# Housing Cooperative FAQ

***Caveat: Please be aware that this statement is not a legal document. However, it does represent the considered position of the Hart's Mill community that consented on January 28, 2016, to move forward with an intention of establishing the eventual dwelling units in the Hart's Mill Village as a Limited-Equity Housing Cooperative. The purpose of this FAQ is to assist Hart's Mill members and potential members in understanding what this intention means. Most papers/books about cooperative housing favor & promote the concept, and that enthusiasm also finds its way into this FAQ (although promoting the concept is not the purpose of this document). Also note: this document pertains to the village portion of Hart's Mill Village & Farm. Farm issues are not part of the discussion here.***

**What is a housing cooperative?**

A housing cooperative is a business, a cooperative corporation, formed under and complying with state statutes.* It is a legally-defined form of home ownership based on clear historical precedent, principles and operational obligations. The cooperative corporation holds title to the dwelling units and directly assumes the mortgage, tax and other obligations necessary to finance and operate the development.

> * In North Carolina support is found in Subchapter IV, Cooperative Associations, NC General Statutes. There are a small number of requirements to be recognized as a co-op under this statute, but Hart's Mill should have no difficulties meeting these requirements. See reference 22. Mention also appears in the NC Nonprofit Corporation Act, Chapter 55A, Article 13, Section 55A-13-02(3).

The purpose of a housing cooperative is to own and operate residential housing exclusively for the benefit of its members. It is an enterprise formed by a group of people to meet their own self-defined housing goals. It is member-owned, member-run, and member-serving.

As an entity that owns property, collects income, and incurs expenses, the co-op must be a formal organization. It must operate in conformance with standard business practices, and it must maintain records according to accepted accounting procedures.

Thus, a housing cooperative is a form of joint ownership established through a corporate entity. It is created when people voluntarily join together to own and control the housing and/or related community facilities where they live. Together, members own 100% of the cooperative, while the cooperative owns 100% of the buildings, land*, and other common areas. Members support the corporation through on occupancy agreement (see below), eliminating the need for each member to be an individual mortgagor.

> * For purposes of this document, our Hart's Mill land is assumed to be part of the total real estate owned by the co-op. However, this is not a requirement of the co-op model. For example, the land could be owned and managed by another entity – e.g., a Community Land Trust (CLT) – and then leased to the co-op entity, which in turn would lease the residential dwellings to co-op members as described below.

For a hypothetical Hart's Mill Housing Cooperative Association (HMHCA), you (yes, you) would become a member of the co-op by purchasing a share in the business. By virtue of your membership, you are entitled to lease one of the cooperatively owned residences and have a voice in the corporation's affairs. Your share purchase entitles you (indeed, obligates you) to participate in overall governance of the co-op. As a co-op member, you have a say on how community needs and costs are managed, including electing the board of directors, amending the co-op bylaws (and other co-op documents), making decisions about the use and disposition of the cooperative's property, etc. It is a form of generative ownership that Marjorie Kelly, fellow at the Tellus Institute, calls "stakeholder ownership" – ownership by people with a *human stake* in the enterprise, as opposed to a purely financial stake (see reference 27, p. 141). In the interest of efficiency, day-to-day decisions generally rest with a co-op Board of Directors, discussed below.

Again, being a share owner gives you the exclusive right to reside in a particular dwelling unit that is owned by the cooperative corporation. This unit is allocated solely to you, and the arrangement is governed by your "proprietary lease" (or occupancy agreement). This right to occupy a specific dwelling unit continues so long as you remain a member of the cooperative in good standing and abide by the terms of the occupancy agreement. Then, each month, as a member of the Hart's Mill Housing Cooperative, you would pay a fee ("carrying cost", described below) to cover your portion of the cooperative's operating expenses and other costs.

So housing co-ops are set up as business corporations. They are in business solely to provide the best possible housing at the lowest possible cost for its members. Further, they are unique businesses in two respects. First, they are operated exclusively for the benefit of their members. But second, and equally important, co-ops are *a way of doing business*. They are democratic organizations, and all members participate in the activities of the co-op. Quoting Coughlan & Franke (Reference 3, p. 187): "If there is one thing that distinguishes co-ops, it's participation. By *participation* we mean that members are active both in the business management of the co-op and in the social activities the co-op may sponsor. We also mean that participation goes beyond the formal decision-making structures. Participation is the social energy for the co-op; it's the members' responsibility."

Every co-op, regardless of its size or type must exhibit certain characteristics to be called a housing cooperative.* That is, we use the term "housing cooperative" here in a very particular and legal sense. The language means something far more precise than simply asserting that people are living with one another “cooperatively”. Said another way, the term housing co-op should not be reflexively identified with multifamily housing arrangements such as definitionally-vague cohousing or ecovillage structures – although certainly either of these two general forms of multifamily living can be accommodated within a housing cooperative structure. Contrasts to housing co-ops include standard rental housing and condominium developments, both of which are discussed below.

> * These general characteristics are the whole point of this FAQ. Individual co-ops, of course, will vary in their underlying structure, management style, covenants, bylaws & occupancy agreements, and some deviate significantly from the basic characteristics discussed here. Typically variations from the basic characteristics emerge as a new co-op begins to form and define itself. Hart’s Mill would have to find and elaborate its own particular course.

This perhaps is perfectly clear, but let’s repeat it. If we were to organize Hart’s Mill in a way that emphasized cooperative ways of living but actually structured our legal organization in some way other than a housing cooperative (e.g., as a condominium, or a Limited Liability Company) we would not be a co-op under state statute.

Housing cooperatives are not well-understood or widely employed in many parts of the U.S., including North Carolina. Their popularity tends to be high in selected states and metropolitan areas. An extreme illustration: roughly 75% of the housing inventory in Manhattan is comprised of co-ops (see reference 8).

**What would I actually own if Hart’s Mill were to adopt a housing co-op model?**

You would own a share interest in the cooperative business, the Hart’s Mill Housing Cooperative Association (HMHCA). The purpose of HMHCA would be to best serve the housing needs of its members within the envelope of overall financial (and legal) constraints. As a co-op, its role is to meet the needs of its shareholders (you & me) while keeping the co-op financially sound and running smoothly and legally.

In an *indirect* way, you actually do “own” the home in which you live because that ownership comes to you through your membership in the co-op. That is, you belong to a business that owns *all* the property. But you do not own “your” home in the traditional sense of homeownership. Thus, the main distinction between a housing cooperative and other forms of home ownership is that in a housing cooperative you don’t *directly* own any real property.* Rather, you are buying a share (a membership, if you will) in a cooperative housing nonprofit corporation. The corporation owns and leases all real estate. As described above, your membership (as a shareholder) in the cooperative provides an exclusive right to live in a specific unit for as long as you wish, provided you adhere to the cooperative’s rules and regulations and meet your financial obligations to the co-op.

* Technically, you own *personal* property (a share in a business), not *real* property (as in real estate).

One way to think of it is like this:  You are simultaneously both the “lessor” of the real estate (by virtue of your ownership share in the business) as well as the “lessee” of your particular dwelling (by virtue of your occupancy agreement with the cooperative).

**What does my share or membership purchase price involve?**

When you buy a share or membership in a housing cooperative, you are paying for just that: a single share of the cooperative housing corporation.  The initial purchase price of a share is largely determined by (1) the overall financial projections of the co-op (sometimes called the “pro forma”) and (2) the number of members of the co-op.  That is:  total costs divided by the number of people covering those costs.  Different housing co-ops structure the share price in different ways.  Many co-ops have a fixed share price and then vary the monthly fees from unit-to-unit depending on the unit’s size, the size of the lot on which it sits, or other amenities.  Occasionally, co-ops build these differentials directly into the share price itself.

**Sounds a bit like renting.  Why is being a cooperative member better than being a renter?**

Here’s a little table to assist in answering this question:

| | ***Cooperative*** | ***Rental Unit*** |
|---|---|---|
| ***Ownership*** | Members own the cooperative | Landlord owns the rental unit |
| ***Control*** | Members govern the cooperative | Landlord governs the rental unit |
| ***Work Requirements*** | Co-op can set forth work expectations for its members | Lease defines the responsibility of the renter regarding maintenance |
| ***Costs*** | Occupancy charges are equal to the actual cost of owning & operating the property.  Co-op members keep any profit | Rents go up faster than actual costs because the landlord is in business to make a profit.  Landlord pockets the profit |
| ***Interview Prospective Residents*** | Co-ops may (generally do) interview prospective residents for compatibility with goals | Landlord generally will screen prospective residents |
| ***Individuality*** | The cooperative allows members to customize their dwelling units | Landlord controls everything in the rental unit |

| | | |
|---|---|---|
| ***Taxes*** | Cooperative passes income tax deductions through to its members | All income tax benefits of rental properties go solely to the landlord |
| ***Equity Growth*** | Cooperative passes equity growth to its members (often with limits) | Equity growth benefits only the landlord |
| ***Overall Value*** | A cooperative maximizes benefits to its members | A rental unit maximizes profits to the landlord |

**And how about the comparison between co-op living and purchasing a condominium?**

There a many comparisons available on the Internet. See, for example, just a few in the references at the end of this document. But here's a table similar to the one above:

| | ***Cooperative*** | ***Condominium*** |
|---|---|---|
| ***Ownership*** | Members own the cooperative | Resident owns the space inside the walls of the dwelling unit and an undivided share of any common facilities |
| ***Control*** | Members govern the cooperative | Condominium association governs the rental unit |
| ***Work Requirements*** | Co-op can set forth work expectations for its members | Residents generally are not held to work requirements; costs of maintenance of the complex are built into the condo association monthly fees |
| ***Interview Prospective Residents*** | Co-ops may (generally do) interview prospective residents for compatibility with goals | Condominium association generally does not interview prospective residents |
| ***Costs*** | Occupancy charges are equal to the actual cost of owning & operating the property. Co-op members jointly keep the profit. There are very few | Costs within the dwelling unit are the responsibility of the owner. Costs to the exterior of the units and costs related to common areas are |

| | | |
|---|---|---|
| | charges relating to changing dwelling units or joining/departing the community | shared by condo owners. Owner keeps the profits. Several standard transfer fees are involved with purchasing/selling the unit |
| ***Individuality*** | The cooperative allows members to customize their dwelling units | Condo owners usually may customize the inside of the dwelling unit |
| ***Taxes*** | Cooperative passes income tax deductions through to its members | Tax benefits accrue to the condominium unit owner |
| ***Equity Growth*** | Cooperative passes equity growth to its members (often with limits) | Equity growth generally follows housing market value and accrues to the unit owner |
| ***Overall Value*** | A cooperative maximizes benefits to its members | A condo owner benefits from appreciation in market value of the condominium unit |

**What will be the cost of a share for members joining the HMHCA?**

At the moment, we do not have a precise answer to this important question. We know approximately what the total cost of building our homes will be. But we don't know very well the level of commitment of our members to living at Hart's Mill. That is, how many people will be sharing that cost. Generally speaking however, the membership share likely will *not* be a trivial sum of money. One of our consultants suggested that we should anticipate an amount situated (vaguely!) somewhere between the cost of a new car and the cost of a house.

A general rule of thumb occasionally discussed in the co-op literature is that the share price should be less than a typical down payment for a similar house or condo in our local area. By way of reference, in recent years the median *value* of owner occupied housing units in Orange County has been estimated at around $285,000. By one estimate, the median *listing price* of homes on the market in Orange County was $399,000. The price of *new housing* units in Orange County generally is said to exceed $500,000. If we assume a down payment of 20% for homes at these prices the numbers work out to:

| Purchase Price | Down Payment |
|---|---|
| $ 285,000 | $ 57,000 |
| $ 399,000 | $ 79,800 |
| $ 500,000 | $100,000 |

Ouch!! Surely we can do better than that!* The down payments shown here likely are considerably higher than the eventual price of a share in our HMHCA. But it is simply too early to even be talking about such numbers in any concrete way. The eventual share price will be one outcome of our formal cost evaluation paired with our ironclad commitment to housing affordability.

* While somewhat irrelevant to our situation, a 2002 study of housing cooperatives in Connecticut reported that shares for market-rate housing co-op units [see below for market rate co-ops] ranged from $30,000 to $40,000. Also, we note that the National Co-op Bank (NCB) in New York offers minimum(!) loans of $25,000 for purchase of housing co-op shares (see references 35 & 36).

Recent discussions by members of Hart's Mill's Financial/Legal Circle have emphasized that how we structure our co-op shares, and decide on a share price, must maintain integrity to (sometimes conflicting) goals of affordability, demonstrating significant financial commitment to potential lenders, simplicity and fairness/equity*.

* Reference 33 (pp. 27–29) identifies four equity/fairness issues as they relate to share prices for limited-equity housing co-ops.

One complication in setting our share price is that the number selected (large or small) is somewhat subjective and within our control. Illustration: when you purchase a home in the conventional sense, you make a down payment and assume a mortgage for the balance of the selling price. If you pay 10% down, your mortgage (principal & interest) will be higher than if you are able to pay 30% down. You are balancing your available equity (money in the bank) against what you can afford on a monthly basis (your income). The same principle holds in the co-op context. With some added constraints, we have the ability to balance share price against monthly carrying costs: high share price and lower carrying costs; and vice versa.

But the question asked, "How much?", so here's one non-evasive (but not final) answer: $40,000. We arrived at this number considering three things: (1) a result of calculations from a worksheet provided in a 1983 book on financing housing co-ops (reference 20, Figure 4, pp. 94-95). Using this worksheet with projected costs for the Hart's Mill project suggested a share price of $41,216 (but note the date of the book: 1983 – 35 years ago!). (2) Knowing that eventually we will need to borrow somewhere between $8 and $10 million to build the Hart's Mill Village, we inquired what level of demonstrated commitment by the Hart's Mill members will be required to qualify for a loan of that magnitude. The answer is approximately $2.5 million. If we meet our goal of 60-70 genuinely committed members who plan to live at Hart's Mill, a share price of approximately $40,000 makes sense (65 members x $40,000 = $2.6 million). (3) We explored what share prices exist at other housing co-ops. Shares in housing co-ops targeting low income families (often with federal subsidies) generally are in the low thousands of dollars. High-end luxury co-ops in NYC can be found with share prices beginning somewhere around $500,000.* It is not uncommon to find co-op shares at well over $1 million.**

* A NYC organization regularly reports average sale prices of NYC housing cooperatives. Their 2017 numbers (based on 4th quarter 2016 results) report average co-op sales price of $499,718 for Brooklyn co-ops and $619,039 for Queens (see Reference 37). A similar report for first quarter 2018, reporting just for Manhattan, found the average sales price of $1.4 million. Some examples by co-op size: 1 BR -- $735,000; 3 BR – $2.3 million (see Reference 38). This latter document also reports separately the sales for the top 10% of all co-op sales ("luxury segment"). Don't ask! From a housing co-op perspective, NYC is another universe – albeit a very large universe (see Reference 42).

** For a bit of a laugh (or cry), consider this story: In May 2017, actress Demi Moore sold her penthouse co-op unit in the San Remo – a luxury apartment converted to co-op in the 1970s. Her share was sold for $45 million ($30 million below her asking price). Her monthly(!) carrying costs (maintenance fee) was $19,322 (Reference 39). For more, just Google "San Remo Demi Moore". The sale received extensive coverage.

Consequently, share prices at other housing cooperatives are not a terribly useful guide. When we have suggested to co-op consultants/experts that we're considering something around $40,000 for our share price, the reaction usually is, "Oh wow, that's not very much money. Are you sure?". When that figure is floated among people considering living at Hart's Mill, the reaction usually is, "Oh wow, that's a lot of money. Are you sure?"

**Yes, that does feel like a lot of money to me. Do I get this money back if I leave the community?**

Yes. If you were to leave the Hart's Mill community, the cost of your original share would be returned to you. It would either be purchased by the HMHCA (first right of refusal) or purchased by a new member joining the community. Note that this can take some time if there is not a waiting list of prospective members. Typically in housing coops, in addition to the price you paid for your initial share you would receive some portion of the cost of any HMHCA Board-approved improvements you make to your residence. And you also would receive an amount of money representing the increased value of your share (e.g., an inflation-adjusted increase in value). These adjustments in share value for departing members will be made according to explicit formulas developed and approved by the HMHCA.

As a highly simplified and hypothetical example, let's say your initial share purchase price was $40,000 and you departed the community 5 years later having spent $1,000 for granite countertops in your kitchen (assuming the countertops were a Board-approved addition and you were given full credit for the improvement). At departure time, you might sell your share for $12,000. Here are the numbers under this hypothetical scenario:

| | |
|---|---|
| Initial purchase price of HMHCA share = | $ 40,000 |
| Capital improvement (with prior approval by HMHCA) = | 1,000 |

| | |
|---|---|
| Annual interest on initial purchase assuming 2% inflationary increase (simple uncompounded interest) 5 (years) x 0.02 x $40,000 = | 4,000 |
| Share price paid to you as departing member = | $ 45,000 |
| Share price paid by an incoming member = | $ 45,000 |

Please understand, this example uses very round numbers to illustrate the concept of changes in share value. The actual HMHCA initial share price has not yet been finalized. See below how these numbers might change under a limited-equity adjustment.

**What if I can't afford the share price?**

There are potential members of the HMHCA who will be unable to afford a share price on the order of $40,000. Sadly, this could prevent some individuals or families from becoming part of our community, and we are working hard to prevent this outcome. There is some good news in this regard, and this comes in the form of a share loan. Quite literally, a share loan is a *loan* obtained by an incoming member to purchase a share in a housing cooperative. And fortunately there are lending institutions aligned with and committed to the co-op movement that provide share loans at very favorable rates (see Reference 36). In particular, these financing advantages are often targeted to co-ops serving low and moderate income people and/or special needs groups.

Again, by way of example, let's say you wish move from where you presently live and you want to buy a $200,000 home. Most likely you would not be able to pay the seller the entire purchase price in cash. Instead, you would make a down payment, and you would get a mortgage to cover the remainder of the full purchase price. Many of us have experience with this ritual and, for most of us, it represents the largest financial transaction we will ever undertake.

By contrast, in a housing cooperative, since you actually are buying a share in a corporation rather than real estate, you could seek a share loan (analogous to a down payment). This loan provides you with borrowed funds to purchase your share from the seller (initially this would be the HMHCA). You then would make your monthly principal and interest payments on the share loan directly to your lender (the co-op probably would not be involved in this transaction). Again, you also would pay a monthly fee to the HMHCA to cover your proportional share of keeping the co-op financially solvent.

**What do my monthly charges cover?**

Virtually all housing cooperatives charge residents a monthly carrying costs (sometimes called a monthly maintenance fee). The amount of this monthly charge typically covers your proportionate share in operating and maintaining the cooperative, which can include debt service on the blanket mortgage for the property (principal plus interest), property taxes, management fees, maintenance costs, insurance premiums, and contributions to reserve funds.

Depending on the size and amenities of the units, monthly carrying costs will vary from one dwelling unit to another.*

> * In some housing co-ops, carrying costs may include household utility costs. In addition, some co-ops choose to collectively share the cost of individual unit interior repairs.

The HMHCA Board of Directors will be responsible for preparing an annual operating budget to cover the cost of operations, reserves, principal and interest on blanket mortgages, property insurance, and property taxes.

So, to be perfectly clear, your monthly carrying cost payment minimally covers your pro-rata share of co-op expenses:

- The basic operating costs and upkeep of the buildings. This would include such things as expenses relating to maintaining and operating the housing infrastructure, heat, water, and electricity for the common areas, salaries for any paid staff, liability & other insurance for the buildings, contributions to the required reserve fund.
- Real estate taxes on the land and entire building infrastructure.
- Your proportionate share of the overall “blanket” mortgage (principal and interest) on the physical infrastructure.

If you have taken out a loan to cover your share purchase, you must make the principal and interest payments directly to the share lender. If utility costs are not part of the cooperative budget, you must pay them directly, as well.

**Do I accumulate any equity over time?**

Part of the answer was given in the hypothetical example, above, and the answer given there is yes, you can accumulate equity on what you own: your share. Remember, what you own is not your dwelling (real property) but rather a share (personal property) in the cooperative enterprise. Thus the question, properly asked, is whether you can accumulate equity in your share value over time, and the answer is yes. Now, however, comes an extension and modification to this answer and the hypothetical example given above.

It actually depends on what type of cooperative HMHCA becomes. There are different types of housing cooperatives and these types of co-ops determine the nature of share equity accumulation. In many respects the type of co-op selected is a question of who holds the debt – the individual or the cooperative. While you will discover reference to many types of co-ops in the literature (e.g., senior cooperatives, student cooperatives, mobile home cooperatives, and others), there are two basic types as seen from a financial perspective:

***Market-rate housing cooperatives***
In a market-rate cooperative you can buy or sell your membership (your share) at whatever price the market will bear. Share prices are determined by the market, and a share price is valued by what one is willing to pay for it in an arms-length transaction. Under this model, purchase price and equity accumulation are very similar to that for condominium or single-family ownership except for the fact that a co-op must approve the purchaser (see, below, "Can cooperatives discriminate?"). Most of the luxury housing cooperatives in NYC are market-rate co-ops.

***Limited-equity housing cooperatives***
In a limited-equity housing cooperative there are restrictions on the proceeds members can get from selling their share. These are usually imposed because the cooperative's members benefit from below-market interest rate mortgage loans, and, sometimes, from grants, real estate tax abatements, or other features that make co-op housing more affordable to both initial and future residents. In most limited-equity housing cooperatives these limitations are voluntarily imposed by the members on themselves out of a desire to make the co-op affordable to future residents. The restrictions are usually referenced clearly in the cooperative's covenants or bylaws, and normally would be specified in a separate document detailing the precise nature and rationale of the equity-sharing process. The purpose behind these equity limits often is to target the special benefits of cooperative housing to individuals and families who most need financial assistance. In some cases the lower limit can be set to zero so that there is no inflationary-generated adjustment in the share value returned to the seller at the time of departure from the community. Many cooperatives that wish to maintain affordability limit the amount of appreciation in share prices to some fraction of the Current Price Index, to increases in the median sale price of homes in the area, to a set (guaranteed) return of some small percent (often between 1% and 3%, annually), of some other desired form of equity increase that is less than market-rate appreciation.

An advantage of a limited-equity approach to housing is demonstrated by the cumulative effect of limiting appreciation. By limiting the rate of equity appreciation, housing units become increasingly affordable. When the Dos Pinos Housing Cooperative of Davis, CA, was formed, the monthly carrying costs for members exceeded the area's average rent, because it was newly built. Thirty years later, the cooperative's monthly carrying costs were 50% lower than the average market rate apartment (Reference 44).

But you can build equity in another way too. Depending on how the HMHCA decides to organize itself, a portion of the *overall equity* in the housing stock could be returned to a departing member. Of course, if the return to members on community equity is high, the objective of long-term affordability of housing is weakened. It also impacts the financial stability of the cooperative enterprise itself. Reduced mortgage debt or increased housing equity for the housing cooperative is not the same as cash on hand, but the cooperative would have to pay out any increased equity to a departing member out of their cash reserves of through additional debt financing. Nevertheless, as the value of the cooperative property increases, so does the value of each member's cooperative interest. And, just as with conventional home ownership, as a cooperative member contributes each month to the pay-down of the co-op's blanket mortgage, the value of their cooperative economic interest increases. Under a limited-equity co-op model, individual return on community property appreciation is, by definition, also limited. But it likely would not be set at zero. The members will make this decision based, in part on the mission of the Hart's Mill community.

The rules governing equity return are *determined by the co-op members themselves* and spelled out in the community bylaws or the proprietary lease agreement. Generally speaking, when members depart the community they recover their share investment, plus appreciation, as indicated above. They also could recover a proportionate share of equity arising from pay down of the blanket mortgage during their period of residence. The term "limited" in a limited-equity cooperative usually implies that individual members do *not* benefit financially from increases in co-op property arising from "background" influences such as rising demand for real estate in a growing urban environment. It is this unique feature that helps to make co-op housing affordable in perpetuity. It also is the feature that lowers the appeal of co-op living for those individuals using housing as their principal investment vehicle or retirement "nest egg".

**Reference to the HMHCA "Board" has come up a couple times. What's the role of the Board?**

The Board of Directors of a co-op is the governing body of democratically elected members. Member residents of the housing co-op elect a Board of Directors which, as in other cooperative corporations, is legally responsible for the successful functioning of the corporation. Generally, such issues as the manner by which directors are elected, the number of board members and rotation procedures, term limits, how often they meet and their form of governance is spelled out in detail in the Bylaws of the corporation. Any co-op resident member in good standing is eligible to serve on the Board of Directors. A cooperative's Board of Directors further has the responsibility to keep its members informed of all its actions. [See reference 5 for detailed information about housing cooperative Boards of Directors].

**Do I pay real estate taxes?**

Only indirectly. Taxes are assessed on the cooperative corporation as the owner of the property. Your monthly payments to the cooperative are, in part, used by the cooperative to pay real estate taxes. Good news: even though you don't pay real estate taxes directly, federal tax law allows you to deduct on your personal income tax return both your share of the cooperative's property tax payments, as well as your proportionate share of mortgage interest payments. This would be in addition to deductible interest on any share loan you may have.*

> * There are nuances in federal tax code that can nullify this benefit based on the particular way a co-op is established and managed. This should not be a problem for the co-op that might emerge at Hart's Mill, but we will need good legal assistance to get this right. See U.S, Code, Title 26, Section 216.

**Can cooperatives discriminate?**

No. Like any other form of housing, cooperatives *cannot discriminate* based on protected classes covered by the Fair Housing Act, which include race, color, religion, sex, familial status, national origin, or disability. Historically, the basic cooperative principles include both open membership without restriction, as required by law, in addition to non-partisanship in politics and non-sectarian in religion.* However, most cooperatives are quite selective in approving memberships. This is one advantages of this type of ownership structure. As a community of people who share a financial obligation and a responsibility for governing how they want to live together, cooperatives can and must ensure that incoming members can meet their financial obligation and will abide by the rules and values of the community.**

> * There's a deep and rich history behind these principles. See reference 16 for the Wikipedia version.

> ** In a well-publicized example of a housing cooperative deciding not to admit a member, the NYC San Remo co-operative (mentioned above) rejected the application of Madonna, who applied to buy a $1.2 million co-op unit in 1985. Stories say the co-op Board was concerned about the undue public attention (paparazzi, e.g.) her presence would bring, but the building was already brimming with famous people (e.g., lots of men named Steve – Jobs, Martin, Spielberg, Dustin Hoffman, Bono, and other glitterati). Rumors are that actress Diane Keaton was the sole Board member to vote in favor of Madonna's membership (See References 40 & 41).

**What do most housing cooperatives look like?**

Cooperatives can be almost any kind of housing, and there is a wide variety in both appearance and size of housing units. Housing cooperatives may be high-rise "apartment" buildings (very common in NYC), garden-style apartments, townhouses, single-family homes, senior housing and college alternative to dormitory or commercial rental housing. Some of the housing units at Hart's Mill will be free standing ("single family") dwellings or duplexes. A third option will be larger dwellings with smaller efficiency units surrounding a common shared space.

**Can I become part of the Hart's Mill Housing Cooperative and then sublet my dwelling unit to someone else?**

Probably not. Subletting likely will be strongly discouraged. In fact, most housing co-ops do place severe restrictions on subleasing, if allowed at all. Among the reasons for discouraging subleasing is the desire to preserve the owner-occupant character of the community. This maintains a stable non-transitory community. Another reason is concern over the loss of control regarding who can reside in the community. Despite this, limited subleasing arrangements (generally spelled out in detail in the covenants or bylaws of the cooperative association) can be established to permit some flexibility. These would typically include restrictions on the maximum length of the sublease agreement and the amount of the rent payment. Some communities, however, do maintain 2-3 residential units specifically as time-limited rental units (e.g., for longer-term visitors or "explorers").

**Do I need homeowners insurance?**

Probably yes. You may want a policy similar to renter's insurance or condominium owner's insurance. The co-op will carry a blanket insurance policy to cover damage to the cooperative's property from fire, water, or other disasters. However, such policies generally do not cover any damage to personal belongs inside your unit. Thus, additional insurance is recommended to cover our personal possessions and for your personal liability in the event of an accident in your home.

**What's the extent of my personal financial liability in a housing cooperative?**

Members have shared responsibility for the financial wellbeing of the community (through an elected and accountable Board) but have no personal liability on the co-op's blanket loan. Members with a share loan are individually liable to their lender for the amount of that loan. Incorporation protects members from personal liability for the debts and obligations of the corporation. In other words, creditors cannot collect from a member personally for what the co-op owes. Creditors are limited to the assets of the corporation, which, of course, does include the money you have invested in the co-op, but not any of your personal assets.

This is an important issue, as different types of legal organization (e.g., co-op vs condo vs LLC) offer different levels of liability protection under the law. Part of the issue goes beyond liability protections afforded individuals, say, in the event of default on a co-op's blanket mortgage. Other forms of liability from which protection is a bit less clear relate, for example, to law suits brought against the community by internal (e.g., disgruntled member) or external (e.g., disgruntled neighbor) forces. There are mechanism for insuring against general liability, but we will need serious legal assistance on the matter. The literature on intentional communities is replete with sad stories (see reference 23).

**What if I want to make improvements to my unit?**

External building improvements once decided and approved often are paid for by the cooperative. Minor improvements to the interior of your unit generally may be made by and paid for by you. Since the community owns the housing, substantial interior improvements become a community matter. The rules for improvements are laid out in the co-op bylaws or occupancy agreements. Proposals for substantial internal unit improvements must be reviewed by the Board before changes can be made.

**What are the benefits of being part of a housing cooperative?**

***Economic Advantages:***

- *Initial Costs (Transaction Costs are Lower)*: Buying into a housing co-op generally is more affordable than other owned housing. This arises for a number of reasons: (1) Because the down payment and loan initiation is for the purchase of a share, not a down payment and mortgage loan for an owned unit; (2) Homes in housing cooperatives often are smaller than other homes in the area (partly the result of the availability and use of cooperatively shared resources such a common eating spaces, work spaces and guest accommodations); (3) Purchasing owned property generally entails several additional costs that are not part of a share purchase arrangement. Examples would be mortgage closing costs, title search and title insurance, realtor fees, mortgage recording taxes, appraisal fees and government recording & transfer charges.*

  * This claim may overstate the actual fees associated with a usual home purchase, as some fees are usually borne by the seller not the purchaser. And, if you were to choose instead to rent the home/apartment in which you live, the initial costs would be lower than those for a co-op, as typically the only initial cost associated with renting is a security deposit (which could be totally refundable when you depart the unit).

- *Long Term Housing Costs (Stable & Affordable)*: Living in a cooperative generally stays affordable. Members have no reason to substantially increase monthly charges (on themselves!) unless taxes or operating expenses increase. Typically monthly charges remain reasonable. In addition, shared resources can lower the costs of maintaining your dwelling and gardens. If you presently are renting, your home/apartment monthly expenses can be considerably higher than co-op operating expenses because generally there is an owner of your rental property seeking to maximize his/her profit and pay down the mortgage on their property, thus building equity. Co-ops eliminate the profit line from housing costs.
- *Tax Deductions*. For income tax purposes, a cooperative member is usually considered a homeowner and, as such, can deduct his/her proportionate share of the

real estate taxes and mortgage interest paid by the cooperative. Co-ops provide the same tax benefits as other types of home ownership.*

- *Equity*. Cooperatives can provide for accumulation of individual member equity on the value of their membership share. For market-rate cooperatives, the accumulation of equity and resale prices are based on the market. Limited-equity cooperatives establish limitations on the accumulation of equity to ensure long-term affordability for new members. Among housing co-op advocates, it has been argued that co-ops are the only means of providing affordable housing (e.g., see Reference 43).
- *Limited Liability*. Members have no personal liability on the cooperative mortgage (sometimes referred to as the "blanket" mortgage). The cooperative association is responsible for paying off any mortgage loans. This can often make it possible for persons whose income might not qualify them for an individual mortgage to buy a membership share in a limited equity cooperative.
- *Reduced Construction and Operating Costs*. Co-op members often reduce construction and operating costs by doing some of the work themselves. For a start-up enterprise like the Hart's Mill Village, sweat equity could significantly cut potential construction costs. A downside of this advantage is that self-construction can sometimes complicate matters of inspection approvals and insurance.
- *Changing Residence*. One advantage accruing to housing co-ops is the ability of an individual or family to more easily change their physical residence within the community (say, in response to life changes) without having to sell their home, move (sometimes long distance) and purchase a home elsewhere. There are significant savings involved in these internal residential moves by the elimination of most transaction costs.
- *Consumer Action*. Through their cooperative association, members can sometimes jointly exert influence to change tax rates and utility prices and obtain improved services from local governments. The cooperative, as consumer advocate, also can join with other cooperative organizations and/or coalitions to strengthen their bargaining power.
- *Savings*. Cooperative members can benefit from economies of scale in cooperative costs (e.g., for housing construction & maintenance, appliance purchases, etc.) as well as from not-for-profit status and operation. Also, when there are "transfers" (i.e., a member leaves the community) only the out-going member's share equity must be financed by the incoming member. As mentioned already, transfers of shares are subject to fewer settlement costs than traditional home sales, although membership transfer is regulated by the co-op's bylaws.

* These statements may not be true forever because of changes made in the 2017 *Tax Cuts and Jobs Act*. This act limited the deduction in ways that will make "itemizing" not worthwhile for many taxpayers who previously benefitted from this deduction. It appears that only a small percentage of taxpayers will be able to continue to deduct their property taxes in 2018 and beyond. Under the *Tax Cuts and Jobs Act,* we still will be able to deduct the interest we pay on our mortgages for up to $750,000 in new mortgage debt. However, things get a bit complicated when these changes are applied differentially to single taxpayers and married couples filing separately. These changes are not likely to affect Hart's Mill share owners due to our lower

costs of our housing.  Without getting stuck in the details, it's safe to say that for you, as a Hart's Mill housing cooperative member, the interest portion of your mortgage payment is tax deductible.  If you itemize your federal income taxes, your share of the property taxes paid by the co-op also are tax deductible.

### *Social Advantages*

- *Elimination of Outside Landlord*.  Cooperatives offer control of one's living environment and a security of tenure not available in rental housing.  As a member of a housing co-op, you are your own landlord.  There's no 3rd party landlord.
- *Security*.  Housing co-ops typically offer their members a very long-term leases (99-years is typical).  On the other hand, most rental properties typically require a 1-year lease, but longer-term leases remain something of a "gentlemen's agreement".
- *Community Control*.  Members have the right to vote on how the corporation conducts its business and participate on the Board of the cooperative.  All residents participate at various levels in the decision-making process regarding the financial & social life of the community.  This is also true (but generally to a lesser extent) for condominium owners and associations.  But it is not true for of tenants who rent and usually do not have the opportunity to exercise input into the landlord's decisions.  Co-op members own the cooperative collectively and can remain in their homes for as long as they wish, provided they meet their monthly obligations, and abide by the cooperative bylaws, covenants, rules, and regulations.  Member control is a means of motivating members to be better stewards of the co-op's assets
- *Member Ownership*:  Housing cooperatives remove the 3rd party profit motive.  Co-op residents realize both tangible & intangible benefits.  They come to depend on stable housing costs, benefit from participating in control of the co-op and reap the social capital that comes from having a broad network of neighbors with which to work and depend on.
- *Vetting of New Residents*.  To protect the interests of the residents, the Co-op Board must have the right to approve incoming members who replace those leaving the cooperative.  A credit check and other procedures established in the bylaws are usually required.  This process also helps orient the incoming member to their rights and responsibilities as cooperative members.
- *Cultural Diversity*.  More so than other types of housing communities, many co-ops make cultural diversity a very high priority.  Cooperative members sometimes say that the possibility for interacting with people from different backgrounds, cultures, and income levels is a positive factor in their decision to become a member.
- *Friendship*.  The community bonds that are formed within a cooperative are significantly closer than found in other types of housing ownership arrangements.  Living in a housing cooperative can establish a community atmosphere that provides support and a sense of "home" to the members.
- *Extended Services*.  By establishing cooperative procedures and working together, people can provide services for themselves that otherwise would be impossible to obtain.  When one cooperatively organized venture is successful, it often becomes clear that people can be successful in another area as well.  As a result, the original

effort often can be strengthened. Examples include athletic teams, cooperative preschools, credit unions, tutoring, food-buying clubs, arts and crafts, and senior health care and support services.

- *Personal Assistance*. Housing cooperatives facilitate bringing community members and friends together for many purposes. This can extend to limited medical assistance when needed or assistance with pets and gardens when away from the community for brief periods.
- *Safety*. In a closely-knit neighborhood of clustered homes, the community is never without residents alert to unusual happenings. Members of the co-op are carefully vetted. You know your neighbors and they are there to assist in the event of an emergency.

### *Physical Benefits*

- *Lower Turnover Rates*. There is ample evidence suggesting that housing cooperatives have lower rates of housing turnover than do standard condominium arrangements or rental property. The same evidence suggests that co-ops have more responsible members than other types of housing
- *Higher Rates of Occupancy*. One interesting aspect co-op living is that typically there is a higher rate of occupancy (lower vacancy rates) than with, say, condominiums. Lower vacancy rates mean safer communities and lower financial losses to the co-op business resulting from vacant unit costs not offset by income. Admittedly, one of the reasons for higher occupancy rates is that housing cooperatives often place severe restrictions on subleasing. But even without such restrictions it's possible that the desire to live in a co-op might lead to this outcome.
- *Shared Maintenance Responsibilities*. Cooperative members usually have limited direct home maintenance responsibilities. The cooperative association is responsible for major repairs, dwelling insurance, equipment replacement and upkeep of common grounds and facilities.
- *Vandalism and Security*. Cooperative members vigorously protect their association's property. Evidence shows that one important benefit of converting rental properties to cooperative ownership is the reduction in vandalism and abuse of property and improved and shared security arrangements.

## Sure, but there must be a downside?

### *Economic considerations*

- *Lower Equity Return*. The post-WW-II period brought unprecedented economic advantages to (disproportionately white) home owners. Federal policies (e.g., VA loans) encouraged homeownership, and events over ensuing decades lifted many people into the ranks of the middle class by virtue of increasing home values alone. For the better part of 60 years, housing values increased at a rate greater than inflation. This created a good deal for those who already owned property and translated into higher rents and fewer affordable purchase opportunities for those hoping to own a home. Increases in homeownership, increases in home size & amenities, and increases in home values became the foundational "truth" of the American Dream.* Many of us look to that history and continue to embrace with enthusiasm the "Dream". Those who chose to live in a housing cooperative generally are deeply questioning some or all of that "Dream", and are voluntarily entering into a living situation that provides a lower equity return on their housing investment. Often they are seeking a different form of "wealth" such as the joy of strong interpersonal relationships, greater self-determination, and a sense of personal satisfaction by contributing their bit to alleviate an out-of-control and unjust system. That said, some members or their beneficiaries may prefer unrestricted equity returns. For such individuals, a limited equity housing co-op may not be a good choice.

* Of course, we all are familiar with how the "Dream" turned to nightmare for many homeowners following the mortgage meltdown that plagued this country beginning around 2008. Despite this recent history, there remain those who are staunchly bullish in the claim that a co-op is not as good an investment as a standard home or condominium. Yet, evidence appears to indicate that co-ops with the ability to screen potential buyers and determine their financial capability were not as hard hit in the housing crisis as other forms of ownership.

- *Unfamiliarity*. Mortgages can be more easily obtained for a standard residential property or a condominium than are loans to pay for a co-op share.* One reason frequently cited is that most real estate attorneys and traditional lending institutions have a lower level of experience and understanding of cooperatives – and, concomitantly, a higher level of apprehension, mistrust, skepticism, and overall reluctance to get involved. Or they will simply charge more. Because the property is really owned by a corporation, some commercial lending institutions do not provide mortgages for co-op housing. This leads to a smaller lender selection pool and potentially overall higher mortgage costs.

  * This may seem counterintuitive given that the share loan will generally be very much smaller than a home mortgage.

- *High Monthly Fees*. Monthly fees in a co-op living situation will generally be higher than monthly fees encountered by those living in condominiums and paying a monthly condominium assessment. The reason is that co-op monthly fees include taxes, mortgage payments, fees for maintaining common areas & facilities, and contributions to reserve accounts. If you live in a condominium, your property taxes and mortgage payments are not part of the monthly condominium assessment. In the end, however, the overall costs are similar. It's the same money, just broken up in different ways.

***Social considerations***

- *Sociability Expectations*. Life in a housing co-op is not for everyone. Many of us want to acquire a place to live, turn the key, close the door, and have a domain that is solely ours. Living in a community that encourages and expects your participation in community activities (e.g., attending meetings, sharing meals, contributing to certain work obligations) is not something that excites everyone. Community bylaws set forth these expectations and generally allow for considerable individual variation in community participation, but living at Hart's Mill will require some level of commitment to community affairs for everyone. Compared to other living arrangements there will be increased responsibilities regarding community participation in community work, governance and celebration.
- *Co-op oversight*. Some individuals will not wish to have constraints placed on what they can or cannot do to their dwelling. Such individuals may chafe under co-op rules and oversight.
- *Governance*. Difficulties sometimes arise in housing cooperatives from differences of opinion between current board members and other members over management of the cooperative.
- *Not Necessarily Easy to Join*. To become a member of a housing co-op, your application will be reviewed by an established co-op review committee to determine if you are a good "fit" for the community. The approval process can be a stumbling point for some aspiring members.* Famously, former President, Richard Nixon was denied membership in a New York City housing cooperative.

  * But, to reiterate something said earlier, under no circumstances can someone be turned down because of age, sex, race, sexual orientation, religion or other categories protected under the Fair Housing Act.

### *Physical considerations*

- *Less Freedom of Choice in How You Treat Your Dwelling*. If you own your own home in a neighborhood without covenants erected by a neighborhood association, you pretty much have freedom to do whatever you want with your home. And there will exist almost no restrictions on what you legally can do in the confines of your home. While you may incur disapproval from your neighbors over, say, the color you choose for your siding, you have immense freedom over the exterior as well. There may of course be municipal restrictions over property line setbacks if you add a garden shed, or how many automobiles you may park in your driveway, but generally there aren't a lot of rules. If you live in a condominium, the covenants of the condominium association will generally be more restrictive than the freedoms granted to standard homeowners. However, in a housing cooperative, there generally will be a rather large and encompassing set of rules regarding the use and upkeep of your dwelling. These rules usually require that significant changes made even inside your home be approved the co-op Board.

**It all sounds so complicated! There must be lots of legal complications?**

Well… yes, there are. But if you were to purchase a condominium you would discover most of the same issues. The difference is that when you purchase your condominium all the legal work likely has been completed long ago, and you simply sign a lot of documents at the time of closing. Here we are talking about actually creating a housing cooperative from scratch, and many legal documents that pertain specifically to a Hart's Mill Housing Cooperative must be crafted. These will include:

- Articles of Incorporation
- Covenants and/or Bylaws
- Member Certificate (a certificate, or share, showing evidence of ownership in the cooperative corporation)
- Subscription Agreement (document supporting the purchase of a share in the cooperative)
- Occupancy Agreement (contract between a member and the corporation that spells out the rights & obligations of the members. This document basically gives the member the right to occupy a unit)
- Cooperative Agency Agreement
- Management Agreement
- Disclosures (required similar to other investment opportunities)

Not only will our documents have to pass muster in terms of legal scrutiny; they must also be easily understood by the co-op members. And, of course, all legal documents must be in a form acceptable to potential lenders.

**Boy… that raises another question: Where's all the money going to come from?**

Stay tuned. That's a topic for a different FAQ.

**What can I expect if I want to know more about living in a housing cooperative?**

A bit of exploring on the Internet reveals that there's a mountain of information freely available regarding housing cooperatives. There exist national housing cooperative organizations that provide advice and assistance to housing co-ops. For example, the National Association of Housing Cooperatives (NAHC) members agree that cooperative housing associations are most successful when operated in accordance with specific recommended practices and the general cooperative principles in addition to rules unique to an individual housing co-op.

You'll be expected to become involved in the life of the co-op community. A regular communication system (e.g., internal information bulletins, meeting notices, solicitation of members for opinions and priorities, etc.) strengthens the relationships within the community and between the Board of Directors and the members. Leader accountability is central to the cooperative concept. The Board of Directors should facilitate transparent two-way communication to guide them in all decision-making. But, make no mistake about it: membership in a cooperative is a unique form of home ownership and typically requires education and full understanding of the benefits and drawbacks of co-op living in general, and the rules guiding co-op participation in a specific housing cooperative such as the hypothetical Hart's Mill Housing Cooperative (HMHC).

You'll also want to keep abreast of the financial health of "your business". The cooperative association must maintain adequate financial reserves to protect the cooperative and its members' interests. These usually include a general operating reserve and a reserve for replacing components of buildings as they deteriorate. Such reserves reduce the possibility of members having to pay unexpected special charges in emergencies. An annual audit must be conducted by professional accountants and made available to all members.

**Is a housing cooperative right for you?**

Maybe yes; maybe no. If you wish to own the home in which you live, have complete freedom over what you do with your home (and surrounding land), and wish to enjoy market-driven appreciation in your investment over time, then you probably will not be interested in a housing co-op (especially of the limited-equity flavor). But if your resources are limited and, especially, if you are presently a renter, then you may find a co-op to be a very pleasing alternative.

**What questions should I ask before buying into a cooperative?**

Remember, since you are buying a share of a corporation that owns real estate, you will want to find out about the corporation's financial health. You will also want a clear understanding of your anticipated financial obligations to the cooperative. Be sure to find out all the rules and regulations of the community. Here are some sample questions to ask before making your investment:

- What is the share price?
- Where can I obtain share loan financing?
- How much are the monthly carrying charges?
- What is the underlying mortgage?
- What is your subletting policy?
- What is the policy for making alterations to my unit?
- How is the project managed?
- Is the Board effective and actively involved? Does it have the requisite expertise to manage such a project?
- What is the financial state of the cooperative?
- Are there adequate reserves?

**Are there any existing intentional communities that are similar Hart's Mill and use a housing cooperative model?**

Probably. But there's no single resource (not even the foundational go-to place, the FIC *Communities Directory*) that could make it easy to answer this question. For sure, they exist, but identifying them is difficult. Do keep in mind that every community has its own unique character and culture; no two are the same. As a practical matter, this FAQ document arbitrarily omits discussion of several categories of housing co-ops. These include the dozens of student housing co-ops around the U.S, highly urban co-ops (e.g., the hundreds of large apartment buildings in Manhattan that have "gone co-op"), co-ops outside the U.S. (there are many in Canada, for example), super-small co-ops (often 4-6 people living in a single dwelling but calling themselves a housing co-op). Anyway, here are some you may wish to check out.

*Winslow Cohousing Group*, Bainbridge Island, WA (established 1992; approximately 70 members). WCG appears to be organized as a market-equity housing cooperative.

*Cobb Hill Cohousing*, Hartland VT (established 2001; approximately 65 members). Cobb Hill maintains a limited-equity policy on home sales, but is not organized as a co-op. [Interesting tidbit: Donella Meadows was one of the founding members of Cobb Hill.]

*Shannon Farm Community*, Afton, VA (established 1972; approximately 60 adults & 30 children). Shannon Farm is organized as a "land-and-housing trust that owns the land and all buildings." Reading about Shannon Farm suggests a limited-equity housing cooperative, but those words don't appear in their descriptions of themselves.

*Los Angeles Eco-Village*, Los Angeles, CA (established 2012; 45 housing units. While located in the heart of a large urban neighborhood, and thus very different from Hart's Mill, LAEV is organized as a limited-equity housing cooperative and leases land from a community land trust.

*Monan's Rill*, Santa Rosa, CA (established in 1974 by a group primarily composed of Quakers). 18 adults; 6 children on 440 acres.

In North Carolina we know of two housing cooperatives, neither of which provide a model for what it is we envision on the Hart's Mill land:

*Weaver Community Housing Association*, Carrboro. Established several years ago, the WCHA is a charitable, 501(c)3 non-profit. It is a thriving, affordable housing organization with three small unique, cooperatively-run communities in Chapel Hill-Carrboro: Bolin Creek Cooperative ("the BOG"), Cedar Rock Co-op, and Hillsborough Road Co-op.

*The Kimberlee*, Charlotte.  Built in the 1960′s, The Kimberlee is a modern urban-style apartment building organized as a housing cooperative of 90 residential units located in the Myers Park neighborhood of Charlotte.  See reference 28.

**So, all together, do we know how many housing cooperatives there are in the U.S.?**

The National Association of Housing Cooperatives occasionally makes such estimates.  The most recent we have seen suggests that there are over 6,000 housing cooperatives in the U.S.  These cooperatives represent an estimated 1.1 million individual co-op housing units. Of these million or so cooperative housing units, roughly 40% are limited- or zero-equity co-op units.  The remainder are market rate co-op units see (Reference 29, p. 7; and Rreference 30, p. 411.

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