense of its training program:

The Denver Housing Authority realized the importance of a complete training program while the co-op was still in the developmental stages. Realizing that we did not have the
necessary experience, qualifications, and expertise to provide this training component, we issued an RFP and sought the best qualified trainers in the nation. The National Federation of Housing Counselors (NFHC) was selected based upon their professional qualifications, experience, and reputation. The DHA worked with the NFHC and the recognized top local housing counseling agencies...to develop and implement a comprehensive co-op training program.

Training was provided to the co-op members and co-op board members as we thought appropriate, under the instruction and guidance of the NHFC. Board members were trained as a group, with other co-op members, and on an individual one-on-one basis. The co-op board was provided training on the appropriate issues relative to their individual office/responsibility. We thought that the training was in depth and understood by the trainees. Until the April 20th presentation to the DHA Board, we had no indication or knowledge that there was any perceived deficiency in the training.

The Co-op Treasurer was provided with intensive individual one-on-one training specifically about budgeting, and financial record keeping. Written book-keeping and record keeping requirements and instructions were developed, along with customized bookkeeping forms. The Treasurer decided to quit attending these training sessions because she believed that she knew how to perform her duties and responsibilities well enough, and that she did not have time for any further training.

In the aftermath of serious communication problems and a less-than-smooth transition to buyer-control, the Upper Lawrence Housing Co-op retained its own legal counsel to "...complete organization of the co-op and insure its smooth functioning." Among other things, counsel assisted the co-op board in its negotiations with the DHA on the resolution of problems having to do with defective rehabilitation work. After several months of strained relations, DHA and the co-op executed a memorandum of understanding in which the housing authority agreed to complete an itemized schedule of repairs at its own expense in return for the board's agreement not to file any legal actions against the authority.

At the time of this writing, relations between the housing authority and the co-op appear better than they have been at any time during the past year. Unlike Paterson and Nashville, where tenant-buyers will take title to their projects up to three years after formation of the co-ops, the Upper Lawrence Co-op had no such luxury. Virtually all of its growing pains have occurred after closing. Whether a longer transition to an independent status would have made the co-op leaders more secure, or whether more systematic training of members and the board would have made a difference, we cannot say for sure but we expect some of these
problems could have been avoided. At this point we simply cannot compare the rocky Denver experience, which spans more than a year of independent co-op operations, with the smoother, pre-closing experiences of the Nashville and Paterson projects, and judge the latter two to be more successful. No matter how smoothly the transition to independent status seems to be going, once the housing authority cuts the strings and the co-op is more or less on its own, unanticipated problems will inevitably arise.

Windfall Profits and Retention Provisions

Denver's way of limiting windfall gains in Upper Lawrence is to require that the co-op share may only be sold to other eligible households, which are restricted to households having incomes at or below 50 percent of area median as defined by HUD at the time of sale. Therefore, it is fair to say that low income use restrictions are permanent.

Because the Arapahoe rental co-op is a partner in a tax credit project, for the first 15 years of operation, co-op shares may only be sold to families and individuals whose incomes are at or below 60 percent of the area median, adjusted for household size. These income restrictions are also likely to be continued once the co-op has acquired its buildings from DHA.

Provision for Maintenance After Sale

Although there is no formal provision for DHA to provide maintenance services after the project closes there has been substantial informal support and DHA has capitalized a reserve fund for each co-op. Because of serious complaints about shoddy workmanship by Upper Lawrence home buyers, some of which still remain unresolved, DHA made a point of informing buyers in Arapahoe of how the warranty issue would be handled in their co-op. DHA's official policy in Arapahoe is as follows:

The units, although renovated, are not covered with a builder's warranty due to cost considerations. Similar to buying any existing home, the buyer will perform a walk-through inspection and accept the unit as-is or subject to a punch list he/she will generate. The appliances are new and, as such, are warranted direct by the manufacturer. DHA will warrant that plumbing and waste lines are in good and operable condition at the time of purchase. As such, plumbing and waste line defects discovered within thirty (30) days of purchase, will be repaired by DHA without cost to the individual buyer.

Despite DHA's indication that the Arapahoe units were rehabilitated to higher standards than Upper Lawrence, members of Arapahoe's board of directors dispute that view. At a meeting we had with three board members in August 1989, rehab problems dominated the agenda. According to the members, several Arapahoe
units have leaks in their shower basins that are causing plaster to rot on the ceilings below the bathrooms. Plaster is also peeling and falling in kitchens and baths. Also, because some of the larger units were configured by merging two units, DHA was unable to extend heating ducts into all the rooms which get very cold during Denver's hostile winter weather. Board members also complained that security alarms in many apartments were not functioning and that a short circuit in an outdoor lighting fixture kept the parking area dangerously dark. Their feeling was that DHA's 30 day warranty against rehab defects was too short for latent defects to show-up.

One member said, and the others agreed, that it takes everything we make just to survive. We cannot afford to make the repairs that DHA should have made in the first place. The concept of a co-op makes good sense, but you have to do it right from the beginning if you want it to work in practice. If we had the money to make all the repairs that are necessary, we could afford to go out in the private market and buy a house.

The general feeling was that construction funds were well-spent, and that DHA misled them about the kind of after-sale support it would provide the co-op. Despite their bitterness, however, they seem committed to making Arapahoe work as it was supposed to. But, even they cannot afford too many more shocks before they walk away like many of their lower-income counterparts at Upper Lawrence already have done.

Handling Non-Participants

All relocation required to accomplish the rehabilitation and reconfiguration of the Upper Lawrence Co-op was completed by DHA before the official start of the PHHD. Because few Curtis Park residents returned to acquire co-op shares, DHA was our primary source of information on how the relocation effort associated with the conversion was organized and implemented. Interviews were conducted with a number of families who were relocated during the Arapahoe conversion.

Due to the demolition of four buildings containing 20 units in each co-op and the extensive rehabilitation work involved, the Denver homeownership project required substantial relocation. A total of 128 families were permanently relocated as part of the project. Few, if any, families who were relocated from the homeownership units returned as home owners.

DHA indicates that none of the relocation was involuntary because of the housing opportunities available to the families in other public housing developments, the authority's scattered site housing, and in the private market, aided by vouchers. These alternatives were viewed as more desirable than Curtis Park.
Also, DHA formed a relocation team that went out of its way to provide families with relocation services. According to DHA:

The team met first with the School Department to discuss the program and receive the necessary paperwork that would be required by the families affected by the moves. The team then met with the representatives of Public Service, Mountain Bell, and Mile Hi Cable for all the necessary forms for these families. The next and most important step, was a one-on-one meeting with each family to discuss the program, its importance to the family and the families' housing options. This took the better part of 90 days, from first contact.

The neighborhood meetings and neighborhood information sessions also contributed to the smooth transition. The neighborhood has responded well in other areas of Curtis Park along with the fixing up of some of the adjacent properties. One of the greatest pluses is the team work that was shown by volunteers of the Housing Authority in getting this job done, from the informational leaflets and counseling on vacating the property with its options, to the actual moving into housing that was obtained through our system. This upfront education and family concern was the single most important factor in a litigation free and "friendly" relocation process.

Impact of Sales Program

The way the demonstration was originally designed, the conversion of part of Curtis Park into co-ops would improve a difficult and costly management situation and ultimately save the housing authority some money. In addition to improving the management situation in the remaining rental segments of the project, the sale of 88 units would also allow the housing authority to close one on-site maintenance office, thus accomplishing additional operating economies. Thus far, however, things have not worked out that way. The conversion of 44 units of Curtis Park into the Upper Lawrence Co-op has had a significant negative impact on the housing authority. Until operating conditions are stabilized and abandoned units resold, the housing authority will continue to be responsible for paying the carrying charges for these units.

Despite some management problems, the financial impacts of the Arapahoe conversion have been quite positive. If all goes well, the housing authority will recover its rehab investment in Arapahoe in the form of rent payments from the co-op during the first 15 years of the project's life, and then in the form of mortgage payments when the co-op acquires the project from the partnership at the end of the fifteenth year. In addition to recovering its rehab investment, the housing authority earned more than a million dollars net by syndicating the rehab tax credit. This sizeable sum has had a very positive impact on the
financial ability of the housing authority to enter the depressed Denver real estate market and acquire additional inventory at good prices to increase its stock of permanently affordable housing.

Conclusions

Despite the significant problems encountered in Denver, it is still too early to conclude that DHA's homeownership will not succeed in the long term. However, several important findings can be made. First, creating a low-income housing cooperative is difficult enough under the most promising conditions. But to do so on an accelerated time schedule without sufficiently preparing participants who have never lived together, and in a region in which cooperatives are virtually unknown, is a recipe for serious trouble. Second, no matter how innovative the financing arrangements might be--and DHA's are, perhaps, the most creative of any PHHD participant--the Denver experiment suggests that no public housing homeownership program can succeed unless the home buyers understand what they are getting into and can be assured that their reasonable needs will be attended to. Third, both real and perceived problems with the quality of the rehab threatens to undermine the long-term viability of both co-ops. Despite formal and informal understandings about warranties and back-up support from the housing authority in the event of latent construction defects, implementing these understandings can be a source of serious conflict.

A fourth issue concerns the relationship between budgeting for the co-op's operations and the incomes of the home buyers. The low incomes of the Upper Lawrence home buyers made it very difficult to fund increases in carrying charges that were made necessary by a serious underestimate of basic co-op operating requirements. A rapid deterioration of the grounds at Upper Lawrence make it more difficult to market vacancies. As operating problems mount, more families are likely to become delinquent in their accounts and, as the economics of the co-op become even more anemic, the cycle of decline will accelerate. Although Denver is not the only site with average incomes hovering around $14,000, it would appear that many Upper Lawrence families simply cannot afford to live there.

Another conclusion we can draw, this one from the rapid turnover of units in Denver, is that concerns about resale restrictions and windfall profit limitations are of no more than academic concern when a homeownership program is not well-designed. Regardless of whether individual shareowners left Upper Lawrence for reasons of personal crisis or just to seek better or cheaper housing, they did not bother to transfer their shares in accord with the co-op's bylaws. They simply left; some under the cover of darkness. The 12 or so cooperators in Upper Lawrence who moved during the co-op's first year of operations must have perceived little difference between owning and renting.
DHA's continuing conflict with HUD concerning how the Arapahoe conversion was financed surely points to the existence of a serious communications problem between the two agencies. DHA formed the limited partnership and transferred ownership of the Arapahoe units to it before HUD officials in Washington ruled that the conversion does not meet the legal provisions under which the homeownership demonstration is implemented. While this is a problem unique to Denver, it does point out the potential difficulty of managing a national public housing homeownership program that provides wide discretion to local housing authorities.
Introduction

The demonstration program in Los Angeles County, Calif. was designed to sell 75 single family, duplex, and small multi-family apartment units to their current occupants. In phase one of their demonstration program the single-family and duplex units were to be sold fee simple, and in phase two, the multi-family units were to be sold as condominiums. The sales that took place were financed through a Los Angeles County bond program that provided FHA insured mortgage loans with an interest rate of eight percent and a term of 28 years. The units were priced at appraised value and a silent-second mortgage held by the housing authority was used to make the units affordable to tenants. Participants paid no more than 30 percent of their gross incomes as determined at the time of qualifying for housing expenses. The PHA paid some of the closing costs and provided assistance with downpayments as needed.

As of July 1989, nine out of the 14 single family units had been sold, and one more sale was expected before closing the program out. After a closer look at what it would take to sell the duplex and small apartment buildings, phase two of the demonstration program was cancelled. The reasons for this decision include the low incomes of the current occupants, the difficulty and expense associated with relocation, the lack of tenant interest in buying properties, the high costs involved in preparing the units for fee simple of condominium sale, and the cost and time involved in counseling and training tenants to assume the responsibilities associated with condominium ownership.

Managing the Demonstration

In Los Angeles County, the demonstration was managed by the Community Development Commission (CDC) which is a combined housing, community, and economic development agency. CDC administers the CDBG program and other federal and state redevelopment programs in Los Angeles County. It manages 3,253 units of public housing, 15,560 Section 8 certificates and approximately 100 housing vouchers. The CDC also sponsors a single-family mortgage revenue bond program to provide low interest loans to qualified moderate-income home purchasers. As of July 1989, there were over 47,000 families on the waiting list for public and assisted housing.

Los Angeles County CDC officials gave several reasons for participating in the demonstration. First, they wanted to provide public housing tenants with an opportunity to own their
own homes. This was expected to increase the participants sense of pride and self esteem and to allow them to benefit from the equity they would accrue in their homes. The second reason was to sell the costly-to-maintain scattered-site units held by the CDC. The extra costs resulted from the scattered locations of these units and their unique mechanical systems and fixtures. The third reason was to use the monies derived from the sales for other housing activities. They wanted the sales proceeds to help provide replacement units that were more efficient to maintain and manage. Finally, senior staff wanted to support the federal administration and be involved in what they saw as an exciting demonstration. According to the executive director, "politically we thought we should participate."

The manager of the CDC's intergovernmental and public relations division was primarily responsible for preparing the original proposal, but she worked closely with the director of the housing division. Once developed, the proposal was approved by the CDC's Board of Commissioners and the Los Angeles County's Board of Supervisors. The only tenant involvement was through the two tenants that sit on the CDC's Board of Commissioners.

In response to HUD comments, however, CDC staff made major revisions in their original proposal. The original proposal, for example, called for the formation of a cooperative to which all the single family units would be sold. In the revised proposal, the means of transferring the units was changed to a combination of fee simple and condominium forms of ownership. The units were thought to be too spread out for a cooperative to be successful.

Four groups were involved in the Los Angeles County demonstration. The Capital Finance section of the CDC was responsible for arranging financing, assisting in program development, and providing legal assistance. The Housing Division of the CDC was responsible for overall program coordination, including communicating with residents. A local consultant, Nancy Lewis and Associates, provided tenant training and counseling. Finally, the Western Bank Mortgage Company handled the loan processing for all sales.

Staff costs incurred in administering the demonstration were estimated to be approximately $64,000. Non-staff costs included appraisal fees at $150 per unit, $6,000 to carry over the bond program to provide financing for program participants, and approximately $500 in printing costs.

Los Angeles County was awarded a technical assistance grant in the amount of $50,000. As of the time of our last site visit, in July 1989, a total of $38,134 had been spent. A total of $25,916 went to a consultant hired to assist in developing the program and in counseling tenants, $8,557 was spent on legal expenses, $3,620 was spent on closing costs, and $41 was spent on miscellaneous items. The CDC plans on using some of the remaining funds for post purchase counseling and expects to give
some back to HUD. According to officials, the technical assistance funds were instrumental in their decision to participate in the program and were critical to its success.

An early administrative problem slowed progress of the demonstration in Los Angeles County. Responsibility for developing the revised proposal was given to a program specialist who was not in the housing division and no one from that agency was assigned to work with the demonstration program. This seems to have been due to ambivalence about selling public housing among housing authority staff. This changed, however, when they realized that the sales proceeds could be used to provide other housing opportunities for low income people. A housing division staff member was then assigned to work on the program and the program moved forward.

Selecting and Rehabilitating Properties

Seventy-five scattered site units were originally selected for sale in two phases. The units to be sold in phase one consisted of fourteen single-family houses, while the units to be sold in phase two consisted of seven duplexes and a number of small apartment complexes. Almost all of these units were in excellent condition. Some were almost new, having been built under the Turnkey program (not to be confused with Turnkey III), and others had been recently acquired from the FHA and rehabilitated by the Housing Production Division.

As of July 1989, nine of the single family units had been sold in phase one of the program and one more was in the sales process. For reasons to be described below, a decision was made not to sell the multifamily units proposed in phase two of the demonstration program.

The cost of these initial repairs for units sold under the demonstration averaged $2,419. The funds for this rehabilitation came from the county's CDBG funds. Additional minor repair work was done immediately prior to the sales but the costs of these repairs were said to be negligible.

The units sold were located in three areas of Los Angeles County. The South-central area was described as housing residents whose incomes were in the bottom 10 percent of all residents in Los Angeles County. It is a primarily black and Hispanic neighborhood composed of mostly modest, single-family houses. Most of the houses in this area are reasonably well maintained. A local realtor familiar with the area said that property values have risen slowly over the past several years but they have not appreciated as rapidly as other neighborhoods. The homeownership rate was estimated to be around 90 percent. Houses are selling in the $67,000 to $79,000 range.

East Los Angeles is a primarily Hispanic area with property values in the $80,000 to $100,000 range. Again, the area
consists mostly of well maintained single-family homes. The homeownership rate was estimated to be approximately 90 percent. This area was said to be appreciating faster than the South-central area but still slower than the area as a whole.

The La Puente area in the San Gabriel Valley is primarily a single-family house area, with a homeownership rate of approximately 70 percent. The houses have been selling in the $85,000 to $90,000 range and, according to a local realtor, the appreciation has kept up with surrounding areas. The area is largely Hispanic, with whites and blacks making up the remainder of the population.

**Attracting and Selecting Owners**

The program was marketed to residents of the single-family units by a letter that described the program, asked them if they were interested in participating and, if interested, to complete a preliminary application. Program staff then held a meeting with prospective participants to discuss the step-by-step procedure for becoming a home owner. A brochure was also developed to advertise the program to the larger public housing community and those on the Section 8 and public housing waiting lists. A special mailing was also done to people renting from the housing authority who had incomes above $14,000.

Current residents were given first priority in purchasing units. Assuming a current tenant had a good employment and credit history, no social problems, and an income between 50 and 80 percent of the area's median, program staff worked with him or her to make the unit affordable, using a silent-second mortgage. The minimum income for participation was set at $14,000 but the lowest income of any of the participants was $16,600. In selecting participants from the waiting list, the staff chose families with the greatest ability to pay the full costs of homeownership. The average income for all program participants was $21,774.

**Property Conveyance**

As mentioned above, the original proposal for property conveyance was to sell the units to one scattered-site cooperative. After HUD officials questioned the feasibility of cooperative ownership given the distance between the units involved, a revised proposal was submitted and subsequently approved. The revised program involved the fee simple sale of the 14 single-family units and the sale of the duplexes and small, multifamily buildings as condominiums. The pricing of the units was based on their appraised value but a silent-second mortgage was used to make the houses affordable to current tenants. The amount on the second mortgage was adjusted so that buyers would pay no more than 30 percent of their income for housing expenses. Assistance in paying the closing costs was also provided to program participants on an as-needed basis. The average amount of the
assistance provided was $4,876 and ranged from a low of $3,480 to $7,800. This assistance came from the local CDBG fund.

The decision to cancel phase two of the sales program was the result of a more thorough analysis of the feasibility of transferring the multi-family units to tenants. This analysis suggested that there was a shortage of tenants who could meet the income requirements of the program and that many tenants in the units to be sold were not interested in buying their units. According to the consultant involved, the major reason for this lack of tenant interest was that the neighborhoods in which the units were located were not very nice and "people were hoping to do better and get out of there." Although these areas look nice, crime and gangs are major problems. The fact that the units were part of multi-family structures also dampened interest. This lack of interest combined with the prohibition against involuntary relocation meant that it would be difficult to match interested buyers with the units to be sold. Furthermore, the process of selling these units as condominiums, including the permits required, engineering reports, and legal work, was said to be expensive and time consuming. Finally, the counseling and training, according to program staff, would have been extensive given the number of condominiums that would have been created. According to one program official, "we would have to support them for three to five years after the sale." Overall, officials felt that there were too many obstacles to proceed with phase two of the program.

Financing

Financing of the sales was provided through a county sponsored bond program offering low interest FHA insured first mortgages and silent second mortgages offered by the CDC. Originally, the first mortgages were going to be financed by a consortium of savings and loan institutions, however, program officials decided to use the county bond program because it offered a lower interest rate. The county bond program provided 28 year loans with an interest rate of eight percent. The downpayment was three percent of the first $25,000 borrowed and five percent of any amount above $25,000. The average first mortgage amount was $35,403 and the range was from $19,800 to $49,720. The silent-second mortgage also runs for 28 years and is forgiven if the original or a low income purchaser owns the unit at maturity. The average amount of the second mortgage was $50,463 and the range was from $37,725 to $75,900.

The loans were processed by Western Bank Mortgage Company, which is approved for the direct endorsement of FHA insured loans. According to a company representative, standard FHA underwriting criteria were applied to prospective participants. The only thing different about these loans was that the housing authority was providing downpayment assistance and helping with the closing costs. None of the loan applications they received were rejected. The only problem they encountered was that many of the
applicants were Spanish speaking and they had no one on their staff that spoke Spanish. This greatly slowed the loan processing.

No special provisions have been made for defaults beyond the assignment procedures offered by FHA. According to program officials, they are not sure they want the properties back in the event of a default. This was part of their desire to pursue private financing rather than money purchase mortgages.

According to a mortgage company representative, the payment record of the participants has been good. There have been no delinquencies and no late fees have been assessed.

The only problems encountered in financing were an early misunderstanding among program staff as to the amount of the downpayments that would be required, and a slowness in loan processing. The program staff originally thought that the required downpayment would be three percent of the purchase price. Later, however, they realized that the required downpayment was three percent of the first $25,000 and five percent of the remaining sales price. Since many of the prospective buyers were unable to come up with the full downpayment, the CDC provided grants to assist program participants. The slow loan processing, according to program officials, resulted from the extensive documentation required of program participants, the language problem mentioned above, and the switching of loan officers during the sales process.

Counseling

A wide range of training and counseling was provided to program participants by both housing authority staff and a local consultant. The housing authority staff held two group meetings: one introducing the prospective buyers to the program and the other to review loan application procedures. The staff also spent much time answering questions posed by potential buyers.

Nancy Lewis and Associates, a local consulting firm, was hired to provide training on a variety of topics and to provide individual counseling to program participants. The consultants provided four, three-hour training sessions on the following topics: consumer credit counseling; maintenance and energy savings; the financial responsibilities of homeownership; and the resale restrictions associated with the program.

Considerably more time was spent by the consultant, however, individually counseling program participants and their families. This counseling involved helping to resolve credit problems, assisting in the filling out of application and loan documents, providing advice on what to do if they run into problems in making their mortgage payments, and the like. The consultants also acted as a liaison between the mortgage company and the buyers. The principle staff member providing the counseling
spoke Spanish and could translate for both parties. According to a representative of the company, the counseling involved "a lot of doing it for these people: taking a typewriter out to the house to write a letter to try and clear up a credit problem." The firm was also involved in designing aspects of the program, including the process for selecting participants, and the terms of the secondary financing and the resale restrictions.

The one-on-one counseling was considered to be particularly important to the success of the counseling program. The counselor interviewed also stressed that it took time for people to think about the information being presented and to develop trust in the counselor. Thus, the process could not be rushed. The firm was paid a total of $25,916 for its work.

Some post-purchase counseling is being provided by the CDC staff member in charge of the program. She has been answering the questions of program participants and "trouble shooting." Periodically she calls the new owners to see if things are going smoothly. More formal post-purchase counseling is being discussed and at least one group meeting is planned for the future.

Windfall Profits and Retention Provisions

Resale restrictions have been written into the purchase agreement and the second deed of trust that should effectively guard against windfall profits and assure that the unit will be occupied by a low-income family for a 28 year period. These provisions stipulate that the unit must be sold to a family with an income that is below 80 percent of the area's median income. The resale price cannot exceed the original purchase price plus an additional sum determined by multiplying the original purchase price by the proportionate increase in the county's median gross annual income. The costs of improvements made to the unit can be added to the sale price but it cannot exceed 10 percent of the original purchase price. These resale restrictions run for 28 years.

Provision for Maintenance After Sale

Although the CDC originally proposed establishing a loan fund to assist participants with major repairs to be capitalized with part of the sales proceeds, this fund was never established. There are no provisions for assisting owners with any major repairs after sale.

Handling Non-Participants

Of the nine sales, six were to the current occupants of the units and three were to former tenants who moved from other units. Only one person was relocated because of the demonstration. The other two units were vacant at the time they were included in the
sales program. The one relocation was a voluntary move facilitated by a Section 8 certificate.

**Amount and Use of Sales Income**

The Los Angeles County CDC received approximately $300,000 from the sale of the units. These funds were deposited in the special fund to be used to help provide new housing opportunities for low income people. They expect to use them, for example, to contribute to joint ventures with non-profits to build new housing or to secure an option on land to be used for future public or assisted housing developments.

**Impact of the Sales Program**

Based on the cost of administering the demonstration program, the executive director described the financial impact of the program on the CDC as negative, even though he considered it to be a very costly program to administer. The director of assisted housing, however, thought that there would be some savings given the cost of maintaining these units as public housing. Actual figures on the impact of the sales on operating subsidies and maintenance and operation costs were not available. One non-financial impact on the CDC was that it caused them to study the feasibility of selling their small multi-family buildings to the tenants. Finding out that this was not feasible was thought to be a valuable learning experience for both the housing authority board and the staff.

The only obvious impact of the demonstration program on the county was that it will increase tax revenues. The nine owners will be paying approximately $10,160 the first year in taxes. Given the small number and the scattered nature of the units sold no impact on surrounding neighborhoods is anticipated.

The major impact, according to program officials, is on the lives of the program participants. According to one staff member, "We made nine people very happy. They have an increased sense of pride."

**Conclusions**

The demonstration program in Los Angeles County clearly fell far short of its original goal of selling 75 units. A variety of problems—including the low incomes of housing authority residents, lack of interest in the multi-family units offered for sale, and the difficulty and expense of converting the multi-family units to condominiums—led the CDC to cancel phase two of the sales program. In phase one they were successful in selling nine single family units. Program staff point out that they were successful in phase one of their program and if they had more time to study the process of selling the multi-family units before they submitted their application they would have never proposed them for sale. They suggest that HUD should allow
housing authorities more time in responding to NOFAs when they involve new and innovative programs.

The extent to which they were successful in selling the single family units seems attributable to good screening of participants, good counseling, and the availability of low-interest financing for the first mortgages. Program officials also emphasized the importance of extensive counseling and training in the success of the sales program and the high cost of providing these services. At the present time there is no interest in selling more public housing units to tenants. The practical constraints limiting the number of units the CDC could sell, according to the executive director, include a high proportion of elderly in the public housing units, the political reaction to expanding a sales program with so many people on the waiting list, the low incomes of housing authority residents, and the lack of suitable units for sale. Based on his experience with the demonstration program, the executive director feels the sale of their multi-family units to tenants is not feasible. They would, however, be interested in a "purchase to sell" program in which the CDC could provide non-public housing units to qualifying public housing tenants.
PUBLIC HOUSING HOMEOWNERSHIP DEMONSTRATION

MCKEESPORT CASE STUDY

Introduction

The Housing Authority of the City of McKeesport, PA has sold nine of 10 scattered-site public housing units to tenants. One unit will not be sold because its occupant, although qualified for homeownership, is not interested in purchasing the unit or in moving. From the perspective of the housing authority management, the demonstration in McKeesport has been highly successful. The authority, in fact, is currently exploring conversion of an eight-story, high-rise structure, originally built for families but now vacant, to one- and two-bedroom condominium or cooperative units, which it hopes to sell to authority tenants who can qualify for homeownership. The benefits of homeownership, according to the housing authority executive director, include the creation of responsible home owners, restoration of community pride in home owners, return of houses to the tax rolls of the community, improved maintenance of homes, and contributions to neighborhood revitalization.

The scattered site houses in McKeesport were sold for their appraised value (prices ranged from $16,000 to $25,000). The housing authority financed the sales itself, with interest set at market rates. Accrued interest, however, will be forgiven after five years if homes have not been re-sold for more than the purchase price. Houses were sold under a lease-purchase arrangement in which tenants paid rent on the house for one year prior to purchase, and the housing authority applied the full amount of the rent to the purchase price as a down-payment. The term of the loan is adjusted to keep housing expenses within 30 percent of income. The minimum annual income for eligibility to buy a unit was originally set at $15,000. This minimum was ignored, however, as program participants had incomes as low as $6,000.

The housing authority has established a mortgage emergency fund and a maintenance fund capitalized from its HUD technical assistance grant and from earmarking three percent of mortgage payments for each fund. Two home owners have been delinquent one or more months on mortgage payments, but in each case the authority was able to provide counseling and to work out arrangements for the household to get its payments back on schedule. Thus, the emergency fund has yet to be tapped. The maintenance fund has also not been used, but an application is pending to use funds in that account to pay for home improvements to one unit.
Managing the Demonstration

The demonstration in McKeesport is managed by the Housing Authority of the City of McKeesport. The authority's executive director designed the demonstration and supervises its day-to-day operation with the assistance of the authority's assistant executive director/comptroller.

The Housing Authority of the City of McKeesport has 1,227 units of public housing under its annual contributions contract and administers 400 Section 8 certificates and 25 housing vouchers. Some 150 families are on the authority's waiting list for public housing and more than 400 families are on the waiting list for Section 8 certificates and housing vouchers. Its public housing stock is located in eight projects. Those projects include row houses, three-story apartments, and four eight-story high-rise buildings, one of which is vacant. The majority of the authority's housing stock, some 700 units, is located in E. R. Crawford Village, where the first units were constructed in 1937.

The primary goal of the demonstration in McKeesport was to provide an additional avenue for meeting the housing needs of moderate income households. The authority says that a need (and a viable market) exists for rehabilitated older housing, and it believes that it has the mission and expertise to serve that need and market. As noted above, the authority is considering converting a vacant high-rise structure, originally built for family occupancy, to one- and two-bedroom condominium units. HUD modernization funds would be used to pay for the conversion. In addition, it would like to acquire homes on the open market, rehabilitate those units, and then make them available to public housing tenants and other moderate-income households who have adequate income to qualify for homeownership. That process may have to take place with federal assistance, since the authority believes the provisions of the Davis Bacon Act will lead to excessive costs, making it impossible to rehabilitate single-family detached housing without large federal subsidies. (For example, the ten housing units the authority is selling in the homeownership demonstration cost about $80,000 each to purchase and rehabilitate in 1984, but they were appraised for purposes of the demonstration at $16,000 to $25,000 each. It obviously would be difficult to operate a local homeownership program which required a $60,000 subsidy per housing unit.)

The authority's executive director conceived the idea of participating in the demonstration program after receiving an announcement from the federal government on December 18, 1984. He discussed selling the authority's 10 scattered site units (Project PA-5-8) with key members of his board, the board as a whole, and with the mayor of McKeesport. All were in favor of the idea and encouraged the authority to apply for participation. The authority board of commissioners unanimously approved a resolution authorizing participation in the demonstration on January 28, 1985. After the motion was approved, at the request
of the authority chairman, the executive director described the demonstration program and explained why the authority wanted to participate: "...to put these units back on the tax roles and give low- to moderate-income families the opportunity to purchase real estate."

None of the authority's tenants were involved in the decision to take part in the demonstration (there is no formal tenants' association for the scattered site project). While tenant councils exist for the authority's multifamily housing, they were not consulted by the authority since none of that housing was involved in the demonstration.

The City of McKeesport viewed the demonstration as an opportunity to add additional property to the city tax rolls (the population of McKeesport has dropped from over 60,000 to 30,000 as steel mills have closed and people have moved away) and to help revitalize one of the poorer neighborhoods in the city, the seventh ward. To achieve those goals, the mayor of McKeesport encouraged the authority to include a 200-unit apartment project in E. R. Crawford Village in the demonstration program. The authority executive director, however, did not believe at that time that there was an adequate market for a condominium conversion project and did not pursue that suggestion. In supporting the authority's application to HUD, the city mentioned tax abatement as one way it could assist in making homeownership affordable. Evidently it was not serious in that proposal and, in fact, putting units back on the tax roles is viewed as one of the benefits of the program.

In 1987, the authority estimated that operating costs for the demonstration were about $700 per month after initial start up; in 1989, it could not provide an updated estimate, possibly because by then the only remaining costs were in servicing mortgages and providing occasional counseling. Staff involved include the executive director, assistant executive director/comptroller, project managers (who helped recruit potential homeowners), and maintenance personnel. Because each of the ten scattered site units was completely rehabilitated during the spring of 1984, minimal costs (under $2,000) were incurred in fixing up units prior to sale (most of those funds were spent for materials used by one purchaser to lower ceilings).

The authority received an $18,811 technical assistance grant from HUD. Those funds were used to defer general expenses associated with the demonstration and were essential in helping get the demonstration under way. The authority executive director reports the authority would not have been able to participate in the demonstration if technical assistance funds had not been available, and he believes the funds would have been more useful if they were made available in a lump sum. Once the demonstration was under way, however, technical assistance funds were less critical.
The authority's executive director is highly satisfied with the way the local demonstration was managed and view it as a success.

Selecting and Rehabilitating Properties

The authority has sold nine of 10 houses that comprise its scattered-site project. One tenant has refused to purchase the unit she is living in, and she has refused to move as well. As noted above, each of the scattered-site units was purchased by the authority in 1984 and completely rehabilitated, at an average cost of $80,000 per unit. Those units were selected for the demonstration because (1) the authority's executive director believed that the quality of the home sold would be an important factor in the success of the demonstration, since low-income home owners would not have to invest in costly repairs; and (2) his belief that an adequate market did not exist for purchase of other units in the authority housing stock.

When the authority joined the demonstration, the 10 scattered-site units were in excellent condition. Each is located in McKeesport's seventh ward. A local real estate agent reported in 1987 that the homeownership rate in that neighborhood was about 50 percent, with homes averaging $15,000-$20,000. About half the families living in the seventh ward were reported to be receiving welfare payments. The racial makeup of the neighborhood was 70 percent white, 30 percent black. The proportion of black households was increasing, however, as former steel workers moved out to find employment and housing in other communities. Housing conditions were deteriorating as ownership units were converted to rental units, and home prices were deteriorating in the face of the very depressed economic conditions existing in McKeesport. Approximately 10-15 percent of the homes in the seventh ward were abandoned, and 30 percent were in poor condition. Average rents were about $250 for a two bedroom unit; the vacancy rate was about 10 percent. The realtor consulted did not believe that purchasing homes in the this area was a good investment for home buyers, since he believed home values would continue to depreciate.

Attracting and Selecting Owners

The authority originally proposed to enter into a contract with Housing Opportunities, Inc. "...for the purpose of selecting tenants to participate; monitor resales, assure long term occupancy of low-income persons, planning for foreclosure prevention, planning for management and funding of the costs associated with the transfer of properties to private ownership; counseling and training of tenants, and marketing of units." The cost of that contract, $3,000 per unit, $30,000 in all, was viewed as excessive by HUD and by the authority and it was never consummated. Instead, each of the functions listed above was performed by the authority staff (principally by the executive director).
Potential purchasers were selected in two ways: one group consisted of the original tenants living in the 10 units selected for the demonstration. Four of those 10 tenants purchased their unit, and five agreed to move out after deciding they couldn't afford to buy or didn't want to buy; one tenant did not want to move, since the scattered site units are the best housing provided by the authority. A second group consisted of tenants nominated by authority project managers based on the managers' knowledge of those tenants' potential ability to become homeowners and based on discussions with the tenants about their interest in taking part in the program. The key attributes authority managers looked for in potential homeowners were the tenants' record in maintaining their rental units and their rent payment record. In addition, a minimum annual income of about $15,000 was viewed as necessary for a household to afford the costs of homeownership but this was not adhered to strictly.

Once potential homeowners were identified, project managers discussed the program with them, showed them the homes available for sale, and discussed the price. If the tenants were interested in buying, a meeting between the prospective homeowner and authority executive director was arranged. At that meeting, the executive director explained the operation of the program in greater detail and assured himself that the prospective buyer could become a successful home owner. If the household was still interested, the authority's attorney then went over the financial arrangements and explained the mortgage and other financing terms. Other counseling steps are described below.

Rather than creating a pool of potential purchasers, the authority lined up prospective purchasers as units were vacated by their tenants. It then entered into a one-year lease purchase agreement with the prospective home owner. The authority viewed the one-year lease as a time for tenants to see if they could meet the responsibilities of homeownership, to be certain they wanted to purchase that particular home, and to identify problems with the homes and negotiate for their resolution with the authority. It provided the authority with an opportunity to test the tenants' ability to keep up with housing payments and to provide counseling.

The initial home buyers were both married and single-parent households. Two of the first four home buyers are employees of the housing authority. Incomes ranged from $6,000 to over $20,000 and ages of household heads ranged from the early 20s to over 60. Household size ranged from two to six persons. Six were white (one is Spanish/American) and three were black.

Six households who were occupying scattered site homes did not want to purchase. Three were single and three, married. The three single persons were women. Income data are not available, except for the one household still occupying one of the units, whose annual income was $15,891 in 1987.
Property Conveyance

All the properties have been sold fee simple. The sales prices were based on the average of two independent appraisals. A political flap arose about that when nearby property owners wanted the authority to sell the units for $40,000 to $50,000 and to take a second mortgage for the difference between that amount and the appraised value of the units, which has run from $16,000 to $25,000. The neighbors viewed that as a way of stimulating home values in a declining market. The authority thought it was unfair, however, and refused to overprice the homes.

The rent accrued during the year prior to purchase (about $3,000 per dwelling unit) was applied to the purchase price as a down payment. Purchasers paid for title insurance ($200-300), and the housing authority paid all other closing costs, which were estimated to run $700-$800.

Financing

Financing for the sales was provided by the McKeesport Housing Authority. The authority's original application to HUD mentioned finding private financing, but, in fact, the authority never looked for private financing since it concluded it would be simpler for the authority to handle it. (According to the executive director: "We are in the rent collection business, so why not collect mortgage payments."

Sales prices were reduced by the previous year's rent receipts, which constituted the "downpayment." The authority charged market interest rates (the average rate charged by three local financial institutions) but will forgive interest if homes are not sold for more than the purchase price for a period of five years. The authority determines mortgage terms by working backward from what households can afford to pay (assuming that they can devote 30 percent of their income to mortgage payments, fuel, and utilities) in monthly payments to the term of the mortgage. Terms of the mortgages have varied from 8 to 25 years.

The authority has taken several steps to minimize the potential for default. First, it selected tenants who had good rent payment records, and monitored rent payment behavior during the year potential homeowners leased their homes. Second, the authority ran standard credit checks on each prospective purchaser. Third, the authority contributes three percent of mortgage proceeds to a revolving loan fund for tenants who run into short-term financial difficulties and have a problem making mortgage payments.

In the event of a default, the authority will first counsel tenants and attempt to help them solve their problems. However, if there is evidence that people are not taking adequate care of
their homes, the authority will not hesitate to foreclose. In cases where homeowners will no longer be able to keep up with their payments and have taken good care of their home, the authority will relocate them back to public housing. It would then sell the unit to another public housing tenant.

Of the first nine units sold, the authority had experienced late payments from two households (one household was in arrears on two occasions). The authority provided financial and other counseling assistance, and the households have been able to resume payments on schedule. There have been no defaults.

The authority management is pleased with the financial arrangements it worked out for the sale of houses.

Counseling

Homeownership counseling was handled by the staff of the McKeesport Housing Authority. After potential home owners talked with the authority's attorney and learned about the financial obligations of homeownership and they wanted to proceed with the purchase, they signed a one-year lease purchase agreement with the authority. During the year prior to assuming ownership of their home, prospective homeowners received counseling and other assistance from the authority's project managers and maintenance staff. The key element of that counseling was advice regarding the financial responsibilities of homeownership, of making mortgage payments on time, and the importance of not becoming overextended financially. In addition, during the one year lease period, the authority maintenance staff trained households in making minor repairs. Counseling was done informally with no group sessions. Counseling costs were absorbed as part of normal authority operating costs.

Since the home owners have purchased their homes, the authority has provided some post-purchase counseling, but that is handled on a case-by-case basis. For example, one household had domestic problems which resulted in late payments on its mortgage. The authority arranged counseling to help resolve the family's problems, and it worked out financial arrangements so that the family would not lose its home. The authority, however, definitely wants to wean people from dependence on the authority for maintenance of their homes, and it will provide assistance with home repairs only in extraordinary circumstances.

The housing authority executive director notes that adequate counseling is vital to the success of a homeownership program. That counseling must include training in financial responsibility and also training on the importance of upkeep and repair of the home and yard.
Windfall Profits and Retention Provisions

Accrued interest will be assessed if home owners sell their property for more than the original purchase price during the first five years of ownership; otherwise, interest on the mortgage will be forgiven. That provision creates a strong incentive for home owners not to sell during the first five years of ownership. In addition, if a home owner receives a bona fide offer for the property at a price less than the purchase price, the housing authority has a right to purchase the property for an amount equal to the balance of the mortgage. After five years home owners can sell their homes and keep any profit. There are also no provisions to prevent owners from leasing their houses at whatever rent, or from renting out rooms.

The housing authority believes those provisions are adequate to stifle speculation on the homes it has sold, particularly given the very weak housing market in McKeesport and in the seventh ward where the homes are located.

Provision for Maintenance After Sale

The housing authority established a revolving loan fund, capitalized with HUD technical assistance grant funds and with setting aside three percent of mortgage payments, to be used for major repairs to units. Since the units were completely rehabilitated in 1984, no major repairs are expected to be needed for some time. As of August 1989, one request was pending to borrow from the fund for home improvements (dropping a ceiling and paneling a room), but no decision had been made whether to approve or deny the application.

The authority is considering putting a cap on the fund of $10,000, after which money formerly deposited in the fund would be put in escrow for use in other low-income homeownership efforts, but it has not made a final decision on that.

Handling Non-Participants

Of the six tenants of scattered-site housing who decided not to participate in the demonstration, one continues to live in her home; one moved out of public housing to occupy the former home of her parents; one moved out of public housing and her address is unknown; and three were relocated to other public housing units. Moves were voluntary, but the authority executive director made it clear to non-participants that if they stayed in their homes they would deprive others of an opportunity for homeownership.

The authority would like to relocate the one household which continues to rent one of the scattered-site units (in fact, the authority has offered to pay her to move), and it chafes at the fact that HUD rules prevent that from occurring.
Amount and Use of Sales Income

The authority will eventually realize approximately $250,000 from monthly payments on mortgages from sale of 10 public housing units. Initially, receipts were used to fund start up costs of the program. In time, $25,000 will be used for program administration; $50,000 for a capital improvement loan fund (as noted above, however, the authority is considering reducing this to $10,000 and switching the funds for the provision of additional homeownership opportunities); $50,000 for an emergency loan fund to help persons in financial distress make their mortgage payments; $50,000 for future homeownership opportunities (as noted earlier, the authority would like to buy additional units and sell them to tenants); and $17,000 to reimburse the authority for extraordinary expenses in rehabilitating the units in 1984.

Impact of the Sales Program

Loss of the HUD subsidy and rents from the 10 units that have been sold has had no appreciable effect on the financial condition of the McKeesport Housing Authority, nor does the authority expect to accrue any appreciable savings from reduced maintenance, utility, and insurance costs.

The return of houses to the tax roles provides a positive benefit to the City of McKeesport from the demonstration. Tax proceeds for the nine units are about $5,836 per year and improved maintenance of the homes by their new owners seems to be having a positive effect on the neighborhoods in which they are located.

Conclusions

The McKeesport Housing Authority is enthusiastic about the demonstration, since it enables the authority to provide a wider range of housing opportunities to low- and moderate-income households. For higher income public housing tenants, the program offers a way to get them into homeownership, with all of the benefits that it provides. The McKeesport Housing Authority would like to purchase, rehabilitate, and sell additional homes for low- and moderate-income households. The opportunity to take part in this demonstration offers the chance to explore and gain experience with a new avenue for meeting the housing needs of the community it serves. In addition, the authority is exploring the conversion of a vacant, eight-story building to condominium or cooperative ownership, as a way of salvaging some value from the derelict structure originally built to serve large families.
PUBLIC HOUSING HOMEOWNERSHIP DEMONSTRATION

MUSKEGON HEIGHTS CASE STUDY

Introduction

The demonstration program in the city of Muskegon Heights, MI was designed to sell all 20 single-family, scattered-site public housing units owned by the city. The original plan called for selling units at 50 percent of their appraised value. Financing was to be provided by private lenders at market rates. After the first two sales were closed, however, the city council raised the sale price to 100 percent of appraised value. Program officials considered this an expression of the council's change in attitude towards the sale of public housing. The effect of this increase was to discourage participation both among potential buyers and potential lenders. After the price increase no more units were sold.

Managing the Demonstration

The Muskegon Heights Housing Commission (MHHC) was responsible for managing the demonstration. The commission also administers the Section 8 program. Since the time the demonstration was approved, the commission has had little change in the number of units it administers. The commission has 360 public housing units under annual contribution contract. It also administers 50 Section 8 certificates. The agency has about 50 people on the Section 8 waiting list and about 400 people on the public housing waiting list. The commission also has 50 people on a separate waiting list for its scattered-site units. The agency contacts those on the waiting list periodically to confirm their continuing interest and eligibility. The agency has an open waiting list and it adds eligible families constantly. Thus, the authority considers the list a good indicator of the demand for subsidized housing in the city.

Since its conception, the demonstration had one major goal: creating homeownership opportunities for low-income families. The MHHC expected that the program would provide buyers, through homeownership, with a stake in the community. Also, the MHHC believed that the program was a good mechanism for putting properties back in the city's tax rolls, thus benefiting the community as a whole.

The MHHC's former executive director made the original decision to participate in the demonstration. He and the former assistant director were the principal authors of the proposal. Later, the new director and a special assistant revised the proposal and developed the guidelines used to implement the program. There was no tenant involvement in the design of the program. The mayor of Muskegon Heights endorsed the city's participation in
the demonstration. Initially, city officials were supportive of the demonstration.

Three major groups were involved in the demonstration program in Muskegon Heights. The MHHC had overall responsibility for managing and implementing the program. A private lender, Waterfield Finance Corporation, provided the necessary mortgage financing. Finally, the mayor had to approve and give permission to the MHHC to hold and transfer units to tenant-buyers because the city of Muskegon Heights legally held title to the units. The commission's executive director and a special assistant had day-to-day responsibility for administering the demonstration.

Initially, the annual administrative cost of the demonstration was estimated to be $15,000. In staff time, this amount represents approximately one-half of a person per year. The annual non-personnel costs were estimated at $1,500. The agency did not request any technical assistance funds in the original proposal submitted to HUD because such funds were not considered necessary. Later, when the proposal was revised, a request for technical assistance funds was submitted and the MHHC received $4,000. The grant money was used primarily to pay for the legal advice necessary to prepare the transfer documents.

Three problems were encountered in designing and implementing the demonstration. The most important problem was the disagreement between the MHHC and the city council over the sales price. According to program staff, this problem was the single most important deterrent to achieving program goals. Program staff believes that the price increase was the result of the city's change in attitude towards the sale of public housing.

The other two problems were encountered at the initial stages of the demonstration. Initially, it was unclear who held legal title to the units targeted for sale. Both the city and MHHC believed they did. This issue was finally settled by the city's legal counsel with the recognition of the city's title to the units. The third problem was the lack of sufficient technical assistance funds to cover necessary costs. This lack of funds was behind the MHHC's decision to appraise only eight of the 20 units targeted for sale. It also led to an overburdening of the MHHC's staff. They did not have the time required to implement the program expeditiously.

Selecting and Rehabilitating Properties

The original goal was to sell all of the 20 single-family, scattered-site public housing units owned by the city. Most of these 20 units had been rehabilitated within the last five years and were in good condition. Thus, except for minor repair work, all 20 units were considered ready for sale at the beginning of the demonstration. In the two units that were sold, only minor repair was required. City personnel inspected these units before the sale agreement was signed and identified repairs needed for
code compliance. Repair work in the units was done by the agency's maintenance staff. Repair work required in other targeted units was to be paid for from the proceeds of these first sales.

The exact number of units to be sold was going to depend on the number of tenants interested and able to obtain private mortgage financing. In general, the targeted units were located in quiet residential areas. The housing conditions in these areas were good, including only a few, poorly maintained properties. These areas were mixed-income neighborhoods, primarily minority, and they contained a combination of owners and renters. In 1987, the average rent for a two or three bedroom unit was about $275 per month, and the average sales price was $23,000. No rehabilitation programs had been targeted for these areas.

Attracting and Selecting Owners

The MHHC was responsible for identifying potential buyers. The staff scheduled personal interviews with families living in the units selected for sale and explained the program to the prospective participants during these meetings. A follow-up letter was sent to assess tenant interest in the demonstration. The staff sent a second letter to those who expressed interest and invited tenants to pick up a copy of the sales contract agreement. The staff advised interested families to seek their own legal advice to better understand the responsibilities of homeownership.

Initially, the MHHC contacted all major lending institutions in the city to explain the scope and characteristics of the demonstration. The MHHC felt that the potential buyers would have a better chance to obtain financing if the lenders were aware of the program. Although the MHHC made the first contact, it was up to the potential buyer to acquire the necessary mortgage financing from a private lender. Based on legal advice, the program was structured so that the private lender was responsible ultimately for screening potential buyers. Since it was the MHHC's interest to replicate the normal homeownership experience as closely as possible, it considered the use of private sector financing one of the demonstration's important characteristics. Also, the staff felt that animosities between the MHHC and the potential buyers, resulting from applications being denied, would be avoided if it was the private lender that ultimately screened applicants.

All the residents living in targeted units were eligible for participation. At the time of the increase in the sales price, two out of the 20 targeted units had been sold, and 15 families were still considered potential buyers. Two of the remaining families were considered non-participants and remained in their units as renters. One family voluntarily decided to move out of public housing. The MHHC selected a new tenant for this unit from its waiting list, based on ability and interest in buying
the unit after one year of residence. The criteria used by the MHHC to screen potential participants included sufficient income so that 30 percent of it could cover all housing costs; a stable income source and employment history; a good housekeeping record; and the appropriate number of people in the household for the type of unit available.

The two households who bought units had similar characteristics. Both were black, married households, with heads aged 29 and 33, with two children under the age of 16. Household sizes were 5 and 4 members.

Property Conveyance

All units were to be sold fee simple. Appraisals of eight of the 20 units were done by the City Appraiser. The initial sale price was based on these appraised values. The actual price to be paid was set at 50 percent of this value. The closing costs were to be paid by the buyer at the time of closing, along with the required downpayment. Each buyer had to have a $350 downpayment and $1,100 for closing costs.

Financing

Financing was provided by a private lender, Waterfield Finance Corporation. The MHHC set the actual sale price at a fraction of the market value (50 percent of appraised value) to reduce the risk to the private lenders. Only one of the units sold used private financing, however, because the second sale was a cash transaction, with the money provided by a relative of the buyer.

Waterfield Financial Co. provided a conventional mortgage for the one unit sold. The MHHC did not offer any guarantee to cure a default or similar problem. If a default occurs, the MHHC intends to buy back the unit for the outstanding loan balance. As of July 1989, program staff was not aware that the buyers of the one unit sold with financing were having any difficulty meeting their mortgage payments.

Counseling

Homeownership counseling was provided by MHHC staff. The counseling program covered areas such as the financial aspects of homeownership, budgeting, credit, money management, repair and maintenance, homeownership responsibilities, and how to obtain a loan. Counseling was provided to each purchasing family in a series of three individual sessions. The sessions were scheduled between the signing of the purchase agreement and the closing date in order to motivate buyers to attend. Attendance at the counseling sessions was voluntary and no penalties were imposed for lack of attendance. The potential buyers were long-term stable tenants. Most of these tenants had been doing some of the maintenance and small repair work on their units. Thus, the
agency did not think that a long counseling and training program was necessary.

The counseling program was intended to be paid for from sales proceeds. Due to the general lack of funds, the agency was dependent on the sale of the first two or three units to have the monies necessary to fully launch the counseling program. However, the action of the city council stalled the program.

No formal post-purchase counseling program has been provided. If buyers have any problem, however, they are welcome to contact the agency for advice.

Windfall Profits and Retention Provisions

The MHHC considered the use of a second, silent mortgage to fulfill HUD's requirement against tenants receiving windfall profits. Legal counsel advised against it, however, fearing that the existence of a second mortgage with such a requirement would make the deal unattractive to private lenders. Ultimately, the agency included a clause in the contract of sale restricting the resale of the unit for five years. During this time, buyers cannot transfer the unit without prior written consent and approval of the MHHC. If the unit is sold within this period, the amount received by the buyers in excess of the demonstration sale price is to revert to the MHHC. After this initial five-year period, the buyers are free to sell the unit and retain any profits.

This same restriction was considered sufficient to assure that demonstration units remain available to low-income families. The MHHC could decide not to approve a sale if it felt that the unit would be lost from the low-income housing stock. As of July 1989, this restriction had not been called into use.

 Provision for Maintenance After Sale

In general, the buyer is responsible for any maintenance needed after the unit is transferred. During the first five years, however, a buyer may apply to the MHHC for a no-interest, extraordinary maintenance loan to cover any such costs. As of July 1989, the proceeds from the sale of the two units that were deposited in this extraordinary maintenance account totalled $14,000.

Handling of Non-Participants

The program allowed families unable or unwilling to purchase their units to remain in them as renters. At the time of the increase in sale price by the city, only two of the families living in targeted units were considered non-participants. These families had expressed no interest in participating and were allowed to remain as renters in their units.
Amount and Use of Sales Income

At the time of sale, the MHHC received lump sum proceeds. The commission used the income generated by these sales to pay for expenses incurred in transferring the units. It deposited the balance in the extraordinary maintenance account to provide no-interest loans to buyers as discussed above.

Impact of the Sales Program

Initially, the demonstration was expected to have a positive impact on the MHHC's financial condition. Single-family, scattered-site units were seen as being more difficult and more expensive to maintain and manage than other public housing units. The sale of these units was expected to eliminate these costs. Due to the limited number of sales that actually took place, however, the impact of the demonstration on the MHHC was minimal.

Conclusions

The demonstration in Muskegon Heights fell short of its goal. Only two units were sold of the original 20 units selected for sale.

The lack of success in transferring the units may be attributed directly to the decision of the city council to raise the sale price to 100 percent of appraised value. This price increase was the result of the council's change in attitude toward the sale of public housing. It effectively discouraged the participation of both potential buyers and lenders. After the sales price was raised no more sales took place. Moreover, due to the lack of city council support, no further sales are anticipated.
Introduction

The demonstration program in Nashville was designed to sell three multi-family developments, containing a total of 85 units, to tenants. All three developments have been sold to a single cooperative whose members include former tenants of those developments as well as tenants from other public housing developments in Nashville. A sale price of $1,825,000 was set by the Nashville Metropolitan Development and Housing Agency (MDHA) based on the appraised value of the property. One million dollars of this price, however, was held by MDHA as a silent third mortgage and is to be forgiven over the first five years of ownership. The remaining $825,000 represented the projected costs of making the necessary improvements to the unit before sale, administering the program and establishing a maintenance reserve fund. The MDHA had originally hoped that the cooperative could secure financing for $800,000, with the remaining $25,000 coming from an escrow account built up with MDHA payment in return for tenants assuming certain maintenance activities during the pre-conversion period. The Consumer Cooperative Bank, however, would only lend the cooperative $550,000. This led MDHA to offer the cooperative a silent-second mortgage for the remaining $250,000. This silent-second will be forgiven at a rate of one-fifteenth per year if the cooperative adheres to a recognition agreement signed by both parties. That agreement, among other things, stipulates that the cooperative operate as a limited-equity cooperative to ensure the availability of future homeownership opportunities for low-income people. After a three year development process, all 85 units were transferred to the cooperative on June 26, 1989.

Managing the Demonstration

The demonstration in Nashville was sponsored by The Metropolitan Development and Housing Agency, which is responsible for economic development, neighborhood development, and public housing in the Nashville metropolitan area. This area encompasses the city of Nashville and the surrounding county. MDHA administers the area's CDBG funds. It also administers 6,336 units of public housing and 2,114 Section 8 certificates and housing vouchers. There were 309 income certified families on the waiting list and another 273 were pending approval. Applications for the Section 8 program number 3,298. Periodically these lists are closed to limit the number of applicants.

The major goal of the demonstration in Nashville was to develop a process for creating homeownership among the public housing tenants. MDHA staff felt that their Turnkey III program was a success and they saw the demonstration as a means of continuing
to offer ownership opportunities. They hoped the demonstration would help them develop an ongoing program to offer homeownership to low-income people. They were particularly interested in developing an effective counseling program for low-income people involved in homeownership programs.

When the idea of participation in the demonstration was first discussed with tenant representatives, they were concerned about possible wholesale divestment of MDHA housing. Once this misconception was cleared up, however, tenant representatives were supportive of the program. Replacement housing did not arise as a major issue since MDHA has received funding for several new public housing developments in the past several years.

Impetus for participating in the demonstration came from the executive director and the housing authority's board and staff. The actual proposal was developed by the assistant director of urban development with the assistance of the staff person responsible for the Turnkey III program. Tenant involvement in developing the proposal was limited by the short time available, but two meetings were held with the residents of the units to be sold: one to present the proposal and receive comments, and the other to vote on the proposal. The proposal had strong support from local politicians and tenants, partly attributable to the successful Turnkey III program administered by the MDHA.

Four major organizations were involved in the demonstration in Nashville. The MDHA had overall management responsibility. This responsibility included marketing the program to tenants, developing rehabilitation plans for the units being sold, overseeing the rehabilitation work, screening applicants, developing legal documents, arranging financing, and developing policies and procedures for the program. The Cooperative Housing Foundation provided training to both MDHA staff and tenants on developing and managing a cooperative. The Nashville Urban League assisted in the screening of participants and collected baseline data on prospective tenants. Finally, the Consumer Cooperative Bank provided a blanket mortgage to the cooperative.

The cost of administering the program over the three and one-half years before the transfer took place was estimated by program staff to be approximately $320,000. This included the labor of staff in the housing management department, and the development department. Beyond this, approximately $30,000 was spent for appraisals, the preparation of two model units, staff training, travel, and supplies. Funds to cover these expenses came from a CDBG grant.

MDHA also received a technical assistance grant from HUD for a total of $49,368. These funds were used for outside counseling services ($32,537), appraisals ($5,410), out of town travel associated with the training of MDHA staff and co-op board members ($4,813), and miscellaneous expenses associated with
training activities and closing costs ($5,608). The funds designated for counseling went to the Cooperative Housing Foundation and to the Nashville Urban League for services provided. According to staff, the amount of the technical assistance grant was woefully inadequate to provide adequate training to the cooperative board and members.

The MDHA encountered several problems in administering the demonstration. Originally, the program was administered by a task force composed of MDHA staff. This caused two problems. First, responsibilities for various tasks were blurred. Second, communications problems arose as residents and other interested parties were not sure where to go for information.

Responsibility for administering the program was then transferred to the homeownership programs coordinator, a new position created in the agency. With this change, responsibilities were more clearly defined and the coordinator began holding monthly meetings with tenants to keep them informed of the program's progress.

Program progress was also slowed by the difficulty of explaining cooperative ownership to tenants. Cooperatives are not prevalent in Tennessee and it took awhile for the staff to learn enough to be able to adequately explain the concept to tenants. Once explained, the staff also had to generate interest in "something unseen" and develop a sense of efficacy among the tenants involved. Program staff believe that generating interest and a sense of efficacy is necessarily a lengthy process that cannot be rushed.

Selecting and Rehabilitating Properties

Nashville selected three projects with a total of 85 units for sale. The three projects included a 48 unit, two-story apartment complex called Edgefield. This development was selected because it was in relatively good condition and the staff felt it was of a manageable size for a co-op. A second development was a scattered site project called Edgehill. It contained 19 units, including both duplexes and triplexes. The third development was also a scattered site development, called South Inglewood. It contained 18 units at two sites, primarily duplexes. The two scattered-site developments were chosen because they were thought to be appropriate for fee simple sale and because they were under construction and had not been occupied. This meant that they would not have to relocate anyone who was not eligible or who did not want to participate in the program.

Since they were new, the scattered site units were in excellent condition but some work was needed to correct erosion and drainage problems on the sites. Edgefield was in fair shape at the time of its selection, needing new heating systems, roofs, moisture protection, and other more minor repairs. MDHA hired an architectural firm to inspect the units to be sold and to prepare a list of needed repairs and improvements. These lists were then
presented to tenants who were given a chance to suggest others. According to program staff, the residents were more interested in cosmetic improvements to the interior of the units such as full wall-to-wall carpeting, while the MDHA was more concerned with improvements to the major mechanicals and the exterior of the structures.

Due to a higher than expected cost estimate, however, a number of the repairs originally agreed upon were eliminated. These items include a playground at one of the developments, full carpeting in the units, a retaining wall at one site, the upgrading of the electrical system, and new heating and air conditioning units.

The total cost of the repairs actually done was approximately $625,000. The repairs were paid for with the CDBG funds managed by MDHA. Upon sale of the units, however, the fund was reimbursed approximately $440,000. Originally, MDHA had hoped to recover the full amount of the rehabilitation costs, but the Consumer Cooperative Bank would not finance the full amount.

Two major problems were encountered in the rehabilitation process. First, the rehabilitation took longer than anticipated and this slowed down program progress. Second, the rehabilitation was more expensive than anticipated, resulting in the deletion of some of the originally agreed upon repairs. Co-op board members were particularly concerned about repairs to the roof soffits that were deleted from the rehabilitation work program. Program staff agreed that not all the needed improvements had been made but felt that the co-op could handle these repairs by drawing on its reserve fund.

The Edgefield development is surrounded on two sides by austere but well kept Section 8 townhouse developments. On the third side is an MDHA owned elderly housing development. This development is in excellent shape. On the fourth side is the back of a fire house and two businesses. The adjacent neighborhood was a community development target area and consists of large old houses. Some gentrification has taken place in the area.

The Edgehill development is on two sites. Site one is surrounded on two sides by Section 235 single family housing. On a third side is a school yard and on the fourth side is a rundown Section 8 development with extensive graffiti and litter. Site two is similar in that it is surrounded on three sides by generally well kept single family houses but on the fourth side there is a rundown, poorly kept Section 8 development. The larger neighborhood is primarily subsidized housing, but most of it is in very good shape.

The South Inglewood development is surrounded on all sides by older generally well kept single family houses. There are a number of vacant lots in the area, however, and the area has drainage problems due to a lack of storm water drains. This may
be rectified in the near future by a CDBG funded project to construct a storm water sewer system in the area. The larger neighborhood is almost all single-family houses occupied by low- and moderate-income people.

Attracting and Selecting Owners

Marketing of the demonstration program to tenants was done through the distribution of brochures, home visits by MDHA social workers and other staff, and meetings held to discuss the program. A periodic newsletter reviewing progress and announcing upcoming meetings was also sent to the residents of the units to be sold.

No set income limit was established for program participation. Rather, program staff set a limit based on the average income of all participants. They wanted to ensure that the average income of participants was at least $10,000. This dollar amount was based on the ability of co-op members to pay the estimated rents needed to cover carrying costs and to maintain a reserve maintenance fund. Prospective participants were also screened based on stability of employment, site manager references, the record of maintenance requests for the unit they occupied, and motivation to participate in a cooperative. This last factor was determined in interviews with prospective participants.

The screening process was initially handled by a task force composed of representatives from the housing management, social services, and development departments. When the tenant cooperative was incorporated in June 1988, however, the interim cooperative board assumed the responsibility for making the final decision as to whom would be able to join the co-op. MDHA staff trained the board in the process of screening and continued to provide the board with the necessary information on prospective participants. The co-op board reviews basic income, family size and reference data on applicants and conducts in-person interviews. These interviews are used to assess the commitment of the applicant to participation in the management of the cooperative. If selected the new members are considered conditional until they complete 14 hours of training on the operation of the cooperative and the responsibilities of members. If they do not complete this training their membership can be canceled. This training of new members is to be conducted by the co-op board's public relations committee. At the time of our visit, this board had not been constituted and a training program had not been developed.

At the time of closing 65 members had been selected. There were 13 vacancies still to be filled and seven tenants were going to continue to rent their units from the cooperative with the assistance of Section 8 certificates provided by MDHA. The qualifying incomes of the 65 co-op board members ranged from $6,204 to $27,385. The average income was $13,993.
Property Conveyance

The means of property conveyance actually used was different from that originally proposed. The original proposal was to sell the units as two separate cooperatives and one condominium. The Edgefield and South Englewood developments were to be conveyed as separate cooperatives and the Edgehill development was to be conveyed as a condominium. The demonstration as actually implemented, however, involved the sale of all the units to one scattered site cooperative.

The major impetus for this change came from the tenants themselves. At one of the first training sessions held by the Cooperative Housing Foundation, the tenants decided to join together and form one cooperative. They felt this would be easier and more secure than forming two cooperatives and a condominium. Those in the units to be sold as condominiums felt that a cooperative would be more flexible if they were to experience financial problems. The MDHA supported this change in program design.

The method used to set the initial cooperative fees also differed from that included in the initial proposal. Originally, the fees were to be based on income and unit size. Occupants of one-bedroom apartments were to pay 28 percent of their incomes, those in two-bedroom apartments were to pay 30 percent of their incomes and those in three-bedroom apartments were to pay 32 percent of their incomes. The pricing method actually used, however, involved three fee structures. The original members of the coop, that is those who joined before November 28, 1988, pay flat rates of $192 for a one-bedroom unit, $233 for a two-bedroom unit, and $279 for a three-bedroom unit. Elderly or disabled coop members, however, pay $150 for a one-bedroom unit and $155 for a two-bedroom unit. Finally, members after November 28, 1988, pay $195 for a one-bedroom unit, $265 for a two-bedroom unit, and $325 for a three-bedroom unit. The reason for this change was staff concern that the original pricing scheme tied to income would have led to problems as people buying similar units would be paying very different prices. This change was said to be popular among program participants since it meant many would be paying lower charges.

Downpayments or membership fees were required of all cooperators. For the original members of the cooperative the downpayment came from a non-refundable "earned credit account" that had been established for each unit at the beginning of the conversion process. Twenty dollars per unit was added to this account each month in return for certain routine maintenance work performed by the residents. At the time of closing the average amount that had accrued per unit was $373. The amount in this earned credit account plus the original security deposit plus a $30 membership fee equaled the price of the membership certificate. No out-of-pocket cash was required of existing tenants. New members of the cooperative, however, are required to pay a subscription price of
$500. Four hundred dollars of this is considered the "value of the occupancy agreement" while $100 is a non-refundable "working capital contribution." The closing costs associated with the blanket mortgage were paid by the MDRA.

The biggest problem encountered in the conveyance of the properties was the lack of state law on cooperatives. This meant that the staff had to do a lot more legal work. Because the co-op will be renting seven units to non-participants it also means that the cooperative will have to pay taxes as if it were a business. State law has no special provisions for low-income cooperatives, but program staff hope to change this in the future.

The cooperative was incorporated as the New Edition Community Apartments Housing Cooperative, Inc. (NECA) on June 8, 1988. The Charter of Incorporation states that the cooperative shall not result in pecuniary gain or profit to the members. It also establishes a seven member board of directors and stipulates that the cooperative may be dissolved with the assent of not less than two-thirds of the members.

The bylaws of the cooperative provide further detail on how the cooperative will be managed. They state that preference for membership will be given to persons who reside in the units at the time of their purchase by the cooperative. For all other vacancies, priority is to be given to persons who have low- or moderate-incomes. The transfer of memberships is highly regulated by the board. If a member wishes to leave the cooperative, the board has the right to purchase his membership at its transfer value. That value is based on the sum of the subscription fee and/or sweat equity paid for initial membership; the value of any improvements installed at the member's expense; the principal amortized by the cooperative attributable to the dwelling unit involved after the first three years; and the amount of any sweat equity performed, as determined by the board of directors. These bylaws also specify that the board of directors shall be elected by a plurality of members voting at an election meeting. Except for some initial staggering, the terms of the board members will be three years. Finally, the bylaws call for three standing committees: a finance committee, a public relations and membership training committee, and a maintenance and operations committee.

The co-op board has also adopted a set of house rules and more specific noise guidelines, pet policy, and grievance procedures. A 10 percent late charge is to be assessed on rents paid after the tenth of the month.

A "Recognition Agreement Between the MDHA and NEHC" contains other important terms of the conveyance. In this agreement, MDHA agrees to provide technical assistance to NECA and agrees that members who default will be given priority for MDHA administered housing programs for which they are eligible. NECA agrees to
give preference for membership to applicants who reside in public or Section 8 housing; to recognize MDHA's $250,000 interest in the property based on the difference between the cost incurred by MDHA and the amount of the first mortgage (which will be forgiven at one-fifteenth per year); to recognize MDHA's $1,000,000 interest in the property based on the difference between the assessed value of $1,825,000 and the sum of the downpayment, first mortgage and second mortgage (which will be forgiven at 20 percent per year); to allow MDHA one non-voting seat on the board of directors; and to grant the MDHA the right to approve or disapprove the initial selection of a professional management agent during the first two years. This recognition agreement is to run for 15 years.

Overall, both the program staff and the cooperative board are very happy with the method of transferring units to the tenants and they are confident that the cooperative will be a success. This confidence is based on the extensive training that the co-op board members received and a conservative operating budget.

Financing

The MDHA had a difficult time finding financing for the sale of the units in the demonstration. MDHA originally expected to finance sales through either a Tennessee Housing Development Agency (THFA) low-interest loan program or through money purchase mortgages. In pursuing THFA loans for the condominium sale originally envisioned, MDHA loans received a "cool reaction" from loan originators because the loans would have been very small (in the $10,000 to 20,000 range). This meant that the lenders would not be making much in the way of loan origination fees. Once MDHA decided to sell all the units to one cooperative they approached the National Consumer Cooperative Bank (NCB) for financing. According to program staff, the NCB was at first reluctant to provide the financing because they had a bad experience with another low-income cooperative in Tennessee. The staff persisted, however, and the NCB finally agreed to provide the financing.

MDHA set an effective sales price of $825,000 based on the direct expenses incurred in rehabilitating and transferring the properties and the need to establish a reserve fund for maintenance and debt service. They originally hoped to finance $800,000 of this with the remaining $25,000 coming from the escrow accounts established for tenant maintenance. In the end, however, the NCB was only willing to provide a $550,000 first mortgage. The remaining $250,000 was covered by a silent-second mortgage held by MDHA.

The term of the first mortgage is 15 years. The payments, however, are based on a 30 year schedule. The initial interest rate is 11.7/8 percent but this will be adjusted at the end of the fifth and tenth years. The interest rate for all loan periods is based on the average yield for U.S. Treasury
securities with five-year maturities plus three percentage points. NCB charged a closing fee of $5,000. NCB also stipulated a number of conditions including the sale of at least 62 units and an 85 percent occupancy rate at closing; a $60,000 deposit in an NCB Savings Association for operating and replacement reserves; and an education and training plan for the board of directors and cooperative members. MDHA also had to submit a final income and experience pro forma providing a three percent contribution to reserve for replacement, two percent to a general operation reserve, five percent to a vacancy and collections loss reserve, and 1.15 debt service coverage, including vacancy loss but excluding reserve deductions.

The cooperative's operating budget shows the following expense and income projections for the first year of operation:

**Expenses**

- Operating expenses (including management fee, water and sewer charges, office equipment, legal fees and board training) **$75,456**
- Maintenance expenses (including grounds, maintenance, structural repairs and heating, plumbing and electrical maintenance) **$31,301**
- Taxes **$27,368**
- Insurance **$10,068**
- Debt service **$69,748**
- Reserves **$19,000**
- **TOTAL** **$233,141**

**Total Income**

- Carrying charges (from 65 co-op members) **$205,356**
- Tenant rental charges (from Section 8 renters) **$31,848**
- **TOTAL** **$237,204**

This operating budget projects a $4,062 surplus for the first year of operation. This, however, does not include carrying charges to be paid by the occupants of the 13 vacancies which are currently in the process of being filled. The potential income
from these vacancies is an additional $38,820. Thus, at full occupancy there would be an operating surplus of $42,882.

Counseling

MDHA provided a wide range of counseling to tenants. First, each tenant in the developments sold was visited by a social worker who explained the homeownership program and who discussed the pros and cons of homeownership with the tenants.

MDHA's maintenance personnel also provided two hour training sessions with some of the tenants to instruct them in preventative maintenance and minor home repairs. This was hands on training where residents watched the maintenance trainer perform a repair and then did the repairs themselves. Tenants were also provided with a well illustrated maintenance manual specifically designed for the appliances in their homes. The housing authority also provided each tenant with a tool box containing basic tools for repair operations. Unfortunately, only about one-half of the buyers received this training before the training resources were exhausted. The program staff anticipate that the management company hired to manage the cooperative will complete the maintenance training.

The Nashville Urban League was also engaged to provide the following services:

1. Interview participants and waiting list applicant to collect home buyer baseline data;

2. Prepare an evaluation of each participant indicating specific budget, social, or other homeownership counseling needed prior to the point of sale or indicate that the applicant will be unable to meet the requirements of the program; and,

3. Provide specific counseling as needed to individual participants as indicated by the initial or follow-up evaluations and provide reports on the progress of the applicant.

Beyond these activities the Nashville Urban League also held group training sessions on resolving financial problems and financial budgeting. They were paid a total of $12,500 for these services.

Finally technical assistance in establishing and running the cooperatives was provided by The Cooperative Housing Foundation (CHF). Their contract specified the following services:

1. Provide MDHA with samples and review basic legal, co-op transfer, cooperative incorporation, and condominium transfer documents;
2. Assist in the formation of condominium and cooperative associations and begin bylaws preparation;

3. Conduct consultant training sessions for tenants on general cooperative and condominium organizations;

4. Conduct training sessions for tenants on condominium and co-op management;

5. Conduct training sessions for co-op and condominium officers; and,

6. Provide follow-up training/problem solving sessions with home buyers and co-op members.

Since the plan for selling some of the units as condominiums was altered after the first training session, the remaining training sessions focused exclusively on forming and managing a cooperative. The CHF held a total of seven training sessions that involved a combination of lectures, discussions and role-playing exercises. The bylaws, house rules, and other governing documents were developed by program participants during these meetings. CHF was paid a total of $25,000 for their services.

Once the interim co-op board was established, its members began attending meetings of the National Association of Housing Cooperatives. They received additional training at workshops held at these meetings and benefited from informal discussions with other attendees.

Co-op board members are very satisfied with the training they have received and feel confident that the cooperative will be a success. They feel that the training sessions held by the CHF were very helpful and they plan on continuing their training by attending meetings of the National Association of Cooperative Associations. Board members felt that they had come a long way in understanding how to manage a co-op. One commented, "When it (the training) started it was like sitting in a Greek class. Now we are running a business. I never thought I would be running a business."

Windfalls Profits and Retention Provisions

A variety of methods have been used to ensure that windfall profits will not result from the sale of the units to the cooperative. First, the cooperative was incorporated under Tennessee's Nonprofit Corporation Act. These articles stipulate that "the purposes for which the cooperative is formed shall not result in pecuniary gain or profit to the members thereof."

Second, MDHA has retained a $1,000,000 interest in the property that will be forgiven at a rate of 20 percent per year. This is part of a recognition agreement signed by both parties. Third, MDHA has retained a $250,000 interest in the property that is to
be forgiven at a rate of one-fifteenth per year. Thus, after fifteen years both interest will be forgiven.

The bylaws of the cooperative regulate the resale value of individual memberships. The value of a certificate is based on the sum of the subscription fee and/or sweat equity originally contributed; any board approved improvements made at the members expense; the principal amortized by the cooperative attributable to the dwelling unit involved after the first three years; and, the dollar value of any sweat equity performed, as determined by the board of directors.

Other provisions ensure that the units will remain available for low- and moderate-income people. The articles of incorporation, the "Recognition Agreement," and the cooperative's bylaws all stipulate that priority for membership will be given to low- and moderate-income people. The recognition agreement further stipulates that priority be given to those living in MDHA public or assisted housing. The cooperative has also retained the right of first refusal in the event a unit is offered for sale. The purchase price of the certificate would be determined as described above.

Both the program staff and the cooperative board are satisfied with the windfall profit and retention provisions. Although no one will be accruing substantial amounts of equity they feel that they will benefit financially from the lower housing costs and from what they expect to be the relatively fixed nature of these costs.

Provision for Maintenance After Sale

Two operating and replacement reserve funds have been capitalized with sale proceeds. Together the funds contain $86,000. Originally there was to be a single fund, however, the NCB required that the co-op invest $60,000 of the reserves with them. The co-op board has invested the remaining $26,000 in a local bank. The program staff and board felt that this local deposit was important in establishing the co-ops credibility with the local business community. The loan agreement with NCB specifies that the co-op maintain a reserve balance of at least 10 percent of the annual shareholder payments. Furthermore, the recognition agreement gives MDHA the right to approve or disapprove any expenditures from the reserve accounts that would exceed 10 percent of the balance on that account for the first years of operation.

The management of the cooperative during the first year is to be handled by MDHA. The original plan for managing the cooperative was to hire a private management company. The co-op board placed requests for proposals in several national cooperative publications and received two submissions. Neither submission, however, was acceptable to the co-op board. One was from a local company with no experience managing cooperatives and one was from
an out-of-town company. This led to MDHA offering to manage the co-op for the first year.

The contract signed between the MDHA and NECA specifies that MDHA shall provide an on-site manager who will work a minimum of 20 hours per week. The manager will be in charge of hiring maintenance and other needed personnel, collecting co-op fees, scheduling maintenance, paying bills, managing accounts, and performing other management activities. MDHA hired a new staff member to act as the co-op manager and has assigned a second staff person to provide part-time assistance. The year-long contract is for $30,000. At the time of our site visit the management staff was in the process of establishing various management procedures. A commercially available software program was said to be very helpful in this effort. It handles record keeping, billing, maintenance scheduling, and other aspects of managing a cooperative. The MDHA has subcontracted the maintenance to a local company.

**Handling Non-Participants**

The need to relocate tenants who did not qualify or who did not want to participate in the demonstration was minimized since approximately half of the units were new and had not been occupied at the time they were selected for inclusion in the program. Those moving into these units were pre-screened to ensure they were both eligible for and interested in participating in the program. In fact, they signed an agreement saying they would move if they did not participate in the program. Several of these people did, in fact, move to other scattered-site units.

Non-participants in the units that were occupied were given two options. First, they were enticed to move with Section 8 certificates or offered scattered-site units. Three tenants chose this option. Second, they could stay in their units and rent from the co-op with the assistance of Section 8 certificates. Seven tenants choose this option. During the three-year period of development other families moved out for reasons such as needing a larger unit or moving to another locality. These units were left vacant so that the co-op board could select new members after the properties were transferred to the cooperative.

**Amount and Use of Sales Income**

The total amount of sales proceeds was $550,000, the amount of the first mortgage. Some of these funds, however, were used to capitalize the reserve funds ($83,000) and to pay for closing costs ($25,086). The remainder of the funds ($441,914) were used to partially reimburse the CDBG loan fund for the costs of rehabilitating the units.
Impact of the Sales Program

For accounting purposes, the units sold under the Nashville demonstration program were part of several projects. Thus, it was impossible to accurately estimate the amount that the MDHA will lose in operating subsidies and the amount that it will save in actual operating and maintenance expenses.

One non-financial benefit of the demonstration program was a great learning experience for MDHA staff in how to develop a limited equity cooperative. Yet, at the present time, there are no specific plans to put this new expertise to use in helping to establish other cooperatives in the Nashville metropolitan area. MDHA is, however, involved in establishing a new nonprofit organization with a major goal of developing affordable housing. The staff's new skills may be called upon to assist the efforts of this nonprofit once created.

The sale of the units to tenants will have a positive impact on the tax revenues of the local government. No property taxes were paid on the public housing units before they were sold to the cooperative. The co-op, however, will be paying $27,368 a year in property taxes. This amount, which is based on a commercial tax rate of 40 percent of assessed value, will be reduced if all but one of the Section 8 rentals are converted to co-op member units or if legislation designed to allow limited equity co-ops to rent some of their units and retain their non-commercial tax status is passed in the state legislature. The non-commercial tax rate is based on 25 percent of assessed value.

It is too early to tell if the demonstration will have any effect on the surrounding neighborhoods. Given that the surrounding properties are mostly public or assisted housing, it is not likely to have a great impact.

Finally, based on staff and co-op board members comments, the demonstration is having a positive impact on the tenants. Staff say they have noticed a change in the appearance of the project since the sale. People, they say, are more active in picking up trash and scolding children for inappropriate behavior in the area. The co-op board members interviewed commented that co-op members are accepting more responsibility for the upkeep of the developments and enforcing the rules established by the co-op membership.

Conclusions

After a three year development process, the MDHA was successful in transferring 85 units of public housing to a limited-equity cooperative composed of former tenants and low-income people from other public housing developments. This is a particularly interesting demonstration program because it involved the sale of three developments to one scattered-site cooperative. It is also
noteworthy for the amount of training and counseling providing to the co-op board and the membership.

When staff members were asked about the major factors that led to the successful transfer of the units, they stressed several aspects of their program. First, being a combined community development, redevelopment, and housing agency they had easy access to CDBG funds which were used to fund and subsidize the $625,000 rehabilitation work done to the units before sale. Second, they developed an extensive screening process that emphasized tenant willingness to participate in cooperative management as well as income, credit rating, and the more standard screening criteria. Third, they were fortunate in that approximately 35 of the units selected for sale were vacant at the time they were included in the program. This meant that the problems associated with relocation were minimized. Finally, they provided extensive training to program staff, co-op board members and to the prospective cooperators over a several year period.

This is not to say, however, that the demonstration program in Nashville did not experience any difficulties. Early in the demonstration, progress was slowed by two major problems: lack of clear responsibility for managing the demonstration, and tenant difficulty in understanding and accepting the concept of cooperative ownership. These problems were overcome when a MDHA staff member with experience in homeownership programs was put in charge of the demonstration and the Cooperative Housing Foundation began its work educating tenants about cooperative ownership. Problems also arose in the process of deciding on and accomplishing the rehabilitation of the units sold. In fact, a number of the improvements originally planned were never completed due to a shortage of available funds. Finally, arranging financing for the sales was difficult. After several unsuccessful attempts to secure financing from other sources they began discussions with the National Cooperative Bank. After protracted negotiations, NCB provided the first mortgage for the sale.

According to the executive director they are not interested in participating in an extended sales program unless it offers replacement housing. An extended sales program without replacement units would result in the sale of the best units to the best tenants. This, he believes, would cause the MDHA problems. Constraints on the number of units they could ultimately sell were said to include the condition of the housing stock and the motivation and financial condition of residents.
PUBLIC HOUSING HOMEOWNERSHIP DEMONSTRATION

NEWPORT NEWS CASE STUDY

Introduction

The demonstration program in Newport News, VA was designed to sell 15 scattered-site, single family houses to their current occupants. A local savings and loan association provided market rate financing for the first mortgages and the housing and redevelopment agency provided silent-second mortgages to make ownership affordable to the buyers, who will be paying a maximum of 30 percent of their incomes for housing expenses. Newport News was the first demonstration program to reach its sales goal. As of September 1986, all 15 units had been sold to former public housing tenants.

Managing the Demonstration

The demonstration in Newport News is managed by the Newport News Housing and Redevelopment Agency (NNHRA). It administers the city's CDBG program, Public Housing, Section 8, Urban Homesteading and other housing programs and undertakes other redevelopment activities. The NNHRA manages approximately 2289 units of public housing and administers 972 Section 8 certificates and 41 housing vouchers. About the time the demonstration was approved there were approximately 600 families on the waiting list for public housing but this is not an accurate indication of the demand. The NNHRA limits advertising to keep the number of applications down to a number that can be accommodated within a one year period.

The management of the NNHRA hoped to achieve three goals with the demonstration program. First, they were interested in divesting themselves of the "non-traditional" single family units that they considered difficult to manage and maintain. These units, which were acquired from the FHA and VA, are scattered throughout the Southeast section of town and have unique fixtures and mechanical systems. According to program staff, "maintaining occupancy of these properties as public housing had proven difficult, time consuming, and expensive."

The second goal of the demonstration was to provide residents with "a stake in the place they live -- more opportunity -- more motivation." Furthermore, residents had been asking to buy these units and the demonstration program provided a means of selling them. Many of the residents had been living in the units for five years or more prior to the announcement of the demonstration.

The third goal was to improve the surrounding community. All the units sold were in a community development target area in which other housing and neighborhood improvement activities were
targeted. According to a description of the demonstration prepared by the NNHRA, "The scattered site units could have been sold to investors and maintained in marginal condition for rental purposes; however, the renovation and maintenance of the units by the PHA encouraged near-by residents to improve their own properties and exhibit an increased interest in their neighborhood. A logical consequence was to contribute to this improved neighborhood stability and renewal by providing owner-occupied homes through the homeownership program."

The idea to participate in the demonstration came from the director of housing management. He along with the director of finance, the director of programs and the executive director of the agency developed the original proposal for the program. Once developed, the proposal was reviewed by the tenants of the units to be sold. According to the program director, the tenants had no objection to its provisions. In fact, there is no evidence of opposition to the program from residents, commissioners, or staff.

Three major groups were involved in the demonstration. The NNHRA was responsible for overall project management, the city's Office of Human Affairs was responsible for providing pre- and post-purchase counseling, and the Community Savings and Loan Association, a local minority-owned lender, provided the first mortgages for all sales.

The director of housing management at the NNHRA had primary responsibility for administering the program. The staffing costs for the demonstration were estimated to be $15,000 per year and an additional $100 was spent on printing. Most of the program activity took place over a year's time. Approximately one-half of the staff member's time was spent administering the program.

The NNHRA management did not apply for a technical assistant grant since they felt that they did not need the funds and they wanted to keep the program as simple as possible. Also, the city's Human Affairs agency did not charge the NNHRA for the counseling services provided.

The only problem encountered in the design and management of the demonstration in Newport News was in obtaining private financing. All the banks initially approached (11 in all) refused to participate in the program. The NNHRA, however, felt that private financing was an important element of the program since they wanted the buyers to be independent of the agency. They were finally successful in involving the Community Savings and Loan, a minority-owned lending institution. Program staff sold the idea to this thrift by suggesting it would be good publicity, by appealing to "community pride and responsibility," and by agreeing to buy back loans in instances of default during the first five years.
Selecting and Rehabilitation Properties

The original goal was to sell all 15 of the scattered-site units owned by the agency. This, in fact, was accomplished by September 1986. These units were in very good shape when they were selected, having been rehabilitated in the late 1970s. Before transfer, NNHRA staff inspected all the units, talked with residents about maintenance problems, and made needed repairs including the replacement or repair of storm windows, screens, downspouts and gutters, and fences. The estimated cost of these repairs was $30-40 per unit and they were paid for by the NNHRA.

All the units sold were in the Southeast section of town which is a low- to moderate-income minority area. It is predominantly single-family, but there are some multi-family developments. In general, the housing in this area is in good shape but there are abandoned and poorly maintained properties scattered throughout the area. The homeownership rate was estimated to be about 50 percent with houses selling in the $25,000-50,000 range. This area has been a target area for the city's CDBG housing rehabilitation and neighborhood improvement programs.

Attracting and Selecting Owners

The NNHRA structured the program so that all current occupants of the units to be sold could afford to buy them. The current occupants had originally been chosen for these scattered-site units because they were employed and showed an interest in taking on more housing related responsibilities. Unlike other public housing residents, these tenants were responsible for maintenance activities, such as yard upkeep, and for paying their own utility bills which they then deducted from their rent payments. Thus, these people had been carefully screened before they moved into the units and had assumed more responsibility for their units than other public housing residents.

At the time the program was approved, 14 of the 15 units were occupied. Only 13 of the families in those units bought them, however, since one family left public housing before the sales. To fill the two vacant units a lottery was held. Flyers announcing the program were sent to all public housing residents in the city. The program was also explained at a tenant council meeting and a separate meeting was held for those who were interested in the program.

Fourteen people participated in a lottery for the four bedroom house and 60 people participated in a lottery for the two bedroom house. The criteria for participating in the lottery were that 30 percent of their income would have to cover housing costs, applicants must have a good house keeping record, a stable income source and history, and the proper number of people in the household for the unit involved.
All program participants were visited in their homes, where the program was explained and questions were answered. A follow-up meeting was also held in the offices of the housing authority to allow residents to go over the sales contract and to discuss the responsibilities of homeownership.

The characteristics of the new owners vary considerably. Nine of the 15 are married while five are single females and one is a single male. Incomes range from $7,659 to $29,639. The average income was $23,909. The ages of household heads range from 27 to 65. Household size ranges from two to seven persons. All the families are black.

**Property Conveyance**

All the properties were sold fee simple. The average sales price was $24,213. The sales prices were based on the assessed value (tax value), although the actual price paid by the new owner was based on affordability. The difference between the assessed value and what could be afforded based on 30 percent of gross income going to housing costs was covered by a silent-second mortgage held by the NNHRA. These silent seconds averaged $7,501. The closing costs, which were approximately $1,525 per transfer, were paid by NNHRA out of the sales proceeds. A total of $22,863 was spent on closing costs.

**Financing**

Financing of the sales was provided by a private, minority-owned bank. Private financing was sought to give the new owners a sense of independence from the housing authority. The PHA approached the bank and after several discussions the bank agreed to finance all 15 sales. The only complication was that at one point in the discussions the bank's board asked for credit references on the tenants. Since most of the prospective owners either had not established a credit history or had a bad one, the housing agency offered to show rent payment histories instead. This was accepted by the board and all applicants were approved. Other factors that influenced the bank to participate were the five year buy-back assurance offered by the NNHRA and a good equity position in the units. Due to the silent-second mortgage, in most cases the amount being borrowed was substantially less than the appraised value.

The bank committed approximately $300,000 to the loans. The interest rate charged was 11.25 percent, which was one to two percentage points higher than what regular customers were paying at that time. Concern over this higher rate was expressed by the executive director of the NNHRA who felt that this rate was unjustified and hoped that if any more units were to be sold, program participants could obtain market rate loans. The terms of the loans varied, depending on ability to pay, from five to 15 years. The bank plans to keep these loans in their own portfolio, at least until they are "seasoned."
In reviewing the loan applications the bank loosened its underwriting criteria in several ways. First, it did not require a downpayment. In designing the demonstration program NNHRA staff felt that requiring a downpayment would prohibit some families from participating and the bank agreed to this provision. Second, the bank did not rely on traditional credit histories of the buyers. Instead, rent payment histories were considered. Finally, the bank allowed higher than normal debt-to-income ratios.

The bank has agreed to notify the PHA in cases of late payments or impending defaults and the Office of Human Affairs has agreed to provide individual counseling to anyone having problems meeting their payments.

According to a bank representative, as of July 1989, there were no foreclosures and although several of the new owners had in the past missed one or two payments, no one was in danger of default. The bank has a counselor who has visited several of the program participants to impress upon them the importance of paying on time. This has apparently been effective. Overall, a bank representative described the payment history of demonstration participants as about as good as their other customers. One program participant has refinanced his home loan with another bank in order to make some improvements.

Counseling

Homeownership counseling has been primarily handled by the Newport News Office of Human Affairs (OHA), a HUD contracted housing counseling agency. This agency has offered program participants individualized pre-purchase and post-purchase counseling on budgeting and money management, repair and maintenance, and the responsibilities of homeownership. Particular attention was paid to financial budgeting and the importance of paying mortgage bills on time. According to the counselor who worked with the buyers, when program participants rented from the NNHRA, many got in the habit of paying their rent last, after they had paid for food and other essentials. The key according to the counselor, is to get people to pay their mortgage first. The housing counselor also accompanied each buyer to the closing. After the sales, the counselor was prepared to provide employment training, child development and care, emergency services and educational assistance, but these services have not been needed. The counselor continues to check with the owners periodically to see if they are having any problems. Few have been reported.

Formal group counseling sessions consisted of one session on what to expect of homeownership and two sessions on how the homeownership program would work and on the responsibilities of both the buyers and the PHA. Attendance at the counseling sessions was mandatory and there was full participation.
Furthermore, counseling on the process of obtaining a loan was handled by the lender. Each prospective buyer met with the lender several times to discuss this topic.

Windfall Profits and Retention Provisions

The NNHRA has retained the right to buy back the house for the outstanding mortgage balance if the family wants to sell or defaults within the first five years of ownership. After this time the family is free to sell the house to anyone and keep any profit. As of July 1989 this buy-back provision had not been called into use.

Provision for Maintenance After Sale

The PHA has provided the new owners with a five year warranty against the total failure of the following items: roof, hot water heater, furnace, refrigerator, plumbing, and the electrical system. This warranty only applies if the item needs to be replaced, not if it needs to be repaired. Funds for replacements come from a reserve fund established with sales proceeds. As of July 1989 a total of $4,416 had been spent on repairs including rewiring a furnace and replacing a refrigerator and a water heater. A balance of $227,824 in the reserve account will be more than sufficient to cover repairs throughout the warranty period.

Handling Non-Participants

With the exception of one household that left their unit due to a family break-up, all of the units occupied at the time of program initiation were bought by the families living in them. Thus, the program involved no relocation.

Amount and Use of Sales Income

The PHA received $250,683 from the sale of the 15 properties. A total of $22,836 of this was used to cover closing costs and $4,416 has been used for repairs covered under the warranty. The NNHRA plans on using the remainder of the funds to provide homeownership opportunities to other public housing residents. With the assistance of the Virginia Housing Development Agency, for example, they are currently building eight houses that will be offered to qualified public housing tenants. Funds from the sale of units under the demonstration will be used to write-down the sales price of these new units. They intend that all the demonstration sales funds will go to providing other homeownership opportunities to public housing residents. This is in keeping with their philosophy of helping families move out of public housing.
Impact of the Sales Program

The sale of the 15 units within the demonstration was said to have a negligible impact on the operating subsidies the PHA receives from HUD. The sale of these units will decrease the operating subsidy by $14,717 per year, which is less than one percent of the total subsidy provided by HUD. Maintenance and operation costs will also drop, which the agency believes will about offset the loss in operating subsidies. No actual figures are available, however, on decreased maintenance and operating costs. The agency is also left with over $200,000 to put toward other homeownership projects. Further, the executive director felt that the program was beneficial in that it generated a lot of good publicity.

The impact of the program on the local government includes increased taxes and some costs involved in providing counseling to program participants. The buyers pay taxes on the full assessed value of the property, which according to Virginia law, has to be 100 percent of actual value. The impact on the program on the surrounding neighborhood was thought to be mildly positive as some owners had made improvements to their units. Given the small number of units involved, however, no dramatic impact has been observed.

Conclusions

The demonstration program in Newport News was a clear success. The goal of transferring 15 units to public housing tenants was achieved in a very short period of time. The program participants have been owners for almost three years and none have defaulted on their loans. Moreover, all those involved in the demonstration have very favorable opinions of it. It relieved the PHA of the responsibility of administering and maintaining scattered site units while fulfilling the objective of housing for low- and moderate-income people.

Several factors appear to have contributed to the success of this program. First, it was a relatively small program, involving 15 units. Second, it involved the sale of single family homes. Clearly the amount of counseling and training required for the sale of these units was much less than what would be needed in the sale of multifamily units. Third, the NNHRA structured the sales so that all the existing tenants could afford to buy their units. This was achieved by writing down the effective sales prices, by not requiring downpayments, and by using sales proceeds to cover closing costs. The fact that tenants did not have to come up with money for a downpayment or for closing costs also meant that the transfers could take place quickly. Finally, the tenants in the units sold had been carefully screened and were already responsible for some maintenance activities and for paying utility bills. Thus, these tenants were probably better prepared to assume the responsibilities of homeownership than are many public housing tenants. The executive director credited HUD
for allowing them the flexibility to design the program the way they wanted.

The NNHRA is interested in selling more public housing units, but only if replacement units are made available. According to the executive director, both the city council and the housing authority board feel strongly that they do not want to decrease the overall supply of public housing in Newport News.
Introduction

Paterson's plan to convert the 242 unit Brooks-Sloate Terrace apartments into a cooperative whose units would remain permanently affordable to low-income households is the most ambitious sales program in HUD's national Public Housing Homeownership Demonstration. It is also somewhat unique in that the housing authority plans to transfer the project to the co-op at no cost, which reduces the qualifying incomes of buyers.

Although the co-op has not yet closed, the Brooks-Sloate interim board of directors is a well organized, sophisticated group of future-owners who have for the last two years overseen the development of a detailed set of operating guidelines, bylaws, rules and regulations. Closing has been delayed primarily due to the extended length of the renovation period. Because modernization is being funded through HUD's CIAP program, title cannot be transferred until all work has been completed.

The future of the co-op has also been clouded by the settlement of a lawsuit brought against HUD and the housing authority over the issue of involuntary relocation of nonbuying tenants of Brooks-Sloate. Under terms of the settlement, the housing authority is prohibited from moving nonbuying tenants from Brooks-Sloate to other public housing units against their will. HUD has agreed to provide the housing authority with sufficient Section 8 vouchers to accommodate all nonbuyers who wish to remain in Brooks-Sloate as tenants of the cooperative. At the time of this writing, the housing authority was conducting a final survey to determine the number of families who wished to join the co-op but had not as yet done so, and the number of families who wanted to continue renting their apartments. Depending upon the split between co-op members (buyers) and renters, (nonbuyers), and the financial implications of this division on the co-op, the decision will be made to either proceed or cancel the conversion.

Managing the Demonstration

The Paterson, N.J. Public Housing Authority has 2,390 units under management, including the 242 unit Brooks-Sloate Terrace project it is converting to a cooperative under the PHHD. A total of 1,698 units are family housing and 692 units are in elderly projects. Brooks-Sloate Terrace consists of 42 buildings on 23.2 acres of land in the city's northwest section. Thirty-nine buildings are row-house type structures consisting of four to eight dwelling units per building. Brooks-Sloate was built in 1950-51.
The Paterson PHA does not administer the city's Section 8 program and therefore cannot coordinate allocation of certificates and vouchers with the PHHD to facilitate relocation. The PHA's waiting list of eligible families is in the area of 1400. With turnover in public housing between 140-170 families per year, the waiting list will last for 10 years.

The PHHD proposal to HUD was prepared by the PHA executive director with the full support of the mayor. Interest in converting Brooks-Sloate Terrace to homeownership originated in 1973 when the city asked HUD for permission to convert the project to a cooperative. Again in 1984, before the PHHD was announced, the PHA hired Joseph Burstein, Esquire, a former HUD official, to write a proposal to HUD utilizing Section 5(h) to convert Brooks-Sloate to a condominium. Burstein's work laid the groundwork for Paterson's PHHD application.

The goals of the project may be summarized as follows:

-to make the homeownership dream possible for low income families through cooperative arrangements;

-to teach the value of saving and accumulating assets that can be passed on to children; and,

-to create "pass-through" or transitional housing for upwardly mobile public housing tenants.

The executive director and other members of the staff and at least one PHA commissioner expressed reservations over the replacement housing issue, this being the first time the authority will have sold any housing under Section 5(h). The PHA has never demolished any public housing units and, according to the PHA executive director, "there is no prospect that we will. We are 100 percent full, save for two units awaiting rehabilitation."

Tenants were not involved in the preparation of the PHHD proposal. The mayor, who is also a state senator, appeared before the PHA board urging it to apply. Although he cannot break out personnel from non-personnel costs, the executive director estimates that total costs of the homeownership demonstration will range between $240,000 and $270,000 over the four years it will take to complete the Brooks-Sloate conversion. This comes to more than $1,000 per unit. In addition to personnel costs, there are fees for planning and designing the demonstration, legal and counseling fees, and appraisal and engineering costs. After the PHHD application was approved by HUD, a newly appointed PHA commissioner raised the replacement housing issue and continues to do so.
The tenant council of Brooks-Sloate Terrace was not very active before the conversion began and has since been replaced by a co-op interim board of directors.

The PHA received a $50,000 technical assistance grant from HUD which it used to fund an initial contract for counseling and overall planning and design with two consultants, and to pay for an outside appraisal of the project and engineering fees. According to the PHA executive director, he would have recommended against participation in the PHHD without the TA grant, although he thinks his board might have overruled him.

From a management standpoint, the project has received continuing high-level support within the housing authority. Despite early signs of city and state support, however, the executive director expressed disappointment over the lack of financial participation in the project by either government. The lack of outside funding is a major reason why the housing authority has been unable to create a city-wide mutual housing association (MHA), of which Brooks-Sloate was to be part. The function of the planned MHA is discussed below.

The Brooks-Sloate co-op conversion is the largest in HUD's national homeownership demonstration, the slowest to come to closing and, because of litigation over the relocation issue, one of the most important projects in terms of national housing policy. The reason for the extended conversion period, which now exceeds four years, has to do with the fact that the extensive renovations are being financed with HUD modernization funds. This means that all work must be completed before title to the project can be transferred to the co-op. While additional financial support from the city and state would not have shortened the length of the modernization period, once all improvements have been completed, money for more staff to work with potential buyers, and to help in paying for appraisals and engineering fees would advance the date of closing.

The outcome of the relocation-related litigation, which is discussed below, requires the housing authority and co-op to allow a substantially larger number of non-buyers to remain in place as continuing renters than the original PHHD plan would have permitted. This means that, should the co-op eventually close, the Brooks-Sloate conversion will test the proposition that a low-income, limited equity co-op can prosper socially and financially as a self-governing community of homeowners, and as landlord of low-income tenants who are either too poor to afford to buy, or who are not interested in buying their apartment.

Selecting and Rehabilitating Properties

Paterson's application calls for the conversion and transfer of 242 housing units. The reason for selecting Brooks-Sloate Terrace for homeownership conversion is simple. It is only one of two family projects in Paterson that consist of low rise,
relatively low density, townhouse units with individual front and rear entrances.

Substantial renovations have been necessary to make the project sales-ready. All repair work is being contracted out. Current repair work follows on the heels of major repairs which were made beginning in 1980. All windows were recently replaced. Entrance doors were replaced. Storm and screen doors have been installed. Improvements were made to the heat distribution system. Bathrooms and kitchens were renovated. Siding is being replaced and extensive street repairs are now underway. All repairs are being financed by HUD through the CIAP program. Estimated repair costs are approximately $28,000 per unit. No relocation due to repair work has been necessary although this has slowed the pace of the modernization work.

As of September 1989, rehab was approximately 85 percent complete. Interiors still needed new doors, patching and repainting, and punchlist work had to be completed. Major exterior work remaining included the resurfacing of interior roadways and the restoration and landscaping of the grounds. The housing authority has been having difficulty getting contractors to return to complete punchlist items. An unexpected and potentially serious new delay in completing renovations has emerged as a result of a new state environmental regulation regarding underground fuel tanks. Under this regulation, all metal fuel tanks must be replaced with new tanks constructed of PCV materials. Preliminary estimates are that it will cost more than half a million dollars to replace the three underground tanks serving the Brooks-Sloate project. HUD turned down the PHA's request for additional CIAP funds for fiscal year 1989. The housing authority plans to reprogram available funds to do the necessary work and to seek additional HUD monies in fiscal 1990.

The neighborhood surrounding Brooks-Sloate in the northwest corner of Paterson is quite healthy. The project is surrounded by single family housing averaging $100,000 a unit in value. One large rental development also abuts Brooks-Sloate and, save for the public housing project, contains the remaining minority population. Redwood Village is about 40-50 percent minority.

Outside of Redwood Village, less than 10 percent of the neighborhood population is minority. The PHA director describes the neighborhood as predominantly middle class with fewer than 10 percent of neighboring families poor. A majority of the Brooks-Sloate neighborhood is owner-occupied (around 55%) and the surrounding housing is in very good condition.

Attracting and Selecting Owners

Eligibility criteria are predominantly economic in nature. Based on anticipated carrying costs and a 30 percent housing expense to gross income ratio, a minimum income of around $9,700 was set for
a two bedroom unit and $11,500 for a four bedroom unit. These income limits were set by staff following the consultant's recommendation, and approved by the PHA board.

Housing authority records indicated that 212 public housing tenants in Paterson (13 percent) had incomes above $17,000, and another 474 (30 percent) had incomes between $10,000 and $17,000. Based upon these authority-wide figures and the executive director's commitment to homeownership, eligibility criteria for joining the Brooks-Sloate co-op were based on affordability. Working backwards from estimates of anticipated carrying charges, the housing authority set a minimum income requirement of $9,700 for eligibility for a two-bedroom apartment. However, as of August 1988, the latest date for which we have PHA estimates, average carrying charges, exclusive of debt service and real estate taxes, were estimated to be $306 a month. Based upon a 30 percent housing expense-to-income ratio, these higher costs would require a minimum income of $12,240, and more than that if the buyer has to finance its equity pay-in. Another increase would be called for if the co-op does not succeed in obtaining a partial exemption from local property taxes.

Because our evaluation design called for in-person interviews with all home buyers, and Brooks-Sloate did not go to closing during the course of our three-year evaluation effort, we conducted no home buyer interviews. Based on a June, 1987 PHA-survey of Brooks-Sloate residents, we are able to describe the resident population in the early stages of the co-op conversion.

At the time of the 1987 survey, 237 of Brooks-Sloate's 242 units were occupied. Three-quarters of the households consisted of a single parent with one of more children, while around 22 percent contained two parents. The average household contained 3.7 persons. More than two-thirds (68.4 percent) of all Brooks-Sloate residents were black and 14 percent were Hispanic.

At the time of the PHA's survey, the average household income of Brooks-Sloate residents was $13,791 and the primary source of income was wages. More than seven of every 10 households contained at least one employed individual.

The average rent paid in Brooks-Sloate was around $314, although 20 percent of all residents paid more than $400 and nearly three percent paid at least $700 in rent.

As of August 1988, the PHA survey of Brooks-Sloate co-op members showed that around 60 households would end up paying less in carrying charges than they were currently paying for rent. While these figures might be lower now, they suggested to the housing authority a means by which the co-op could tap a portion of the windfall gains that higher income buyers could expect to realize from the conversion, to create a safety net for financially-strapped cooperators who fall behind in their payments through no fault of their own. The safety net would be in the form of a
special reserve fund that would be capitalized as follows. First, every member must pay a basic monthly carrying charge based on the costs of running the co-op. If this is less than the rent the member was paying to the housing authority, for the first 18 months after the co-op closes, those higher income cooperators would continue to pay their previous rent, with the difference helping to fund the reserve. In no event would the surcharge be permitted to exceed 50 percent of the co-op's base carrying charge, and the full surcharge would be eliminated after 18 months.

The project was marketed to current Brooks-Sloate tenants through public meetings with PHA staff explaining the program and through a newsletter answering questions about it. Managers of the other four family projects were advised of the PHHD and their tenants were advised that they could apply for homeownership although Brooks-Sloate tenants have priority. Since the demonstration began, all transfers into Brooks-Sloate have expressed interest in the program, and have been found eligible to become homeowners.

**Property Conveyance**

The conversion is being organized as a limited equity membership cooperative. As a membership co-op, the cooperative is not authorized to issue any capital stock, and memberships have no par value. A cooperative form of ownership was elected over a condominium for philosophical reasons. An advocate of mutual housing, the PHA director saw the Brooks-Sloate conversion as the centerpiece of what he hoped would become a major cooperative/mutual housing movement in the city of Paterson.

Since all renovations are being financed by HUD modernization funds, the housing authority plans to transfer the project to the co-op free of any mortgage debt. Individual co-op shares are being priced at $3,500, $4,000, and $4,500 for a proprietary right to occupy a two-bedroom, three-bedroom, and four-bedroom unit, respectively. When fully capitalized, the co-op should have paid-in capital of nearly a million dollars:

\[
\begin{align*}
88 & \text{ 2-BR } @ \$3,500 = \$308,000 \\
118 & \text{ 3-BR } @ \$4,000 = \$472,000 \\
36 & \text{ 4-BR } @ \$4,500 = \$162,000 \\
\text{Total Equity} & = \$942,000
\end{align*}
\]

The housing authority intends to pay all closing costs from the co-op's capital reserves, and it reserves the right to request from the co-op a contribution of up to $100,000 to support other local low-income housing initiatives and for additional funds to reimburse the PHA for some of its out-of-pocket demonstration costs.
To join the co-op, a family or individual first executes a subscription agreement and pays a nonrefundable $500 fee that the PHA will use to help create a citywide mutual housing association. The housing authority has also arranged for co-op members to finance part of their equity requirements with short term share loans. Payments of those loans would be on top of the co-op carrying charges which were originally expected to range between $236 a month for a two bedroom apartment to $341 for a four bedroom unit. As indicated earlier, these costs will probably be higher by the time the co-op finally closes.

The PHHA would like to transfer title of Brooks-Sloate subject to a long-term ground lease to be held by the housing authority. The ground lease would contain various covenants relating to limited equity sales beyond the 10 years specified in the co-op's bylaws. Another reason for the housing authority's interest in maintaining title to the land is the development potential of a portion of the project's site for the construction of 20-30 additional housing units. The PHA also speculates that if it retains ownership of the land and the co-op fails, it may be possible to regain public housing status for the project. HUD, however, has not agreed to this arrangement and anticipates a fee simple transfer of land and buildings at the appropriate time.

Governance of the cooperative will be by a 12 member board of directors. An interim board, consisting of 11 members, was elected at a general meeting held for residents on July 8, 1985 and has been meeting on a regular basis. Prior to closing the sale the powers of the board include, but are not limited to, all powers necessary to operate and prepare the premises for conversion. After closing, the powers will be expanded to include the establishment of monthly carrying charges, the price of membership and transfer values, terminating memberships, issuing rules and regulations, and the right to engage professional management services.

All necessary legal documents pertaining to the transfer and governance of the co-op have been prepared. The Articles of Incorporation establish the co-op as a membership cooperative. The Subscription Agreement, which is an application for admission to the co-op, specifies the co-op's purpose and the minimum carrying charges that will be levied upon shareholders once closing has occurred. The occupancy agreement, which will replace the PHA's lease once the closing takes place, details the rights and obligations of co-op members including those pertaining to subleasing, which is limited to a one-year period with the prior approval of the board.

Bylaws specify the composition and powers of the co-op's board of directors, including the setting of carrying charges, standards for membership and membership transfers, and other rules and regulations. Unlike other public housing co-ops that are being formed under the PHHD, the Brooks-Sloate bylaws specify that "in establishing monthly charges, the Board may take into account the
ability of the Member to pay." This provision reflects the PHA's desire to create a financial safety net for the most financially vulnerable co-op members. Bylaws may be amended by a vote of the majority of the entire membership at an annual or special meeting or, prior to conversion, by a majority of the entire board. Amendments may be proposed by the board or by petition signed by at least 25 percent of the members. The bylaws prohibit the use of proxy votes.

The bylaws also detail standards for approval of new members, which differ from those used by the housing authority in recruiting initial members to the co-op. In addition to financial ability, for example, a potential new member's interest in cooperative living and any special skills that he or she might bring to the co-op will also be assessed.

The Brooks-Sloate Cooperative has been going through a lengthy gestation period. The PHHD began officially in October 1985 when the housing authority sent letters to residents soliciting interest in buying their apartments. Even if all goes well, title to the project could not pass from the PHA to the cooperative until early 1990. Although the rehab work is the main cause for delay, the lengthy 50-month conversion is undermining the program. It is very difficult to maintain the initial enthusiasm of families who wanted to buy their apartments. It is also difficult for the interim board to maintain an independent legal standing while sharing management responsibilities with the housing authority for what in reality is still a conventional public housing project. A September 1988 meeting with the Brooks-Sloate board of directors illustrated some of these problems and frustrations.

At this meeting, a summary of expenditures the housing authority had charged to the board's budget was presented. The PHA had allocated $10,000 to the board to cover its expenses during the co-op's organizing period. The board indicated some surprise at the amount of money the PHA had charged against the co-op's budget. The issue immediately confronting the board was whether to send two members to Atlanta to attend a conference being held by the National Association of Housing Cooperatives. Although the board had sent two representatives to the same meeting the prior two years, it decided not to send anyone to the conference because the $3,000 that remained in its budget was needed for other purposes, including the renovation of the new offices the housing authority had assigned to it.

Several members of the board indicated that they had never seen an itemized accounting of the charges the PHA had debited against their budget and that they had not participated in the decisions to approve many of those expenditures. How, they wondered, could they be trained to plan and manage their own affairs if they did not have control over their own budget during the organizing period.
The institutions being created to support Brooks-Sloate and to spur the development of additional low-income homeownership projects in Paterson revolve around the mutual housing concept. Mutual housing is a form of rental tenure where the "tenant" leases from an association of residents and community members who are the owners of the property. The tenant has an indefinite lease and participates in the governance of the association. Unlike a cooperative, the tenant does not "own" a share of the corporation.

The proposed Mutual Housing Association (MHA) is to be a state chartered 501(c)(3) organization governed by a board whose members include not only residents, but members from a local partnership of lenders, local government, etc. The MHA is the housing developer and it maintains a continuing role in the management of the property.

The MHA model has a unique financing arrangement. The MHA raises capital to build or acquire housing for low and moderate income families. Under ideal conditions, most of this capital would be in the form of a grant. The greater the grant relative to total development or acquisition cost, the more affordable the housing becomes. Tenants pay a one-time membership fee to the MHA of a few hundred dollars. This paid-in capital is also used to help finance the housing. Tenants pay a monthly fee to cover operating costs and a contribution to repay the original capital grant to the MHA. There is no interest on the capital grant so there is little or no debt service depending on the size of the first mortgage. The result is monthly housing costs that exclude profit, interest and most capital debt. The funds repaid to the MHA's capital fund may be used to construct new housing, maintain the quality of life in the initial project, or to meet urgent needs of the residents.

The Brooks-Sloate conversion is based on this mutual housing model, although how closely it will resemble the pure MHA model remains to be seen. Paterson's original application to HUD proposed the formation of a two-tier organization, a citywide mutual housing association and a project-based mutual housing association (the daughter MHA). The city-wide MHA would:

- provide ownership and management for non-public housing developments;
- use contribution and shareholder capital as working capital;
- guarantee shareholders a suitable apartment/home or return of investment after five years;
- contract for development services;
- arrange financing for projects;
- use earnings from project development as equity and subsidies; and
- back-up "daughter" MHAs.
The citywide MBA would involve community participation by public and private interests in promoting better housing for low, moderate and middle income families in Paterson. Its board would include the mayor and other public officials concerned with housing, community development and economic development, representatives of lending institutions, builders, and real estate management, and representatives of non-profit organizations involved in housing and social and health services.

It is planned that this citywide MBA be developed to provide not only volunteer-type community support, but also concrete technical and financial support, and to involve business enterprises in the development and management of housing and the furnishing of services, including those that may be needed by the elderly and handicapped.

The Brooks-Sloate Mutual Housing Association, as "daughter" of the citywide MBA, would be part of the greater association. Under this plan, the Brooks-Sloate MBA would also benefit from the support and assistance of the citywide MBA and the stability and strength it would provide.

The Brooks-Sloate and the citywide MHAs would be held responsible under the purchase agreement for professional management and operation of the project. This could be accomplished initially by contract with the housing authority, or with a management firm. However, the MHA would be obligated to provide maximum opportunity for training and employment of the residents. The MHA would also be held responsible for initial follow-up education and training of the residents on the benefits and responsibilities of ownership. Brooks-Sloate residents would be voting members of that MHA and would pay dues to it.

Non-Brooks-Sloate residents wishing to become owners could buy shares in the citywide MHA as an equity deposit for their apartment. According to the PHA, the mutual housing concept may be crucial to the ultimate success of the Brooks-Sloate conversion:

After looking at the successes and failures of homeownership opportunity plans for residents of public housing projects, the question arises whether self-motivation of the residents and the cooperation of the Public Housing Authority are sufficient to assure success. It appears that public housing projects organized as cooperatives or otherwise providing for homeownership fail, when they do so, because of inability to meet production costs, or carrying costs, in addition to inability to plan to maintain affordability. It may also be that an organizational structure which forces a cooperative to turn in upon itself, absent the ability to reach out to a higher organizational level for technical, managerial, and financial assistance, augurs the demise of the
individual cooperative or other non-profit housing entity, when financial strength has not been built in.

Exactly how the transfer of Brooks-Sloate from the PHA to MHA will take place is also spelled out in Paterson's PHHD proposal. It should be understood, however, that, at this time, while the Brooks-Sloate cooperative corporation has been organized, no citywide MHA has been created.

While there is no mortgage to default upon, the co-op is making provisions for dealing with delinquencies in carrying charges. Over-income buyers whose rents exceed co-op carrying charges are capitalizing a reserve fund to assist late-paying tenants for no more than three months. Beyond this form of assistance, plans call for the mutual housing association to have the right to purchase co-op shares of defaulting cooperators.

Financing

As indicated earlier, the co-op will receive title to the property free of any long-term debt. The housing authority has made arrangements with the Sixth Avenue Credit Union in New York City to extend share loans to Brooks-Sloate buyers who cannot finance their equity payments from their savings or current earnings. Share loans up to 70 percent of required equity will be available for a five year term at an interest rate of between 11 and 13 percent. The co-op will indemnify the lender in the event of the shareowner's default. Loans will be made on the basis of a credit check and the individual's record of timely contributions to his or her equity account.

Counseling

Given his interest in cooperatives and mutual housing, the PHA director devoted a substantial amount of time, energy, and resources to the task of interesting Brooks-Sloate families in the cooperative concept. A major part of that job is being carried out by two third party contractors. Back in October 1985, the director turned to two individuals experienced in mutual housing to provide both technical assistance and counseling to tenants who resided in the Brooks-Sloate project. Shirley Boden and Eugenia Flatow were awarded a technical assistance and counseling contract by the PHA in the total amount of $35,625.

The agreed-upon work program provided for a total of 475 hours of consultant assistance to the PHA as follows:

-100 hours--assisting the housing authority to establish both a central, city-wide mutual housing association; and
-a local Brooks-Sloate mutual housing association (1st and 2nd months);
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-100 hours—developing a fund raising strategy for the
citywide mutual housing association (1st and 2nd
months);
-50 hours—developing housing options for families
unable to achieve homeownership (3rd-6th months);
-50 hours—assisting in the development and training of
tenants in the advantages and responsibilities of
homeownership (6th-13th months);
-100 hours—establishing an equity loan program (7th-
18th months); and,
-75 hours—developing a list of partners; preparing a
prospectus; meeting with prospects; and preparing a
public campaign around mutual housing (14th-18th
months).

According to the consultants, they held three of four general
information meetings where the concepts of mutual and cooperative
housing were discussed and the requirements for participating in
the homeownership program were explained. In the ensuing months,
they met individually with approximately 150 families who had
either failed to indicate whether they were interested in joining
the co-op or who had not made good on their prior commitment to
join, or, in some cases, to discourage families who were viewed
as poor risks for homeownership. Boden and Flatow also held a
total of six formal training sessions with the initial board of
directors of the Brooks-Sloate Co-op. In a variant of the
"train-the-trainers" model used in Denver, the training sessions
were intended to provide board members sufficient technical and
communication skills to enable them to educate, as well as to
lead, the remaining co-op members. This was an important part of
the training because the Paterson co-op was so large and the
recruiting and marketing period has been so long that the
trainers' contract would have expired by the time all apartments
are sold.

Despite the "train-the-trainer" model, the growth in co-op
membership failed to keep pace with PHA expectations, and in
February 1988, the housing authority found it necessary to
execute a second counseling contract--this one at a total cost of
$40,000 for a period of eight months--with a private firm called
Two Rings, Inc. Two Rings' work program called for the firm to
"provide residents of Brooks-Sloate with homeownership skills
development; support and reinforcement necessary for pre-purchase
participation, purchase, and post-purchase adjustment; and also
to increase each household's awareness of housing options and
responsibilities." The counseling program involved three stages.
The first, screening, required Two Rings to review housing
authority records to determine the income eligibility of those
who failed to sign subscription agreements. Orientation kits
were then provided to income-eligible families, and appointments
were scheduled with each family to follow-up the marketing
effort.
The second stage of the Two Rings counseling program involved group counseling sessions on money management, purchase procedures, property maintenance and contracts, and helping households who had already signed subscription agreements to understand all of the co-op's technical documents; the third stage involved individual follow-up meetings with families who had further questions about buying their units.

An example of the services Two Rings provided the PHA is detailed in their monthly report for February and March 1988. During that period, the counseling firm provided 50 hours of group counseling to households who had joined the co-op. Twenty one-hour sessions were devoted to the subject "Financing for the Non-Financial Person"; another 20 one-hour sessions were devoted to "Co-op Terminology"; and another 10 one-hour sessions were devoted to "Participation." In addition, 19 hours of individual pre-purchase counseling was provided to 15 households who had already joined the co-op, but had unanswered questions. In April, Two Rings devoted most of its counseling efforts to more than 50 households who had not joined the co-op. These households received information on Section 8 certificate rules and were counseled on available housing options for non-participants. Also during April, 40 hours of group counseling sessions were held for members of the co-op to review details of the subscription and occupancy agreements and the co-op's bylaws.

Under the best of circumstances, it is difficult to assess the quality of counseling services. That difficulty is compounded when the process is on-going and the assessors are limited to several brief site visits. While we cannot determine the quality of the services rendered, we agree that the PHA was correct in concluding that it needed more than one type of counseling and technical assistance. While Flatow and Boden provided invaluable program design assistance and helped introduce Brooks-Sloate residents to the co-op concept, without the one-on-one meetings conducted by Two Rings, there probably would be no closing. Housing authority staff believe that membership in the co-op increased dramatically after Two Rings completed its intensive meetings with tenants, although co-op board members with whom we spoke were not so sure.

One final note on counseling has to do with qualifying residents to buy a unit. In qualifying tenants for eligibility to join the Brooks-Sloate co-op, Two Rings counselors found that some individuals disclosed sources of income that may not have been reported to the housing authority for rent determination purposes. Having pledged confidentiality, the counselors did not report these individuals to the housing authority. This is an area that needs to be considered by the PHA and HUD as a matter of policy.1 It is also a matter of some research interest.

1 We understand that this matter has been referred by HUD to its Inspector General for appropriate and expeditious investigation and action.
because we do not want to confuse the unreported incomes of public housing tenants with an increase in earned incomes due to greater individual initiative that was stimulated by a move into homeownership.

Windfall Profits and Retention Provisions

As indicated earlier, Brooks-Sloate is a limited equity membership cooperative whose by-laws provide that there shall be no appreciation of equity for 10 years except for annual adjustments based on increases in the cost of living and for tenant-installed improvements that had the prior approval of the board of directors. At the end of 10 years, the limited equity policy will be reviewed. The co-op's bylaws spell out the method of transferring memberships.

First, the seller, or outgoing member, notifies the board of its intent to leave the co-op. The board then selects the next approved applicant on the co-op's waiting list for whom the unit size is appropriate. The outgoing member returns his/her membership certificate to the board, which issues a certificate to the new member. The new member makes an equity payment based on the transfer value of the co-op share and the board pays the seller the new member's equity less any amounts due the co-op. Costs due the co-op could be for putting the unit back into marketable condition and for any costs incurred by the cooperative in finding a new member.

Provision for Maintenance After Sale

The housing authority has some warranties for portions of the rehab and will pass them through to the co-op. However, because of the lengthy conversion period, some of these warranties are likely to expire before the co-op takes over formal control of the project. Nevertheless, the co-op should begin life with a sizable extraordinary maintenance and replacement account that will be capitalized by the shareowners' paid-in equity. According to the PHA, at the time of closing, these reserve accounts should contain around $500,000. Their exact size will be a function of the amount of capital contributions that the PHA claims as reimbursements for costs incurred in carrying out the demonstration. Whether the co-op approves an allocation from its reserves to support other PHA-sponsored low-income housing initiatives, as was initially contemplated, will depend upon the size of the reserve account. This, in turn, is a function of the number of families who join the co-op. Although the housing authority originally intended that this be 242 families--the number of apartment units in Brooks-Sloate, it is now clear that the co-op will contain a sizable number of non-buyers who will remain as renters. Because, as we discuss below, continuing renters will receive housing vouchers, it is possible that their presence will have a positive net effect on the co-op's financial operations. This would, in turn, affect the co-op's ability to deal with post-sale maintenance problems. Only time will tell.
The Treatment of Non-Participating

In an ideal world, the Brooks-Sloate Cooperative would contain 242 shareowners, all of whom occupied the project as public housing tenants when the Paterson Housing Authority began the conversion process in 1985. In the real world, of course, this cannot be expected since some families will be too poor to join the co-op while others will not be interested in buying their apartment for other reasons. Therefore, the original program design provided that "residents who do not choose to buy or who cannot afford the carrying costs will either be transferred to other housing authority developments or, if qualified, will be given vouchers that will allow them to rent housing from private sources." In fact, the housing authority had on hand from the very beginning, 50 section 8 vouchers to aid in the relocation of non-participating Brooks-Sloate tenants. To reduce the number of tenants that would have to be relocated, the PHA has been replacing families in Brooks-Sloate through normal turnover with families who have been selected on the basis of their interest and eligibility for the ownership program. The authority has a file of 294 income-eligible tenants from other developments who wish to become members of the cooperative. Since 1985, 105 families who could become home owners have been admitted to Brooks-Sloate through this process.

Under the original program design all non-participants would be replaced by income-eligible public housing residents currently residing in other public housing developments who wished to become members of the Brooks-Sloate cooperative. In no case was it envisioned that a sizable number of non-buying families would remain in their present apartments as tenants of the Brooks-Sloate Co-op. But as part of the settlement of a legal action against the housing authority over the issue of involuntary relocation, this is what is about to happen.

The legal action, Frierson v. Pierce, et al. was filed in the United States District Court in New Jersey in October 1988 on behalf of three tenants living in Brooks-Sloate apartments, a low-income family on the waiting list for public housing in Paterson and by the Paterson Coalition for Housing, Inc., an organization that helps homeless people find apartments. The plaintiff's action had three major parts. First, they challenged the validity of HUD's PHHD regulations that require only a five year minimum restriction limiting the resale of public housing units to low-income families. Second, plaintiffs alleged that the PHA's relocation plan to transfer non-buying tenants to other public housing developments or to provide them with housing vouchers constitutes a form of involuntary relocation that frustrates the purposes of the National Housing Act and is prohibited by the PHHD regulations. The plaintiffs' third complaint cited alleged violations of New Jersey's Cause for Eviction Statute which applies to all involuntary displacement of tenants in all multifamily housing in New Jersey. Pursuant to
this statute, the State of New Jersey has promulgated regulations regarding the conversion process that require "tenants be provided with a 60 day 'notice' and a three (3) year Notice to Quit before eviction proceedings may be commenced against the tenant. Within the first 18 months of that three (3) year period, the tenant has the option of demanding of the landlord comparable rental housing. If the landlord does not provide comparable rental housing, the tenant is entitled to stays of eviction for up to five (5) years beyond the first three (3) years." According to the plaintiffs, the PHA has failed to provide any of these required notices.

The relief sought by the plaintiffs was of two kinds. First, they requested the court to set aside HUD's approval of Paterson's homeownership demonstration because it allowed involuntary displacement of tenants, and to prevent the PHA from relocating non-buying tenants from their Brooks-Sloate apartments against their will. Second, they also requested the court to set aside HUD's approval of Paterson's PHHD program because it lacked perpetual resale restrictions.

On July 18, 1989, a compromise settlement was reached between the parties to the litigation. The settlement prohibits the housing authority from subjecting tenants of Brooks-Sloate apartments to involuntary relocation. "This means that tenants may not be moved, and threatened with being moved, against their will from their present dwelling units. However, involuntary relocation does not encompass offering a tenant the choice of accepting either a 'Section 8' certificate or voucher or accepting another public housing unit."

To accommodate the needs of non-buying tenants who will remain as tenants of the Brooks-Sloate co-op, the settlement includes HUD's promise to the PHA that "it will make every effort to provide all housing vouchers necessary for all current Brooks-Sloate residents who wish to remain in the development but who do not wish to purchase." This agreement by HUD is made in view of the Brooks-Sloate Cooperative Board's representation that for all current Brooks-Sloate residents who wish to remain in the development but who do not wish to purchase, the Board will include in its lease (1) provisions limiting rent to fair market rent and, (2) contain a clause stipulating that the lease will not be terminated for a business or economic reason which is related to a desire to obtain a higher rent.

Finally, the agreement also contains an understanding that the failure to receive a housing voucher of any Brooks-Sloate resident who wishes to remain in the development and who does not wish to purchase shall be the equivalent of the involuntary relocation of such resident.

The parties to the compromise agreed to exclude two legal issues from the settlement: whether the requirement that all PHHD programs contain a recapture mechanism for a minimum of just five
years is a violation of the U.S. Housing Act; and, whether the PHA's plan, which includes a 10 year recapture mechanism, is invalid under New Jersey statutes. Presumably, these issues will be litigated further.

In anticipation of the settlement, the PHA director wrote a letter to HUD requesting a sufficient number of housing vouchers to restructure the Brooks-Sloate conversion. As of June 1, 1989, the director estimated that as many as 92 vouchers might be necessary to accommodate non-buying tenants. These continuing renters fell into four categories:

-Prior to the settlement, as a matter of policy, the Brooks-Sloate board of directors had agreed to permit up to 13 families who had not joined the co-op, (five percent of all units) to remain as continuing renters. These families would need vouchers.

-In addition to the above families, 16 residents who joined the co-op in late 1987 and paid a $500 membership fee have since made no equity payments. Presumably, they will not buy their units and under the consent decree, they cannot be moved.

-Another 40 members "have been so slow in making equity" payments as to warrant the assumption that they will choose not to pursue membership in the Cooperative, confident in the knowledge that they will not be required to transfer. Therefore, voucher assistance will also be needed for these households."

-Finally, 23 units in Brooks-Sloate are vacant, "in regard to which it is not certain that they may be filled on a priority basis by persons who would join the Cooperative, a prudent working assumption is that the units may be filled from the working list, thus requiring voucher assistance."

In a letter to Executive Director Raymond, dated June 5, 1989, HUD agreed "to make every effort to provide housing vouchers for all current Brooks-Sloate Terrace residents who do not wish to become members of the cooperative and who desire to remain as renters in the development." Both the PHA and HUD are in agreement that a viable housing cooperative requires that a significant majority of the units be owned by members of the cooperative although the PHA has not yet decided where to draw the line. It is clear, however, that the 92 vouchers it requested from HUD, which account for 38 percent of all the units in Brooks-Sloate, represents a worse case scenario that would put extraordinary management pressures on the co-op.

HUD and the housing authority also agreed that a critical mass of buyers was needed to make the transfer viable and, on that basis,
decided that the conversion would proceed if 75-80 percent of all residents chose to join the co-op.

As of October 1, 1989, PHA officials place membership in the co-op at around 200 hundred families which means that the number of non-buying tenants might end up being just half as many as there seemed to be three months earlier. Moreover, some non-buyers will probably choose to use their voucher in the private housing market which would free-up units to sell to interested home buyers who currently live in other public housing developments. In short, it is difficult to tell exactly what the distribution of buyers and non-buyers will be in Paterson. Intensive efforts to market the co-op are again under way and the question of whether the project can proceed to closing upon the completion of the modernization will be answered shortly.

Handling Non-Participants

A potentially large number of Brooks-Sloate tenants are either financially unable or not interested in becoming home owners. The PHA and Interim Board of the Brooks-Sloate Co-op feel very strongly that the co-op cannot succeed unless all 242 units are owned by cooperators. This means that the co-op does not want any non-participating families to remain as tenants of the PHA after the conversion. Depending upon the size of the positive response of existing tenants to the PHHD, their ability to meet minimum selection criteria, and their willingness to move out of Brooks-Sloate into other public housing, or private housing with voucher assistance, the relocation problem in Paterson could be formidable.

In anticipation of the relocation issue the PHA has been replacing families in Brooks-Sloate through normal turnover with families who have been selected on the basis of their interest and eligibility for the ownership program. The authority has a file of 294 income-eligible tenants from other developments who wish to become members of the cooperative. Since 1985, 105 families have been admitted to Brooks-Sloate through this process who should become homeowners under the PHHD. But even with this kind of help, the number of non-participants and families requiring relocation could be as high as 75-80. In anticipating the need for relocation, 50 housing vouchers have been earmarked for relocating Brooks-Sloate tenants who cannot or will not participate in the homeownership demonstration.

Amount and Use of Sales Incomes

The two sources of the gross sales proceeds from the conversion are the $500 co-op membership fees and the equity payments of each cooperator, which range between $3,000 and $4,000. With the number of non-buying residents who will remain in their units as renters still undetermined, we cannot estimate the extent of the gross sales proceeds. However, they should be in the neighborhood of $800,000, the major portion of which will be used
to capitalize a replacement reserve fund. Closing costs will be paid from the sales proceeds, as will certain other demonstration expenses. While the housing authority speaks of these funds as "belonging to the co-op," it has reserved the right to request reimbursement for a portion of out-of-pocket expenses associated with the conversion such as appraisal and engineering fees.

**Sources and Uses of Sales Proceeds**

The way in which the co-op will be financed produces relatively little sales proceeds to the PHA. Plans call for the majority of co-op membership fees and equity payments to go to the co-op corporation. The PHA is considering requesting the co-op to make two one-time payments to the PHA of $100,000 each. The first payment would be used to help establish a citywide mutual housing association and the second payment would help reimburse the PHA for a variety of expenses incurred in administering the PHHD.

**Impact of Sales Program**

Because Brooks-Sloate has not yet gone to closing, we cannot formally assess the impact the PHHD has had on Paterson's public housing program. We do know, however, that the PHA has devoted much time, energy, and housing authority resources to bring the conversion to fruition, without receiving hoped-for grants and loans from the city or the state. Moreover, the litigation over the relocation issue has had its own impact on the housing authority and the shape of its homeownership program. As a result of the compromise settlement, should Brooks-Sloate proceed to closing, Paterson will test the efficacy of a substantially mixed-tenure limited equity cooperative. While seven of 85 units in Nashville's New Edition Co-op will be occupied by non-buyers, they not only constitute a much smaller fraction of all occupants, but all are elderly individuals and couples. A larger number and percentage of non-buyers in Brooks-Sloate are families with children.

Brooks-Sloate is located in a strong neighborhood. Therefore, the conversion itself is not likely to have any significant neighborhood effects. Rather, should the conversion succeed and resale restrictions not be renewed beyond the currently mandated 10 years, its location will be a positive factor in the future market value of co-op shares.

Although the city stands to benefit financially from the conversion when Brooks-Sloate is added to the tax rolls, the PHA is attempting to obtain abatements for the co-op. Aside from the generally positive effects of expanding homeownership in the neighborhood, at this time it is not possible to assess financial impacts that the PHHD might have on the city.

Exclusive of any modernization monies, the PHA receives an average operating subsidy from HUD of $64.34 a month. When the title to Brooks-Sloate is eventually turned over to the
cooperative, the housing authority will lose approximately $186,000 per year in HUD operating subsidies. The impacts of this loss cannot be determined a priori, although as one of the PHA's best family developments, we can assume that Brooks-Sloate's average operating costs are below average. If this is the case, it may be that the project's sale will have a somewhat negative effect on the PHA's overall financial condition. Moreover, since Brooks-Sloate accounts for approximately ten percent of the PHA's conventional inventory, the PHA's full overhead costs will have to be pro-rated over the remaining 90 percent. What additional effect this will have on the housing authority's financial status, we cannot say for sure.

Conclusions

Paterson's homeownership project is extremely ambitious. At the time of our initial site visit it was too early to tell how many families would have to be relocated in order for the 242 unit Brooks-Sloate cooperative to be fully occupied by home owners.

The Brooks-Sloate conversion is also very interesting for other reasons. The extensive repairs are being financed by HUD modernization funds and must be completed before property transfer can take place; this has allowed them to organize a lengthy training and preparation phase. An elected board of directors has been working together with PHA staff and potential cooperators on various homeownership issues and (if the property is conveyed in the spring of 1990) the preparation phase will have lasted nearly four years. Whether such an extended period of training and preparation will result in a more successful conversion will be determined over time.

The Brooks-Sloate conversion is of particular interest because of the deeply subsidized sale prices, which range between $3,500 and $5,000, and the fact that where current rent exceeds projected co-op carrying charges, a portion of the excess payment will capitalize a reserve fund to help temporarily financially strapped owners meet their obligations to the coop. Paterson's PHHD is also significant because it is planned to be part of a citywide mutual housing program that the PHA is trying to stimulate.
Introduction

The demonstration program in Philadelphia, PA was originally designed to sell 300 of its over 5,400 scattered-site units to current tenants. The program design called for fee-simple sales to be made to tenants with incomes as low as $8,000, with counseling to be provided by the PHA staff. After a long delay caused by conflict over replacement housing and internal management problems, however, the demonstration program was revised. The current plans call for a pilot program designed to develop effective procedures for selling units to tenants. The goal of this pilot program is to sell 15 units. If it goes well the authority intends to expand it to sell more units.

Based on an analysis of the costs of maintaining a single-family home in the Philadelphia area the minimum income for participation in the pilot program has been set at $12,150. At the present time 22 tenants have been selected for the pilot program from a total of 69 eligible applications received by the PHA. It is expected that some of these will be dropped from the program for bad credit or other problems resulting in approximately 15 buyers. Financing for these sales is to be provided by the Philadelphia Mortgage Plan (PMP), a consortium of local lenders. As in many of the other single-family sales programs, the amount of the first mortgage will be based on the buyer's income. Thirty percent of the buyer's household income will go toward housing expenses. A silent-second mortgage will cover the difference between the amount of the first mortgage and the appraised value of the units and also will include the costs of repairs done to the units prior to their sale. The silent second is designed to preclude windfall profits for the first five years of ownership. After five years, the second mortgage will be forgiven. Counseling of program participants will be handled by the Philadelphia Council For Community Advancement, a local non-profit housing counseling organization.

To date none of the 15 units has been sold. Sales are expected to take place throughout the fall of 1989. After that time the PHA plans on adjusting the program as needed and expanding it to sell up to the 300 units originally approved for sale.

Managing the Demonstration

The demonstration in Philadelphia is managed by the Philadelphia Housing Authority (PHA). The PHA manages approximately 15,000 units of public housing and 6,000 housing vouchers and certificates. Of the public housing units over 5,400 are scattered-sites units, almost all of which are single-family
dwellings. The PHA has over 7,000 on their waiting list for public housing and approximately 16,000 for Section 8 assistance. The PHA is also participating in the Turnkey III program. It administers 207 Turnkey III units in two projects initially occupied in 1981 and 1982. As of 1985, however, none of those units had been sold.

City housing officials gave two major goals for participating in the demonstration; (1) to provide homeownership opportunities to housing authority tenants; and (2) to reduce the authority's inventory of scattered-site dwellings, which the city's housing director termed "an administrative and management nightmare."

The major concern expressed in discussions about participation in the demonstration was the need for replacement housing. This concern was expressed by housing authority staff members, the housing authority board, and by the mayor. These local actors did not want to sell units unless they were to be replaced with new units on a one-for-one basis. In fact, participation in the program was made contingent upon availability of funds from HUD for replacement housing. HUD was unwilling, however, to provide one-for-one replacement and a stalemate ensured. This stalemate was broken when HUD awarded Philadelphia 200 units of new public housing, although HUD officials contend that this award was not directly linked to the homeownership demonstration. When the housing authority had difficulty finding building sites for these new units, according to local officials, Section 8 certificates and housing vouchers were substituted for the allocation of new public housing units.

Philadelphia's original application for participation in the demonstration was authored by a housing authority program director. Tenants had input into program development through the tenant members on the housing authority board. The revised pilot program was designed by the head of a newly created special projects division within the PHA, with the assistance of staff from the Philadelphia Council For Community Advancement, a local non-profit housing counseling agency.

The demonstration program in Philadelphia involves four major players. First, overall management of the demonstration is the responsibility of the special projects division within the PHA. It handles the selection and rehabilitation of units, attraction and selection of program participants, the development of legal documents, and overall program coordination. Second, the financing is being provided through the Philadelphia Mortgage Plan, a consortium of local lenders created in 1975 to provide mortgages to moderate-income home buyers. Third, counseling of program participants is being handled by the Philadelphia Council For Community Advancement. Finally, a tenant advisory committee has been established to act as a liaison staff, and to advise on program guidelines. The three members of this committee are not eligible to participate in the demonstration.
Demonstration staff includes the head of the special projects division, who devotes approximately one-third of her time to the project, clerical support, legal support, and some involvement of the housing management staff. The total costs of administering the demonstration are estimated to be $40,000 per year.

Philadelphia did not apply for a technical assistance grant from HUD. According to HUD's PHHD manager, the original demonstration staff in Philadelphia knew of the availability of funds but chose not to apply for them. They intend to cover much of the cost of the sales program from the sales proceeds.

Beyond the early controversy over replacement housing, management problems have been a major cause of the delay in implementing the demonstration program in Philadelphia. In the beginning, according to PHA officials, there was no logical person at the senior staff level to administer the PHHD. The original proposal was written by the Section 8 division and since it also administered two Turnkey III projects, it was given the initial responsibility for managing the demonstration. But, since neither of the Turnkey III projects had gone to sale, the staff in this division had no experience in selling units. This staff was also busy with other responsibilities associated with the normal operations of the Section 8 and Turnkey programs.

In late 1987 there was a major reorganization in the PHA. The executive director left the authority, the deputy director was promoted to director, and a new deputy director was hired. This reorganization also led to the creation of the special projects division to which the demonstration program was assigned. A senior staff person was promoted to direct this new division. This division has no operational program responsibilities which has allowed it to devote more time to designing and implementing the demonstration. According to the director of the special projects division, the current staffing levels have been adequate but she is concerned that they will be "stretched thin" as they become involved in inspections and the closing of sales. She hopes to rely on staff from the housing management division to do inspections and is concerned that they may not be able to do this work in a timely manner.

**Selecting and Rehabilitating Properties**

The Philadelphia Housing Authority's initial proposal to HUD was sell 600 units of scattered-site housing. In authorizing the demonstration in Philadelphia, HUD only approved the sale of 300 units. After experiencing the difficulties discussed above, the PHA decided to start with a 15 unit pilot program. As of August 1989, no units had been sold. The PHA staff, however, recently selected 22 tenants to participate in the program and has notified them of their acceptance. It purposefully selected more than 15 tenants since it expects some will not be able to meet all the program requirements.
As mentioned above, one of the major goals of the PHA is to reduce its inventory of scattered-site, public housing units. Those units are located in neighborhoods throughout the city and vary in condition from units in excellent repair to units that are vacant and completely uninhabitable. Between 1981 and 1986, 1,700 scattered-site dwellings were rehabilitated with CDBG funds, and as a result, there is a large inventory of homes suitable for sale to tenants.

Rather than pre-selecting specific units for sale, Philadelphia intends to sell units occupied by interested and eligible tenants. Thus, the first step in the selection process was notifying all tenants of the demonstration and soliciting their interest in buying. The pool of interested buyers constitutes the pool of units being considered for sale. Units will only be sold to their current occupants. The units occupied by the tenants selected for the program will be inspected by housing authority staff. CIAP funds will be used to pay for any rehabilitation work needed.

Attracting and Selecting Tenants

The selection of participants for the demonstration began with a notice sent to all tenants of the scattered-site units. The notice stated that participation in the program was open to any tenant of a scattered-site unit with an income above $12,150, who had lived in his unit at least one year, and who had a good rent paying history during this time. The $12,150 figure was based on an analysis of the costs of homeownership in Philadelphia. A public hearing was then held to discuss the program details. A total of 262 applications were received but many of these were from people who did not qualify for the program for one reason or another. After verifying the information on the application, the number of eligible applicants was reduced to 69.

In selecting the final 22 tenants to participate, program staff wanted to make sure to include units in all three areas of the city and to choose the lowest income people from among those who qualified. The decision to give preference to the lowest income people was in response to the board's concern that those least likely to be able to afford a home on the private market be included in the program. The income of those selected range between $13,000 and $16,000. The 22 tenants selected for participation still have to qualify for loans before they can purchase their units. The PHA is estimating that seven of these potential participants will be unable to qualify because of a bad credit rating or other problems. The Philadelphia Counsel For Community Advancement will be counseling these prospective participants on how to qualify for a loan.
Property Conveyance

Housing units are to be sold to tenants fee simple. The sales price will be based on household income, and will be that which can be supported by 30 percent of the income going to housing expenses. The maximum sales price will be the appraised value of the unit.

The PHA intends to assist program participants in paying closing costs to the extent allowed by the private financial institutions originating the loans. Similarly, the PHA intends to assist them with the required down payments as allowed.

In order to minimize the potential for defaults, the authority proposes to provide counseling to tenants on budgeting and money management, and delinquency and default prevention.

Financing

Financing for the sales is being provided through the Philadelphia Mortgage Plan (PMP), a consortium of local lenders. The exact terms of the loans are uncertain. They will depend on the sources of financing available at the time the loan applications are made. The PMP participates in the state's housing revenue bond program and they are likely to rely on this program if funds are available. The rate of the most recent bond program is 8.5 percent. The length of the loans will be decided between the lender and the buyer. The PHHD program director expects that program participants will be required to provide a five percent down payment. The PHA will assist buyers in making this payment if allowed by the particular lending institution originating the loan.

The PHA will provide a silent-second mortgage covering the difference between the size of the loan program participants can support and the full sales price of the units. The second mortgage will also include the costs of any repairs made to the units before transfer. The second mortgage will be forgiven after a buyer lives in the unit for five years, and will be due if the unit is sold prior to that time.

Counseling

The original proposal approved by HUD called for counseling to be done by the PHA itself. After further thought, however, the PHA decided to seek outside help in order to "establish the necessary distance between the PHA and the tenants." The PHA wants to dissuade tenants from believing that they will be able to stay in their units if they do not meet their financial obligations as home owners. Thus, program participants will receive counseling from the Philadelphia Counsel For Community Advancement (PCCA), a non-profit housing counseling agency in the city. This group was originally selected because it offered to provide the counseling on a no fee basis. It subsequently changed its position,
however, and will be charging $75 per referral and $200 per successful participant.

The counseling to be provided will primarily consist of instruction on the financial aspects of homeownership. Pre-purchase instruction will cover the costs and responsibilities of homeownership and financial budgeting. Post-purchase counseling will involve working with families who are having difficulty keeping up with mortgage and other housing payments. PCCA will contact each program participant every three months during the first two years after sale and every six months for the next three years. If participants are having trouble they will be referred to the appropriate local program to seek assistance.

The new homeowners will also receive a booklet on the obligations of homeowners and a listing of the city agencies responsible for various municipal services.

Windfall Profits and Retention Provisions

To prevent owners from reaping windfall profits, the authority proposes to attach deed restrictions that, for a period of five years, would limit the sale of units to persons whose income does not exceed 80 percent of the median income of the area, as determined by HUD, and would limit the sales price to the price paid by the initial purchaser. The silent-second mortgage will also be payable in full if the unit is sold within a five year period.

Provision for Maintenance After Sale

The authority's original application makes no mention of provision for maintenance of units after sale. According to the program director, however, the PHA will be establishing a major systems repair fund to help program participants if major problems are encountered. It plans on capitalizing this fund with sales proceeds. The details of how this fund will operate has not yet been worked out. The PHA will also provide a one year warranty on any major system repairs made prior to property transfer.

Handling Non-Participants

The system being used to select program participants effectively avoids the need for any relocation. Only those units that are occupied by those willing and able to participate in the program will be sold.

Amount and Use of Sales Income

The authority proposes to use some of the sales income to defray project costs, including the cost of inspecting the units. Sale proceeds will also be used to capitalize the major systems repair fund described above. Finally, the authority will use the funds
to help program participants come up with the necessary closing costs and down payment.

**Impact of Sales Program**

Given the size of the pilot program, it is not anticipated to have a significant impact on the PHA. Even if the pilot is expanded to the original 300 units, the 200 Section 8 certificates received by the authority will cushion any major impact on the amount of operating funds received by the PHA. The sales should also contribute the city's tax base, but the exact amount is not known at this time. Given the widely scattered location of the units to be sold, no significant impact on the surrounding neighborhoods is anticipated.

**Conclusions**

The sale of public housing units in Philadelphia has been delayed by a protracted conflict over the provision of replacement housing for the units sold and by internal management problems. The original goal was to sell 300 units. At the present time, however, none has been sold. Progress has been made in implementing a 15 unit pilot program designed to test program requirements before expanding to a larger sales program. Twenty-two tenants have been selected and are scheduled to begin counseling.

The first sales are expected in the fall of 1989. Philadelphia still hopes to reach its original sales goal sometime in the future.

Although based on limited experience, the manager of the demonstration program in Philadelphia thinks that the keys to a successful sales program are the selection of program participants who can qualify for private mortgages, have sufficient incomes to maintain the units, and are highly motivated to become home owners.
PUBLIC HOUSING HOMEOWNERSHIP DEMONSTRATION

READING CASE STUDY

Introduction

The Reading Housing Authority has accomplished its goal for the homeownership demonstration, selling eight units of single-family, scattered-site public housing to tenants. One house was resold after the original owners could no longer keep up with required mortgage and utility payments due to marital difficulties. One other owner had difficulty keeping up with mortgage payments after suffering a heart attack, but that problem was resolved. The Reading Housing Authority management is very satisfied with the demonstration. According to the authority's executive director, the homeownership program has made it possible for poor households to achieve a sense of dignity in the community, while also providing them with an investment that can add to their future security. Furthermore, the demonstration has returned units to the City of Reading's tax rolls, and it has contributed to the city's housing stock, helping to revitalize deteriorating neighborhoods.

Houses in Reading, PA priced at 70 percent of fair-market value, were sold from a low of $6,065 to a high of $19,000. The average price was approximately $12,000. The authority provided financing, offering 10-year mortgages at seven percent interest. Owners made a five percent downpayment and paid a portion of closing costs. Each house was rehabilitated to some degree prior to sale: one house required extensive work (approximately $10,000), while the seven other houses required only minor work (about $500 each). The authority maintenance staff performed most of the rehabilitation work.

No formal counseling was done in Reading, but the housing authority management has counseled residents individually about the importance of prudent financial management, and the housing authority staff has assisted program participants when they have called with problems. The authority has established a fund from sales proceeds to be used for major maintenance; however, since houses sold were in good condition, management is discouraging any use of those monies for at least five years after each sale. Beyond that use of sales proceeds, management has yet to determine how those funds will be used (the issue, however, has been raised by the authority's auditors, and a plan for the use of sales proceeds is being prepared).

Managing the Demonstration

The demonstration in Reading is managed by the Reading Housing Authority. The authority has 1,600 housing units under annual contribution contract, administers 425 Section 8 certificates and a small, but fluctuating number of vouchers, and manages 128
The authority executive director authored the PHHD proposal. Tenants were not involved, since the scattered-site project did not have a tenant council, and the authority did not anticipate converting multifamily projects (which had tenant councils) to ownership units. Although the authority's original proposal to HUD anticipated a role for the Neighborhood Services Program staff, they were not involved in the demonstration since their services were not needed. The scale of the demonstration was such--only eight dwellings were involved--that it could be handled adequately by authority staff.

The authority estimated that its costs for operating the demonstration were about $500 per unit. The authority did not apply for a technical assistance grant. The executive director felt that he could easily handle the demands of the program without federal assistance and the attendant paper work that would be involved. Counseling was provided directly by the executive director of the authority and did not involve any extraordinary expenditures.

Selecting and Rehabilitating Properties

The Reading Housing Authority's goal was to sell the eight units that comprised its scattered-site project. As of August 1989, it had sold all of them.

After deciding to sell the scattered-site houses, the authority's executive director inspected each unit to determine repair needs. Of the eight houses, seven were in a good state of repair and needed little effort to rehabilitate them prior to sale. One unit was in very poor condition, and it was rehabilitated at a
cost of approximately $10,000. For each unit, the executive
director listed repair needs and shared that with prospective
buyers, who could suggest additional repairs. Buyers then used
the agreed upon list as a check list to be sure the units met
their expectations. All repairs, except plumbing and electrical
work, were made by authority staff.

Renovation costs for the seven units requiring little work ran
about $500 per unit and required about 100 man hours of labor.
The unit with major rehab work cost about $10,000 and took longer
to complete. Those costs were financed out of on-going housing
authority operating budgets. None of the work required
relocation of tenants since the tenant living in the unit
undergoing major renovation was able to move into a vacated sale
unit.

The scattered site units were located in two neighborhoods:
Pear/Front Street and Church Street. The housing stock in the
Pear/Front Street neighborhood was in fair to poor condition,
according to a local realtor. Two thirds of the housing was
rental, with rents running $225-250 per month. Home prices
ranged from $3,000-$9,000 for the row houses that comprised the
Pear/Front Street neighborhood. Rents and prices, after going
down steadily for several years, had stabilized. Nevertheless,
this was one of the worst neighborhoods in Reading. According
to the realtor consulted, the market for housing consisted mainly of
speculators looking for low cost units. The Church Street
neighborhood, on the other hand, consisted of housing in fair to
good condition with 65 to 70 percent of the units owner occupied.
Housing prices ranged from $23,000 to $31,000 and rents ran from
$300-325 per month. The neighborhood was stable and, if
anything, housing prices were appreciating slightly. Both
neighborhoods have a predominantly black and Hispanic population
(40 percent each).

**Attracting and Selecting Owners**

After deciding to participate in the demonstration program, the
authority executive director wrote letters to the occupants of
each of the eight units selected for the demonstration to explain
the program and solicit their interest. He then met with them
individually to tell them about the advantages of homeownership.
Of the nine home buyers (one unit was sold twice), three were
tenants of the scattered-site units. After learning that some of
the existing tenants did not want to or could not participate,
the director instructed his project managers to screen
prospective participants for the program. Criteria used to
screen tenants included income, rent-paying habits, and past
relationships with authority management (i.e., were they good
tenants). Based on that screening, it was determined that about
25 tenants would be eligible for the program. However, no list
of potential participants or applicants was prepared.
Three of the nine units were sold to married couples; six to single women with children. Two households were black and seven were Hispanic. Household size ranged from three to five persons. Incomes ranged from $4,561 to $18,000.

Authority management is satisfied with buyer selection procedures, emphasizing that key factors are adequate income and the household's interest in becoming a home owner. The latter is important, authority management believes, because homeownership is a big step for people living in public housing and many tenants are hesitant about undertaking the responsibilities that it entails.

**Property Conveyance**

Housing units were sold fee simple. The price was set at 70 percent of the average of two independent appraisals. A five percent downpayment was required. Interest on the mortgage, which was carried by the housing authority, is seven percent. The term of the mortgage is 10 years. The five percent downpayment, seven percent interest charge, and 10 year term were set by the authority board of commissioners based on what they perceived the federal government would accept. Home buyers and the authority shared closing costs, with the PHA paying one half of state and local realty transfer taxes and buyers paying all other costs. The authority executive director estimated that buyers needed $2,000 to $2,500 at closing to cover the downpayment and closing costs. No legal issues arose over the conveyance of properties, and the authority executive director is happy with the process used in Reading.

**Financing**

The authority made no effort to involve private lenders or the state housing agency in financing sales of public housing units, since it believed it could handle financing itself. With an option to buy the units back from purchasers at the outstanding balance of the mortgage, the authority believes it has protected its interests adequately.

The authority has used a personal approach to minimize the potential for default. It has encouraged home buyers to contact it immediately if they anticipate problems meeting their mortgage obligations so that alternative arrangements can be made. In cases of hardship, the authority will allow households to pay only interest due, rather than principal and interest. However, it will not hesitate to foreclose if households fall more than two months behind in their payments without a reasonable excuse (such as illness).

After one family had marital problems and fell far behind on its mortgage and utility payments, the authority did not foreclose, since the household would have lost its substantial equity in the house. Instead, the authority took back the title, refunded the
household's equity in the unit, and resold the house. The authority experienced one other problem with late payments after a home owner had a heart attack and could not work for some months. In that case, the authority allowed the owner to delay payments until resuming work.

Counseling

The Reading Housing Authority did not establish a formal counseling program. The authority's executive director preferred to work with people one-on-one, explaining to them the advantages and responsibilities of homeownership. He was willing to help new home owners deal with problems as they arose. In addition, he has met with each owner after the sale to ask them about their satisfaction with the sales process and with their homes. He reported that owners were uniformly satisfied and enthusiastic about the program. The authority executive director also emphasized the importance of bringing all home owners together in a group meeting at least once per year so that they could share experiences with each other.

Windfall Profit and Retention Provisions

In Reading, the housing authority deals with the windfall profit issue by retaining a right of first refusal to repurchase units at the outstanding balance of the mortgage until the mortgage is paid off. At that point, home owners can realize a profit from sale of their units. The authority has a policy against home owners leasing their units, but there are no deed restrictions regarding leasing the entire unit or renting rooms.

Provision for Maintenance After Sale

The Reading Housing Authority provides continuing advice to home owners about how to deal with maintenance problems. For minor problems, such as clogs, authority maintenance personnel show home owners how to solve those problems themselves. For more serious problems, the authority will refer households to the yellow pages. In addition, it has set up a loan fund to finance major repairs, but funds are not available until three years after the owners purchased their units, and the authority will discourage home owners from using the fund until five or more years after the purchase of their homes. Since each of the houses sold was in good condition at the time of sale, the authority does not believe that restrictions on the use of loan fund monies will create any hardships.

Handling Non-Participants

At the beginning of the demonstration, one of the eight houses selected for sale was vacant. Of the remaining seven units, three were sold to their tenants and four were sold to other public housing residents after tenants vacated the units. Of those four units, one resident left public housing almost
immediately. The authority initially allowed the three remaining tenants who did not want to purchase to remain in their units. Once they no longer qualified for those units (i.e., they were over-housed), however, they were transferred to other public housing, and the units were sold. No information is available regarding the characteristics of non-participating households.

**Amount and Use of Sales Income**

The Reading Housing Authority will eventually realize $101,535 plus interest on the sale of the eight public housing units. The authority has not determined how those proceeds will be used. Since the use of the funds was raised as an issue in its 1989 financial audit, however, management is now preparing a plan for the use of sales income. (Its original application to HUD indicated that sales proceeds would be used for a fund to help owners finance major repairs in future years and for tenant counseling and debt service.)

**Impact of Sales Program**

The sale of eight units has had little financial effect on the authority. Loss of the HUD subsidy on the units sold is more than offset by relief from utility costs and maintenance required by those units. The authority, however, has no data on the net financial effects of the sale of the eight scattered-site units.

The City of Reading formerly abated property taxes on the scattered site units, and it now receives taxes (about $600 per unit per year) from those properties.

The neighborhoods surrounding the units sold will benefit to some extent from the conversion of the houses from rental to ownership since the housing authority invested in rehabilitation of those units, and home owners tend to invest more of their time in maintenance and upkeep than tenants. Since the units are widely scattered, however, with no more than one unit on any given block, their contribution to neighborhood revitalization will not be large.

**Conclusions**

The homeownership demonstration in Reading was a success. Eight houses targeted for sale were sold, and after three years only one of the eight new homeowners was not able to maintain mortgage payments. The housing authority executive director believes the keys to a successful homeownership program lie in motivating tenants to become home owners and providing adequate one-on-one counseling to help tenants realize that it is in their long-term self interest to invest their time and money in owning their own home. Although housing authority management has no interest at this time in selling additional units from its housing stock (which now consists entirely of multifamily units), it believes there is a need for a program that would acquire run-down
housing, rehabilitate it, and then sell to low- and moderate-income families who are ready to take the step from tenancy to homeownership.
Introduction

The St. Mary's County Housing Authority in Maryland has sold 30 public housing units from among 50 units available for sale in its Tubman Douglass Estates Housing project. Two additional qualified tenants are interested in purchasing units, and the remaining 18 tenants will be relocated to a new townhouse project that the housing authority has under construction. Once those households (who either are not interested in purchasing a home or who lack the necessary income) are relocated, the housing authority expects to complete sale of all 50 units. That could occur as early as mid 1990.

The single-family detached homes in Tubman Douglass Estates have been priced at $40,000 for a four-bedroom unit and $45,000 for a five-bedroom unit. Those prices are approximately 60 percent of their assessed value. Home buyers have been asked to pay a down payment of up to $1,000 (a portion of which is used to prepay taxes and insurance) and an additional $1,000 for closing costs. The authority established joint accounts with interested tenants at a local savings and loan association into which tenants could deposit funds to accumulate enough money for the down payment; if tenants established such an account and made regular payments into it, the housing authority reserved a home for them to purchase. Residents not participating in the savings plan and who otherwise lacked funds for the down payment were not guaranteed that a home would be available for them should they raise the required funds. The St. Mary's County Community Development Corporation holds a $9,000 first mortgage and the housing authority holds a 15-year silent-second mortgage for the remainder of the purchase price ($30,000 to $35,000 depending on unit size).

The establishment of a collective escrow account (which includes funds for insurance, taxes, maintenance, fuel oil, water and sewer, trash collection, and civic association dues) is a unique aspect of the St. Mary's County demonstration. The monthly payment to the escrow account ranges from $207.94 to $245.50, depending on whether the unit has four or five bedrooms.

Terms of the first mortgage are set after determining how much a household can afford to pay for principal and interest, given that total escrow, principal, and interest payments cannot exceed 30 percent of household income. Among the first 30 houses sold, interest rates on the first mortgages have ranged from one percent to 13 percent, and the length of the loans have ranged from one to 15 years. Total principal and interest payments per month have ranged from a low of $55.30 to a high of $223.97.
Thus, households who can afford as little as $300 a month have been able to purchase homes.

As of August 1989, no foreclosures have occurred, but one home was reconveyed to the housing authority when its owner was jailed on drug-related charges. That house has been resold. Fourteen of the 31 new homeowners have been delinquent on their payments by at least one month on one or more occasions.

The technical assistance grant provided by HUD covered $37,500 of the total of $38,448 in administrative costs of the homeownership demonstration in St. Mary's County. Most of those costs went toward tenant screening and counseling. Counseling of new owners involves their participation in a 20-hour training program staffed by housing authority employees and various other personnel from local and state agencies.

Although the demonstration has produced a sharp reduction in housing authority revenues from HUD (a decrease of $145,292 in 1988 from 1987 HUD subsidy payment levels) and from the loss of rents received from tenants—which have not been offset by reduced operating costs—housing authority management is highly pleased with the demonstration. Benefits cited by management include increased political acceptance of the authority and subsidized housing, improved upkeep of the Tubman Douglass Estates neighborhood, and the benefits to homeowners, who now have a stake in their neighborhood and community.

Managing the Demonstration

The demonstration in St. Mary's County, MD is managed by the St. Mary's County Housing Authority, a division of the St. Mary's County Department of Economic and Community Development. The department director designed the demonstration. Day-to-day management of the demonstration is handled by the project manager of Tubman Douglass Estates.

At the beginning of the demonstration, the St. Mary's County Housing Authority had 50 units of public housing located in one rural subdivision, Tubman Douglass Estates (MD 021-001), and it administered 200 Section 8 certificates. It has been approved for additional units of conventional public housing, which are under construction, and it now administers 43 housing vouchers. Some 260 families are on the authority's Section 8 waiting list, and 240 on its rental allowance program waiting list.

St. Mary's County is one of the most rapidly growing counties in Maryland, and that growth has led to an increase in demand for moderate-priced housing. Although predominantly rural (the only incorporated place is the county seat at Leonardtown, population under 2,000), the population of the county increased from 47,388 in 1970 to an estimated 64,700 in 1985. The unemployment rate was about 3.5 percent. A major economic stimulus has been the Navy's Patuxent River Naval Air Station. That has led a number
of high-tech firms (Sperry, Dynamac, Veda, Tracor, and Bendix) to locate facilities in the county, and one thousand new defense-related jobs per year are projected.

The primary goal of the demonstration in St. Mary's County is to provide homeownership opportunities to the current tenants of public housing. The authority's management views ownership as desirable for a number of reasons: (1) that is the traditional form of tenancy in rural St. Mary's County and is evidence that a family is an established member of the community; (2) it provides families with a sense of dignity and community responsibility; and (3) it helps encourage a sense of self-sufficiency, lessening families' dependence on others. Another goal or benefit from the demonstration is to return property to the tax roles. Although not a formal goal, the authority's management also notes that with the low rate of turnover of Tubman Douglass Estates homes (less than one per year), the present tenants would be there a long time whether tenure is rental or ownership, and it is more efficient for the authority and more beneficial for the tenants for them to own their homes rather than to continue renting from the housing authority.

Tubman Douglass Estates has a tenants' association (Tubman Douglass Civic Association) that from time to time is very active. Tubman Douglass Estates was built in response to black citizens' protests over the proposed demolition of their former homes in the Carver Heights section of the county. That leadership was instrumental in forming the civic association. The officers of the association were informed of the county's intention to participate in the demonstration, and members of the association actively endorsed the concept. In its application to HUD to participate in the demonstration, the authority estimated that 75 percent of the residents of the subdivision supported participation.

The county viewed the demonstration as an opportunity to return property to the tax roles and as a way of contributing to the future development of the rapidly growing area near the Tubman Douglass subdivision. Whereas public housing might have stigmatized the surrounding area and drawn complaints from nearby property owners (in fact, initial occupancy of Tubman Douglass Estates in the early 1970s was delayed due to a suit by surrounding property owners who tried to stop the project), that would be less likely to occur after tenants bought their homes.

County officials agreed to support the demonstration in a variety of ways. These included providing an $18,000 loan to the housing authority to pay for surveying the subdivision and other front-end costs; allowing the civic association to purchase fuel oil from the county, thus assuring a lower price; and making county staff available to help in various ways with the demonstration.

Local government agencies have a long history of working with the housing authority and leadership of Tubman Douglass Estates. The
county parks and recreation department, for example, helped build and maintains a recreation area with playground equipment and a basketball court adjacent to the subdivision. The Lexington Park Metropolitan Commission extended water and sewer lines to Tubman Douglass Estates after septic tanks failed. The Tri-County Community Action Agency and Maryland Electric Coop both helped teach residents about home weatherization and no cost-low cost measures to conserve energy. The extension agents from the University of Maryland Extension Service regularly provide services to the subdivision.

The St. Mary's County Housing Authority estimates that it has incurred little net costs from taking part in the demonstration, since all of the staff involved are already on the county or housing authority payrolls or are paid from HUD grant monies for the demonstration. The demonstration entailed front-end costs for surveying, but those costs will be recovered from sales proceeds. Legal costs were contributed by a law firm operated by the director of the housing authority and by the county attorney's office. Staff involved in the demonstration include the authority director, the project manager, a housing counselor, (who moved to a position with the St. Mary's County Community Development Corporation in 1988), and a maintenance worker, and part-time clerk.

The demonstration was originally structured so that two of the housing authority staff members, the project manager and the housing counselor, would continue to be employed in service to the residents of Tubman Douglass after title was transferred to the homeowners. As described in more detail below, the authority proposed to set aside $3,000 per dwelling from mortgage proceeds into a revolving reserve maintenance fund. Interest on that fund, estimated to be about $15,000 per year, would be used to pay part of the salary of the executive director of the civic association. Residents also contribute $10 per month to the civic association, with that payment made mandatory by conditions of their mortgages. The terms of sale also require residents to make $40 per month payments into a maintenance fund to be used for day-to-day maintenance. That would generate $2,000 per month, and the initial thinking is that the civic association will contract with the project manager and the current maintenance person to continue to provide maintenance services after residents become homeowners.

The authority received a $37,500 technical assistance grant from HUD. Those funds provided partial support for the housing counselor. If additional technical assistance funds were available, the authority would expand its counseling effort (in 1987, the housing counselor noted that a key weakness of the authority's current counseling effort was the necessity to work on emergencies, with no attention to "preventive" counseling). Although lack of technical assistance funds would not have dissuaded the authority from taking part in the demonstration, it believes that the role envisioned for the civic association--
basically taking over the maintenance functions of the authority—was critical in persuading tenants that the demonstration would work out in their best interests.

Overall, the housing authority management is very satisfied with management of the demonstration. In particular, it is pleased that while the authority has provided a considerable amount of counseling and guidance, the residents--through the Tubman Douglass Civic Association--are becoming increasingly involved in decisions about the future maintenance of their homes.

Selecting and Rehabilitating Properties

Tubman Douglass Estates, the project chosen for the demonstration, was the only public housing operated by the St. Mary's County Housing Authority. The project is a rural subdivision located off Norris Road near the town of Lexington Park, Maryland and Maryland Route 275. Nearby rural subdivisions contain homes priced from $40,000 to $80,000, and new homes in area are selling for from $45,000 to $125,000. The area is racially mixed and is middle class.

The homes in Tubman Douglass Estates are one-story, four- and five-bedroom, aluminum-sided, modular frame ramblers erected in 1972 on one-half acre lots (but not occupied until 1974 because of a suit from surrounding landowners that opposed the project). Between 1982 and 1985 HUD modernization funds were used to complete $650,000 in improvements, including a new sanitary sewer system, improved storm drainage, regrading, landscaping, and exterior repair and repainting of all of the units. Built with "20-year" shingle roofs, however, homes were in imminent need of re-roofing at the time the authority applied for participation in the demonstration. After entering the demonstration, the authority used the remainder of the HUD modernization funds it had been allocated to have the roofs reshelmed and fences built around the backyards of each unit. Also, the authority installed new appliances in each of the units, including stoves, refrigerators, washers and dryers (but not including furnaces). Thus, the authority has no need to spend its own funds rehabilitating units immediately prior to sale.

Attracting and Selecting Owners

The primary criteria used in selecting initial purchasers was their ability to come up with approximately $1,000 to cover closing costs and an additional $1,000 downpayment and to make monthly payments of from $250-$300, which included principal, interest, and payments to a comprehensive escrow account (see below). Also, the authority looked at tenants' rent payment records while they had lived at Tubman Douglass and their need (which was defined as having two or more children) for a four- or five-bedroom home. Other criteria mentioned in the authority's application to HUD include tenants' employment history and its desire to achieve a racial mix in the subdivision.
Because a number of tenants lacked the required savings ($2,000) to pay the required downpayment and closing costs, the authority established joint accounts with interested tenants at a local savings and loan association into which tenants could deposit money to accumulate those funds. If tenants established such an account and made regular payments into it, the housing authority reserved a home for them to purchase. Residents not participating in the savings plan and who otherwise lacked funds for the down payment were not guaranteed that a home would be available for them should they later raise the money needed.

The tenants of Tubman Douglass Estates are the primary pool from which the authority has drawn potential home owners (26 homes have been sold to existing tenants, four homes have been sold to persons who had not previously lived in Tubman Douglass Estates). Since not all of the tenants will be eligible or will want to buy, the authority is using its pool of Section 8 certificate holders and the pool of households on its waiting list for Section 8 housing as a backup pool of potential low- and moderate-income home owners.

The authority has used a series of letters and follow-up meetings with tenants of Tubman Douglass Estates and Section 8 certificate holders to inform people of the demonstration and to solicit their participation. Initially, all residents of Tubman Douglas Estates and all Section 8 certificate holders were sent a letter informing them of the demonstration and eligibility criteria (income of $10,000 per year, two or more children, willingness to work with the civic association and, later, required settlement cost). The authority then began with those tenants and Section 8 certificate holders with the highest incomes (the first group of home owners were paying in excess of $400 per month rent) and scheduled personal interviews with them to explain in greater detail how the demonstration worked, the responsibilities of homeownership, their financial responsibilities, and how to fill out a mortgage application form. As of August 1989, it has proceeded through that step with all 50 households in Tubman Douglass Estates and had also set up a waiting list of other people who were interested in purchasing a home from the authority.

The new home owners in Tubman Douglass Estates are black families with a wide range of incomes—from less than $10,000 per year to more than $30,000 per year. Ages of household heads range from less than 30 to over 50, while household size ranges from three to seven persons. Most, but not all, households have children living at home.

**Property Conveyance**

Properties are being sold fee simple. The sales prices ($40,000 for a four-bedroom home and $45,000 for a five-bedroom home) are based on the authority director's estimate in 1985 of their worth.
based on comparable housing in the county (subsequently, homes were assessed at more than that by the county assessor, reflecting escalating home prices; as of August 1989, the sales prices of homes in Tubman Douglass Estates are approximately 60 percent of assessed value). Closing costs of $1,000 are paid by purchasers. Those costs include recording costs, state transfer tax, and state tax stamp. The county and housing authority provide attorneys for the closing, and they paid for surveying. (The county's legal aid office reviewed initial sales, but it has not participated in subsequent closings and buyers have tended not to secure their own legal representation at closing).

Initially, property conveyance was delayed because the mortgage to Tubman Douglass Estates was not held by HUD but by the Bank of Tennessee, which would not divide its interest in the project into 50 units and release title to individual houses as they were sold. Thus, the authority was not able to deliver a clear title to the first 10 purchasers, and the project was delayed while a solution was sought.

To understand that situation, a brief history of the Tubman Douglass Estates will be useful. The project originated when the owner of Carver Heights, a surplus World War II Navy housing project, decided to demolish the project in the early 1970s. After organizing efforts by VISTA volunteers and protests by low-income black families living in Carver Heights, the county set up the St. Mary's County Leased Housing Corporation to participate in HUD's Section 23 leased housing program. The corporation used revenue bonds secured by unit rents to pay for the 50-unit Tubman Douglass subdivision to house families displaced from Carver Heights. The assets of the Leased Housing Corporation were transferred to the St. Mary's County Housing Authority in 1974 along with the $1.3 million indenture used to finance the project. HUD provided the authority with additional funds each year to pay off the revenue bonds.

The problem was resolved in the following manner. HUD agreed to make a $650,000 administrative loan to the housing authority so that it could pay off the outstanding loan from the Bank of Tennessee. The authority is using annual contribution funds from HUD (it has a contract for $120,000 a year for 20 years) to repay the loan to HUD (that could occur as early as 1994). That solution cleared the way for additional sales of houses in Tubman Douglass Estates.

The inability of the authority to provide clear title led to changes in the way home sales have been financed. Initially, two local banks had agreed to provide $10,000 mortgages for the first 10 homes sold, but they backed out of that arrangement. In order to continue with the demonstration, the housing authority had the St. Mary's County Community Development Corporation (the director of the housing authority is also director of the community development corporation) hold the first mortgages while the issue of title to the property was being negotiated. Buyers were
notified, and signed an acknowledgement form, that the authority and HUD were making their best efforts to satisfy the outstanding indenture, but until that was accomplished, the buyer did not have clear title.

The fact that banks could not finance the sale of the first ten homes created a serious cash flow problem for the authority, since it did not have the anticipated front-end funds it expected ($100,000 from the sale of 10 homes at $10,000 each). Therefore, rather than underwriting closing costs, it has had to require down payments from all buyers. Also, it has not been able to fund the revolving loan fund it expected to establish to finance major repairs to units when they are needed or to repay the county for funds the county loaned the authority for surveying and other start-up costs.

The authority explored use of the limited equity cooperative housing approach to sales and was impressed with the approach being used in the Denver Homeownership Demonstration. The major advantage of cooperative housing for the authority would have been that a cooperative could borrow funds and provide the county with some cash for the Tubman Douglass project. The cooperative would rent units to public housing tenants at market rates and tenants could use Section 8 certificates to make the units affordable. Thus, the county would receive funds for the project which it could put into other low-income housing programs and tenants could remain in their homes as cooperators. That approach was abandoned, however, due to the authority director's concerns about red tape associated with Maryland's laws concerning the conversion of rental units to condominiums or cooperatives and HUD's concerns about the authority using money for Section 8 certificates to pay itself rent for units it would continue to hold in the cooperative.

The housing authority management is satisfied with the method used to transfer property, but it suggests that the provision of seed money to finance early sales would speed participation in a demonstration, since few low-income households have funds on hand for closing costs and a down payment. Without seed money or outside financing, the authority has had to deal with serious cash flow problems.

**Financing**

Financing for the initial sales of homes in Tubman-Douglass Estates is provided by the St. Mary's County Community Development Corporation, which holds the first mortgage of $10,000 less whatever buyers pay as a down payment (the authority is seeking $1,000 down from those able to pay in order to raise operating capital and subsidize closing costs for those less able to pay). The St. Mary's County Housing Authority carries a silent second mortgage of $30,000 or $35,000 depending on whether it is a four or five bedroom home. (Before it discovered it could not obtain clear title, the authority had used personal
friendship networks—one of the authority board member's father was president of a local bank—to persuade two banks to hold $10,000 first mortgages on the first ten homes sold.) Interest rates have varied from 1 to 13 percent with mortgage terms up to 15 years, in each case depending upon what is needed to make the home affordable (with that being defined as mortgage and escrow payments amounting to $250 to $300 per month).

The authority originally thought that at least 10 of its tenants would be able to secure first mortgage financing from two banks that had agreed to cooperate with the demonstration (those ten tenants had high enough incomes to be good credit risks) and that would provide the $100,000 it wanted as front-end money to finance the demonstration. When it could not provide a clear title, however, the arrangement with the banks evaporated and the county's community development corporation picked up the first mortgages. (The community development corporation was established to administer a community development block grant-funded revolving loan fund in which the CDC makes loans to households for lots on which to build their homes or for mobile or modular homes.) Because it had experience administering loans, it was chosen to hold the first mortgages rather than the housing authority. That, however, did not provide the housing authority with any cash.

When financing from local banks became impossible to obtain, the authority did not consider use of the Maryland Housing Finance Agency because it felt the red tape involved in the administration of that agency's programs was not worth putting up with in terms of any advantages gained.

The authority has taken a number of steps to protect its interest in the property conveyed. The first mortgages require owners to carry hazards insurance and pay property taxes or the mortgage can be foreclosed. The second mortgages contain a rider that requires owners to make payments to an escrow account which covers taxes, insurance, water/sewer fees, trash collection, maintenance fund, and civic association dues. Required payments to the escrow account have ranged from $207.94 (four-bedroom) to $245.50 (five-bedroom) per month. The following is a typical list of items covered by the escrow payment:

<table>
<thead>
<tr>
<th>Item</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Taxes</td>
<td>$37.50</td>
</tr>
<tr>
<td>Maintenance</td>
<td>40.00</td>
</tr>
<tr>
<td>Fuel oil</td>
<td>56.00</td>
</tr>
<tr>
<td>Hazard insurance</td>
<td>27.00</td>
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<td>Water/sewer</td>
<td>42.00</td>
</tr>
<tr>
<td>Trash/services</td>
<td>6.00</td>
</tr>
<tr>
<td>Civic association dues</td>
<td>10.00</td>
</tr>
</tbody>
</table>

The escrow account funds for maintenance, fuel oil, water and sewer, trash services, and the civic association dues are to be disbursed by the Tubman Douglass Civic Association (which now has a part-time secretary who is also a homeowner); the St. Mary's
County Community Development Corporation handles payment of insurance and taxes from the escrow account.

The authority has used counseling, buyer selection procedures, the escrow funds noted above, and the reservation of funds for a catastrophic loss revolving loan fund to minimize the potential for default. Counseling ensures that tenants are well aware of the costs of homeownership when they buy their homes. The escrow accounts ensure that households do not get hopelessly behind in utility and fuel payments.

As of August 1989, no foreclosures have occurred, but one home was reconveyed to the housing authority when its owner was jailed on drug-related charges. That house has been resold. Fourteen of the 31 new homeowners have been delinquent on their payments by at least one month on one or more occasions. The authority's application for participation in the demonstration listed several procedures it will take in case of default. They include counseling, deferral of payments on a month-to-month basis for up to six months, and refinancing of the mortgage for five years. Initially when payments are late, owners are sent a letter requesting payment. That is followed by a second, more threatening letter if payment still has not been received.

Counseling

Homeownership counseling is the responsibility of the manager of the Tubman Douglass Estates project. A housing counselor who joined the authority staff in 1979 as an assistant to the manager and tenant counselor, also participated in counseling until she joined the staff of the St. Mary's County Community Development Corporation in 1988. Pre-purchase counseling involves meetings with tenants in the authority's office at Tubman Douglass Estates to explain their rights in the property transfer process and the financial and other responsibilities they would assume as homeowners. Fact sheets about the sale are provided and, at the tenant's request, a copy of the homeownership demonstration proposal. Two interviews with interested household heads are held: one to explain the program and the costs and responsibilities of homeownership and the second to learn whether the household wants to participate. In addition, households meet with the authority director, to review their mortgage application.

In addition to those formal aspects of pre-purchase counseling, the Tubman Douglass project manager has taken a number of other steps to help tenants understand what is involved in homeownership. He arranged for a person from the county's Legal Aid program to meet with tenants and review the first and second mortgages (that led to some misunderstandings because, initially, the legal aid person did not understand the process and thought some tenants were being treated unfairly). He holds weekly rap sessions with tenants in his office to discuss the demonstration
and a variety of other matters of interest to tenants. And, for a number of years, he has held regular educational programs for tenants that feature presentations from various resource people.

All home buyers at Tubman Douglass Estates are required to attend 20 hours of counseling led by the project manager on home maintenance, financial management, and civic responsibility. Six sessions are held. They began in September 1987, at the rate of two per month over a three-month period. The process is repeated for succeeding groups of tenants. Handout materials dealing with home maintenance and other matters have been prepared for new home owners. Because counseling has been provided by housing authority staff no estimates of its costs to the authority are available.

After households purchase their homes, they are served by the Tubman Douglass Civic Association, which will provide all of the services previously provided them by the housing authority, including counseling, as needed, regarding home maintenance and other matters. Also, as noted above, the escrow account is structured such that the association will be arranging fuel oil purchases and trash collection, and administering a maintenance contract for repair of members' homes as needed.

Housing authority staff stress the importance of counseling, and they note that if additional technical assistance funds were available, those would have been devoted to extended counseling efforts.

Windfall Profits and Retention Provisions

The silent-second mortgage held by the housing authority in the amount of $30,000 or $35,000 is designed to prevent owners from reaping windfall profits and to prevent speculators from buying units. Payments on the second mortgage ($250 per month beginning five years after purchase) are forgiven if the owner remains in residence, retains ownership during the full term of the mortgage, and makes payment into the escrow account. The authority expects to forgive second mortgage payments for five homes every year during years six through 15 of the term of the second mortgages.

As of August 1989, windfall profit provisions had not been used. When one owner was jailed, title to the home was reconveyed voluntarily to the authority and the house was resold.

Provision for Maintenance After Sale

As noted above, the terms of the second mortgage require owners to pay $40 per month into a maintenance escrow account designed to defray routine maintenance costs after sale. Money will accumulate in that fund until a $1,000 per unit maintenance reserve is attained. The escrow account is administered by the civic association, which might contract with the current project.
manager and maintenance person to continue providing maintenance services. The authority has agreed to set aside $3,000 of principal payments on each sale for use to defray major repair costs.

No funds have been used for major repairs, but the maintenance escrow accounts are drawn on regularly for routine repairs, which are made by authority maintenance staff under contract to the civic association.

Housing authority management is satisfied with the maintenance provisions it has established.

Handling Non-Participants

The housing authority expects to sell all 50 homes in Tubman Douglass Estates. Households who are not purchasing their home will be relocated to other housing in the county using Section 8 certificates or the additional public housing the authority has under construction, and the county will handle moving expenses as required by federal relocation laws. No estimate of those costs has been made.

Until additional public housing is available, however, some 18 to 20 tenants who are not purchasing their homes will continue to live in them. Many of those who will be relocated now have housing needs which are not met by Tubman Douglass Estates, according to housing authority staff, since over the years their households have become smaller and they do not need a four- or five-bedroom home.

Amount and Use of Sales Income

The St. Mary's County Housing Authority expects to realize approximately $450,000 in proceeds over 15 years from the sale of 50 houses in Tubman Douglass Estates. The authority expects proceeds from the sale will enable it to expand its housing programs for low- and moderate-income households. Detailed plans for use of the proceeds, however, have not been formulated.

Impact of Sales Program

The authority estimates that the annual amount of the HUD operating subsidy lost due to the sale of homes in Tubman Douglass Estates was $145,292 in 1988. No savings in maintenance, utility, and insurance costs are evident from data submitted by the authority but this should change as more units are sold. Also, a substantial, but unknown, amount of rent revenue has been lost.

The demonstration has had a positive effect on county revenues, however, since the county now receives approximately $700 per year in property tax revenue from each of the homes that has been sold in Tubman Douglass Estates.
New home owners have invested in landscaping, and the maintenance of homes and grounds has improved with homeownership; thus, the image of the project is improving, and the authority expects that the program will have a positive effect on the surrounding area.

Finally, the program appears to have had a positive effect on the new home owners, giving them a stake in the community. In addition, three marriages occurred and three people sought and obtained full-time employment so that they could become homeowners.

Conclusions

Initially, the authority expected to have completed all sales within 12 months of the first sale, which occurred in June 1986, but because of problems in conveying clear titles, by August 1987 only 10 units had been sold, and two years later, 20 units still remained to be sold. There are a number of factors that account for the delay. They include the problem in obtaining clear title, the need for residents to assume closing costs, and some hesitancy among residents about participation in the program. (Also, the authority director notes that unlike conventional real estate sales, where realtors have an incentive to move sales along as rapidly as possible, in this case that incentive is missing—in fact, since this is the only public housing development in the county, the demonstration requires housing authority employees to work themselves out of a job.)

Nevertheless, the St. Mary's County Housing Authority has developed a carefully structured homeownership demonstration. The authority's program is designed to minimize households' individual responsibilities for homeownership and to ensure that homes are adequately maintained during the period in which it continues to have a financial interest in them. The authority initially intended to obtain $100,000 in cash through private financing of the first 10 sales and to use those proceeds to finance closing costs and other expenses for the sale of the remaining 40 homes in Tubman-Douglass Estates. When it could not obtain clear title to the project, however, that scheme could not be implemented. As a result, it is using $1,000 down payments from tenants who can afford it to subsidize closing costs for those of more limited means.

The authority believes the keys to a successful homeownership program include tenants who are interested in purchasing a home and a receptive community with strong political leadership. The major hurdle is the provision of adequate counseling to show tenants that homeownership is within their means financially and will be in their self-interest as well.
Introduction

The Demonstration in Tulsa, Okla., was designed to sell 100 single-family, scattered-site units. FHA insured private financing was arranged for potential buyers who would pay 75 percent of market value for the units. The other 25 percent of the appraised value was to be covered by a silent-second mortgage held by the Tulsa Housing Authority. This silent-second would be forgiven after 10 years of ownership. No downpayment was required of buyers. A one year renewable lease-purchase arrangement was planned to allow a gradual transition from renting to full-ownership responsibilities. Tenants who met eligibility criteria were given the option to sign a renewable one year lease purchase agreement. Tenant-buyers who assumed responsibility for maintenance of their units during the lease-purchase period were given a maintenance credit of $25 a month. The buyers could apply these maintenance credit(s) to cover all or part of the buyers' closing costs. After a minimum of one year under this type of agreement, the authority could schedule the actual sale of the unit.

The demonstration in Tulsa sold only one of the 100 units targeted for sale and at this point the housing authority and HUD consider the program suspended. According to program staff, the reason for this was the extremely soft housing market. The depressed economy has resulted in a large number of vacant units in the city. It is estimated that FHA alone has 1,500 foreclosed houses in the Tulsa market, and foreclosure proceedings are pending on 2,000 more units. FHA is offering these houses to prospective buyers with as little as $100 down and is applying relaxed underwriting criteria to potential buyers. The officials responsible for managing the demonstration did not want to compete with FHA by selling public housing units. If the local housing market improves they may resume the sales program.

Managing the Demonstration

The Tulsa Housing Authority (THA) was responsible for managing the demonstration. Within the agency, PHHD's Project Manager had day-to-day responsibility for administering the program.

The THA has 2,952 units under its annual contributions contract (ACC). It also administers about 2,464 Section 8 certificates and 363 housing vouchers. At the time the demonstration was approved, it had about 1,100 families on the public housing waiting list and an additional 1,821 families on the Section 8 waiting list. When available, the THA offers housing vouchers to families on the Section 8 waiting list. The THA does not screen its waiting lists for income eligibility. However, it
prioritizes households based on composition, place of residency, and several other factors. The agency certifies income requirements at the time a unit becomes available. It maintains open waiting lists, and it adds families to them constantly. Thus, the THA considers the waiting lists an accurate measure of the demand for low-income rental units in the city.

The demonstration had one main goal: homeownership for low-income families. It was expected to provide program participants with an opportunity to feel the pride of homeownership and a stake in the life of the community. The demonstration's lease-purchase agreement was perceived as a motivating force, an incentive to initiate these changes in attitude and self-perception.

The THA's executive director and the board of commissioners made the decision to participate in the demonstration. The principal authors of the proposal were the executive director along with other THA staff. The agency had direct tenant input in this process because the president of the tenant association was a member of the board of commissioners which was involved in all decisions affecting the program. The THA also got input from individual tenants when it presented the proposal during the tenant association's regular monthly meetings. Initially, THA staff recognized that tenants had concerns over the possibility of involuntary relocation. Once the agency publicly presented the proposal however, the tenants' views changed. In general, then, the agency felt there was support from all parties participating in the demonstration. Three major groups were involved in the demonstration. The THA was responsible for the overall management and implementation of the program. From early on in the program, Mercury Mortgage Company, a private lender, indicated willingness to provide necessary financing to qualified buyers. This company provided the mortgage to the single sale under the demonstration. Finally, the Tulsa Urban League was initially responsible for providing the counseling and training to program participants. After a six month period, however, the THA decided that the services being provided by the Tulsa Urban League were not adequate, and the THA took over the responsibility of providing the necessary counseling to tenant-buyers.

Initially, PHHD annual administrative costs were estimated to be $40,000, including legal and accounting fees. Non-personnel costs were estimated to be $2,000 annually. Eight people were involved in implementing the demonstration: six of them spent 25 percent of their time, and two others spent 50 percent of their time in administering the program.

Selecting and Rehabilitating Properties

Originally, 100 single-family, scattered-site units were targeted for participation. Scattered-site units were considered easier to sell than other types of units, and they were also the most
desirable units in the stock. Thus, they were judged ideal for inclusion in a homeownership program. The units were acquired by the THA after 1969. Since 1969, the units have been rehabilitated once and regularly maintained.

Because FHA insured financing was used, FHA inspections were scheduled when units were ready for transfer. Two units were actually inspected by FHA prior to their scheduled date of sale. One of the units required only minor repair work totalling $300. The potential tenant-buyer of this unit lost her job and the unit was never transferred. The second unit required more extensive rehabilitation work totalling $5,160. This second unit was actually sold. The THA was then responsible for undertaking the repair work required by FHA in both units. No tenant relocation was necessary.

All units were located in low- and moderate-income minority neighborhoods. Housing in these areas primarily is composed of single-family units in fair condition. The extent of abandoned units in these areas is perceived to be a reflection of the depressed economic condition in the state of Oklahoma and the city of Tulsa rather than a reflection of the quality of the neighborhoods. No other revitalization program was targeted in these areas.

Attracting and Selecting Owners

The THA structured the program so that all of the occupants of their single-family, scattered-site units were potential buyers. Initially, the THA presented the program in meetings of the tenant association, and it also published an announcement of the existence and characteristics of the program in the tenant newsletter. The agency contacted the tenant managers of each of the single-family, scattered-site projects and asked them to identify potential buyers. Tenant managers screened and identified those families with higher incomes and better housekeeping and rent payment histories. The THA contacted these potential buyers, and it invited those strongly interested and able to acquire their units to participate in the demonstration.

Potential participants submitted an application. This application and the information already on file were the basis for the THA's determination of eligibility. Potential buyers had to have a stable employment and income, potential income growth, good rental history with the agency, and an acceptable credit history. (Families were considered to have potential income growth if they could be expected to have the necessary income to meet homeownership obligations after a year of leasing.) If these requirements were met, tenants were given the option of signing a one year, lease-purchase agreement. Families found ineligible for participation could reapply for consideration if their employment or financial situation changed.
After a minimum of one year under the lease-purchase agreement, the agency could schedule the actual sale of the unit. If, however, the agency felt that the tenant-buyers had not improved their financial situation enough to obtain the necessary mortgage financing, it allowed these families to renew their agreements for another year.

If a PHHD unit became vacant, the THA contacted the tenant managers in multifamily units and asked them to identify potential program participants: those able and willing to move to a PHHD unit and purchase it through the lease-purchase agreement. If no potential buyer was found, the THA chose a family from the public housing waiting list that could afford to buy.

**Property Conveyance**

All properties were to be sold fee simple after the one year lease-purchase period. The sale price was based on the appraised value of the units. The first mortgage, held by a private lender, was to cover 75 percent of the sale price. The other 25 percent would be covered by a silent-second mortgage held by the THA.

Tenant-buyers who assumed responsibility for maintenance of their units during the lease-purchase period were given a maintenance credit of $25 a month ("sweat equity"). The buyers could apply these maintenance credit(s) to cover all or part of the buyer's closing costs.

**Financing**

Private mortgage financing was used in the only demonstration sale. The one actual buyer received a credit of $280 ("sweat equity") that was applied to pay part of the closing costs. The private lender offered a FHA 221D2 insured loan for the one unit sold. The closing costs, totalling $2,675, were shared by both buyer ($1,597) and seller ($1,078).

**Counseling**

The THA counselor met on a one-to-one basis with each family several times during the lease-purchase period. When the tenants signed the lease-purchase agreement, the counselor explained the program in detail. A second meeting was held to go over the issues identified above. Because of the long history of some of the tenant-buyers in public housing, the maintenance aspects of the counseling were not emphasized. Participation in the counseling program was mandatory and meetings were rescheduled at the family's convenience. No formal post-purchase counseling was offered.
Windfall Profits and Retention Provisions

Windfall profit and retention provisions are included in the second-mortgage instrument. The second mortgage limits the right of the borrower to sell the unit for a period of ten years. If during this period, the borrower attempts to sell or conveys the property to an individual who does not qualify as a low-income person, or otherwise would have been considered ineligible to participate in the PHHD, the THA will consider the borrower in violation of the terms of the silent-second mortgage and may foreclose on the mortgage and evict the borrower. The agency considered this restriction sufficient to limit the possibility of buyers reaping windfall profits, as well as to maintain the unit in the low income stock for a period of ten years.

Provision for Maintenance After Sale

Tulsa's demonstration program did not include any special provisions for assisting participants with repairs after the transfer. The purchasing household is responsible for maintenance after sale.

Handling of Non-Participants

If tenants in targeted units did not want to, or could not participate, they were allowed to remain in the units as renters. No relocation was necessary.

Amount and Use of Sales Income

Initially, the demonstration was expected to have negligible effect on the THA's financial condition. All the proceeds from the single demonstration unit sold, $21,422, were used to pay for closing, rehabilitation work, and other costs associated with the implementation of the program.

Impact of the Sales Program

The sale of the one unit within the demonstration was said to have a negligible impact on the operating subsidies that the THA receives from HUD. Impacts on maintenance and operating costs were also considered negligible.

According to THA staff, however, the program has had some beneficial impact. First, it allowed the THA to develop a closer relationship with tenants both during the initial THA-tenant contacts and during the counseling sessions. Second, and more importantly, the program staff feels that the demonstration has shown many tenants that homeownership is a feasible goal even for low-income families, as long as they are committed to improving their situation.

A final impact of the sales program concerns the purchasing family itself. The program staff contends that the positive
impact on this family can be seen in the care they take in maintaining and improving their unit. The program has given the opportunity for the family to feel the pride of homeownership without increasing its financial burden (i.e., debt payments are about the same as the old rent payments).

Conclusions

The demonstration program in Tulsa has fallen way short of its initial goal. Of the 100 units targeted for participation only one was sold. The reason for this, however, lies beyond program control. According to program staff, the lack of success is the result of an extremely soft housing market in Tulsa. This is unfortunate because the program presented some interesting characteristics such as the lease-purchase period and the maintenance credit ("sweat equity") concept. Due to the lack of sales, a clear evaluation of the effects of these characteristics on the sales program cannot be undertaken.

In general, however, those contacted had a positive opinion of the program. If the housing market changes, the program staff would like to see the program expanded to include other single-family, scattered-site units as well as multifamily projects. Because the agency feels that home owners are going to take better care of their units, homeownership is seen as a desirable goal for the purchasing family as well as for the community.
PUBLIC HOUSING HOMEOWNERSHIP DEMONSTRATION

VIRGIN ISLANDS CASE STUDY

Introduction

Built in the 1950s, Pearson Gardens is a 240 unit family complex located on very valuable land just across the street from the St. Thomas waterfront where major tourist ships come to port. Plans call for the conversion of half of Pearson Gardens into a co-op with the other half of the project to remain part of the public housing inventory. In addition to this formidable challenge, St. Thomas's homeownership demonstration also features the lowest income limits of any housing authority participating in the PHHD. Because the housing authority plans to turn the project over to the co-op at no cost, buyers will have no debt service obligations. Moreover, the co-op successfully petitioned the government for a 20 year exemption from local taxes, which should lower monthly carrying charges still further.

Another unique feature of this project is that it is being designed and managed almost entirely by a consultant who was engaged by the housing authority. Unfortunately, the consultant's contract expired more than a year ago and has yet to be renewed by the housing authority. However, despite his not getting paid, the consultant is continuing to work with a very dedicated group of co-op members to push the project forward. Another interesting aspect of this project is the effort being made on the co-op's behalf by a dedicated legal service's attorney. Although legal service attorneys are playing key roles in two homeownership demonstration projects, the issues in Paterson and St. Thomas are very different. While legal services brought suit in Paterson to stop the conversion, they are doing everything within their power in St. Thomas to facilitate the conversion. The feeling in St. Thomas is that the co-op could do a much better job of managing the housing than the housing authority and that the sooner the project closes the better it will be for Pearson Gardens' residents.

Four years into the demonstration, the Pearson Gardens co-op has yet to close, and will not close in the foreseeable future unless the housing authority makes the conversion a higher priority matter. Complicating matters and slowing progress is the stalemate over the relocation of non-buyers to the rental side of the project, and the relocation of co-op members who currently reside on the rental side who want to move to the homeownership segment. At the time of our last site visit, the housing authority had not yet approved a relocation plan and was continuing to fill vacancies in the homeownership segment of the project with rental families selected from the PHA's waiting list.
Managing the Demonstration

The demonstration in the Virgin Islands is administered by the Virgin Islands Housing Authority which manages 4,471 units of public housing. Approximately half of those units are in 14 developments on St. Thomas. Most of the others are in 17 developments on St. Croix and there is one development on St. John. The authority also manages 277 Section 8 certificates and has 195 Turnkey III properties yet to be sold. The Turnkey III program provided the authority with homeownership program experience.

As of April 1989, VIHA had a waiting list of 1,470 eligible applicants, and another 692 applications that were being reviewed for eligibility. Most of the applications were for two-, three-, and four-bedroom apartments. Despite this high demand for units, a sizable portion of VIHA's public housing stock is vacant and uninhabitable. Within the past two years approximately 100 of VIHA's 756 seriously deteriorated vacant apartments have been repaired and reoccupied. The housing authority is working on the backlog and is committed to recovering virtually all of these units.

Public housing in the Virgin Islands is a much larger share of all housing compared to most American cities. Approximately 20 percent of all housing units on the island are public housing. This is at least partially the result of the tourist economy which raises housing prices to levels that are well beyond those that most indigenous islanders can afford.

The goals of the demonstration program are as follows:

1. Helping lower income Territorial families to share in the American goal of owning their own homes;

2. Building a sense of responsibility and a homeownership stake in the community that would lead to neighborhood stability and ultimate improvement;

3. Providing tenants who are already involved in the management of their public housing projects an opportunity to take the next step to ownership; and

4. Improving the quality of life for both those families remaining as tenants of public housing and those who move into homeownership.

Several concerns were raised in discussions of whether or not to participate in the demonstration. First, residents were very concerned about the units ending up in the hands of private developers. The Pearson Gardens development is on very desirable and very valuable real estate. In fact, one recent editorial suggested that the development be sold to developers and the funds used to build new units elsewhere. The residents are
adamantly against this. In fact fear of being displaced is one of the main reasons many residents want to participate in the co-op. They see it as a means of assuring that developers will not be able to acquire the property. Second, the VIHA staff was concerned about replacement housing. This concern was not strong enough, however, to stop them from supporting the program. Finally, concern was expressed over the co-op form of ownership. A number of residents either didn't understand how it worked or simply wanted to have fee simple ownership in the form of a condominium.

The initial impetus for participating in the demonstration came from the board of commissioners. After what was considered to be a successful experience with the Turnkey III program, the board wanted to be able to continue providing homeownership opportunities and the demonstration would allow them to do this. The actual proposal was developed by the special assistant to the director of the housing authority. In preparing the proposal, the assistant consulted with the tenant council at Pearson Gardens and with representatives of legal services.

Four major groups are involved in the demonstration. The housing authority has the responsibility of overall management. It, however, has contracted most of the work, including assessing the feasibility, to a local consulting firm, Ed Phillips Associates. Legal services has agreed to provide legal counseling to prospective cooperators and assistance in developing legal documents, such as the Articles of Incorporation. Finally, the tenant organization at Pearson Gardens has been very active in explaining the program to tenants and in assessing interest in participating. At a later date, the group hopes to bring in professional co-op trainers but it has not reached this stage. The local government has not had much involvement in the demonstration although legislation has been enacted that will grant the cooperative complete tax abatement for the first 10 years and a graduated tax rate for the next 10 years.

Annual administrative costs of the PHHD were estimated to be in the range of $14,000 in staff time. This represents five percent of the special assistant's time, a small portion of other PHA employees' time and 100 hours of the consultant's time. Another $2,000 was spent on reproduction, supplies, printing, and the like.

The VIHA received a technical assistance grant of $26,000. Of this amount, $15,000 was paid to the project's consultant, $2,000 was spent on VIHA staff travel, and $3,000 was spent for supplies and miscellaneous items. According to the proposal submitted to HUD, the remaining $5,000 would be held by the housing authority for use by the co-op for board training after closing. According to program staff, more technical assistance funds could have been well spent and would have helped to move the co-op along much more quickly.
One major problem encountered in administering the program has been developing interest among tenants in cooperative ownership. Since the idea of a co-op is new to almost all of the tenants it has taken considerable time and effort to explain the concept and its advantages. Only one other co-op exists in the Virgin Islands and that is relatively new. Many people were initially discouraged that they would not own their individual units. This may also explain why attendance at several organizing meetings was less than expected. As of August 1989, however, 91 families had joined the co-op. The goal is 120 participating families. Efforts are continuing to generate interest in the co-op.

A second major problem has been getting VIHA to place the conversion of Pearson Gardens on a high enough priority to see it through closing. As of August 1989, virtually all of the pressure to move the project along was coming from the co-op’s extraordinarily dynamic president, the consultant (who because the housing authority has yet to extend his TA contract is working on a pro bono basis), and a very dedicated legal services attorney. For a variety of reasons, including a major reorganization of the Virgin Islands Housing Authority, VIHA has not yet approved the necessary legal paperwork to make the project happen.

Moreover, as explained in later sections, VIHA has also slowed the conversion process by continuing to rent-up vacancies that occur in Pearson Gardens through normal turnover with families from the housing authority's waiting list, rather than using those vacant apartments to facilitate transfers of buyers and nonbuyers between the two sections of the project. Clearly, for reasons that we were unable to determine, the conversion of Pearson Gardens is a lower priority activity of VIHA in 1989 than it was in 1985-86.

Selecting and Rehabilitating Units

In its original application to HUD, VIHA proposed selling two developments: William's Delight on St. Croix, and Pearson Gardens on St. Thomas. After discussions with HUD staff only the Pearson Gardens development was included in the demonstration, primarily because it was in much better condition. William's Delight needs much rehabilitation. Pearson Gardens is considered to be one of the best public housing developments on St. Thomas and has been recently modernized. The board and staff felt that the desirability of this development would encourage tenant interest in assuming ownership.

The goal is to sell 120 of the 240 units in Pearson Gardens. The plan calls for bisecting the development, selling one-half to the tenant owned co-op and retaining the other half as conventional public housing. This will allow those who can not afford, or who do not want to participate in the co-op, to remain in the development. Non-participants in the half of the project going co-op will be voluntarily relocated to the other half of the
development. The decision on which section of the development will be sold to the co-op is being based on the location of those who have expressed interest in participating. More of those interested are located in the eastern section of the development. The current plan then calls for the development to be divided along a north to south or front to back line. This means that both the co-op and the remaining public housing will have equal access to the main street (Long Bay Road). The eastern section of the development also has a good mix of one-, two-, three- and four-bedroom units and has more open space and parking. Four of the buildings also have cisterns to provide a supplemental water supply.

Built in the 1950s, the Pearson Gardens development consists of 30 two story apartment buildings, each containing eight units. There is a mix of one-, two-, three- and four-bedroom apartments. Fifteen of these buildings would be included in the proposed co-op.

The condition of the units in Pearson Gardens is good. Approximately $10 million in TPP, HUD modernization monies, was spent on rehabilitating Pearson Gardens over the past eight years. The repairs were extensive enough to require the staged relocation of all tenants to a nearby VIHA development. The modernization work was completed in 1985, before the demonstration began. A recent appraisal estimates units to be worth $50-85,000 depending on the number of bedrooms. That places the project's value at around $17 million. Most of that value is in land.

Pearson Gardens is surrounded by a mix of commercial and residential properties. To the south, across Long Bay Road, is Ramada/Yacht Haven, a motel and boat marina. Adjacent to the Ramada Inn is an open area recently created by filling the bay, which is scheduled for intensive tourist and port-related development. To the west is a VIHA elderly low-rise apartment building. To the north is an upper middle class residential area with one row of houses that back up to Pearson Gardens. These houses are separated from the development by a chain link, barbed wire fence. The adjacent houses are all in excellent repair.

The east side of the development is bordered by an industrial building.

The development is conveniently located with respect to shopping. The residential area to the north was described as approximately 80 percent owner occupied with houses selling in the $85-150,000 range. Staff does not expect the demonstration to have an effect on the bordering neighborhood since it is already in good shape and the Pearson Gardens development is separated from it.

Because just half of Pearson Gardens is scheduled to be sold to tenants, there is a need for additional modifications to utility lines and internal roads that would enable the co-op to function independently of the rental portion of the project. A $55,000
application for community development block grant funds, prepared by the co-op's consultant, was rejected by island officials. As of the time of our final site visit, co-op leaders were unable to secure funding from any other source for the necessary improvements.

Attracting and Selecting Owners

Marketing the program to tenants has been a joint effort of the consultant and the Pearson Gardens tenant organization. Several meetings were organized by the consultant. An initial meeting was designed to introduce the program, explain the concept and management of a co-op, and address resident concerns and questions. Approximately 70 people attended. After the distribution of written material describing co-ops and answering other questions raised by tenants at the first meeting, a second meeting was held. A disappointing 21 residents attended. Yet, members of a tenants' group called the Tenants Coalition Committee agreed to begin developing an ad hoc committee to provide tenant leadership to the cooperative effort. This committee was established at a third meeting and it proceeded to survey tenants to assess interest in participating. The survey showed 80 families interested in joining the co-op, 95 families still undecided, and 62 families not interested in joining. Meanwhile, the consultant joined with the tenant representatives to establish sales prices and to develop a four page description of the proposed co-op. This was provided to all tenants. On June 24, 1987, tenants met again and voted to form a non-profit housing corporation to be named Pearson Gardens Cooperative, Inc. Officers of this corporation were also elected. Approximately 60 persons attended this meeting.

Participation in the co-op is open to all Pearson Gardens residents without criminal records, a history of substance abuse, and who have good rent-paying histories and can afford to pay the monthly carrying charges. As of August 1989, 91 residents had joined the co-op. All of these families paid a $15 application fee. Of the 91 co-op members, 41 have made their full equity contributions, which are calculated at five percent of their unit's appraised value. These range from $375 for a one-bedroom unit to $725 for a four-bedroom unit.

Based upon anticipated operating costs and the fact that the project will be transferred to the co-op at no cost, the minimum incomes established for eligibility are the lowest in any of the public housing homeownership demonstrations. They range from a low of $6,240 for families requiring one-bedroom units, to a high of $10,800 for those requiring four-bedroom units.

As discussed below in the section on non-buyers, not all co-op members presently live in the co-op half of Pearson Gardens, which means that some kind of exchange of apartments will have to take place among buyers and non-buyers in the divided project.
The sorting out of buyers and non-buyers is turning out to be no simple matter.

In addition to the current residents of Pearson Gardens who have indicated an interest in joining the co-op, another 10-15 young families who are currently doubled up with their parents have also voiced an interest in buying a Pearson Gardens unit. However, because these young families technically are not now tenants of Pearson Gardens, they are not eligible to participate in the demonstration. The co-op has also received 140 applications from public housing tenants in other projects in St. Thomas; lack of demand for units seems to be of little concern to the project's planners.

Property Conveyance

The cooperative form of ownership was chosen in order to assure that the units would remain available for low income families over the long term. The VIHA staff discussed the possibility of converting the project to a condominium but felt they would not be able to assure that the housing would remain available to low income people under that form of ownership.

Like Paterson's Brooks-Sloate co-op, Pearson Gardens units will be transferred to tenants debt-free. The pricing policy established in St. Thomas is that cooperators will make a down payment or equity contribution equal to five percent of the appraised value of their unit and then be responsible for paying a pro rata share of the co-op's operating costs. Thus, the co-op will carry no blanket mortgage, nor will any of the cooperators have any debt service burden. This extremely deep discount is necessary because of the modest incomes of the tenants who will buy their Pearson Gardens apartments.

Although they are subject to change prior to closing, monthly carrying charges are currently estimated to range from a low of around $156 a month for a one-bedroom apartment to a high of $270 for a four-bedroom unit. According to the project's consultant, the estimated carrying charges are based upon a market survey of comparable rents in St. Thomas and are set at around 55 percent of market rents. This, he thinks, is reasonable given that the co-op has no mortgage to carry nor a profit margin to build into its cost structure. Moreover, unlike any of the other PHHD sites, Pearson Gardens successfully petitioned the Virgin Islands legislature to exempt the co-op from local real estate taxes. Enacted on June 14, 1989, the legislation provides for full exemption declining in 20 percent increments for each additional five year period until the twentieth year when the co-op will file taxes.

Currently proposed downpayments and carrying charges for Pearson Gardens Co-op are as follows:
<table>
<thead>
<tr>
<th>Unit</th>
<th>Sales Price</th>
<th>Monthly Payments</th>
<th>Down Payment</th>
</tr>
</thead>
<tbody>
<tr>
<td>1 bedroom (N=20)</td>
<td>$7,500</td>
<td>$156</td>
<td>$375</td>
</tr>
<tr>
<td>2 bedroom (N=40)</td>
<td>$10,000</td>
<td>173</td>
<td>500</td>
</tr>
<tr>
<td>3 bedroom (N=40)</td>
<td>$12,500</td>
<td>225</td>
<td>625</td>
</tr>
<tr>
<td>4 bedroom (N=20)</td>
<td>$14,500</td>
<td>270</td>
<td>725</td>
</tr>
</tbody>
</table>

Plans call for the $67,000 that would be raised by the sale of all 120 co-op shares to capitalize a reserve fund.

Despite the fact that the co-op has not yet closed, an interim board of directors has been elected and all necessary co-op documents have been prepared. These include subscription and occupancy agreements, articles of incorporation, which have been approved by the Department of Licensing and Consumer Affairs, and bylaws, which were approved at a meeting of 30 tenants.

The co-op's president, a wheelchair-bound woman who has lived in Pearson Gardens for many years, is a tremendously active, energetic, and aggressive leader who refuses to let the conversion fail. Despite Dorothy Lafong's heroic efforts, as of mid-August 1989, the Virgin Islands Housing Authority still had not approved Pearson Gardens' conversion plan. In an interview with the chief executive officer of VIHA, we were told that legal papers necessary to affect the transfer were still under preparation and that such complicated dealings cannot be rushed. These are very discouraging words to a group of dedicated tenants who have been working on the conversion for more than four years.

Rather than the complexity of the project, co-op leaders and their advisors believe that VIHA is dragging its feet for political reasons. Under a reorganization of the island's government, the director of the housing authority no longer reports to the board of commissioners. Instead, he is appointed by and reports to the governor and, in addition to his duties as head of the housing authority, he is also commissioner of housing for the Virgin Islands, head of the Virgin Islands Housing Finance Agency, and has other official responsibilities that make the Pearson Gardens conversion less important in the overall scheme of VI housing issues. During one period in 1988, for example, VIHA's board of directors did not meet for a period of more than six months because of differences with the CEO. This unofficial hiatus was caused when the CEO let a number of procurements without consulting the board of commissioners. During this period, too, the housing authority failed to deal with a number of critical issues regarding the conversion.

Another reason the co-op leaders believe the housing authority is dragging its feet is the possible impact on VIHA of losing HUD operating subsidies once the transfer takes place.
Financing

Although the original proposal called for VIHA to finance the sale, the housing authority ultimately decided to contribute the property to the co-op. Although buyers must make downpayments equivalent to five percent of the appraised value of their unit, the co-op will carry no permanent financing.

Counseling

All counseling is being handled by the consultant. His contract called for the delivery of the following services:

1. Conduct feasibility analysis including property appraisal, assessing tenant's interest in ownership and ability to pay, and occupancy conditions;

2. Advise and train tenants on organizing and establishing a cooperative;

3. Provide training in maintenance, resident controls, and budgeting;

4. Secure financial arrangements and provide tenant purchasers with advice on financing;

5. Provide homeownership counseling and training programs; and

6. Determine tenant's long term eligibility, financial needs, and responsibilities.

As of August 1989, the consultant had completed tasks 1, 2, and 4. The bulk of his time has been devoted to explaining the co-op form of ownership to tenants, conducting surveys to assess tenant interest in joining the co-op, developing proposals for outside funding, and pressuring the housing authority to move ahead with the conversion.

The consultant was paid $15,000 for technical assistance and counseling services, which the housing authority paid from the proceeds of a $26,000 TA grant received from HUD. The consultant's contract expired in June 1988, and despite continual pleas to the housing authority by co-op leaders to extend his contract, VIHA has not yet done so. Nevertheless, for more than 15 months, the consultant has continued to work without compensation to help make the home ownership demonstration a success. This is yet another indication of the housing authority's apparent lack of commitment to the Pearson Gardens conversion.

According to the initial PHHHD proposal, future plans call for both board and member training. In fact, $5,000 of the original TA contract was retained by the PHA for such a purpose. However,
the housing authority's CEO indicated that post-closing training of the co-op board would depend upon the future availability of funds, which implies that VIHA did not set aside the $5,000 in TA money for co-op training as it implied it would.

No formal plans have been developed for managing the co-op after closing. The housing authority will probably provide management on an interim basis until the co-op makes its own management plans.

Windfalls Profits and Retention Provisions

The transfer of units to a limited equity co-op is designed to guard against windfall profits. The proposed bylaws give the board of directors the power to establish the sales prices of membership shares. The specifics of equity sharing have not been detailed, however. The board has been discussing either placing a cap on the cooperators' equity in the range of two or three percent per year or, because the VIHA is giving the units to the co-op, allowing no equity appreciation at all. The board of directors will also have the right to authorize transfer of membership which will allow them to select new members. These provisions are to be in force for the life of the project.

Provision for Maintenance After Sale

The major provision for maintenance after sale is a cooperative fund that will be capitalized from $67,000 on resident down payments. The VIHA also expects to continue providing certain maintenance services to the co-op for the first year or two until it is ready to assume complete responsibility. They may also keep the co-op's books for the first year or until the responsible parties can be bonded. The consultant tried to get the VIHA to guarantee the appliances for the first five years but it would not agree to do this.

Handling Non-Participants

At first, neither the consultant nor the VIHA project manager felt that relocation would be an issue in the conversion. The original intention was to offer those who could not or did not wish to join the co-op several options. First, non-buyers who wished to, would be moved to the non-co-op half of the Pearson Gardens development which remains part of the public housing inventory. Voluntary relocation to other public housing developments would be another possibility, although low vacancy rates in habitable projects make this a low priority alternative. Finally, if the number of non-buyers who wished to remain in the co-op half of Pearson Gardens was small enough, VIHA could lease a sufficient number of units from the co-op to permit these residents to stay.

In reality, the relocation problem has turned out to be one of the major barriers to converting Pearson Gardens. A substantial
number of residents in the co-op half of Pearson Gardens do not want to join the co-op and would willingly move to the non-co-op half of the project. Similarly, a sizable number of residents in the non-co-op half of the project would like to buy into the co-op.

So, conceptually, a substantial portion of the problem could be solved through a simple exchange of units, with non-buyers trading apartments with renters who want to move into the co-op and buy a unit. There are three problems with this scenario, however. First, the size of the two groups is not equal. There are 30-35 families in the co-op portion of the project who do not want to join the co-op and just 24 families in the non-co-op side that want to buy a unit. Second, these respective groups' space needs are not the same so that a simple exchange will not work. Moreover, before even a partial exchange can take place, apartments need to be painted and prepared for their new occupants. Co-op members have volunteered to paint the apartments in the non-co-op part of the project rather than wait for the housing authority to do it if this would speed up the process. Thus far, VIHA has taken the position that full apartment inspections must be done and all necessary repairs completed before any voluntary transfers would be permitted to take place. Since both manpower and resources to complete the repairs are in short supply, this could take some time.

Finally and most importantly, throughout this very difficult period, VIHA has continued to fill vacancies in the co-op portion of Pearson Gardens that occur through normal turnover with new renter families taken from the St. Thomas public housing waiting list. Rather than saving these units for families in the non-co-op portion of Pearson Gardens who wish to join the co-op, VIHA is renting them to new public housing tenants without regard to their ultimate interest in homeownership. Letters from the co-op sponsors to VIHA urging the authority to cease such actions have, thus far, gone unheeded. According to VIHA, there are too few available public housing vacancies to withhold apartments from the market when the demand for low rent housing is so great.

In sum, as of September 1989, there was no plan for the relocation of non-buying tenants in Pearson Gardens, and no prospect that this problem would be satisfactorily resolved in the near future.

Amount and Use of Sales Income

As indicated earlier, the $67,000 raised from down payments or initial equity contributions will be used to capitalize the co-op's reserve fund. Since the project will be transferred to the co-op at no cost, there will be no blanket mortgage and no additional sales proceeds generated by the conversion.
Impact of the Sales Program

Because Pearson Gardens has not yet closed, the conversion has had no impact on housing authority finances or operations. Indeed, to the extent that VIHA continues to fill vacancies in the co-op half of the project with rental families from the authority's waiting list, it appears that little effort is being made to facilitate the conversion. If and when the co-op does close, however, housing authority operations could be affected by virtue of the division of Pearson Gardens into ownership and rental segments that share the same physical site. Up to now, on-site management of Pearson Gardens has not been outstanding. Unless the quality of management in the rental part of the project is brought up to the higher level that the co-op leaders have planned for their community, friction and divisions can undermine the project's success and cause difficulties for VIHA.

Conclusions

The bright spot in St. Thomas is the dedicated group of individuals associated with the conversion who are committed to seeing the Pearson Gardens Co-op close. The co-op's president is an inspiration to all who work with her; their consultant continues to work on a pro bono basis because he wants to complete what he started; the legal services attorney works unceasingly on the co-op's behalf. If dedication and belief in a project is sufficient to make it happen and succeed, then Pearson Gardens will eventually work.

More realistically, however, the project faces enormous obstacles. Should the relocation problem eventually be solved and the necessary site improvements be made so that the co-op can create its own physical community, it will still face significant financial and social challenges. With respect to the former, the co-op continues to work with financial estimates that were prepared four years ago. The very low level of resident incomes in Pearson Gardens means that the co-op's budget will have to be kept to a minimum, and the planned reserves will not go very far to fill a budget gap. Moreover, although the general condition of the buildings is good, a walk-through of the site reveals the need for some renovation work that has not been programmed by the housing authority. Should Pearson Gardens go to closing in the coming months, it will face some very rough seas before the sailing gets much smoother.
Introduction

Wylie Courts, a 28 unit townhouse development in the Capitol Hill area of Washington, DC, is the only multifamily PHHD site to sell units as condominiums. It is also just one of three multi-family sites to have gone to closing during the demonstration period. As of September 1989, 23 units had been sold to residents while the five unsold units remained part of the District of Columbia's public housing inventory. As with most other sites, unit prices were set at the appraised value and then discounted for affordability, with the housing authority taking back a silent-second mortgage for the difference between the size of the first mortgage that the buyer could carry and the fair market value of the unit. Despite an average buyer income of close to $20,000, the average second mortgage still exceeds $40,000 because the appraised values of Wylie Courts' units average more than $60,000.

The Wylie Courts condominiums have been in occupancy for more than two years and an elected board of directors which oversees the homeowners association's activities, including setting condominium fees and management policies, is now in place. A committee of the association also screens public housing tenants who indicate an interest in buying one of the remaining units.

Managing the Demonstration

The PHHD application was written by a homeownership specialist at DHCD who subsequently became the program director. According to the director, the program's goal is to make ownership feasible for those who cannot qualify for ownership in the conventional market. She believes that homeownership will break the cycle of dependency of long term public housing residents and allow families to stand on their own two feet.

The director of DHCD initiated the idea for the program. The PHHD was seen as a way of selling two Turnkey III projects that the PHA never sold. Residents of Wylie Courts were used as a sounding board to hear and to react to the PHA's ideas, but were not really involved in the preparation of the proposal. In addition to the homeownership specialist, the only other DCHD employee involved in designing the program was an assistant corporation counsel who drew up the condominium papers.

Until the PHHD, the PHA had never sold any public housing under Section 5(h). The homeownership specialist and other DHCD staff are very concerned about the permanent loss of housing units involved in the PHHD. Her desire is to use what is learned from
the Wylie Courts conversion to design a program involving the non-public housing stock.

Other actors involved in the demonstration are MUSCLE, a local non-profit organization skilled in counseling. They conducted a 23 week, 46-hour training session for Wylie Courts residents. Also, Mutual Housing Association, another local non-profit housing organization, is under contract to manage the Wylie Courts Condominium. The PHA received a $50,000 technical assistance grant from HUD which was used to pay for training and which will be used to pay the cost of legal and accounting services to the condo association for the first two years of its existence.

When it began, the PHHD was administered by the Washington Capital Housing Authority, which was part of the Department of Housing and Community Development (DHCD). The housing authority side of DHCD administers approximately 12,000 public housing units and more than 4,100 Section 8 new construction and substantial rehab units, rental certificates, and housing vouchers. The housing authority oversees a waiting list with approximately 13,000 applicants. The waiting list has been closed for some time so it is not a true indication of the tremendous demand for low-income housing in Washington, D.C. The D.C. government administers a variety of housing assistance programs that complement public housing, including homeownership financing and a locally financed housing voucher program.

Within the last two years, there has been a major change in DHCD which, in turn, has affected the management of the public housing homeownership demonstration. The combined housing and community development functions of DHCD have been separated, with the housing functions moving to a new department of public and assisted housing. The PHHD, however, was not moved to this new department, partly because the renovation of Wylie Courts was financed with Community Development Block Grant funds and, so, for budgetary purposes, was treated as a community development project.

There are two important implications of the reorganization of DHCD. First, the PHHD has lower priority with the new director than it had with his predecessor. In the beginning, the PHHD was assigned a full-time director and one other full-time staff person. Now the PHHD director is half-time on the program with no other staff assigned. While a phase-down of staff time dedicated to a public housing sales program is to be expected once all the units have been sold, the cut-back in Washington, D.C. occurred before the issue of continuing renters had been resolved, and prior to the time that all the units had been sold. One result of the scaled down personnel commitment to the PHHD was that more recent buyers have received less up-front training and homeownership preparation than the earlier buyers. In partial response to this change in local policy, the board of
directors of Wylie Courts has hired its own trainer who held the first training session in August 1988.

The reorganization of DHCD has also caused problems with plans for capitalizing an account to cover extraordinary maintenance expenses for the project. Originally, the housing authority promised to provide the condominium association with $30,000 for this reserve fund which would come from net sales proceeds. However, the new director of DHCD, who now has no public housing responsibilities, decided to use all available sales proceeds, including mortgage payments from the buyers, to reimburse the CDBG fund for the costs of renovating Wylie Courts. Thus, no funds have been made available to capitalize the condominium association's maintenance reserve account or, for that matter, to pay the association the monthly condo fees for the four unsold units that the PHA still owns. These latter delinquencies totaled between $3,000-$4,000 as of August 31, 1988.

Selecting and Rehabilitating Properties

DHCD's application to HUD originally proposed that two projects be converted to condominium ownership under the PHHD: Wylie Courts and Frontier. Both projects were built initially for homeownership under the Turnkey III program, but the PHA never administered these projects under the Turnkey III regulations, which included setting up tenant equity accounts and establishing homeowner associations. Wylie Courts has been converted under the PHHD, while HUD has not yet granted approval for the sale of Frontier. Whereas, Wylie, built in 1980, needed only modest renovations and required no relocation, Frontier needs extensive modernization which requires that all units be temporarily vacated. HUD modernization funds are available for the renovations, but without additional PHA staff assigned to the PHHD program, Frontier is not likely to be converted anytime soon.

Not only does the townhouse-style and high quality of construction make Wylie Courts so special, but it also consists of large units. More than half the units (16) contain four or five bedrooms, while the remaining apartments (12) each have three bedrooms. Their size and quality are also reflected in relatively high appraised values, which averaged nearly $65,000 a unit in 1986. Continued market recovery in the Capitol Hill area would likely cause Wylie Courts' property values to increase substantially.

As of September 1989, all 28 units had been rehabilitated and made ready for sale. Of the total, 23 units had been through final closing. The five unsold units, two of which were occupied and three of which were vacant, remain under Annual Contribution Contract as part of the District of Columbia's public housing inventory.
Since Wylie Courts is only seven years old, it was in excellent condition prior to sale. DHCD assessed the minor repairs that were needed, which consisted of painting, upgrading heating systems in the largest units, repairing some floors, and replacing refrigerators and ranges. Parking lots were also resurfaced and exterior lights were installed in parking lots and courtyards. No relocation was required during renovations. Repairs were paid for with CDBG funds.

Wylie Courts is located in a rapidly gentrifying Capitol Hill neighborhood having generally low vacancy rates, scattered boarded up units and a high percentage (60 percent) of poor people. The PHA estimates the neighborhood to be somewhat more renter than owner-occupied. On the whole, housing conditions are fair and much public/private reinvestment is taking place in the neighborhood.

Attracting and Selecting Owners

Eligibility criteria vary depending upon whether the buyer is a resident of Wylie Courts, who has first priority, or is a tenant from other projects. The criteria for Wylie Courts residents are:

1. Ability to support costs of ownership (taxes, insurance, utilities, condo fees, and some first mortgage);

2. Attendance at homeownership training sessions;

3. Good rent payment record; and

4. No outstanding lease violations.

The criteria for non-Wylie Courts residents are as follows:

1. Public housing residency for at least one year;

2. Current in rent payments and no delinquency in past 12 months;

3. No lease violations for last two years;

4. Employed or have steady income from disability, social security, etc.;

5. Income sufficient to support ownership;

6. Good housekeeping record;

7. No antisocial behavior; and

8. Acceptable credit history.
Little marketing outside of Wylie Courts was necessary. A resident advisory committee of Wylie Courts buyers was set up to screen outside potential buyers. PHA staff screened outsiders for financial eligibility and the resident advisory committee made final selections.

The PHA backed into the income needed to participate. It was initially set at $18,000 but a few buyers do have lower incomes than this. The average income of Wylie Courts buyers is approximately $23,000 a year.

**Property Conveyance**

Wylie Courts conversion was structured as a condominium rather than as a co-op because tenants wanted to own their units without having to worry about whether their neighbors will keep up payments on their mortgages. Families didn't want the failure of one to become the failure of all.

Sales prices were set at their appraised value:

- 3 bedrooms $60,000
- 4 bedrooms $65,000
- 5 bedrooms $72,000

Buyers were required to make a five percent down payment, although grants for this purpose were provided by the D.C. government's Housing Payments Assistance Program (H-PAP). The housing authority decided to make down payment grants to buyers because Wylie Courts was originally built as a Turnkey III sweat equity homeownership project in which part of the tenants' rent was supposed to be deposited by the PHA into individual equity accounts that would compensate families for taking on some of the routine maintenance responsibilities associated with their housing. In fact, the PHA had never opened equity accounts for the tenants. Providing down payment grants made up for this failure by the PHA.

Closing costs are being financed by a loan from a DC housing program and secured in the mortgage. Closing costs average around five percent of the sales price.

There are two legal documents that pertain to the governance of Wylie Courts: one, the Declaration of Condominium Ownership and the other, bylaws of the condominium.

The Declaration of Condominium Ownership is the legal document that creates the condominium under District of Columbia law. Each unit owner of the condominium has exclusive fee simple ownership of his unit and an individual fee simple interest in the common elements of the property based upon the par value assigned to his unit. Par value varies with the number of bedrooms or size of the unit: 3 BR $1,029 (3.12 percent); 4 BR $1,190 (3.61 percent); 5 BR $1,455 (4.41 percent). Par value is
not related to market value. The declaration establishes that
the condominium will be administered by an owners' association in
accordance with this declaration and bylaws of the association.
Initial bylaws were promulgated by the PHA and can be changed by
the association as provided under the bylaws.

The bylaws provide for a six person board of directors to be
elected by members of the association. Each unit owner is by
definition a member of the association and each member's vote is
equal to the total of the individual interest percentage of
ownership of the common elements. The bylaws provide that the
board of directors shall elect officers of the association,
going a president, vice president, secretary and treasurer.
The president and vice president must be members of the board.

Until such time as the PHA had sold units aggregating 25 percent
of the value of all units, the PHA exercised all powers, rights,
duties and functions of the board of directors. When 25 percent
of value was conveyed, the PHA called the initial meeting of the
association and a board was selected. Four directors were
appointed by the PHA and two were elected by majority vote of
association members other than the PHA. The PHA retained 4-2
control over the board until 75 percent of the value of all units
had been sold to residents. At that point, buyers assumed
majority control over association activities. The condominium's
bylaws provided for PHA control over the board to last for no
more than two years after the first unit was sold, regardless of
the 75 percent threshold. This provision would have prevented
the PHA from dominating condominium policies and practices for an
indeterminate time in the event that sales moved more slowly than
anticipated. The two-year rule is a good one because unit owners
began to resent the PHA's continued control of the board once
sales had reached more than 50 percent, but had not yet gone over
the 75 percent of value threshold.

The board of directors has the power to adopt rules and
regulations, including those pertaining to the amount and payment
of dues, use of common areas and facilities, the conduct of the
members and their guests in those facilities, and the penalties
for violating such rules and regulations. The required duties of
the board include keeping an official record of all actions of
the association, having an independent audit of the association's
financial records completed each year, and causing such officers
or employees of the association having fiscal responsibilities to
be bonded.

The bylaws require the board to create three committees: a
representation committee, a rules committee, and a nominating
committee. Other committees can be formed at the board's
discretion.

Bylaws also provide that unpaid assessments shall become a lien
on the unit and accrue interest at the lesser of 10 percent per
year or the maximum first mortgage interest rate permitted to be
charged in Washington, DC. Assessments for the coming year must be set on or before December 1 of each year.

If a member is in default for 30 days, the board may bring suit to enforce collection. Costs of legal fees and interest are added to assessments due.

Bylaws also provide that the board shall build up and maintain a reasonable reserve for contingencies and replacements without defining its level. The board can charge members additional assessments if emergency needs cannot be met out of the reserve. Bylaws may be changed by a vote of 75 percent of the value of all units.

Financing

The PHA financed all sales at Wylie Courts. While the director indicated that she had extensive discussion with private lenders, the most any one lender would carry (we are speaking here of bankable loans) was one or two loans. She said as a one woman show with no other staff help, she could not deal with private lenders on such a small scale. She said that the mayor would have "to twist some arms" and show that the PHHD was a high priority program before the private lending community would respond with volume commitments. She indicated that even though the PHA is the mortgagee, down payment grants and closing costs are being paid with H-PAP funds so that the housing authority as mortgagee has to make no financial outlays.

Of the 23 sales closed, the PHHD director thinks that just a handful have been bankable. This means that even with private participation there still would need to be a public partner in the financing of Wylie Courts condominiums.

The first mortgage is based on affordability defined as 35 percent of gross monthly income less taxes, insurance, condominium fee and estimated utility costs. The amount left is applied to the first mortgage payment. First mortgages can be for a term of either 15 or 30 years. All first mortgages are at 9.5 percent interest. How the housing authority backs into the minimum first mortgage that a potential buyer can afford to carry is illustrated below for a 30 year loan:

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Gross monthly income</td>
<td>$2,071</td>
</tr>
<tr>
<td>35% of gross monthly income</td>
<td>+%725</td>
</tr>
<tr>
<td>Estimated monthly taxes &amp; insurance</td>
<td>- 102</td>
</tr>
<tr>
<td>Condominium fee</td>
<td>- 100</td>
</tr>
<tr>
<td>Estimated monthly utility costs</td>
<td>- 191</td>
</tr>
<tr>
<td>Amount of income available for principal and interest</td>
<td>$332</td>
</tr>
</tbody>
</table>
$332 can carry a $39,600 30 year first mortgage at 9.5 percent.

The difference between the sales price (net of down payment) and first mortgage amount is secured by a silent-second mortgage held by the PHA. This second mortgage is written at zero percent interest. Settlement costs are paid by the city and secured by a third deed of trust, also held by the city. Along with the first, both the second and third mortgages must be paid off at time of resale. If, however, the PHA buys back the unit to keep it affordable to low-income families, the second mortgage can stay in place. However, regardless of who acquires the unit on resale, the third mortgage, which secured the housing authority's settlement cost advances, must be paid off.

Settlement costs averaged $2,257 a unit. Settlement costs included the costs of credit reports, title examination and insurance, recording and transfer taxes and three prepaid items. The prepaids included two months property taxes and hazard insurance, and two months condominium fees.

Based on affordability, the average buyer qualified for a $17,279 first mortgage, with the housing authority taking back an average deferred payment second mortgage of $44,220.

Settlement takes place at DHCD. All papers, including buyer's down payment grant are sent to a title company for recording. A check is deposited in a district account to the credit of PHA. Mortgages are serviced by a commercial S&L. Monthly mortgage payments are made to the S&L, which issues a payment book to buyers just as it would if the mortgage were from a commercial lender. The S&L issues monthly reports to PHA on the status of each loan and follows up on late payments just as it would on a loan of its own origination. The difference is that PHA enters the picture on late payments to see what the problem is and how it can be resolved. Thus far just a few buyers have been late with payments to any significant degree. One delinquency resulted from a family problem, one from a car repossession problem and the third, the most frivolous, was because the buyer needed the money to attend a family reunion.

Counseling

The PHHD program director distinguished between counseling, which is one-on-one hand-holding, and training, which is formal training in a group setting. The director did all of the counseling, which took place from the program's inception through sales closing. Most counseling involved straightening out credit problems, including taking care of outstanding judgments. Also, several of the single parent buyers did not have formal separations from spouses. PHHD director helped them legalize their separations to protect their new asset, their home.
Formal training was carried out by a local non-profit training and counseling organization named MUSCLE under a $9,000 contract. The training took place in group settings for two hours a week for 23 weeks. The curriculum was divided into three phases: pre-purchase, purchase, and post-purchase. The pre-purchase phase included sessions on responsibilities of homeownership (two sessions); costs associated with homeownership (two sessions); group decisionmaking (three sessions); communications systems (one session); property management (two sessions); resident-performed home maintenance (two sessions). The purchase phase included one hour-long session and 28 half-hour sessions on the settlement process. The post-purchase phase included sessions on the board of director's fiduciary responsibilities (one session); committee structure (one session); financial planning and financial security (one session); membership development (one session); wrap up session (one session).

As well attended as the counseling sessions were (24 or so attended each week) two leaders of the Wylie Courts Board of Directors indicated that the sessions were superficial, not very informative, and that they are in urgent need of additional training in how to organize and run a condominium. One of the board members wanted HUD to finance a series of visits for Wylie Courts Board members to other tenant-owned or managed housing projects. This high degree of insecurity among board members was common across the other multifamily sites visited (e.g. Paterson, Denver). MUSCLE's counseling contract was paid out of the PHA's $50,000 technical assistance grant from HUD. In addition to the cost of training, the technical assistance grant will cover the first two years of the condominium's attorney and accountant's fees.

Windfall Profits and Retention Provisions

DHCD adopted a complicated set of recapture and equity sharing arrangements that are designed to discourage the resale of Wylie Courts condominiums for at least seven years and to reduce the possibility of windfall profits to the initial owner. The resale restrictions have three components. First, the purchaser must agree to occupy and not sell the property for seven years, or be subject to severe penalty for early resale. The penalty would impose interest on the deferred payment second mortgage at a rate equal to the lesser of the interest rate on the buyer's first mortgage or the maximum legal interest rate that could be charged under the District's usury laws. The interest would be charged from the date of settlement up to the date of sale. Thus, a premature sale would trigger the full recapture of the original principal of the second mortgage loan, plus accrued interest.

Second, DHCD retains the right to purchase any resale of a Wylie Courts condominium, with the price determined by an appraisal obtained by DHCD. In the event that the buyer disputes the appraisal, he/she may secure a second appraisal from a competent professional and DHCD's purchase price would be determined by
averaging the two appraisals. In the event of a DHCD purchase, the low income character of the condominium would be preserved by rolling over the silent second mortgage and, perhaps, adding to it.

Third, the DHCD resale policies guard against windfall profits by requiring sellers to share their net equity with the housing authority. If the initial buyer sells at the end of seven years, he/she must repay the full principal of the deferred payment second mortgage at zero interest, as well as fifty percent of net appreciation. The District's share of net appreciation declines by seven percentage points with each year beyond seven years that the original owner resides in the property.

Provision for Maintenance After Sale

As indicated earlier, the PHA promised to provide the condominium association with a $30,000 maintenance reserve when it was formed. It has yet to make good on that commitment. The PHA is monitoring the operations of the condominium association to the extent that staff resources allow and has assisted with minor maintenance on an as-needed basis. Plans are to withdraw this support after two years of.

When the PHA had control over the board of directors, the board executed a management contract with the district-wide Mutual Housing Association (MHA) to manage the condominium. Although the homeowners are now in control, the board decided to keep MHA as its management agent. The MHA charges a flat management fee of $15 a month per unit. Among the manager's responsibilities are maintenance of the condo's common grounds, maintenance of the exterior of the units, collection of the maintenance condo fee, and generation of various financial reports.

The MHA's fee is paid from the condo fees which are $100 per unit per month. These fees also include pick-up of trash (since DC law provides that city trucks pick-up for private multi-family structures only where there are four units or less), legal and accounting fees, equipment and supplies, liability insurance, and a replacement reserve.

The PHA also warranted major building systems for two years after completion of all renovations, and has had to make some repairs under its warranty program. Two air conditioner compressors have been replaced in five-bedroom units for failure to cool the third floor level. Moreover, other owners of five-bedroom units have expressed dissatisfaction with the heating systems and these systems have been improved. Some concern has been expressed by residents over the vague language of the warranty offered new owners.
Handling Non-participants

There will be very few nonparticipants in Wylie Courts. At the time of our site visit, we were told that, perhaps, two residents would not be acquiring their units. The PHA was considering selling the units occupied by the non-participants at a very low price and giving the tenants vouchers to pay their rent. Condo association officials want the PHA to relocate these non-participants prior to the condo board taking control of the project. This issue has yet to be resolved.

Amount and Use of Sales Income

Because the PHA financed the sales, there are no substantial net sales proceeds. The only dollars coming to the PHA at time of sale was the five percent down payment, and even this was an intergovernmental transfer. The DHCD will receive first mortgage payments from the buyers, a portion of which was to be used to capitalize the association's maintenance reserve. As reported earlier, an agency reorganization and change in administrators resulted in a decision to recapture all sales proceeds for use in the District's community development programs. Thus, no sales proceeds have been made available to the association.

Impact of the Sales Program

Because of its small size, the sale of Wylie Courts will have little impact on the financial or management condition of the District's housing authority. In fact, because Wylie Courts is a Turnkey III development that was initially developed for sale to public housing residents, one could argue that its conversion is long overdue and potential impact on the housing authority is not a relevant issue.

Conclusions

Wylie Courts was built in 1980 under the Turnkey III program. Because it was originally built for the purpose of extending homeownership opportunities to public housing families, the replacement housing issue is less sensitive in the District of Columbia than in some other programs. The excellent quality of the project, its Capitol Hill location, and the sales prices being set at their appraised values, means that Washington has the highest priced units in the PHHD. With home buyers' incomes averaging $20,000 a year, Wylie Courts buyers are also among the highest income buyers in any of the ownership demonstrations.

Potential buyers also participated in the most formal classroom training program of any other PHHD program. The training program involved 23 weekly two-hour meetings on a wide range of homeownership and condominium issues.

Finally, while relocation was not a major issue at the time of our site visit, the subject did come up in reference to buying
the units. At one point, the PHA contemplated selling the two units occupied by the non-buyers to the Homeowners Association at a very low price, which would then rent the units to the families. The PHA would provide the families with either vouchers or Section 8 certificates to enable them to afford the units. In contrast, members of the board of directors did not want the units in question to remain as rentals. They preferred that the PHA relocate the two families out of Wylie Courts and make their units available to other qualified public housing tenant buyers. At this time, the unsold units continue to be rented by tenants of the housing authority with little or no adverse impacts on either the operations or activities of the condominium association.
PUBLIC HOUSING HOMEOWNERSHIP DEMONSTRATION

WICHITA CASE STUDY*

Introduction

The demonstration program in Wichita, Kan. was originally designed to sell 50 scattered-site, single-family units to tenants whose incomes were $10,000 or more. The sale price was to be based on the appraised value of the unit, discounted for affordability. A silent-second mortgage was to be used to cover the difference between the appraised value and the amount of the first mortgage. Private lenders were to provide financing. As of July 1989, however, no program had been implemented.

The program encountered several problems that impeded its implementation. First, according to program staff, Wichita Housing Authority intended to sell the worst units in its stock, 51 units to the highest bidder, in order to obtain funds for program implementation. Part of these sale proceeds were to be deposited with lending institutions to induce lenders to lower the mortgage rate to be charged to program buyers. The rest of the proceeds of this separate disposition were to be used to rehabilitate the units to be sold under the demonstration. Second, the agency proposed the use a "sweat equity" mechanism to assist in the rehabilitation of the PHHD units to be sold. Neither of these two components of the Wichita application were approved by HUD. Lacking the necessary funding for rehabilitation, the city could not make the units ready for transfer. Moreover, the city could not interest financial institutions in providing financing for prospective program participants. Also contributing to the demise of the program was a turnover in the city administration that resulted in the decision to terminate Wichita's participation in the demonstration.

* Because the Demonstration was never actually implemented, much of the information presented here is derived from four documents currently on file: (1) WHA's initial application for participation in the PHHD project (January 11, 1985), (2) HUD's review of the WHA application, (3) HUD Regional Office's comments on Kansas' PHHD application (March 1, 1985), and (4) HUD's memorandum selecting Wichita for participation in the pilot project (March 20, 1986). Additional information was provided by Miss Pat Miller, Wichita Dept. of Housing and Economic Development, and Mr. Steve Isrealite, HUD Regional VII Office (personal communication, 8/25/89 and 8/29/89 respectively).
Managing the Demonstration

The demonstration in Wichita was to be managed by the Wichita Housing Authority (WHA). Except for its projects for the elderly, the agency's stock consists of single-family, scattered-site units exclusively. As of December 1984, the Agency administered 515 Section 8 existing units, 22 units under the Rental Rehabilitation Demonstration program, and 27 units under the Rental Rehabilitation Entitlement program. As of January 1985, there were 300 families on the WHA's waiting list.

WHA's application identified five program goals. First, the demonstration was seen as a mechanism to provide low-income families with the opportunity to become homeowners. Second, the program was seen as a way for the agency to gain experience in administering a homeownership program. Third, the demonstration sought to reduce the number of vacant units through the sale of some of the larger-size units for which demand had declined. Fourth, program participants were expected to feel a homeownership pride that would result in better maintenance and up-keep practices and a general upgrading of the residential areas in which these units were located. Finally, since the targeted units were scattered, single-family sites, the program was seen as an opportunity to lower total operating and maintenance costs inherent in the scattered-site program.

The WHA was responsible for preparing the city's proposal. There was extensive tenant and citizen involvement during the initial stages of the program. A survey was sent to all WHA tenants regarding their interest in a homeownership program, which also requested program content suggestions. Several public meetings were scheduled with the commissioners of WHA's board of housing to discuss and define specific program characteristics. The WHA kept tenants and other interested parties informed through the WHA newsletter. The newsletter provided periodic program development status information. In January 1985, there was high tenant enthusiasm and support for the demonstration.

In its application, Wichita identified three major groups as having significant roles in program implementation. WHA was to have overall responsibility. The Wichita Urban League was proposed as the agent to provide purchasers with appropriate counseling and training in the responsibilities of homeownership. Private lending institutions were to be the main source of mortgage financing. As such, the private lenders were expected to have an active role in determining tenant loan eligibility. WHA did not request a HUD grant to cover program management support activities. The city of Wichita pledged Community Development Block Grant funds to the project. No specific amount, however, was identified.

After approval, the program encountered several problems that contributed to its demise. First, according to WHA staff, the agency originally intended to sell the worst units in its stock
to the highest bidder in order to obtain funds for program implementation. Part of these sale proceeds were to be deposited with lending institutions to induce lenders to lower the mortgage rate to be charged to program buyers. The other part of the proceeds from the this sell-off were to be used to rehabilitate the units to be sold under the demonstration. Second, the agency had proposed the use a "sweat equity" mechanism to assist in the rehabilitation of the PHHD units to be sold. The HUD Regional office objected to these two components of the Wichita proposal, i.e., the sale of units to the highest bidder and the use of a "sweat equity mechanism." HUD's final authorization for participation did not include these two components in the approved program design. Lacking the necessary funding to rehabilitate PHHD units, the city could not make them ready for transfer.

Given the poor condition of the units to be sold under the demonstration, and the lack of a mechanism to lower program interest rates, the WHA was unable to interest private financial institutions in providing financing for prospective program participants.

According to HUD Regional staff, a change in city officials also contributed to the demise of the program. After taking office, the new city commissioners and city manager re-evaluated the WHA application, and Wichita's participation in the demonstration, and decided against it.

Selecting and Rehabilitating Properties

HUD authorized the sale of 50 single-family, scattered-site units in the Wichita demonstration. The properties to be sold were located in two scattered-site projects, one in the Northeast quadrant (37 units), the other scattered in the Southwest quadrant of the city (13 units). As of January 1986, Wichita was in the process of completing a physical need assessment of all WHA units. This assessment was undertaken by a professional architectural/engineering firm. Within the two identified projects, only those units which met housing codes were going to be eligible for homeownership.

A central component of the WHA application was the Owners Provided Repair (OPR) arrangement. Under this arrangement, the tenants would have undertaken the necessary cosmetic repairs to their units with WHA provided materials. Major repairs would be handled by the WHA, and their cost added to the final purchase price, up to an additional 10 percent. The HUD Regional office objected to OPRs arguing that the "sweat equity" arrangement was generally unworkable because: (1) the quality of repairs was dependent upon the qualifications of the tenant in question, (2) no checks and balances were provided to assess whether the materials furnished by the WHA were in fact used for repairs, (3) the WHA did not have any recourse if the repair work was unsatisfactory, and (4) the cost of repairs was going to affect
directly the affordability of the homes. HUD did not approve the OPR component of the application.

In its authorization for WHA participation, HUD only approved the sale of units in good condition. Unfortunately, many of the units chosen for participation were in such poor condition that, as far as the WHA was concerned, it was not feasible to rehabilitate them. The units selected for the demonstration were given finally to Habitat for Humanity so that they could rehabilitate them and sell them to low-income families.

The potential units to be targeted for participation in the two scattered-site projects were located in single-family, minority areas, in neighborhoods generally considered good.

Attracting and Selecting Owners

The 1984 WHA Survey identified about 230 tenants who appeared to meet program eligibility. A second survey in December of 1985 indicated that 190 out of the 209 tenants who responded were interested in purchasing their home under the program. In addition, based on the number of calls to city hall each time the program received media notices, the WHA considered that a large untapped pool of income eligible potential purchasers existed. The following factors were to be considered in determining tenant eligibility: (1) residency in public housing, (2) motivation to become a homeowner, and (3) a credit history acceptable for private financing. A minimum income of $10,000 was necessary.

The city's Department of Housing and Economic Development was to be responsible for the initial screening of interested tenants living in targeted units. This initial screening was to determine income adequacy, rent payment history, and housekeeping practices. Those tenants found eligible were to be referred to private lenders. Private lenders were expected to decide ultimately on the loan eligibility of potential buyers. Vacant units targeted for sale were to be offered to eligible tenants who indicated a desire to purchase a home. Tenants desiring to purchase a unit, but ineligible at the initiation of the project, were to be offered training and counseling sessions to improve their standing.

Property Conveyance

Housing units were to be sold fee simple. In WHA's initial application, the proposed sale price was based on the appraised value of each unit as identified in the physical needs assessment. It was estimated that the appraised value of potential units ranged from $18,000 for a four-bedroom home to $45,000 for a six-bedroom unit. First mortgages were expected to range from $18,200 (four-bedroom unit) to $25,000 (six-bedroom unit). The effective price paid by program participants was to depend upon tenants' incomes (30 to 35 percent of the purchaser's gross income had to cover all major housing costs). WHA was to
assume a silent-second mortgage covering the difference between the appraised value and the amount of the first mortgage.

Financing

Private mortgage financing was proposed for program sales. As of March 1986, a typical sale was expected to consist of a downpayment equal to 10 percent of the sale price, with no less than a $500 cash payment, with the balance in "Owner Provided Repairs (OPR)" to bring units into compliance with city housing codes. Primary financing was to consist of a 30 year, nine percent (or less) mortgage.

Counseling

The WHA was to provide counseling to tenants regarding their rights to participate or not to participate in the demonstration. After this initial counseling, the Wichita Urban League then would be responsible for providing the appropriate tenant counseling and training in the responsibilities of homeownership. In addition, the Legal Aid Society of Wichita was to provide legal and financial counseling, while WHA maintenance staff would have given maintenance training.

The counseling was to be completed prior to loan closing. If problems arose later, e.g., repeated late payments or non-payments, additional counseling was to be provided.

Windfall Profits and Retention Provisions

To prevent windfall profits from the resale of demonstration units, WHA proposed to attach deed restrictions limiting net sale proceeds to the tenant-purchaser for the first 15 years of ownership. To avoid the loss of the demonstration unit from the low-income housing stock, WHA also reserved the right-of-first-refusal to repurchase units at a predetermined price. The price was to be the original purchase price plus a three percent appreciation for each year from the date of original purchase.

Provision for Maintenance After Sale

WHA's application made no mention of providing any post-purchase assistance if program participants encountered extraordinary maintenance and repair costs.

Handling of Non-Participants

In general, no relocation was expected to result from program implementation. Non-purchasing tenants were to be offered other appropriate and comparable WHA units if they were willing to move from units the authority wanted to sell.
Amount and Uses of Sales Income

Sale proceeds were to be used for three main purposes. First, the agency proposed to deposit part of the proceeds with the lending institutions providing mortgage financing to buy down the program mortgage interest rates. Second, proceeds were to be used to cover the cost of repairs and improvements in the units to be sold. Finally, the agency proposed to acquire replacement units with any proceeds left at the end of the demonstration.

Impact of the Sales Program

Because no units were sold, the demonstration did not have any impact on the operating subsidy that the WHA receives from HUD. There were also no impacts on other WHA operations.

Conclusions

Though the program never really took off, based on file documentation, it is possible to identify several areas that presented insurmountable problems. First, two components considered essential by the WHA were not approved by HUD. HUD did not approve the use of sales proceeds from the separate property disposition to subsidize the interest rate to be charged to program participants, nor the use of the owner provided repairs (OPR) arrangements to rehabilitate program units.

A second problem was the poor physical condition of the properties to be sold. Although the Wichita proposal did not identify specific units to be included in the demonstration, the WHA staff gave assurance to HUD that no units would be sold unless rehabilitation work was completed. On this basis, HUD approved only the sale of units in good condition. Ultimately, the WHA selected units in such poor condition that rehabilitation in many of the units proved financially unfeasible.

Given the poor condition of the units to be sold under the demonstration, and the lack of an alternative mechanism to lower program interest rates, a third problem was the inability of the WHA to interest private financial institutions in providing financing for prospective program participants.

A final issue that contributed to the demise of the program was the turnover on the city council and of the town staff. According to HUD regional staff, the turnover on the council and town staff led to the city's reevaluating its participation in the demonstration and deciding against it. Once this decision was made, the WHA did not attempt to find solutions to the program problems.
Introduction

The City of Wyoming Housing Commission has sold eight scattered-site public housing units (five in 1987; one in 1988; two in 1989) from a stock of 63 scattered-site units scheduled for sale. Two additional sales are imminent, and the commission intends to sell its entire stock of scattered-site units as soon as qualified buyers can be found from among the clientele served by the commission. Sales have been slow in Wyoming due to a lack of qualified buyers. Very few tenants have sufficient income to afford the costs of homeownership, and some of those with adequate incomes are screened out for other reasons, including bad credit and no savings for a downpayment. Still others simply have not been interested in participating.

The commission sells houses at 50 to 60 percent of their appraised values, which have ranged from $32,500 to $45,000, and takes back a silent-second mortgage covering from 40 to 50 percent of that amount in order to increase the affordability of units for public housing tenants. The second mortgage is forgiven in stages between the fifth and tenth year of ownership if the house remains with the original owner. Home buyers are required to make a three percent down payment (which has ranged from $426 to $1378). Closing costs (which have ranged from $1349 to $2903) are paid by the City of Wyoming from CDBG funds. FHA-insured first mortgages are arranged by a private mortgage company. The company qualifies public housing tenants for those mortgages using conventional FHA insured loan criteria. As a result of careful screening by the housing commission staff and lender, no late payments, delinquencies, or foreclosures have occurred.

Overall, the commission staff has been pleased with the demonstration, since it provides a rare opportunity for low-income households to become homeowners. But, the staff is somewhat concerned about the cost of the program in terms of lost revenues, which have run about $3,750 per unit per year and far exceed any savings from reduced operating costs. Possibly because of lost revenues from houses sold, in 1988 the commission reduced its staff (by converting to contract maintenance) in order to build its operating reserves to levels required by HUD. Lost rental revenues may be offset by revenues and interest which have accrued to the authority from the sales but the commission has yet to consider how sales revenue will be used once they are no longer needed to cover acquisition of any foreclosed units. Thus, problems occasioned by lost rental revenues are immediate, while benefits from sales proceeds are indefinite, at least at this point.
Managing the Demonstration

The city of Wyoming, located southwest of Grand Rapids, Michigan, occupies approximately 25 square miles with more than 60,000 inhabitants. The city is part of the Grand Rapids MSA. For more than a decade the Wyoming Housing Commission has provided housing opportunities to low-income people. The demonstration is managed by the Wyoming Housing Commission.

The commission has a total of 215 units under annual contribution contract and administers 169 Section 8 certificates and 100 housing vouchers. In June of 1987, the commission had 563 families on its public housing waiting list (403 families and 160 elderly). It also had an additional 213 families on its waiting lists for Section 8 certificates and housing vouchers (45 Wyoming residents and 168 non-residents). Two years later, in July 1989, the commission still had over 600 households on its waiting lists. Once screened for income eligibility, all eligible families are added to the lists. Consequently, the waiting lists can be considered an accurate measure of the demand for subsidized housing in the city of Wyoming.

In implementing the demonstration, the commission sought to provide a mechanism by which low- and moderate-income families residing in public housing could become property owners and taxpayers in the city. There are five specific program goals. First, the Wyoming City Council and the Wyoming Housing Commission are interested in providing an incentive for families currently living in public housing to have an opportunity to purchase their unit and share in the dream and responsibility of homeownership.

The second goal is to promote neighborhood acceptance and stability. Many of the tenants are long-term residents and the program is expected to provide them with a stake in the place they live. Families are expected to become an established part of their neighborhoods rather than transient residents. The third goal is to decrease the stigma traditionally associated with public housing residency.

The fourth goal is to gradually reduce the inventory of scattered-site single-family units. Because of their location and structural diversity, these units have been difficult to manage and maintain. The demonstration is expected to reduce the maintenance, repair, and operational costs associated with such housing.

Finally, the last goal is to return the units sold to the tax roll. The city will thus rescind the current property tax subsidies granted to the scattered-site units as they are sold.

The idea of participating in the demonstration originally came from the commission's executive director who was also the principal author of the proposal. Once the proposal was outlined
in general terms, the Wyoming Planning and Community Development Department prepared the Public Housing Sales Manual containing the guidelines governing the sale of public housing units to tenants.

The tenants were not involved in the design of the program. In general, no important objections to participation were raised by residents, commissioners, staff, or the Wyoming City Council. Initially, however, the housing commission had some questions about the image buyers would have for having bought the units at a fraction of market value. Questions were also raised about the ability of low-income families to obtain mortgage financing due to their low income and their lack of credit history. These initial questions were answered during the design phase of the program.

Three groups are involved in the demonstration. One, the housing commission, is responsible for overall project management. Second, an outside contractor (initially Mr. Gary Lorge of Grand Valley College and currently Mr. Patrick Gaffney, an employee of the Wyoming Community Development staff), is responsible for providing the financial and budgeting components of the counseling and training program (other aspects of the training program are provided by PHA staff). The third group, Fleet Mortgage Company, is arranging the financing, qualifying tenants for mortgages, and supervising closings.

The annual administrative costs of implementing the demonstration ran about $4,000 per year during 1986-87, with an additional $3,500 needed for non-personnel costs in the sale of the first three units. Over the past two years, administrative costs have been less than $2,000 per year and the program has required a small amount of management oversight (about 2 percent of the commission's executive director's time). Wyoming received a $35,000 technical assistance grant, but it has drawn down only $17,290 of that amount, some of which has yet to be spent. These funds have been used to pay for repairs to units before sale, pay for appraisals and other transfer costs and assist some buyers with their closing costs. In addition, to assist participants in paying closing and transfer costs, the City of Wyoming provided access to $20,000 in Community Development Block Grant funds, but these funds were not needed.

In the course of designing and administering the program two problems were encountered. First, delays occurred as a result of administrative changes in agency personnel. Time was needed for the new executive director to become familiar with the characteristics of the demonstration project. A second problem was the initial inability to find an interested private lender to provide mortgage financing. After contacting many lenders, the housing commission was able to secure a commitment from Fleet Mortgage Company, which has arranged mortgage financing for all sales. The mortgage company provides standard FHA insured loans.
Overall, the Wyoming housing commission staff is very satisfied with arrangements that have been worked out for managing the demonstration. The management process requires little staff time and appears to be working satisfactorily. The only difficulties encountered have been associated with turnover in commission management and the time required for a new executive director to learn how the demonstration program operated.

Selecting and Rehabilitating Properties

Sixty-three units are targeted for participation in the demonstration. Sales have been slow: only eight houses have been sold, although two additional sales appear to be imminent. All targeted units are single-family scattered-site units. The commission staff considers it easier to sell single-family units than any other type. Consequently, all such units in the commission's stock were targeted for participation.

In general, the units are in very good condition. The last repair and rehabilitation work done on the units was in 1981, except for repairs required by FHA prior to sale or requested by buyers and agreed to by the commission staff ($6,312 for the eight units sold as of July 1989). Since the major repair work undertaken in 1981, maintenance has been good and consistent, but the staff is concerned that a lack of HUD modernization funds for units targeted for the demonstration may result in some deterioration. Sales have been slow and the commission lacks adequate funds from its own sources, apart from sales proceeds, for continued investment in their repair. Repairs required prior to sale were performed by commission staff and contractors. Repairs to one of the first houses sold ($1,050) were financed from sales proceeds; subsequent repairs have been paid for from the Public Housing Homeownership Demonstration technical assistance grant funds provided by HUD. No tenant relocation has been necessary.

The targeted units are scattered throughout the city. In general, the units are located in low density, stable neighborhoods of mostly single-family residences. Housing in these areas is in good condition. These areas are blue collar neighborhoods, with a predominantly white population. Residents are a mix of renters and homeowners. The average rent in these areas is about $300 per month, and the average housing price is about $37,000. In general, the program appears to have had a moderate effect on the neighborhoods, mainly associated with improvements to landscaping and yard maintenance by the new owners. No other improvement program is taking place in these areas.

Attracting and Selecting Owners

Before the demonstration in Wyoming was formally approved by HUD, the housing commission staff held an initial meeting with all families living in its single-family, scattered-site units.
During that meeting, the scope of the demonstration program was explained. After the initial meeting and approval of the demonstration by HUD, the commission staff sent letters to all families probing their interest in participating. Those letters included copies of the Public Housing Sale Manual. The manual includes blank pre-application forms that the family had to complete before a second meeting was scheduled. In the second round of meetings, the housing commission director met individually with each family and went over the pre-application form to determine if there were any problem areas. Income eligibility is the first factor to be considered (38 percent of the after-tax income has to cover all housing costs). In addition to income, other criteria used in determining eligibility includes length of residency (one year in public housing), household composition, length of gainful employment (one continuous year at a minimum), and the tenant's housing and rent history. As a result of that pre-screening, families with problems which precluded their participation were asked to try to solve their difficulties and, if still interested, to submit a new pre-application one year after the date of the second meeting. Those families that passed the initial pre-screening were asked to submit a loan application to the private lender. A meeting was scheduled with the lender, the family, and the director. Those applications considered acceptable by the lender were then referred to HUD for FHA approval.

The housing commission staff now views all current tenants of the scattered single-family units and other clientele of the housing commission as potential buyers. The commission staff monitors tenants' incomes (about $11,000 per year minimum), credit records, employment status, length of residence in public housing, and other factors to identify potential buyers. When such a household has been identified, the commission's executive director checks to be sure the household is aware of the homeownership program and arranges a meeting to explain it in detail. If the tenant is interested in participating, the household is referred to the private lender, which secures necessary mortgage application forms and determines whether the household can qualify for an FHA insured mortgage. Because the private mortgage lender is offering standard FHA insured loans, potential buyers have to meet the income, credit, and other eligibility criteria set by FHA.

In most cases, only those tenants living in the scattered site units are eligible to acquire their units. Those who do not want to or who cannot buy will remain as tenants in those same units. Consequently, no relocation of tenants has occurred as a result of the demonstration. If a family living in one of the targeted units decides to move out, then the unit may be sold if an eligible household is living in one of the commission's other public housing units. Otherwise, the next person on the public housing waiting list is assigned to that unit. If the new family is interested and found eligible it can apply for participation.
As of July 1989, the characteristics of the new owners (eight) at the time of sale were somewhat similar. All were caucasian; seven of eight were married; six of eight were thirty years old or less; and six of eight had four or five persons living in the household. The median income was about $15,500, and the range of incomes was from a low of $13,582 to a high of $30,580.

The tenant selection process has been conservative, but the commission staff believes that is important to ensure that owners will be able to meet their mortgage obligations and maintain their property adequately. The use of a private lender and FHA-insured mortgages has also been important, in the staff's opinion, since that has relieved the staff of much of the burden of qualifying tenants for ownership.

Property Conveyance

All the properties are sold fee simple. The sale prices are based on the appraised value, although the actual sale price to the purchaser is a percentage of this value. It is commission policy that sales prices be set at 60 percent of the appraised value. For families that cannot afford this sale price, a sale price as low as 50 percent of the appraised value may be set, but that requires written authorization from the commission. The difference between the appraised value and the sale price is covered by a second silent mortgage held by the commission. The closing costs, which have ranged from $1349 to $2903, are paid with CDBG funds allocated by the city.

No legal issues have arisen with regard to the conveyance of houses sold by the commission.

The commission staff believes its pricing policy is fair, and it is happy with the transfer process as a whole, which, once a prospective buyer is located, is largely managed by the private lender.

Financing

The private lender, Fleet Mortgage Co., was contacted by the commission's executive director and, after several meetings, the lender agreed to consider handling the loans. The lender is providing FHA insured loans (FHA 203B). Two factors make these loans unconventional. First, the size of the downpayment, only three percent of the sale price, is small compared to other conventional loans. The second factor is the existence of a second silent mortgage.

In general, the lender considers these mortgages low-risk loans. There are three main reasons for this. First, due to the price write down, the sale price is only a fraction of the market value. Second, the second mortgage includes a buy-back clause that assures payment of outstanding debt balance in case of
default. Finally, the loans are FHA insured, giving the lender a double payment guarantee.

The interest rate and term of the loans offered by the lender are conventional. In the eight sales that have taken place, the interest rate charged has ranged from a low of 7.5 percent to a high of 11.5 percent on a 30-year loan. The lender may sell these loans in the secondary market while retaining the servicing.

In reviewing the loan applications, the lender uses conventional FHA insured loan criteria. Those found acceptable are sent to HUD for FHA approval.

The lender is a branch office of a larger Milwaukee-based company. Once the loans have been approved, they are passed to the central office for servicing. The lender is happy to participate in the program. Loan financing is provided as long as program criteria are met. Because of the small number of demonstration loans that have been handled, the lender feels that loan processing for the program takes about 20 percent more time than conventional loans. The lender has to refamiliarize himself with the guidelines contained in the Public Housing Sale Manual every time a program loan application is submitted.

No loan repayments have been late, no defaults have occurred, and no mortgages have been foreclosed. The commission staff is very happy with the financial procedures devised for the demonstration, and it plans no changes.

Counseling

The commission staff is primarily responsible for implementing the counseling program. Counseling has been divided into two areas. First, the financial, budgeting, and credit aspects are being offered by an outside contractor, initially a social worker from a local college and more recently a moonlighting staff member of the Wyoming City Community Development staff. Training in home maintenance and repair is offered by the commission's maintenance director.

Financial counseling initially was done in two sessions, both in small-group meetings. During the first session, the counselor explained the basic financial, budgeting, and credit concepts that the purchaser will need to assume full homeownership responsibilities. At the end of this first session, the counselor distributed a homework sheet containing some budgeting and financial exercises. The second session was scheduled three weeks later. During this session, the counselor went over the homework with each of the families. Over the past year, the two sessions have been collapsed into one session. That session costs $142.50 to conduct (7.5 hours of the contractor's time at $15 per hour plus expenses). In general, the commission staff believes that people who can qualify for an FHA-insured mortgage
do not need much financial counseling; they already know how to budget their income and pay their bills promptly.

The maintenance and repair counseling is offered in two sessions. The first one is a small group session where general maintenance concepts are explained. The second session, about two weeks later, is offered individually in the family's home. The content of the individual counseling sessions differs with the level of knowledge and need of each family. The maintenance director is given compensatory time off for any night meetings.

Counseling on the process of obtaining a loan is handled by the director in the pre-application screening session. In our interview in 1987 with her, the director expressed the importance of scheduling as many sessions or meetings as were necessary for each individual family due to the importance of the counseling component in the overall success of the program. No formal post-purchase counseling is planned.

The commission staff is pleased with the effectiveness of its counseling efforts, although, as noted above, it believes the most important aspect of counseling is in steering people into homeownership rather than in providing advice about financial or maintenance matters.

Windfall Profits and Retention Provisions

The PHA has retained the right to buy back the unit for the outstanding mortgage balance if the family wants to sell or defaults within the first five years. That restriction is included in the silent second mortgage. The amount of the second mortgage is equal to the difference between the sale price and the market value. After five years, 50 percent of the second mortgage is forgiven, and an additional 10 percent is forgiven annually for the next five years. After year ten, the second mortgage is completely forgiven, and the family is free to sell the unit and keep all the profit. If the property is leased by the owner during the first ten years, the second mortgage is called due. There are no restrictions that would prohibit the owner from renting a room in the unit to another person as long as the unit is the owner's primary place of residence.

Since the commission has had no experience with early resales or with defaults and foreclosures, it could not evaluate the efficacy of its procedures for dealing with those situations. It believed, however, that the procedures were adequate to prevent new owners from reaping windfall profits.

Provision for Maintenance After Sale

The purchaser is charged a periodic maintenance fee of two percent of the mortgage principal and interest, which goes into a maintenance fund. The commission also expected to provide additional monies to this fund from sales proceeds, but it has
not done so. It feels that adequate funds are in hand from sales proceeds to handle any maintenance requirements without specifically earmarking those monies for maintenance fund use. Originally, the lender was to collect maintenance fund payments from owners, but the lender failed to do that; instead, the commission had to bill owners for past due maintenance fund monies. In the future, the commission will bill owners annually for payments to the fund. The owners can draw from the fund to pay for major maintenance work. This fund is administered by the commission. As of July 1989, one withdrawal had occurred to pay for a new water heater ($153).

Handling Non-participants

Of 63 houses targeted for the demonstration, tenants living in 14 applied to buy a house (of those eight bought the house, two sales are pending, and four did not qualify for a mortgage), and tenants living in 49 units were either found to be not eligible after the initial screening or were not interested in homeownership.

If tenants do not want to participate or cannot participate in the demonstration they are allowed to remain in the units as tenants. No relocation has been necessary.

The primary causes of nonparticipation appear to be insufficient income (households with incomes of less than $11,000 are not referred to the mortgage lender) and an inadequate credit rating.

Amount and Use of Sales Income

The revenues that have resulted from the demonstration are being held for the first five years after the sales take place. The monies are deposited in a bank account to be used to purchase units in case of default. The commission staff is uncertain about how it will use those monies and the accrued interest after that time.

Impact of Sales Program

The sale of eight units has had a substantial negative effect on the finances of the Wyoming Housing Commission, mainly associated with the loss of approximately $30,000 per year in rent revenues. In addition, operating subsidies lost per year ($1,058) exceed estimated savings in maintenance, insurance, and utility costs ($651), further aggravating the adverse financial effects of the demonstration. In 1988, HUD noted that the commission had insufficient operating reserves, a condition the commission staff suggests may be due to the loss of revenues from houses sold. It dealt with that problem by reducing its maintenance staff and replacing work previously performed by its own staff with work performed by contractors. Those adjustments were adequate to bring operating reserves back to within levels approved by HUD.
Since property taxes are not abated for new owners, the demonstration has had a positive fiscal effect on the City of Wyoming, which now collects taxes on the sold properties. Tax proceeds from the first eight units sold are approximately $5,000 per year.

According to the commission staff, the demonstration is having a small, but positive, effect on the neighborhoods in which the scattered-site units are located. Some new owners have invested in landscaping, which improves the appearance of the neighborhoods, and as a rule, yard and exterior building maintenance by the new owners far surpasses the previous level of maintenance provided by the housing commission staff and contractors.

Finally, the commission staff believes the demonstration has benefited home buyers by giving them a home they own, which is something they can feel good about, something they can build equity in, and which adds to their sense of belonging to their neighborhood and community.

Conclusions

In general, the commission staff and others interviewed during two site visits had a positive opinion of the demonstration. They considered low-income homeownership to be a desirable goal. The commission staff intends to continue selling houses until its inventory of 63 scattered-site houses has been liquidated, even though, as noted above, the sale of those units has some negative (at least in the short term) fiscal consequences.