City-CLT Partnerships

In Search of Best Practices

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1. Municipal Support for Community Land Trusts[1]

There were only a handful of community land trusts in the United States at the start of the 1980s, all of them located in rural areas. By 2008, over 200 CLT programs were up and running – half of them established since 1999. Now concentrated mostly in cities and suburbs, these CLTs are busily acquiring scattered parcels of land, developing affordable housing, and revitalizing communities in 40 states and the District of Columbia.

The recent proliferation of CLTs has many causes, but none more influential than the investment and involvement of local government in starting, expanding, and sustaining CLTs. Such municipal support has increased dramatically during the past decade. The number, size, and productivity of CLTs have increased on the same trajectory, over the same span of time.

The earliest CLTs were started by grassroots activists with little or no support from local government.[2] Indeed, most of the CLTs that arose prior to 1990 were organized in opposition to municipal policies, projects, and plans, especially in neighborhoods beset by alternating cycles of disinvestment and reinvestment. In many communities of color that is still true today, where CLTs are being erected as bulwarks against market pressures of speculation, gentrification, and displacement made worse by the actions of City Hall.

There are a growing number of cities, counties, and towns, however, where a CLT has become a partner of municipal government – an ally rather than an antagonist. Especially in places where a local government has put a social priority on promoting homeownership for lower-income families, while placing a fiscal priority on protecting the public's investment in affordable housing, CLTs have become favored recipients of municipal investment.

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[1] Research for this report was supported by the Lincoln Institute for Land Policy

[2] There were exceptions. In 1983, a progressive government in Burlington VT instigated and provided administrative support and a $200,000 start-up grant to establish the Burlington Community Land Trust (later renamed the Champlain Housing Trust). In 1986, Time of Jubilee Inc., a CLT established in Syracuse NY, partnered with the City's Community Development Department to build affordable homes in a disinvested African-American neighborhood.

- ❖ They receive administrative support from municipal staff or financial support from municipal coffers in planning and starting the CLT.
- ❖ They receive donations of city-owned land, grants of municipally-controlled funds, and low-interest loans in developing and financing the CLT's projects.
- ❖ They receive capacity grants, development fees, and revenues from marketing and managing resale-restricted housing, funds directed toward sustaining the CLT's operations.
- ❖ They receive equitable tax assessments on CLT homes, ensuring that low-income homeowners are not taxed on values they can never claim for themselves.
- ❖ They partner with municipalities in enforcing long-term controls over the eligibility, occupancy, and affordability of housing extracted from private developers through inclusionary zoning, density bonuses, and other regulatory mandates or concessions.

As welcome as the recent growth in municipal assistance has been, such assistance has sometimes been less than helpful. There are too many cases where municipalities have inadvertently structured their assistance in such a way, regulated the CLT in such a way, or taxed the CLT's property in such a way as to undermine the productivity or sustainability of the very model they have decided to support. A conclusion we have reached after examining a variety of municipal programs and after interviewing a number of municipal officials and CLT practitioners is that there are better ways – and worse ways – for a municipality to support the projects and operations of a community land trust. This report is both descriptive and prescriptive, therefore. We not only describe the **types of assistance** currently being offered to CLTs by supportive municipalities. We also take a few tentative steps toward recommending the **best and worst practices** for rendering such assistance.

2. Supporting CLT Startups

A municipality's leaders are willing to assist a CLT – and a CLT's organizers are willing to accept such assistance – because both believe their interests will be served by working together to get the CLT off the ground. During the process of planning and starting a CLT, however, the interests of the parties sometimes diverge. There are issues where those who speak for the municipality and those who speak for the CLT can find themselves at odds. The two most divisive issues that commonly appear during the start-up phase are the following:

- How extensively (and how early) should residents of the CLT's intended service area be involved in planning, designing, and governing the CLT?
- How equitably are the rights of the homeowner and the landowner to be allocated in designing the CLT's ground lease?

Community Participation

Among the many tasks involved in starting a CLT, none is more important than systematically introducing the model to a wide array of constituencies in order to win their informed support. The municipal agencies to whom the CLT must look for project funding, regulatory approvals, and equitable taxation are a high priority for any such campaign of outreach, education, and organizing. Equally important are several constituencies outside local government, especially those individuals who call the CLT's service area their home and institutions serving the same population as the CLT. Experience has shown that these nongovernmental constituencies must be intimately involved in the process of planning, designing, and governing a CLT if this unusual model of affordable housing is to have any chance of being accepted and supported by the larger community. The municipality, however, may be resistant to working with neighborhood activists with a history of criticizing city hall or may simply be reluctant to relinquish control over a fledgling organization to which the municipality is planning to make a major commitment of money or land.

Municipal Concern: A municipality wants the process of planning a CLT – and the organization that results from that process – to reflect the municipality's policies and priorities.

CLT Concern: A CLT is committed to the extensive participation of community residents, CLT leaseholders, and "public-interest representatives" in its corporate membership, on its governing board, and in the process of planning the CLT.

Worst Practice: Participation Deferred – or Eliminated

Whenever the start-up of a CLT is dependent on a municipality's resources and dominated by a municipality's priorities, there is a danger that constituencies outside of local government will not be invited into the planning process until **after** the decisions have been made that lay the foundation for the new CLT. Even worse, the preeminence of city government in planning a CLT may come at the price of the model's more democratic components, where leaseholders no longer have a place on the board and where accountability to city hall replaces accountability to the local community.

Best Practice: Early and Ongoing Participation of Community *and* Municipality

The CLT, in its "classic" configuration, combines an innovative approach to the **ownership** of real estate, the **operation** of affordably-priced housing to preserve its affordability, and the **organization** of the CLT itself. Municipalities that are drawn to the CLT because of ownership and operation, sometimes place a lower priority on the model's distinctive organizational features. Most public officials eventually recognize, however, that the active participation of community residents and CLT homeowners can be a precious asset, helping the CLT to mitigate opposition to its projects, build a market for its homes, and win acceptance for an unconventional model of tenure among funders, lenders, and the community at large. The best way for a municipality to support a CLT is to weave participation and accountability into its organizational fabric, ensuring CLT's continuing connection to the community it serves.

Allocation of Rights Between Homeowner and Landowner

The "model" ground lease used by most CLTs in the United States has been refined over a thirty-year period of trial and error.[3] It is a two-party contract that is written in favor of neither party. The rights and responsibilities of the landowner (the CLT) are limited and balanced against the rights and responsibilities of the lessee (the homeowner). A municipality's desire to protect its investment in the CLT, however, can sometimes threaten this delicate balance.

Municipal Concern: A municipality wants any recipient of its subsidies to have sufficient powers to impose conditions, enforce compliance, and cure defaults in the housing produced with municipal support.

CLT Concern: A CLT wants to protect the integrity of the homeownership "experience" being offered to prospective homebuyers, ensuring that a homeowner's privacy and independence are not compromised by unnecessary oversight and interference by the landowner or the municipality.

Worst Practice: Rewriting the Ground Lease in Favor of the Landowner

The temptation of some attorneys, when asked to review the "model" ground lease that has become standard practice for CLTs across the country, is to begin re-writing it. There is something about the lease's carefully wrought balance between the parties, equitably protecting the rights of homeowner and landowner alike, that sends some attorneys running for a red pencil as soon as a client asks them to "read over" the proposed lease. Many city attorneys, in particular, have been inclined to rewrite the lease to grant the landowner more sweeping powers of inspection, approval, and enforcement than are granted a CLT under the model lease. This can create enormous headaches for the CLT in marketing, financing, and administering its resale-restricted homes.[4] A few city attorneys have even tried to write their

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[3] A hard copy of this model lease, along with an excellent commentary explicating every article, can be found in *The Community Land Trust Legal Manual*, published by the Institute for Community Economics in 2002. Copies can be purchased from Equity Trust, P.O. Box 746, Turners Falls, MA 01376 (413-863-9038). Electronic copies of the model lease and the commentary can be downloaded free of charge from the National CLT Network (www.cltnetwork.org) or the *CLT Resource Center* (www.burlingtonassociates.com).

[4] Significantly altering the lessee's rights in the CLT model ground lease can make it harder for a CLT's homebuyers to obtain mortgage financing. The model lease has been designed and revised over the years in consultation with both private lenders and secondary market institutions to safeguard their interests and to standardize key lease provisions, eliminating the need for a lengthy review by lenders of each new lease.

cities into the ground lease, giving a municipal agency the right to approve the financing, subletting, or improvement of buildings located on the CLT's land – or the right to approve the transfer of the CLT's land. This is the wrong vehicle for asserting the municipality's interests, since the city is not a party to the ground lease.

Best Practice: Maintaining the Model Lease's Equitable Balance of Interests

The model CLT ground lease has been carefully developed, tested, and refined to grant the CLT all of the rights and powers the CLT will need to prevent absentee ownership, to promote good maintenance, to cure defaults, to prevent foreclosures, and to preserve affordability in the owner-occupied housing under the CLT's stewardship. At the same time, the model lease is designed to respect the privacy and autonomy of the CLT's leaseholders, intruding as little a possible on the experience of homeownership. Just as important, the model lease has created a degree of standardization among major lenders and national intermediaries like Fannie Mae in the mortgage underwriting of CLT homes on leased land. A municipality has many options for protecting its investment in a CLT's land and housing that do not require completely overhauling a model lease that has proven its worth over a span of many years. This does not mean to suggest that the model lease must never be altered in any way. With or without municipal involvement, CLTs make dozens of refinements in the model lease in the process of adapting it to local priorities and needs. Key decisions are made about the precise terms and conditions for regulating occupancy, subletting, inspections, improvements, eligibility, and the pricing and resale of CLT homes. The "best" practice in making these refinements is not to leave the model lease entirely alone, but to respect the lease's equitable relationship between landowner and homeowner.

3. Building the CLT Portfolio

There are many times when those who are offering municipal assistance for the development of a CLT's projects and those who are seeking such assistance disagree over the best way to put these resources to work. These disagreements are most commonly provoked by the following issues:

- Does a municipality support – or undermine – a CLT by providing loans directly to the buyers of CLT homes?
- Does the municipality work constructively with the CLT and with private developers when the CLT is asked to act as the steward for affordable housing created through municipal mandates like inclusionary zoning?
- Does a municipality need to alter its existing housing assistance programs in order for them to work well with the CLT's unique approach to homeownership?

Loans to Homebuyers

Many jurisdictions operate homebuyer loan programs which have been developed and refined over many years. Sometimes a local government, recognizing the need for a CLT to protect long-term affordability but reluctant to alter an existing program, will try to combine the two approaches. They ask the CLT to hold the land and impose resale price restrictions but instead of (or sometimes in addition to) subsidizing the CLT, they hope to continue to provide subsidy in the form of homebuyer loans. While this combination has been made to work in some communities, it is important for policymakers to understand that CLTs represent a very different approach from homebuyer loan programs. CLTs require a **permanent** investment of subsidy funds while most loan programs involve only temporary investment in exchange for temporary affordability.

Municipal Concern: A municipality with a long history of making homebuyer loans may be unwilling – or unable – to re-tool its existing programs to loan (or to grant) such funds directly to a CLT.

CLT Concern: A CLT can only preserve the long-term affordability of housing subsidized by a municipality if the municipal subsidy remains in the housing, reducing the price for the next low-income homebuyer.

Worst Practice: Removable Subsidies Offered Directly to Initial Homebuyers

If municipal subsidies that are offered to the initial buyer of a CLT home are either removed by the homeowner at resale or repaid to the municipality, these funds will not be available to subsequent buyers – unless the municipality is committed to reinvesting repaid loans in the same homes. Even though the CLT restricts the rate at which the price increases, without access to the municipal loan, subsequent buyers of these CLT homes will need to borrow more on their first mortgage, increasing their monthly payments. Generally, this means that future buyers will need to have higher incomes to afford the same home or the CLT will have to find additional subsidies to replace the repaid loan every time the home resells. For example, a home that is made initially affordable to a household at 70% of AMI because of a subsidized loan to the first buyer, might require a future buyer without such a loan to earn 90% of Area Median Income or more. This loss of affordability creates a serious problem for a CLT committed to maintaining the affordability of its homes for families earning under 80% of AMI. A CLT cannot maintain the affordability of its housing if local government takes its money out of the project.

Better Practice: Assumable Loans for Permanent Affordability

When a municipality insists on providing loans directly to a CLT's homebuyers, these loans must be assumable by all future income qualified buyers. By making its homeownership loans assumable by subsequent buyers of a CLT's resale-restricted homes, the municipality ensures that its funds will be recycled within the same housing stock, enabling the CLT to maintain affordability on an ongoing basis. The City of **Albuquerque NM,** for example, provides grants to the Sawmill CLT that are equal to the cost of the land underlying the CLT's homes and then offers interest-free, permanently deferred-payment loans to the buyers of these homes, loans that are assumable by future homebuyers earning less than 80% of AMI. Similarly, the Northern Communities CLT, in **Duluth MN** has developed most of its resale-restricted, owner-occupied housing using assumable loans that are offered to the homeowner, not to the CLT.

Best Practice: Permanent Investment in the Community Land Trust

It is worth noticing, however, that loans to homeowners which are assumable by future buyers require a permanent commitment of subsidy funds very much like a deferred loan to the CLT. Subsidy funds are permanently tied to an affordable unit with no real expectation of repayment. Unlike a loan or grant to the CLT, these loans have to be rolled over at each resale, involving significant legal work and recording fees with each sale. And in jurisdictions where

CLT homes are taxed on the basis of the below-market price for which these homes are sold and resold, a CLT's homeowners may pay additional property taxes when the municipality's investment is structured as an assumable loan to the buyer rather than as a grant or loan conveyed directly to the CLT. It is likely that over the long-term these loans will be much more difficult and costly for the municipality to administer. The best practice, therefore, is simply to invest municipal subsidies permanently in the project through the CLT. A grant to the CLT or a deferred-payment loan secured by the CLT's interest in the land allows the CLT to sell the home at a below-market price which is affordable for one generation of homeowners after another without additional investment by the municipality.[5] A number of municipalities have revised the regulations for their existing homebuyer loan programs, therefore, to allow the program to make deferred payment, forgivable loans directly to the CLT instead of loaning these funds to individual homebuyers.

Supporting the CLT as the Steward for Inclusionary Housing

Many of the earliest inclusionary housing programs, including those in **Montgomery County MD** and **Irvine CA**, originally required homeownership units to remain affordable for a short period of time, five years or fifteen years at the most. These pioneers learned the hard way, however, that without long-lasting affordability controls the impact of their programs was limited, as thousands of inclusionary units were converted back to market-rate prices when the controls expired. Today, a majority of the nation's inclusionary housing programs, whether mandatory or voluntary, require long-term affordability for any residential units produced under these programs.[6]

Once these inclusionary units have been created, they must be marketed, monitored, and managed in such a way as to preserve their occupancy, eligibility, and affordability over time. Some municipalities carry out these responsibilities themselves. Others ask a nonprofit partner like a CLT to shoulder these responsibilities on the municipality's behalf. The interests of the partners can sometimes diverge, however.

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[5] Most CLTs, when funds are granted or when lands are donated to them, have used these municipal subsidies to reduce the purchase price of a CLT home. In the on-going debate between affordable prices versus affordable payments, most CLTs have come down firmly on the side of the former.

[6] This is true even for many of the pioneers. In 2005, **Montgomery County** amended its Moderately Priced Dwelling Unit ordinance to require 30-year affordability for inclusionary owner-occupied units. The City of Irvine created a CLT in 2006 to preserve new inclusionary units, both renter-occupied and owner-occupied, in perpetuity.

Municipal Concern: A municipality wants to reduce its role, responsibilities, and administrative costs when delegating oversight responsibilities for inclusionary homes to a nonprofit partner.

CLT Concern: A CLT wants the municipality to ensure a developer produces the quantity and quality of inclusionary housing required, while steering the developer toward the CLT. The CLT also wants to be able to cover its costs of marketing and monitoring these inclusionary homes on the municipality's behalf.

Worst Practice: Municipal Abdication

Municipalities that partner with a CLT in marketing, monitoring, and enforcing inclusionary housing have acknowledged the need for someone to assume long-term responsibility for the stewardship of these units. They have rejected the enticing idea of use and resale controls that are "self-enforcing." However, some municipalities wash their hands of all responsibility for making an inclusionary housing program work for the CLT. They require a developer to set aside a certain percentage of "affordable" units, but do not insist on those units being of the same quality and appearance as the other units in the developer's project. They require a developer to give the municipality or its designee the first option to purchase the inclusionary units, but neither steer the developer toward the CLT nor back the CLT in its endeavor to ensure that whatever units are produced will be appropriate and acceptable for the lower-income households to whom the CLT will be selling these homes. They expect the CLT to monitor and enforce long-term contractual controls over the occupancy and resale of inclusionary units but they make no provision for helping the CLT to cover the cost of stewardship.

Worst Practice: Failing to Plan for the Cost of Stewardship

Another harmful practice occurs when a municipality acknowledges the need for oversight of inclusionary units, either by a municipal agency or by a nonprofit partner, but provides no mechanism for covering the cost of these administrative responsibilities. **Denver, Colorado** is a case in point. Since it was adopted in 2002, Denver's inclusionary housing ordinance has produced over 700 units of affordably-priced, resale-restricted, owner-occupied housing. The City's Division of Housing and Neighborhood Development administers the inclusionary program, but no staff were initially assigned to the program and no money was appropriated from the general fund to create a new position. Eventually, the Division found the funds to

hire a single full-time employee to oversee the City's inclusionary housing program, although at least three people would be needed to administer a portfolio of this size.[7]

Best Practice: Encouraging Developers to Partner with a CLT

Some municipalities formally or informally steer private developers of residential projects with a municipally-mandated affordability component toward the local CLT. Inclusionary housing programs rarely designate a particular organization outside of city government as the only possible steward for a municipality's inclusionary units, but some programs are crafted in such a way as to make the CLT the preferred partner of the municipality when it comes to marketing inclusionary homes and preserving the long-term occupancy, and affordability of these homes. Even after the CLT is identified as the municipality's designated steward for the inclusionary units, however, municipal officials stay in the picture, ensuring that the inclusionary units are constructed in compliance with the municipality's requirements and encouraging the CLT's early involvement in shaping the units' design, location, and marketing.

For example, **Burlington VT** requires inclusionary units to remain affordable for a minimum of 99 years, with prices that rise no faster than the resale formula used by the Champlain Housing Trust. Further, Burlington's inclusionary zoning ordinance gives the city's Housing Trust Fund or its designee the first right to purchase every inclusionary unit. The Champlain Housing Trust has been the designee for nearly all of the homeownership units created through inclusionary zoning.

Boulder CO provides another example. The City's inclusionary ordinance has so far produced a portfolio of 500 resale-restricted, owner-occupied homes, with roughly 50 new homes being added every year. Developers have occasionally been encouraged to pre-sell inclusionary units to Thistle Community Housing, a local CLT. This has been a boon to all parties. The developer's risk is reduced, because 20% of the project is pre-sold before ever breaking ground. Thistle's risk is reduced, because it is not holding land or constructing houses, but accepting units at completion on a turn-key basis. The price to the homebuyers is reduced. The last has happened because Thistle is usually able to negotiate a lower sales price from the developer – generally 5%-9% lower than the city-mandated inclusionary price – in return for Thistle's contractual commitment to purchase and market all of the developer's

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[7] More recently, the Division has been exploring a better way of stewarding the city's inclusionary units. Working with the Colorado Land Trust, the Division is in the process of transferring the first inclusionary units to the CLT. One advantage of working with the CLT is that the CLT can support ongoing monitoring through lease fees and other charges. However, because such fees are not charged to other homeowners in the city's inclusionary housing program, it may be harder to sell these homes than if appropriate fees were imposed on all projects from the start.

inclusionary units. Thistle's cost of serving as the long-term steward for these units is covered through the collection of monthly lease fees and the collection of a 3% "Lease Reissuance Fee" on the resale of every CLT home.

Programmatic Compatibility

Many CLT projects will require public subsidies from multiple sources. These sources of project support may come from multiple jurisdictions such as the city and county governments or from different programs administered by the same municipality. In these situations it is important to ensure that the performance requirements imposed on the CLT by all of these sources of municipal support are compatible, both with each other – and with the CLT.

Municipal Concern: Most municipalities prefer to support CLT projects through their existing housing assistance programs with as few administrative or regulatory changes as possible.

CLT Concern: The CLT wants full access to the municipality's existing housing assistance programs, but needs program requirements to fit the CLT model and to complement, not conflict with the requirements of other funding sources.

Worst Practice: Incompatible Requirements

There are two worst cases here, both arising out of a municipality's failure to reexamine and retool existing programs to accommodate a new way of doing affordable housing. In the first scenario, different funding sources impose different (and sometimes contradictory) performance requirements when granting or loaning funds to a nonprofit or for-profit developer of affordable housing. Although a problem for every recipient of municipal assistance, the administrative burden of incompatible requirements may be especially difficult for CLTs to bear because so many are still in a formative stage, with a small staff. The second "worst case" scenario is unique to the CLT. It occurs when a municipality imposes grant or loan conditions on a CLT that were originally designed either to subsidize rental housing for lower-income tenants or to help lower-income homebuyers in purchasing market-rate homes. Many of these conditions are not be conducive to the leased-land, resale-restricted model of the CLT, making CLT homes more difficult to develop and to finance, impeding the CLT's productivity and undermining the CLT's viability.

Best Practice: Coordination among Municipal Programs

Contradictions between the requirements of various subsidy providers can cause enormous administrative and legal headaches for a CLT. If two government agencies intend routinely to support the same CLT projects, it makes sense to make sure not only that what is required of the CLT is compatible, but that grant agreements, loan agreements, liens, and covenants used by different programs within the same municipality or used by different municipalities supporting the same CLT actually match. The Community Housing Trust of Sarasota County, for example, was able to work with the **City of Sarasota FL** and with **Sarasota County** to develop a project development grant agreement that was acceptable to both municipalities. The Orange Community Housing and Land Trust developed a restrictive covenant that was approved for use by both the **Town of Chapel Hill** and **Orange County**. Using a single document to satisfy the needs of both jurisdictions has allowed OCHLT to layer funding from both sources without worrying about regulatory conflicts.

Competing Programs

Most cities see the CLT as but one option for helping lower-income households to purchase a home, one tool among many in the municipality's toolbox. While a CLT does not need to be the community's only homeownership program, the success of a local CLT can be undermined by other governmental programs if different programs do not offer different levels of assistance and do not serve different populations. A CLT asks assisted homebuyers to accept certain restrictions on the use and resale of their homes, including an obligation to pass along the benefits of any public subsidies to future homebuyers of limited means. When a municipality offers similar subsidies to the buyers of market-rate homes without imposing restrictions and obligations similar to those imposed on the CLT, the latter's buyers are given good reason to question the fairness of the deal they are being offered.

Municipal Concern: Recognizing that CLT homeownership may not be for everyone, municipalities often operate multiple homeowner assistance programs, some with resale restrictions and some without.

CLT Concern: The CLT will have difficulty selling homes with use and resale controls if lower-income homebuyers can receive the same level of municipal support to purchase market-rate homes that have no controls whatsoever.

Worst Practice: Competing Programs

Even worse than municipal programs with incompatible requirements are municipal programs that produce competing homeownership products. In the latter case, a municipality supports the CLT's production of resale-restricted, owner-occupied homes while continuing to provide the same per-unit subsidy for less-restricted housing that is offered for sale on the open market to the same population in the same neighborhoods as those served by the CLT. Lower-income homebuyers have access, in other words, to two competing homeownership programs. They can either purchase a home and a parcel of land with few restrictions on the property's use and no restrictions on its resale (except, perhaps, for being required to return a portion of the subsidy when the home is resold) or they can purchase a CLT home on leased land with many restrictions on use and resale. If the size of the city's subsidy is similar and the price of the homes is similar, none of the CLT's homes will sell until all of the unrestricted homes have sold. The CLT is set up to falter or fail.

Best Practice: Differentiation among Municipal Programs

A few municipalities, having embraced a three-fold policy shift toward subsidizing homeownership, preserving public subsidies, and preserving the affordability of publicly assisted homes described in an earlier chapter, have made a local CLT the priority recipient of *most* municipal investment in the production or preservation of affordable housing. This is not common, however, nor is it necessary. What is necessary for a new CLT to thrive is being able to access existing programs on terms that do not undermine the CLT's ability to market its resale-restricted, owner-occupied housing. If the municipality is going to continue to subsidize both unrestricted market-rate homes and resale-restricted CLT homes, it would be best for these homeownership assistance programs to be as different as possible, instead of nearly the same. Even better is for the municipality to subsidize homes with permanent restrictions on their use and resale more deeply than homes with no provision for lasting affordability. Buying more through the CLT – more oversight, more affordability, more "backstopping" of publicly-assisted homes and newly-minted homeowners – a municipality should be willing to invest more to make this enhanced form of tenure a reality.

SAM versus CLT in Portland, Oregon

Few municipalities have been more supportive of their local CLTs than Portland, Oregon. But the same city government that played a leading role in helping to start the Portland Community Land Trust in 1999 – and has continued to provide both operating support and project support ever since – promoted, until recently, a ***competing*** homebuyer assistance program to the detriment of the PCLT.

A lower-income household wishing to purchase a market-priced home could receive a shared appreciation mortgage (SAM) of up to $71,000 from the Portland Development Commission, the city's urban renewal agency. Up to $14,000 in additional funding was made available to this same household for necessary repairs. Few restrictions were placed on the use of this subsidized home. No restrictions were placed on the eligibility of the buyer or the price of the home on resale. The homeowner could resell to anyone who was willing and able to pay the full market price. PDC recaptured the amount of its original subsidy out of the proceeds from the sale, along with 25% of any appreciation that had occurred in the property's value. Nothing was recaptured if the homeowner remained in the home for longer than twenty-five years. Either way, the home resold for a market price that no lower-income household could afford to pay.

Meanwhile, the Portland Community Land Trust was developing homes for the same population of lower-income homebuyers, using funding from the Portland Development Commission and the Bureau of Housing and Community Development. These city subsidies reduced the purchase price of a PCLT home by roughly the same amount as the maximum SAM, about $70,000 per home. The PCLT's homes, however, unlike those assisted with SAMs, came with many restrictions on their use and resale in order to protect the homes' occupancy, condition, and affordability. This put the PCLT at a competitive disadvantage. Savvy homebuyers were less likely to purchase a resale-restricted home from the PCLT when they could purchase a market-priced home with the city's help with no continuing obligation except to replenish the city's coffers when the home resold for whatever the market would bear.

Portland discontinued its SAM program in 2007.

4. Sustaining CLT Operations

When it comes to municipal support for a CLT's operations, the issues most likely to generate a degree of discord between the staff of the municipality and the staff of the CLT are the following:

- Can the municipality make a predictable, multi-year commitment to support the CLT's operations?
- What is the most effective and least burdensome way for the municipality to ensure a CLT's performance in exchange for the municipality's support?
- What is the mix of project support and operating support most likely to strengthen and sustain the CLT, especially in the CLT's early years?

Predictable Operational Funding

Regular operating support from a municipal partner is extremely valuable, especially for a young CLT that has yet to grow to the point where it can cover most of its stewardship costs out of revenues that are generated internally. If a CLT can plan on receiving a predictable level of operating support from external sources, the organization's staff can be more aggressive in their growth plans; they can develop new programs much faster; they can offer more stable jobs, enhancing their ability to attract more qualified staff. Operational funding that a CLT can count on receiving from a municipality over a multi-year period can also help the CLT to secure additional funding from other public and private sources, leveraging the municipality's investment many times over.

Municipal Concern: The municipality wants maximum discretion and maximum flexibility in making year-by-year allocations of available housing funds.

CLT Concern: The CLT wants maximum predictability in the revenues that it receives for the organization's general operations.

Worst Practice: Annual Grant Competition

Many municipalities refuse to commit operating funds beyond a single year. Some are actually prevented from making multi-year commitments by their charter or by conditions attached to pass-through funds they are administering on behalf of a federal or state agency. Even when they are not legally prohibited from committing funds for future years, however, munici-

palities often insist on dispensing funds on an annual basis. They either negotiate annual grant agreements with a few favored nonprofit partners or conduct open competitions in which every housing nonprofit must compete against their peers for a share of the city's funding. More experienced municipal staff usually recognize that building the organizational capacity of a young CLT is a multi-year proposition. They know the CLT needs several years of predictable funding if it is likely to show meaningful progress. No organization should be guaranteed funding in the face of poor performance, but time-consuming annual applications for capacity building grants can stand in the way of growing toward sustainable capacity[8].

Best Practice: Multi-year Commitments

Some municipalities that have decided to back a CLT have made a formal or informal commitment to provide a basic level of operating support over a period of several years. Both the municipality and the CLT are able to rely on this multi-year commitment in preparing future budgets and planning future projects. Each year during this multi-year period, municipal officials and the CLT's staff meet to discuss the CLTs progress, identifying mutual goals for the coming year and setting the amount of the grant renewal. If the municipality concludes that the CLT is failing to perform as promised or if sufficient funds are not available, municipal staff may decide to reduce the annual grant, relative to the municipality's original commitment. If the CLT exceeds expectations, however, or makes a convincing case for increased funding, municipal staff may recommend increasing the grant beyond the initial multi-year commitment.9 The City of **Albuquerque's** five-year plan includes providing CDBG grants to the Sawmill CLT for operating support. Initially, the city allocated $150,000 per year for the CLT, but increased its annual grant to $200,000 in 2007 because of the CLT's project success and operational needs.

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[8] The most common argument made on behalf of annual competitions is that they level the playing field, providing for the fair and equal treatment of all potential recipients of a municipality's funding. Precisely because capacity building requires an ongoing commitment of operational funding, jurisdictions have every reason to be careful and fair in selecting recipients and monitoring their progress over time. Once selected, however, recipients should be able to count on ongoing support for a specified period. Annual competitions not only waste the time of the CLT and other would-be recipients; they are unfair to organizations that don't receive municipal support, when the municipality is already predisposed to supporting an organization whose capacity the municipality has been building for years.

[9] **Portland OR** provides an excellent example of this approach. The Portland CLT is a line item in the City's budget and has been assured of on-going operating support over a number of years.

Ensuring Organizational Performance

Some municipalities allow operating grants to be relatively unrestricted, allowing the CLT to use municipal funds on general organizational capacity such as staff salaries, rent and other operating costs. Other municipalities structure operating support more narrowly, asking the CLT to submit a proposal for specific programs and tasks the CLT is expected to complete in a given year, such as predevelopment tasks for specific real estate projects or homebuyer education. Either approach is workable, but the municipality must be clear in declaring what is expected of the CLT and then embody those expectations in its grant agreements and other contracts with the CLT.

Municipal Concern: The municipality wants to assure political leaders, local taxpayers, and federal agencies (if discretionary funds are being passed through) that any recipient of operating funds is producing and performing as promised.

CLT Concern: The CLT wants maximum flexibility in using any funds received from a municipality, with minimal requirements for reporting on these funds.

Worst Practice: Micromanagement of Operating Grants

Operating grants are often provided to CLTs – and to other nonprofit developers of affordable housing – on terms that require recipients not only to use those funds quite narrowly, but to report on their use quite extensively.

Best Practice: Annual Performance Goals

Municipalities act properly and prudently in requiring CLTs to identify a set of annual goals against which the organization's performance can be measured. These goals should allow the grantor to assess whether the CLT has performed as promised, without being so detailed that the CLT is forced to do something that is unnecessary merely to satisfy the terms of the grant agreement. For example, **Bellingham WA** provides annual operating support to the Kulshan Community Land Trust from the city's general funds. In 2006, the city provided $140,000 to support staff salaries and costs related to achieving the following outcomes:

- Initiating new development projects
- Building a Revolving Acquisition Fund
- Increasing homebuyer educational opportunities
- Responding to landowner/developer opportunities
- Working with neighborhoods to identify opportunities to add small homes

Under the terms of the grant, the Kulshan CLT could use the funding for eligible costs including staff salaries and benefits, office overhead, an independent financial audit, and speaker and travel fees. While the specific goals are likely to change annually, the staffing and overhead costs are likely similar year to year as is the level of the jurisdiction's grant.

Mixing Operating Grants and Development Fees

CLTs tend to rely less on project development fees than do many other nonprofit housing organizations. Indeed, many housing nonprofits exist primarily for the purpose of developing new housing, while most CLTs do more than just development. A growing number of CLTs do no development at all, serving instead as the long-term steward for housing produced by nonprofit (or for-profit partners) or for housing mandated by inclusionary zoning. Where CLTs do earn significant development fees, however, there is an obvious relationship between operating grants provided by a municipality and project development fees allowed by the municipality. Both can be used to pay for staffing and overhead. When municipal officials are thinking about how best to support a CLT's operations, it is important to recognize that developer fees are generally considered "at risk" during the development phase. The fees are earned when the project is completed on time and on budget, but may be reduced in the event of cost overruns. This risk provides a strong incentive to CLTs to manage costs and to complete projects quickly. In many cases however, cost increases or project delays are beyond the CLT's direct control. The CLT's projected developer fees can end up being used as a "back-up" contingency, poured into the project. Organizations that rely too heavily on development fees are precarious. Delays in one large project can lead to layoffs or cutbacks which reduce the organization's ability to earn future fees. Operating grants from local government can be the key to a CLT surviving the inevitable ups and downs of the real estate development process. The CLT in **Highland Park IL,** for example, is usually able to take only a $3,000 - $5,000 development fee on the initial sale of each newly-constructed home, less than 2% of the Total Development Cost. The Highland park CLT is able to sustain itself in spite of this relatively low fee because it also receives an annual operating grant from the city's Housing Trust Fund. This grant is used to support the CLT's programs, its fundraising efforts, and its stewardship of homes created through the city's inclusionary housing program.

Municipal Concern: The jurisdiction has an interest in tying funding to completion of successful projects, while ensuring that development fees don't significantly erode affordability.

CLT Concern: CLTs need a reliable source of operating revenue, allowing it to weather the ups and downs of the development cycle.

Worst Practice: Forcing Dependency on Development – and then Limiting Fees

Funders want to make sure that scarce housing subsidies are used to build or rehabilitate housing units and many choose to impose limits on the amount a CLT or other nonprofit developer can charge to a project for its development fee. Without such a limit, the concern is that a CLT could charge too high a fee, increasing the total development cost and ultimately driving up the necessary level of local project subsidy funds. It is important for local governments to acknowledge, however, that if strict limits are placed on the level of development fees which can be charged per unit, then adequate funding for operations must be provided from other sources, such as grants from local government sources

Best Practice: Diversity of Income Sources

Jurisdictions should expect CLTs to rely on a mix of operating grants and development or marketing fees rather than depending on any one source exclusively. Operating funds should not be provided indefinitely to organizations that can never produce results but neither should the availability of development fees be seen as a substitute for ongoing capacity building grants – especially in the early years of a new CLT.

Best Practice: Flexible Limits on Development Fees

Many jurisdictions, rather than setting formal limits on the level of development fees, instead review fees as part of the overall project development budget when awarding funds to a project and then limit the level of subsidy rather than the development fee itself. A proposal may include a generous development fee but the jurisdiction knows that cost increases are a real risk. If the jurisdiction commits to a reasonable level of funding per unit created, any cost increases are likely to decrease the developer fee and any savings will increase it.

Generally the jurisdictions that place the strictest limits on a CLT's ability to charge development fees to project budgets are those that provide the most generous operating support.

For example, Church Community Housing in Rhode Island generally charges a combined development fee and marketing fee of about $7,000 -$10,000 per unit. CCH does not receive grant support for its operations, however, from any of the several small municipalities within which the CLT is working. Similarly, while the City of **Madison WI** does not provide grants to the Madison Area CLT to support operations, it allows the CLT to take a generous development fee of up to 15% of the total project costs on all projects for which the municipality provides funds.

5. Taxing CLT Property

Municipalities have an interest in maximizing revenues from property taxes. A growing number of cities, counties, and towns are also insisting, however, that owner-occupied housing that is made affordable using the municipality's dollars or powers must remain affordable for many years. Since property taxes can erode affordability when they are pegged to a property's market value instead of its affordable price, a municipality committed to lasting affordability must make a choice: either increase the level of its own subsidies, giving out with one municipal hand while taking back with another, or adjust its assessment of resale-restricted homes – not removing property from the tax rolls, but recognizing what the New Jersey Appellate Court once called the "patent burden on the value of the property."

CLTs and local taxing authorities have been working together to negotiate assessments that allow the jurisdiction to collect a fair level of property taxes to support the services provided by local governments without undermining the initial and continuing affordability of the CLT's homes. Achieving a fair assessment of CLT lands and resale-restricted homes can be a challenging and protracted process, however. Local assessors are sometimes unsure of what is permissible under state law, so conservatively decide they are unable to accommodate the special circumstances of the CLT's treatment of land and housing. Other assessors, with or without state guidance, labor mightily to consider the impact of long-term land leasing, lower lease fees, and durable resale restrictions and come up with very different methods for valuing and taxing CLT lands and CLT homes in their communities.

Municipal Concern: Municipalities have an interest in protecting their tax base, ensuring that all homeowners pay their fair share of local property taxes.

CLT Concern: CLTs have an interest in protecting the affordability of their homes, ensuring that low-income homeowners pay property taxes that take into account the long-term resale restrictions on their property.

Worst Practice: No Adjustment for the Encumbered Value of CLT Homes

There is no attempt at balancing the competing concerns of the municipality and the CLT when a municipal assessor systematically ignores the "patent burden on the value" of lands and buildings under a CLT's stewardship. Although fewer now than in the recent past, there

are still many assessors who look at a CLT home selling for $100,000, despite being appraised for twice that amount, and proceed to enter that home on the local tax rolls at a value of $200,000. There are assessors who look at a parcel of CLT land leased by a low-income homeowner for 99 years at $25 per month, despite being worth four times as much, and proceed to enter that land on the local tax rolls at a value reflecting a market-rate rent of $200 per month. There are assessors who look at the contractual restrictions encumbering the resale and subletting of a CLT home and proceed to increase the value of that home at a rate of appreciation equal to that of a market-rate home without these encumbrances. The worst practice is to force CLT homeowners to pay taxes on property values that will never be theirs.

Taxation of Resale-Restricted Housing in New Jersey

In the 1989 case of Prowitz v. Ridgefield Park Village (568 A.2d 114) the New Jersey Appellate Court upheld the lower taxation of resale-encumbered property, stating: "The deed restriction limiting resale price constitutes a patent burden on the value of the property, not on the character, quality or extent of title. It is, moreover, a restriction whose burden on the owner is clearly designed to secure a public benefit of overriding social and economic importance, namely, the maintenance of this State's woefully inadequate inventory of affordable housing."

Although long-term control over the resale price was imposed by a deed restriction instead of a ground lease in a New Jersey case, the court's reasoning is "on point" for the taxation of CLT homes. The opinion of a New Jersey court is, of course, not binding on the courts of other states. Even so, when CLTs have provided local assessors with a copy of the written opinion from Prowitz v. Ridgefield Park Village many have agreed that the reasoning is sound.

Worst Practice: Unpredictable Adjustments

Even when assessors acknowledge "the patent burden on the value" of leased lands and resale-restricted homes in a CLT's portfolio, there must be a clear and consistent strategy for quantifying this "burden." While any downward adjustment in the assessed value of a CLT's property is going to be welcome, since it eases the tax burden borne by a CLT's low-income homeowners, such adjustments must be based on a defensible rationale and systematic methodology. A CLT needs to be able to predict how any newly developed housing will be valued by the local assessor in order to factor the cost of property taxes into its affordability

calculations in pricing, financing, and selling its resale-restricted homes.[10] A CLT's homeowners need to anticipate how their taxes are likely to rise over time. A jurisdiction's taxpayers and policy makers need to understand why it is reasonable, legal, and fair for a resale-restricted home on land that is leased for a below-market rent from a CLT to be taxed at a lower rate than a comparable market-rate home. Case-by-case adjustments, based on calculations and criteria understood by the assessor alone, are almost as bad as no adjustments at all.

Best Practice: Fair Taxation Based on Restricted Values

There are a number of strategies and methodologies for equitably taxing a CLT's lands and homes for balancing the concerns of both the municipality and the CLT, of the best practice is to assess the CLT land based on the income stream from ground lease fees, to assess the homes based on the initial below market price to the homebuyer and to increase that assessment no faster than the rate of increase in the formula resale price.

- ***Value of the Homes:*** The assessed value of any buildings that are located on the CLT's land should reflect the perpetual restrictions that the CLT's ground lease has imposed on the use and resale value of these buildings. Thus, the building's assessed value should be lower than the assessed value of a similar building that is not so encumbered. Because it is unlikely that a reasonable person would ever pay more than the CLT's affordable formula price for a restricted unit, this formula price is generally the best indicator of the "fair value" of a CLT home.

- ***Value the Land:*** The assessed value of the CLT's land should never be more than the Net Present Value of the income stream which the CLT can collect from a parcel of land in monthly fees over the term of the lease. Given that the ground lease fees are usually far below a market rent, the value of CLT land should be far below its market value. This valuation should only increase as the ground lease payments increase.

- ***Rate of Increase:*** The formula-determined price of a CLT home, under most resale formulas and under most market conditions, tends to rise on a trajectory that is lower and flatter than the trajectory followed by market-priced homes without resale con-

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[10] For example, the resale-restricted condominiums in the portfolio of the Orange Community Housing and Land Trust are assessed at less than their full market value by the Town of **Chapel Hill NC**. OCHLT staff gratefully acknowledge that this reduced rate is both beneficial and welcome. These reductions have been granted on a case-by-case basis, however, with little understanding on OCHLT's part as to the formula used by the local assessor in determining the taxable value of the CLT's homes. This creates an uncomfortable level of unpredictability when OCHLT is developing a project and selling homes. As one staffer put it: "we would love for there to be a formula so that we could tell people and explain it to people" before they are asked to buy a resale-restricted home.

trols. Post-purchase adjustments to the assessments and taxes of CLT homes should take these long-lasting controls into account. Ideally, tax assessors should calculate the maximum price for which a CLT home could sell, based on the resale formula appearing in the home's ground lease, and adjust the home's assessed value accordingly.

Taxation of Resale-Restricted Housing in Vermont

In 2008, the Vermont Department of Taxes issued Technical Bulletin 41 (TB-41), recommending a "uniform approach for determining the listed value of owner-occupied homes subject to perpetual resale restrictions." Although the specific methodology proposed for calculating the value of such resale-restricted housing was needlessly complex, its underlying rationale was quite straightforward. In the Bulletin's words: "These homes remain affordable to future buyers because the owner's resale price is restricted and public grants that assist buyers in purchasing the properties remain with the property, thereby reducing the price of the property for a subsequent buyer(s). . . . The Department interprets Vermont law to require municipalities to list these properties at a value that reflects the restricted equity that the owner of such property has upon resale."

Best Practice: Fair Taxation Based on Reasonable Tests

The guidance given to local assessors in the valuation and taxation of resale-restricted housing varies greatly from state to state. The question of whether resale-restrictions impose a "patent burden on the value of the property" has sometimes been settled by a state court, sometimes by a state legislature, and sometimes by a state board of equalization. More often, it has been left to local assessors to decide for themselves ***whether*** to recognize the affordability restrictions contained in the ground leases of a CLT or in the deed covenants used by other forms of shared equity housing and to decide ***what*** the encumbered value of these homes should be. Across the country, these decisions have rested on a series of "tests" of eligibility for a decrease in value that most CLTs have been able to pass. The most reasonable of these tests, either imposed on local assessors by their respective states or invoked by local assessors in exercising the discretion granted to them by their respective states, are the six that follow.

Diminished return: the monetary return that the owner can derive from a parcel of real property must be significantly reduced as a result of the contractual restrictions that encumber the property. This should be an easy test for a CLT and its homeowners to meet.

The CLT's ability to realize market-rate returns from leasing its lands is limited by the long-term leases it has signed with its lessees and the homeowners' ability to realize market-rate returns from subletting or reselling their homes is limited by the same lease.

Duration: affordability controls cannot be "impermanent"; they must endure for many years.[11] The 99-year term of the typical ground lease, restricting returns to the landowner and the homeowner alike, should easily enable a CLT to meet this test.

Irrevocability: affordability controls must irrevocably bind both current and future owners and must have a high likelihood of remaining in force during the entire control period. Most CLT's should be able to pass this test. Except in the case of foreclosure, where affordability controls may be terminated, the CLT's restrictions over use and resale are likely to remain binding and enforceable for the entire term of the lease.[12]

Disclosure: affordability controls must be disclosed to the prospective buyers of a resale-restricted home; they must fully understand and freely accept these controls as a condition of purchase.[13] CLTs that do a careful job of orienting and preparing would-be homebuyers for the purchase of a CLT home should have no trouble passing this test.

Recording: affordability controls must be embedded in covenants, ground leases, or other contractual documents that are recorded in the local land records. Since most CLTs record a long form or short form of their ground lease for every home in their portfolio, this test is usually met.

Public benefit: the affordability controls must benefit the public. As the NJ Appellate Court put it in the Prowitz case: "It is not a potential benefit to any specific affordable housing owner with which the resale restriction is concerned, but the benefit to the public

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[11] Different states have adopted different standards in deciding when the duration is "long enough" to qualify for a lower assessment. For example, Vermont expects restrictions to last for 99 years. In New Jersey, a 30-year restriction is "long enough."

[12] Should foreclosure result in the home being resold by the lender for its full market price – and should the CLT then begin charging a full market rent for the underlying land, which is permitted under the model ground lease – the home and the land would both be reassessed, allowing the municipality to collect taxes commensurate with the property's unrestricted market value.

[13] In the Massachusetts tax case of *Truehart v. Montegue Assessors* (Appellate Tax Board Docket Nos. 198055-57, April 21, 1999), disclosure was part of the Tax Board's rationale for ruling that resale restrictions must be considered in arriving at the "fair cash value" of homes to which the Massachusetts Housing Finance Agency had attached affordability covenants: "A willing, informed buyer of the subject properties is presumed to know that he or she must grant MHFA a right of first refusal and that he or she will be limited to a maximum resale price based on the discount rate applicable to the property."

that is vouchsafed by indefinitely maintaining that unit in the affordable housing stock." To the extent that either state policy or municipal policy has explicitly recognized the economic and social importance of maintaining a stock of affordably-priced housing for persons of modest means, a CLT should have no difficulty passing the test of public benefit. The same should be true in jurisdictions where resale controls have had a public genesis – that is, where such controls are required by a public agency or imposed by a public agency. Only in jurisdictions where public policy and public practice do not favor the preservation of affordability should CLTs have to work harder to convince local assessors that resale controls provide a lasting benefit for the public at large.14

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14 The State of New York, through its Office of Real Property Services, has made the opposite argument in ORPS Opinions 10-34, characterizing resale restrictions as a "private benefit." Because the homeowner personally benefits from the use of a resale-restricted home and because the homeowner has realized a personal "windfall" in purchasing a home for at a below-market price made possible by public subsidies, ORPS asserts that most of the benefits derived from restricting a home's resale price are derived by the home's owner. Furthermore, the owner *chose* to buy the home, voluntarily accepting the resale controls encumbering it. These restrictions are "personal to the owner," in the opinion of ORPS, not a benefit to the public. Courts, tax departments, and boards of tax equalization in a number of other states have reached the opposite conclusion, agreeing with the *Prowitz* decision that resale controls are "clearly designed to secure a ***public*** benefit of overriding social and economic importance."

6. Regulating CLT Activities

A municipality's oversight of a CLT's activities can occasionally clash with the CLT's relationship with its own homeowners. Such oversight can also clash with other interests or priorities of the CLT. To whatever extent the CLT is expected to perform monitoring and administrative functions "on behalf of" the municipality, the two parties must negotiate a common set of policies that serve their separate and mutual needs. The municipality must then ensure that the CLT implements these policies. Among the more challenging issues are the following:

- Does the municipality rely entirely on the CLT to perform these functions?
- Which options for protecting the municipality's interests are the least likely to interfere with the CLT's interest in securing private financing for its projects and its homeowners?
- What is the municipality's flexibility (or rigidity) in requiring the CLT to "guarantee" the future affordability of its resale-restricted, owner-occupied homes?

Regulating the CLT's Homeowners

Municipalities that provide significant subsidies to make homeownership units affordable to lower income households have a responsibility to ensure that those resources are appropriately used and that the occupancy, condition, and affordability of publicly-assisted homes are permanently preserved. Sometimes attorneys representing local governments will argue that the municipality can only meet this obligation by having a direct regulatory relationship with homeowners. CLTs argue, on the other hand, that the municipality's regulatory relationship should be with the CLT, allowing the CLT to bear primary responsibility for monitoring municipal requirements for the continuing occupancy and affordability of these assisted homes.

Municipal Concern: A municipality may want to establish a direct contractual relationship with assisted homeowners, thus retaining the option of directly enforcing the use and resale controls that encumber those homes.

CLT Concern: The CLT has an interest in maintaining a direct and equitable relationship with its homeowners, one that is not modified or mediated by another party.

Worst Practice: Pricing Homes to Match the Maximum Eligibility of Homebuyers

There is a necessary and important distinction to be made between the percentage of Area Median Income that is used in setting the ***price*** of a CLT home and the percentage of AMI that is used in setting the ***eligibility*** of the CLT homebuyer. Too often, this distinction is blurred, leaving these maximums to be set at the same level. The CLT then finds itself with a marketing nightmare, where it may be required by a municipality to price its homes to be affordable to households earning exactly 80% of AMI and to sell those homes only to households earning no more than 80% of AMI. Pegging price and eligibility to the same percentage of AMI results in too small a pool of prospective homebuyers.[15]

Worst Practice: Double Regulation of Homeowners

Some municipalities insist on recording covenants or deed restrictions against the CLT's homes, supplementing – and usually duplicating – the regulatory agreements the municipality has already executed with the CLT. Homeowners are then regulated by both the CLT's ground lease and the municipality's covenant. At best, these double documents contain similar provisions. At worst, they contain provisions that confuse or contradict the meaning of each. Indeed, in at least one case, a municipality was discovered to have recorded a covenant on a CLT home that contained a resale pricing formula very different than the one contained in the CLT ground lease.[16]

It seems unrealistic to expect buyers truly to understand the myriad restrictions contained in multiple regulatory documents. While direct (and redundant) regulation might make it easier for the municipality to act should the CLT fail to perform as promised, the enforceability of resale restrictions relies, to a significant degree, on both the clarity and consistency of the contracts containing these restrictions and the informed consent of the persons who are signing these contracts. When different – and sometimes conflicting – provisions are scattered among a number of regulatory documents, the opportunities for misunderstanding, conflict, and legal challenge tend to multiply.

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[15] A better practice, under this scenario, would be for homes that are limited to eligible buyers earning 80% of AMI or less to be priced so that buyers earning 70% of AMI could afford them, broadening the pool of eligible buyers.

[16] A court would have to decide, in this case, which of the two resale formulas should take precedence, with the municipality possibly arguing for the formula yielding the lower price and the homeowners arguing for the formula yielding the higher price.

Best Practice: Regulate the CLT, Not the Homeowner

The best way for a municipality to ensure that CLT homeowners comply with the municipality's own requirements for the continuing occupancy, condition, and affordability of municipally-assisted housing is to require the CLT to include these requirements in the ground lease that the CLT executes with each of its homeowners. This approach can necessitate an initial investment of time, for the municipality must identify any requirements imposed by its ordinances, regulations or funding sources and then negotiate with the CLT to ensure that the CLT's lease contains the language necessary to satisfy all municipal requirements. For example, if municipal regulations limit subletting to no more than three months per year, a lease that allows subletting for only two months might be acceptable, while one allowing six months of subletting would have to be modified.

In exchange for project subsidies, a municipality will typically insist on the right to approve the CLT's ground lease and any subsequent amendments to the lease. Some jurisdictions have specified in their grant agreements or loan agreements certain key terms and key provisions that the CLT ground lease must contain. Rather than regulating and monitoring individual homeowners, in other words, the municipality regulates and monitors the CLT, watching to make sure the CLT enforces restrictions of most concern to the municipality. If the CLT ever fails to take appropriate action, the municipality retains the right to step in to protect its interests. This indirect regulation of homeowners may take slightly more time to implement for the first CLT project, but the resulting structure is far easier for all parties to understand and much easier to administer over the long term. A single document, the CLT ground lease, contains all of the relevant provisions protecting the public's interest in the home. As the home subsequently sells from one lower-income owner to the next, only this one document needs to be assigned or re-executed.

Best Practice: Back-up Notice to the Municipality

The Model CLT ground lease requires homeowners to notify the CLT whenever they decide to resell their home. The lease also gives the CLT a preemptive option for a period of time to purchase the home for the formula price. Once this notice is received, the CLT typically has 45 days to indicate whether it will exercise its option and then purchase the home or assign the option to an income-eligible homebuyer. Some municipalities, fearing the CLT might fail to act during this critical period, have suggesting that perhaps the CLT's homeowners should be required to notify the municipality, as well as the CLT, of their intent to sell. A better solution has been developed by the City of **Santa Monica CA.** Santa Monica requires the own-

ers of CLT homes to notify the city of their intent to sell and to offer the city an option to purchase their homes at the formula-determined price – but only in the unlikely event that the CLT fails to respond to the first intent-to-sell notice submitted by the homeowner to the CLT. Municipal staff are thus freed from the burden of receiving routine notices they do not need to act upon, but they are still able to step in and take effective action to preserve the affordability of CLT homes if the CLT falters or fails

Municipal Options for Enforcement

Generally, a loan secured by a mortgage or deed of trust will give the lender the option to force the sale of the land through foreclosure if the borrower defaults on its obligations. In the case of a deferred payment, forgivable municipal loan for a CLT project, the municipality would typically foreclose only after the CLT had committed a fairly serious violation of the terms of the loan agreement and had failed to take necessary steps to correct such a violation. Although unlikely that a municipality would ever foreclose on such a loan, some municipalities find this worst-case protection reassuring. Certainly the threat of foreclosure may provide additional motivation to the CLT to comply with the terms of the loan.

Consider, however, the position of a CLT's homeowners and the private lenders from whom they are hoping to secure a mortgage. The value of a homeowner's property is dependent upon the rights conveyed through the 99-year ground lease. Were the CLT to fail and were a new landowner to take title to the land and terminate the lease, the homeowner's property would be worthless, since the home is affixed to the land. When a municipality wants to record a lien on the CLT's land, therefore, the homebuyers and their mortgage lenders need to be assured that, if the municipality were ever to foreclose on the land, the ground lease would survive and the new landowner would be bound by all of the terms of the ground lease.

To this end, Fannie Mae has developed a Uniform CLT Ground Lease Rider which was designed to protect the interests of both the homeowner and the first mortgage lender. Fannie Mae will only approve liens on a CLT's land when such liens benefit a state or local governmental entity and when there is a nondisturbance clause with respect to the ground lease.[17]

[17] The FNMA rider does not prohibit liens on the land that are subsequent to the execution of the lease, but it does prohibit the lessor and the lessee from ***subordinating*** the lease to such liens.

Municipal Concern: A municipality wants to be able to compel the CLT to comply with performance standards contained in a grant agreement or loan agreement. In the event of the CLT's failure or dissolution, the municipality wants to protect its investment in the CLT's land and housing.

CLT Concern: The CLT wants to ensure that its homeowners have access to mortgage financing and that homeowners are protected from the negative consequences of the CLT's failure or dissolution.

Worst Practice: Municipal Loans with Boilerplate Documents and Superior Liens

A number of municipalities have recorded mortgages or deeds of trust against a CLT's land as security for their investment in a CLT's projects. In too many cases, municipalities have used legal documents that were originally drafted for loans on rental housing, without modifying them to reflect either the special nature of the CLT model or the important interests of homeowners and their lenders. Since these liens are generally recorded ***before*** the CLT ground lease, subordinating the lease to the lien, foreclosure under these loans could effectively terminate the CLT lease. The ability of a CLT's homeowner to obtain mortgage financing under these conditions is made difficult or impossible (although some mortgage lenders have failed to notice the danger a superior lien can pose to their security and have proceeded with the loan.)

Better Practice: Loan Agreement Protecting Homeowners' Interests

A municipality that is planning to donate a large tract of land or to invest a large amount of money in a CLT project wants to be in a strong position to recover its investment in the event of a CLT's failure. A well-designed loan agreement can protect the municipality's interests without jeopardizing either the homeowners' access to mortgage financing or the homeowners' security of tenure, should the CLT fail.

Best Practice: Grants Secured by Covenants

Although structuring a local government's subsidy in the form of a loan secured by the CLT's land has been made to work in some jurisdictions, a governmental lien on the land adds undesirable barriers and complications to homebuyer financing, while providing very little additional security for the municipality. Loans recorded against the CLT land also have a negative

impact on the CLT's balance sheet because the loans must be listed as liabilities. The land securing these loans is generally booked at a greatly reduced value, moreover, because of the CLT's long-term lease. Many CLTs and their municipal partners, therefore, have concluded that grant agreements coupled with covenants or deed restrictions can protect the municipality's interests as well as loans – with fewer problems for the CLT.

A number of municipalities have, in fact, combined grant agreements and covenants to give a municipality a range of options for curing a CLT's failures. As one example, **Orange County NC** provided housing bond funds and HOME funds to the Orange Community Housing and Land Trust (OCHLT) for a 32-unit development in Chapel Hill, NC. Orange County and OCHLT executed both a Development Agreement outlining OCHLT's project development responsibilities and a Grant Agreement spelling out the CLT's long-term obligations in maintaining the occupancy and affordability of these units. The County then required OCHLT to record a Declaration of Restrictive Covenants which secures performance of the requirements of the other two documents, requires OCHLT to preserve affordability of the units through a 99-year ground lease, and declares both the County and the Town of Chapel Hill to be "third party beneficiaries of and successors to each and every remedy intended to insure the long term affordability of the housing" The Declaration further stipulates that :

> *"each may, in the event of the failure or default of the Lessor in each such ground lease to insure the long term affordability of the housing unit as provided for in the ground lease, exercise all rights and remedies available to the Lessor in the ground lease for that purpose."*

Other municipalities have incorporated similar rights to intervene in their own grant agreements and covenants. The common goal here is to give the municipality the opportunity and authority to do more than simply require repayment of a municipality's money. The municipality needs to be able to take direct action to protect the security and affordability of the homes created with the municipality's assistance.

Ensuring Affordability in the Face of Rising Costs

Many municipalities decide to support a CLT because of the model's past performance and future promise of preserving the affordability of publicly-assisted, privately-owned housing across successive generations of income-eligible homebuyers. A CLT's resale restrictions combat the greatest threat to ongoing affordability – land values that appreciate more quickly than wages. Even when price appreciation is limited, however, a number of other factors can erode the future affordability of CLT homes. Rising insurance or utility costs, for example, ris-

ing property taxes or, even more critically for future homebuyers, rising mortgage interest rates can drive up the monthly cost of even an affordably-priced home. These are costs that are outside the purview of most resale formulas and beyond the control of the CLT.

A municipality and a CLT share a reasonable expectation that the resale prices of CLT homes will remain relatively affordable for the same targeted group of income-eligible homebuyers for many years. When mortgage interest rates or other operating costs rise rapidly, however, the price produced by a CLT's resale formula may be significantly below a home's market value, but still remain out of reach of a lower-income homebuyer.

Municipal Concern: Municipalities want CLTs to perpetuate the affordability of publicly-assisted homes, keeping resale prices permanently within the financial reach of lower-income homebuyers.

CLT Concern: CLTs have the same interest in preserving affordability, but they may sometimes need supplementary assistance from a municipal partner in coping with factors beyond their control that can erode the affordability of resale-restricted homes.

Worst Practice: Guaranteed Affordability for Future Resales

Some municipalities, in their quest for permanent affordability, require a CLT to ***guarantee*** that publicly-assisted CLT homes will stay affordable forever for future homebuyers earning no more than a targeted percentage of the local AMI and paying no more than a specified percentage of the household's annual income. A guarantee of ***initial*** affordability on the pricing of a new CLT home is both reasonable and achievable. A guarantee of ***permanent*** affordability is not, since affordability can be affected by more than the rising value of land and housing – the one factor entirely within a CLT's control. A municipality's insistence on a CLT guaranteeing affordability forever becomes especially problematic (and indefensible) when this requirement is imposed on a CLT but not on other recipients of municipal aid.

Best Practice: Shared Responsibility for Maintaining Affordability

The best way to balance the competing concerns of the municipality and the CLT is for the parties to ***share*** long-term responsibility for ensuring that publicly-assisted, resale-restricted homes remain affordable in perpetuity. When mortgage interest rates or other operating costs make a CLT home ***un***affordable for future buyers, despite the below-market price produced by the CLT's resale formula, the CLT has three options:

1. secure additional public or private subsidies to allow the CLT to push the home's purchase price even lower than the below-market price determined by the resale formula;
2. require future homebuyers to pay a slightly higher percentage of their income; or
3. set the income eligibility for future homebuyers at a slightly higher level than was required for the previous generation of CLT homebuyers. [18]

Without guaranteed access to future subsidies, however, or without the flexibility to adjust the eligibility requirements for future buyers, CLTs cannot absolutely ensure that their resale-restricted homes will always be within the financial reach of this targeted group of lower-income homebuyers.

[18] It would also be possible, as a fourth option, for a CLT's resale formula to require homeowners to reduce their resale prices to an "affordable" level in this circumstance, a requirement implicit in the mortgage-based resale formulas mandated by some municipalities. Most CLTs (and most municipalities) choose not to impose this kind of requirement because it can result in homeowners receiving very little equity at resale. It can even result in lower-income homeowners being forced to resell for ***less*** than they initially paid for their homes. Without imposing this unacceptable risk on their homeowners (and their mortgage lenders), however, CLTs have no way to guarantee that prices will ***always*** meet an affordability standard that requires homes to resell for a price that is within the reach of households at a targeted level of income, no matter what happens to interest rates, utility rates, etc.

A Partnership for Permanent Affordability in Chapel Hill

The Town of Chapel Hill requires the Orange Community Housing and Land Trust to sell its municipally-assisted homes to households earning less than 80% of Area Median Income. These homes are initially priced so that homebuyers earning 70% of AMI must pay no more than 30% of their monthly income, including mortgage, property taxes, insurance, and the CLT's land lease fee. (By pricing to 70% rather than the maximum 80%, the CLT has a wider range of potential buyers and some ability to absorb future increases in interest rates or other housing costs.) At resale, the CLT calculates the maximum sale price according to the formula included in its ground lease. The Town has reviewed and approved the use of this specific formula and has reason to expect that, under most circumstances, future buyers earning 80% of AMI or less will be able to afford homes that are priced in this manner. The Town's Performance Agreement requires OCHLT to make sure that its homes are always sold to buyers who earn less than 80% of AMI. Any sale to a higher income household would constitute a violation of the Agreement. But the Town also recognizes that OCCLT's resale formula is not, by itself, a guarantee of permanent affordability. If the resale formula fails to perform as promised or if other costs or conditions inflate the resale price of an OCCLT home beyond what a household at 80% of AMI could afford, the Agreement requires OCCLT and the Town Manager to consult with each other before either takes action.

This provision recognizes the Town's and the CLT's mutual commitment to maintaining affordability, without requiring the CLT to promise more than it can deliver. It encourages the Town to work cooperatively with the CLT to resolve what is likely to be a temporary affordability problem.