AN ASSESSMENT OF LOAN REGULATIONS FOR RURAL HOUSING COOPERATIVES

Research conducted for the United States Department of Agriculture Rural Business-Cooperative Service

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SUMMARY

USDA's Rural Housing Service has a loan program in place to provide assistance for rural housing cooperatives. Although the program has been available for many years, it has been used very rarely. This research assessed the reasons for this lack of use. Case studies of four existing cooperative housing projects were conducted, along with a review and critique of the USDA regulations that affect the cooperative housing program.

All of the cooperatives were organized in the late 1970s or early 1980s. They range from eight to thirty-nine units, located in either the countryside or on the edge of small towns. The members are all low income, and many of them have lived for years in the co-op. Each of the co-ops has faced major crises, and they all struggle with issues of ownership and governance. Unfortunately, they have largely struggled in isolation, remote from any mutually supportive networks, or even contact with other cooperatives.

These are the key conclusions reached in this study:

- There must be a support system for development and operation of rural housing cooperatives. This support system should include partnerships with existing housing and cooperative resources, along with adequate compensation for services provided.

- A separate set of cooperative regulations and guidelines should be developed. Guidelines should address the major challenges in development and operation of housing cooperatives, and should be targeted for at least three audiences: agency staff, advisors, and members.

- Regulations governing the development of housing cooperatives should allow for maximum flexibility, creativity, and involvement of members.

- HUD insurance and direct lending programs should be considered as good models for rural co-op housing.

- Clear guidelines regarding opportunities for member financial benefits, member selection, and resident management will encourage a sense of ownership among members.

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INTRODUCTION

Most cooperative housing in the United States is less than 50 years old. Very little cooperative housing was built prior to World War II, but the 1950 National Housing Act created the very successful Section 213 program, which contributed to a huge rise in the number of co-op units built in the 1950s and '60s. By 1971, there were 154,000 units in about 2,500 cooperatives. Most of them were located in urban areas. The Farmers Home Administration (FmHA) established the 515 low and moderate income rural loan program in 1963, but very few cooperatives were ever built. Rental and single-family housing form the vast majority of the Rural Housing Service portfolio. There are no definitive statistics on the number of housing cooperatives financed, converted or operating under the 515 program, but at least five are currently operating as co-ops. The reasons for this lack of co-op development are not clearly understood. (Foundation for Cooperative Housing, 1980)

The purpose of this project is to make recommendations that will improve USDA's ability to assist new and existing cooperative housing complexes. In order to do this, an evaluation and critique of the Rural Housing Service's cooperative regulations was undertaken, along with an evaluation of four existing Rural Housing Service (RHS) cooperatives.

All four of the cooperatives studied for this report began their development process in the 1970s and early 1980s. Concern about the lack of rural housing cooperatives had led to the creation of the Rural Cooperative Housing Demonstration (RCHD) program in 1979. It was funded by the FmHA and HUD's Office of Policy Development and Research. The project was designed to test the viability of small housing cooperatives in rural areas and determine whether a loosely knit federation of Technical Service Organizations (TSOs) could have an impact on the delivery of cooperative housing. Three of the four cooperatives in this study were formed by two of the TSOs in the Demonstration Program network: the National Council of La Raza (NCLR) and Tierra del Sol Housing Corporation. The fourth cooperative was organized before the RCHD started, and there is no evidence that it was ever involved in the program.

An evaluation of the RCHD program was published in 1982. Its principal conclusion was that "low-income rural housing cooperatives can work!" Other findings identified a number of the same issues discussed in this study. For example, because housing cooperatives were an unfamiliar model for most people, effective technical assistance was extremely important. Since cooperatives are process intensive, communication among members, agencies and advisors was critical. One of the major hurdles for the TSOs was communicating the concept of cooperative "ownership". Another area of concern was a "perceived inconsistency and arbitrariness within the Farmers Home Administration." The problems included gaps between policies and practices, insensitivity to local customs, and lack of continuity in the agency. (Duga and Martineau, 1982).

The Final Report of the RCHD program includes 35 case studies of cooperative housing projects. A history of the Rural Cooperative Housing Demonstration program is beyond the scope of this study, so it is not clear what happened to many of them. At least two of them were eventually built, and they are included in the current study: Cielo Azul and Eleven Mile Corner. (Rural America, 1982)

Although the record of rural housing cooperative development is sparse, there has always been a much greater level of activity in urban areas. More research is available, and much of it is relevant to the discussion of rural housing co-ops.

Several studies have looked at the financial performance of cooperatives. Parliament, Parliament and Regmi analyzed financial statements of 18 urban housing developments for a four-year period 1981-1985. Eight were rental and ten were cooperatives. Savings on variable expenses were estimated at 16% for the cooperatively owned developments. Most of these savings were in the maintenance area. The authors report anecdotal evidence that co-op members reported problems earlier, which may have led to lower maintenance costs. (Parliament, Parliament and Regmi, undated). Another study by Calhoun and Walker analyzed loan performance of HUD's multi-family insured mortgage programs. They found that HUD-financed cooperatives in the Section 221(d)3 Below-Market-Rate Program out-performed all other ownership types. (Calhoun and Walker, 1994)

Other research has looked at the success of cooperatives in creating better housing and neighborhoods. Member ownership is considered a very social capital-intensive form of housing. In their introduction to a 1998 issue of Fannie Mae's *Housing Policy Debate*, Lang and Hornburg discuss the importance of the concept of social capital in creating innovative strategies for housing policy: "Foremost among these is the idea that housing policy should promote the formation of social capital, or the "glue" of civic networks that binds people to their communities. " (Lang and Hornburg, 1998).

A recent study of New York City's reprivatization of distressed housing examines the role of cooperatives in building social capital in neighborhoods:

> "Resident ownership was strongly related to better building security and quality and to lower levels of crime. Social capital was higher in tenant-owned co-ops and mediated the effect of ownership on building conditions… This study indicates that social capital, even among very poor tenant populations, can add value to government investment in housing. The New York City experience with reprivatization of distressed housing documents the success of tenant-owned co-

> ops in creating or sustaining social capital and in providing good housing conditions". (Saegert and Winkle, 1998)

The same study also recognized the importance of a support structure to the success of resident ownership:

> "Strong intermediate associations linking co-ops to each other locally and nationally would improve their political and practical viability".

The first section of this report presents the case studies of four rural housing cooperatives funded through the 515 program. A detailed regulatory review follows the case studies. Recommendations and conclusions, based on the regulatory review and the case studies, are included in the final section.

INTRODUCTION TO THE CASE STUDIES

Four cooperatives in three states were selected for case study. No selection criteria were needed, since these were the only 515 program-financed cooperatives identified by the national RHS office. A presentation at a multi-family housing policy conference, in August 1999, elicited the discovery of one additional cooperative in Arkansas. This brings the total to 5 cooperatives out of the entire multi-family portfolio.

These cooperatives were studied:

Cielo Azul - Taos, New Mexico
Eleven Mile Corner - Casa Grande, Arizona
Happy Acres - Queen Creek, Arizona
Hope Village - Wolcott, New York

All four are fairly small, ranging from 8 units to 40 units. Cielo Azul is on the edge of Taos, but the others started in isolated rural areas. Happy Acres is in an area that's experiencing rapid development due to its proximity to Phoenix, but Hope Village and Eleven Mile Corner are still miles from a city or town.

Although each of the co-ops developed quite differently, they share some common characteristics. They were all started in the late 1970s or early 1980s, although Cielo Azul wasn't actually opened until 1996. The co-ops each had a connection with farm labor housing. The original impetus for Hope Village, Eleven Mile Corner and Cielo Azul was to provide housing for farm laborers. The first members of Happy Acres included people who did occasional farm work, and, like Eleven Mile Corner, they received technical assistance from the National Council of La Raza (NCLR). NCLR and Tierra del Sol, the non-profit developer of Cielo Azul, were both listed as Technical Assistance Organizations in the Rural Housing Cooperative Demonstration program, which was funded in 1979-81 by FmHA and HUD.

All of the co-ops are currently in reasonable financial condition, although there have been significant financial and management problems in the past. Two of the three older cooperatives recently had substantial renovation, and the third is in the midst of a rehabilitation project. In each of the co-ops, the board president has assumed significant duties, with a fairly inactive board of directors. Happy Acres and Cielo Azul have contracts with property management companies that are familiar with the 515 program, Eleven Mile Corner contracts with a local Housing Authority, and Happy Acres will probably sign a contract soon with a small management company.

Protocol and approach

Research and analysis of the four cooperatives was undertaken to answer these questions:

- Have regulations have presented barriers to rural cooperative development and operation?

- How have support systems operated in the development and operations of the rural housing cooperatives?

- Are cooperatives a viable alternative to rural rental and/or homeownership?

Each of the cooperatives was visited once between April and July 1999. Interviews were conducted with co-op members, board presidents, members of the boards of directors, management company staff, and representatives from the organizations that helped develop the co-ops. RHS staff were also interviewed, including the servicing staff and the multi-family housing specialists. It was impossible to interview the co-op developer at Hope Village (due to her poor health), but an interview was conducted with a retired FmHA staff member, who had worked closely with the co-op. The files of each co-op were reviewed for incorporating documents, bylaws, budgets, financial statements, and other items documenting the history of the co-op.

CASE STUDY SUMMARIES

CIELO AZUL COOPERATIVE

Cielo Azul is a 22-unit housing cooperative in Taos, New Mexico. The residents are all very low income, receiving rental assistance. 48% are Hispanic, 20% Native American, 5% Asian, and the rest are white non-Hispanic. Women are listed as head-of-household in 86% of the units.

History

Although Cielo Azul held it's Grand Opening in 1996, the project has a long history. The cooperative was incorporated in 1980. Ten families initiated the idea of building housing for themselves in the Taos area. They went to a local non-profit, but were referred to Tierra del Sol (TDS), which had more housing experience, although it was based in the southern part of the state. The families' income was too low for the Self-Help Housing program, but they liked the concept of working toward homeownership, so the housing cooperative idea was attractive. Tierra del Sol was interested because they were one of the technical service organizations involved in the Rural Cooperative Housing Demonstration project, and they thought this co-op might be a vehicle for organizing more housing in northern New Mexico.

The project was supported by the FmHA office in Albuquerque from its inception. The Taos area needed housing, and there was a feeling that the co-op concept could work in that area, possibly because incomes were a little higher. TDS incorporated the co-op, with bylaws, and they applied for a FmHA loan and purchased the land. The land and preliminary costs were paid for through a partnership between TDS ($18,000), HELP ($25,000), and the Housing Assistance Corporation ($8-10,000). FmHA obligated the loan, with a 20 year Rental Assistance contract. During this period, political issues surfaced in Taos, where the community considered TDS an "outsider". TDS finished the application, but then turned the project over to a local non-profit. There was no progress for over 10 years. Most of the original families remained interested in the project during this time, and eventually TDS was asked to return. They subsequently initiated a new market survey and developed new plans and budgets.

Financing from multiple funders

Since the value of the obligated dollars had shrunk due to inflation, the group had to downsize the number of units originally planned, and seek additional funding. In 1995, the sources and uses statement listed these funders:

RECD	$1,024,450
New Mexico State Housing Division HOME (93)	155,000
New Mexico State Housing Division HOME (94)	100,000
Neighborhood Reinvestment Corp. FY (96)	100,000
Federal Home Loan Bank	125,141
McCune Foundation	15,000
Tierra del Sol Housing Corp.	58,000
Irrevocable Letter of Credit	163,192
TOTAL	$1,740,783

The HOME loans are forgivable, as long as the units are occupied by very low income residents for at least 10 years. Similar guidelines apply to the loans from the Federal Home Loan Bank and the McCune Foundation.

Construction problems

There were continuing problems during construction. They had major problems with the contractor, who eventually defaulted. The co-op had to sue, and the project halted during three years of litigation, with the half-finished site a major eyesore in the community. All these delays were costly and time consuming, but the new contractor finally finished the project in 1996.

Governance and management challenges

During the sixteen years between formation and construction, the co-op met regularly. Seven of the original families were still involved, and there was a long waiting list. At the time of move in, 35 families had applied for membership in the co-op.

The first year was difficult. TDS contracted with HELP, a non-profit with housing management experience, but there were numerous problems. The most severe problems were related to finance. The reserve account wasn't funded, non-budgeted items were purchased, and accounting records were poor. The reserve losses were eventually reimbursed, but other problems weren't solved so easily. For instance, the co-op had budgeted $12,000 for landscaping and erosion control, but it never completed. This caused problems with the city of Taos, and the co-op is still dealing with costs and requirements related to erosion.

Co-op members had problems with both the site and resident managers hired by HELP. There were also conflicts between co-op members. Within a year, four of the original families had moved out, after damaging their units significantly. There were tensions between residents, and the co-op had to hire security for three months. The damaged units were eventually repaired, new people moved in and the atmosphere improved. A new board was elected, and the co-op considered management alternatives, including self-management. TDS continued to play an advisory role, helping with policies and procedures. RHS staff recommended hiring one of their approved management companies, and Monarch Properties was eventually chosen by the co-op board in September 1998.

Current issues

As a professional management company, with diverse multi-family management experience, including other 515 program projects, Monarch Properties has stabilized the financial situation, has good relations with RD office, and has provided continuity in their on-site manager. The vacancy rate is very low, maintenance is improving, and the co-op provides decent subsidized housing to 21 very low income families in a costly housing market. Nevertheless, Cielo Azul faces some major challenges:

- A low level of member involvement
- Lack of outside assistance in implementing the co-op model
- Confusion about equity and ownership
- Management company resistance to the co-op model
- Isolation from the larger community

Without a stronger sense of member ownership, the co-op structure at Cielo Azul will become increasingly marginalized, with less tenant input or control. Rental is the customary, comfortable environment for most people of the people involved, including members, RD staff, and management. Cielo Azul is the only co-op in the 107 rural rental projects serviced by the RD office, and Monarch has no other co-ops under contract. The new board hasn't received training, and many members didn't know they were joining a co-op when they moved in.

New members are asked to pay a $195 "co-op fee" in addition to their security deposit, and receive documents that mention co-operative policies, but most of the interviewed members reported that they didn't know they were living in a co-op until they were invited to a membership meeting.

Not surprisingly, attendance at meetings is low. There are supposed to be monthly board meetings, but it's difficult to get everyone together. Most of the board members have involvement in other community organizations, and are interested in getting involved, but their role isn't clear. The board president is often overburdened -- she serves as a liaison between management and residents on maintenance issues, in addition to fulfilling her co-op responsibilities.

There is no evidence of contact with the broader cooperative community, on either a local, state or national level. TDS continues to act as an occasional advisor to the board, but they don't provide systematic training. There is a general lack of understanding of ownership and equity. A TDS staff member believed that the members wouldn't own the co-op until they had paid off the loan. No one seemed to be aware that membership in the co-op could provide financial benefits to members, even within the limitations of the RHS regulations.

Discussions with a Monarch staff member made it clear that he believes that the co-op structure requires time from the residents without returning any benefits. He believes that there are no tangible ownership privileges. Since Cielo Azul is currently managed very similarly to a 515 rural rental, his statements are fairly accurate. For instance, he believes that RHS regulations forbid any alterations on units. He didn't know that the co-op regulations make specific provisions for allowing members to increase the value of their unit through individual alterations.

Although the literature reports that co-ops are higher in social capital than other forms of rental housing ownership, Cielo Azul seemed relatively isolated from the local community, and some members reported a sense of isolation within the project. The small community room at the co-op is rarely used, except for co-op meetings. There were no connections to non-profits that might provide children's programs, health screening or other services to this group of very low-income residents.

On the positive side of the social capital issue, the board has investigated grants for school supplies, playground equipment, and a Kellogg-funded technology training center. One of the board members recently joined the policy council at her children's school, and another advises the student government group at her college. Members reported that Cielo Azul was a "quiet" place to live, with no safety or security problems.

Notes on the Interviews:
Interviews were conducted April 19 – 21, 1999, with the following:
Carmen Lopez, USDA-RHS, Albuquerque, NM
Buddy Stow, Property Supervisor, Monarch Properties
Jack McIlvrey, President, Monarch Properties
Isabelle Padilla, USDA-RHS, Santa Fe, NM
Gene Gonzales, Property Manger, Tierra del Sol
The board president, vice president, secretary and treasurer
Co-op members

ELEVEN MILE CORNER COOPERATIVE

Eleven Mile Corner Housing Cooperative is a 16 unit complex located in a rural area outside of Casa Grande, Arizona, about 50 miles south of Phoenix, Arizona. Turnover is low, with the average length of occupancy 47 months. 87% of the residents are Hispanic. 14 of the 16 households receive rental assistance. Household incomes range from $3,300 to $28,392.

History

Eleven Mile Corner is on the site of a farm labor camp built for displaced dust-bowl-era farmers by the U.S. Farm Security Administration. The camp was built in the 1930s and closed during the Eisenhower administration. Pinal County eventually got title to the land, which was in an isolated area. The buildings had deteriorated, but there was still a good infrastructure for housing. Local growers were anxious to have more housing available for their workers, so the Pinal County Housing Authority began looking at options for building new housing on the site.

At the same time, there were many groups in the Southwest during the 1970s and 1980s who were organizing and advocating for farm worker housing, including the co-op model. The National Council of La Raza (NCLR), along with Tierra del Sol in New Mexico, were involved in the rural co-op housing effort at a national level. Pinal County asked them to assist with the Eleven Mile Corner project. It wasn't hard to find a group of interested members. Outreach through the growers was very effective. A group of potential members was identified who participated in the design process. Their application for $800,000 was approved in June 1981. The complex was 100% funded by FmHA. NCLR received some payment for their development work, although it was well below their actual costs.

Governance and management challenges

The co-op opened in 1983. It quickly became obvious that there were problems with the design, which was characteristic of housing in Puerto Rico. NCLR served as manager for the co-op, but this wasn't their area of expertise. There were financial problems and deferred maintenance issues. As early as July 1984, a FmHA inspector reported that the project was "a disaster".

During this same period, there is evidence that co-op members were actively involved in the co-op. They were part of the member selection process, and participated in the decision making. Staff at NCLR were knowledgeable about the co-op model, and letters from FmHA staff indicate a similar understanding.

Eventually, NCLR decided to withdraw from management, and the contract was transferred in 1992 to the Pinal County Housing Authority, which has an office close to the co-op, and manages several HUD sponsored complexes on the same site. Because of the deferred maintenance and problems related to the original design, the RD office recommended that the co-op apply for a rehabilitation loan. The $356,800 loan was approved in 1997. At this time, the unpaid principal was $615,675, so the co-op essentially increased its debt by 50%.

RHS staff worked with the members on design issues before the rehabilitation process started. The rehab included re-designing the doors, windows, walls and breezeways, replacement of plumbing and electrical fixtures, flooring and kitchen countertops, interior and exterior painting, and converting the grounds to desert landscaping.

Current issues

According to everyone interviewed, there is a good social network with Eleven Mile Corner Co-op, and members participate in the larger community through the schools, cultural events, and the Family Resource Center. The Family Resource Center is located in the co-op's community room, but it serves all of the Pinal County Division of Housing residents. The Center offers many services, including free clothing, training, access to social services staff, children's programming, and health screening.

RD and Housing Authority staff reported that families in Eleven Mile Corner seem to have closer ties than families in rural rental complexes. Co-op members agreed that neighbors support each other, and have created a quiet, safe community. They volunteer in the schools and the Family Resource Center, and helped to raise over $700 recently so that a member's child could go to Washington DC.

The co-op president is concerned that board members aren't very active, but he's pleased about good attendance at membership meetings. He has a background as a farm labor organizer, and is familiar with agricultural co-ops and co-op housing. He feels there are lots of opportunities for co-op members to take advantage of their ownership status and make improvements. He initiated work on the parking lot, which was finished recently, and plans to start fundraising so that they can offer ESL and GED courses in the community room.

Maintenance issues are a source of frustration for co-op members. The board president would like to encourage self-sufficiency by asking people to do their own maintenance, but the Housing Authority discourages it by imposing penalties if there are problems. This is an example of the Housing Authority's reported reluctance to manage the co-op any differently than their other complexes. RHS staff have assisted the cooperative and the Housing Authority in working through some of these issues, but there is legitimate confusion about policies and procedures. The Housing Authority handles only one cooperative, the RD office has only two, and they are working in isolation from a larger support network.

Eleven Mile Corner also faces the problem that leaders in the co-op may leave the co-op to purchase their own homes. Cooperatives are a form of group-based home-ownership, but this is not a widely understood model. Most of the people involved in Eleven Mile Corner view true ownership as devolving to members when the mortgage is paid off. There seems to be no recognition of the possibility of financial benefits for current members, based either on appreciation of the value of the unit, or payment of a percentage of the principal. This mindset leads most people to view single-family home ownership as the obvious alternative strategy, and this option is currently affordable and well publicized.

Notes on the Interviews:
Interviews were conducted May 19 – 21, 1999 with the following:
Steve Langstaff, Multi-family Housing Coordinator, USDA-RD, Phoenix, AZ
Johnna Vargas, Multi-family Housing Loan Specialist, USDA-RD, Phoenix, AZ
Walt Ellsworth, Architect, USDA-RD, Phoenix, AZ
Delia O'Neal, Pinal County Housing Authority
Adeline Allen, Director of Housing, Pinal County Housing Authority
Mark Van Brunt, Deputy Vice President, National Council of La Raza
The board president
Co-op member

HAPPY ACRES COOPERATIVE

Happy Acres is located in a fast growing area outside Phoenix, Arizona. This area was once very rural and isolated, but is now considered a semi-rural suburb of Phoenix, with exclusively single family homes. Happy Acres is an 8-unit complex of separate single family homes, with a large community center or "clubhouse". There are six 2-bedroom units, at 861 square feet, and two 3-bedroom units at 1,221 square feet. Turnover is low, and most of the members are connected through family or friendship ties. Household incomes range from $5,520 to $14,332, and all of the residents receive rental assistance. Tenant records list 7 households as white and one as Hispanic.

History

Happy Acres is located on property that was originally owned by one of its founding families. The family moved to Arizona in the 1950s, bought 2 acres, and set up a trailer. Family and friends joined them on the site, and it became a destination for an informal network of people during the next 20 years.

By 1978, 23 people were living at the site and the area was becoming less isolated. Maricopa County officials were threatening to remove the mobile-housing units, which didn't conform to zoning ordinances, and houses, which didn't meet Health Department code standards. A number of solutions were explored, with assistance from a Maricopa County planner and a Community Legal Services attorney.

The residents were a tightly knit, independent community. According to their attorney, "The people of the community have demonstrated adaptability to their limited resources, creating a lifestyle perceived by them as satisfactory, but one that has not kept pace with modern county standards of zoning, health and safety. In order to maintain current community status and sustain their interdependent support system, it appears necessary that they remain together." (Preapplication 1978). They were advised to form a cooperative, and apply for a loan through Section 515. A FmHA loan was approved in 1980 for $370,000. The original owner donated the land to the cooperative, and the project received $23,500 in county revenue-sharing funds, to provide support financing. The complex was completed during the same year, or early in 1981.

Management and governance

The co-op continued to receive assistance from the Legal Service attorney during the 1980s, as well as from staff at the National Council of La Raza (NCLR). The attorney had contacted NCLR for help in applying the FmHA loan, since NCLR had gained experience at near-by Eleven Mile Corner cooperative. NCLR was contracted to act as an advisor to the co-op: helping them prepare budgets, run meetings, file reports. The co-op also contracted with a property management company to handle collection of rents and bookkeeping. Both of these relationships apparently ended in the mid-1980s. The co-op then became self-managed, with assistance from RD staff.

The original owner of the property and "patriarch" of the group served as board president until he died in 1981, when his wife took over the role. She currently also manages the co-op finances and handles maintenance, member selection, and other operational issues. RD staff have encouraged her to find a replacement, and have offered to help train interested co-op members. They also helped the co-op directly by setting up budgets and bank accounts. Because progress on identifying a viable replacement seems slow, and RD staff time is limited, staff is currently recommending that the co-op contract with a small management company for services.

Community, rehabilitation

Happy Acres residents have maintained their close ties, although the board president is nostalgic for the old days, when people shared more activities. RD staff members believe that many of the members are still related, or at least friends. The turnover rate is low, so they rarely have vacancies. It is a very homogenous community.

They have maintained what RD staff refer to as a "rural lifestyle", with homemade sheds for farm animals, including pigs, chickens and horses. RD files include comments on this issue from as early as 1982: "There is a problem with living standards – animals in homes and very low standards of home maintenance. Occupants need guidance". With the encroachment of high value suburban homes, members of the co-op began to get complaints about the unsightly appearance of the property and the presence of the farm animals. Three years ago, the site inspection report was very poor, and an overflowing septic system caused health concerns. RD staff urged members to consider applying for a rehabilitation loan. Members were originally resistant, but eventually began to cooperate with the planning process. In early 1999, the co-op received a rehabilitation loan for over $200,000. It will pay for extensive renovation of every unit, exterior painting and clean up, standard storage sheds, fencing, and new roofs. When the co-op was visited in May 1999, members were complying with their obligation to clean up the area around their units, prior to the beginning of the rehab.

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Johnna Vargas, Multi-family Housing Loan Specialist, USDA-RHS, Phoenix, AZ
Walt Ellsworth, Architect, USDA-RHS, Phoenix, AZ
Mark Van Brunt, Deputy Vice President, National Council of La Raza
The board president

HOPE VILLAGE COOPERATIVE

Hope Village is a complex of 39 units in an area outside of Wolcott, New York, in rural Wayne County. The co-op owns 25 acres, and is divided into two distinct neighborhoods: an area of 25 single-family manufactured homes (5 – 4 bedroom and 20 – 3 bedroom), and another area of 15 2-bedroom townhouses. It began as a diverse community, and has remained diverse. There are 13 African American families (34%), 23 white families (60%), one Hispanic (3%) family and one Asian (3%). Annual household incomes range from $2,860 to $28,005, and all of the units are eligible for HUD Section 8 funds.

History

Hope Village was the second cooperative financed by the FmHA under the Section 515 program (Hope Village Monitoring Committee, 1981). The first 25 units were built in 1978, with a $825,400 loan from FmHA and a $279,380 grant from HUD for water and sewer installation. They had earlier received an interest-free loan of $31,168 from the Housing Assistance Council for land acquisition and start-up costs. This loan was repaid with funds from the FmHA loan.

The project grew out of a migrant educational program directed by a local social worker in the mid-1960s. Housing conditions for farmworkers in the area were poor, and there were few options available, particularly for African Americans. The social worker, Mrs. Maudie Weeks, worked with a group of farmworkers to explore options for building new housing. The cooperative model seemed attractive, because it offered elements of ownership and independence to the group. Although the project received support from a "large group of professionals in the housing and banking industries" (Hope Village Monitoring Committee, 1981), it met strong resistance from the local community. This was the first subsidized housing built in the three adjacent townships of Huron, Wolcott and Rose. The group struggled for ten years against racial prejudice, an illegal retroactive zoning ordinance (imposed specifically to block the project), and initial resistance from funding agencies. During that period of struggle, the group developed strong personal relationships and strong ties to Mrs. Weeks. Current members of Hope Village still credit Mrs. Weeks for the success of Hope Village.

Early management

Since the co-op was interested in self-management, and FmHA had no experience with self-managing co-ops, the agency stipulated in its loan agreement that a committee be established to monitor and evaluate the project. The chair of the committee was the Director of the Office of Community Investment at the Federal Home Loan Bank Board, and committee members included an attorney with the National Committee against Discrimination in Housing and an Extension Associate at Cornell University. In 1981, they submitted a report to the co-op, FmHA, and HUD. For 10 months, the Committee attended board meetings, examined financial records, interviewed members and representatives of local organizations. This is a summary of the Committee's conclusions:

> "[The report's] basic findings are that Hope Village is on sound footing financially, that its members have come to understand and embrace the idea of cooperative ownership, and that on the central issue of self-management, Hope Village is moving in a positive direction towards developing leadership capabilities among its members. By so doing, Hope Village has done invaluable groundwork for future rural coops, for which it also stands as a viable prototype." (Hope Village Monitoring Committee, 1981)

The report provides an invaluable summary of the issues confronting this co-op in the first years of operation:

- Although members who were part of the organizing group had received training on FmHA regulatory documents, most members had little experience with finance, home care, or self-government.

- The board was reluctant to enforce rules against their peers, including non-payment of rent and maintenance violations. Arrearages became a problem very quickly.

- Although the board received significant training and assistance from Mrs. Weeks, FmHA staff, and an Extension specialist from Cornell University, there was concern that the board was too dependent on these advisors.

- There were some initial tensions between the organizing group and families who joined the co-op after it was built. The co-op developed a "well-organized communications network", including a newsletter, informal meetings, an extensive committee structure, and youth activities. By 1981, the Committee reported that a collective spirit had replaced the earlier tensions, and a "strong and positive Hope Village identity has developed".

Additional building on the site

Hope Village was considered so successful during the mid-1980s that the co-op was encouraged to build more housing on the 25-acre site. The co-op had a long waiting list, and was beginning to receive support from local community leaders. An application to build 15 units was approved in 1983, but there were disagreements about the design, and the complex wasn't completed until 1986, for a total cost of $666,900. These units were also eligible for HUD Section 8 assistance.

Although there were 40 units in the complex by 1986, the co-op had no central place for meetings, classes or social events. A co-op member who grew up in Hope Village remembers crowding into peoples' living rooms for 4-H meetings and other events. In order to raise grant funds to build a community center, Maudie Weeks formed a separate non-profit, Hope Services, Inc. The non-profit also seemed like a good mechanism for getting people outside the co-op involved in supporting and providing services for the co-op, since the board could be drawn from the broader community. The co-op gave Hope Services a small section of land for the Center, and a building was built in the early 1990s, with space for offices, laundry and a large community room.

Management problems

Happy Acres was self-managed during the 1980s, and, although there were occasional concerns about financial issues, the problems became a crisis in 1992-93. The co-op's expenses were significantly higher than its income, reports had not been filed with FmHA, there were conflicts among board members, and there were concerns about Mrs. Week's leadership. She had continued to be very closely involved as an advisor the co-op, but at this point she was in her early 80s. Her close personal relationship with some of the co-op members, and strong personal identification with the co-op, may have contributed to some of the problems. In February 1993, 19 out of 40 families were behind in their monthly fees, and arrears totaled over $17,000. Board minutes reflect discussions of the arrears, and eviction policies, but in the spring of 1993 serious concerns arose about the long-time treasurer, who was also a co-op member. She was eventually charged and convicted of embezzling $20,000 from the co-op. During this period, Mrs. Weeks left her official position as advisor to the co-op, and FmHA requested that the co-op contract with a professional management company. The current company, Baldwin Real Estate Corp., was selected in 1994.

Rehabilitation

Although a management company had been hired, FmHA was still threatening liquidation of the project in June 1994. There were health and safety violations, an IRS lien for payroll withholdings, and over $67,000 in property taxes owed. Baldwin Corp. had discovered that the project should have received over $400,000 in HUD subsidies that were never applied for, and eventually negotiated a recovery of these funds. Although members still received Section 8 assistance, Baldwin also negotiated an increase in the monthly subsidies paid by HUD to the co-op. These changes helped to solve the co-op's financial problems, and paid for an ongoing rehabilitation project, which started in 1996. 23 out of the 25 units have received new siding, heating, insulation, and other improvements. The last two units will be completed this year.

Current community and management issues

The current president of the Hope Village board grew up in the co-op, and her mother was one of the original members. Although she's nostalgic for some of the activism of the past, and wishes the board was more active, she reported that members attend meetings, participate in the Selection committee, and plan social events for families and children. Members also contact her with their concerns about maintenance and the behavior of other members. They expect her to act as a liaison with the management company.

Members expressed satisfaction with the community atmosphere, safety and security at the co-op. They appreciated the low monthly charges, and the chance to express their opinions through the co-op structure.

Baldwin Real Estate staff also reported that co-op members knew each other well, and considered Hope Village home. Many co-op members have a long history of involvement, and a reciprocal relationship has developed between staff and members. Co-op members help staff understand community traditions, and staff has helped organize board meetings and re-started publication of the co-op newsletter.

Notes on the Interviews:
Interviews were conducted July 19-21, 1999 with the following:
Micky Sergent, USDA RD, Cannandaigua, NY
George Von Pless, USDA RHS, Syracuse, NY
Mark Meyer, Maintenance, Baldwin Real Estate
Sue Decker, Site manager, Baldwin Real Estate
Bill Durdell, President, Baldwin Real Estate
Carolyn Hensler, Baldwin Real Estate
Dick Howard, retired, FmHA
The board president
Co-op members

CASE STUDY ANALYSIS

This section examines each of the hypotheses in light of the case study findings, using examples from the four cooperatives studied.

<u>Have regulations have presented barriers to rural cooperative development and operation?</u>

Regulatory barriers manifest themselves in three ways:
- The actual content of the regulation is a barrier.
- The regulations are contradictory or unclear.
- The form of the regulation is a barrier because instructions are scattered and difficult to locate.

Barriers existed in both the development and operational phases of the cooperatives studied, although they assumed varying importance.

Concern about the challenges presented by the cooperative housing regulations is not new. The challenges were discussed 18 years ago in an “Evaluation of Hope Village”, written in 1981 by a FmHA and HUD-appointed Monitoring Committee. This comment refers specifically to the form of the regulation:

> "An ongoing problem for all rural coops is that FmHA has never written self-contained regulations for cooperative ownership. Such regs as exist dangle as an incomplete and terribly confusing addendum to FmHA's Section 515 Rural Rental Housing. It would seem that with the growing interest in rural coops, FmHa should publish comprehensible regulations. Not only would this facilitate coop development, but it would also make it possible to analyze trends of coop use." (Hope Village Monitoring Committee, 1981).

The RHS regulations' specify that the ideal cooperative will be self-managed. In their evaluation of Hope Village, which had been in operation for almost three years, the 1981 Monitoring Committee reported that:

> "The present Board and committee will soon be able to take over full management of the project. By their own admission, another year to 18 months will be needed before full mastery of the intricate and complex regulations of FmHA and HUD can be assured."

Evidence of regulatory barriers to cooperative development

The regulations limit the amount of compensation available for a non-profit advisor to a cooperative. Non-profit cooperative developers risk being minimally compensated to implement an innovative model with very few guidelines and many potential obstacles. In three of the four co-ops studied, there is evidence that the development phase of the cooperative required resources beyond the capacity of the advisors.

Hope Village. Maudie Weeks acted as an individual advisor to Hope Village. She was a retired social worker, with no formal connection to a non-profit. According to all reports, she spent countless hours supporting the development of the co-op, and received no compensation. Her efforts were critical to successfully developing the co-op, but this was a unique situation that would be impossible to advocate as a model. After the co-op became operational, Weeks continued her voluntary work as an advisor. This provided a critical continuity to the co-op, but eventually the effort of being in involved in the day-to-day operations of the co-op became too great. Weeks finally left her advisory position in the midst of a serious financial crisis.

Cielo Azul. Tierra del Sol was the non-profit developer of this cooperative. Although the original budget for the project had been approved in 1980, Cielo Azul wasn't actually finished until 1996. This time lag meant that all of the finances had to be re-negotiated, and funds were short. In 1994, they submitted a budget to the RD office which included a request for compensation:

> "The developer fee to Tierra del Sol is applicable under FmHA Instruction 1994.212(j). This is for the technical assistance and developer services provided

> by Tierra del Sol. The amount represents a 1% fee as a minimal consideration for services provided by Tierra del Sol." (Letter from Sal Estrada, 1994)

This line item was eventually eliminated from the budget. In a letter to the RD office dated August 23, 1995, the director of Tierra del Sol commented on the elimination of the developer fee:

> "The developer fees in the amount of $25,000 to cover the costs of Tierra del Sol have been eliminated. These fees would include costs associated with the preparation of application documents, staff time, travel and other associated costs. The amount eliminated was minimal vis a vis the costs incurred by Tierra del Sol." (Letter from Rose Garcia, 1995)

Happy Acres. This co-op was developed with significant in-kind assistance from a Community Legal Services Attorney and a staff member from the Maricopa County Budget and Research Department. The co-op contracted with the National Council of La Raza (NCLR) for advisory assistance during its first years of operation. NCLR helped the co-op prepare annual budgets, run meetings, complete reports, and certify members for Rental Assistance. This relationship eventually ended. The Attorney continued his association with the project for several years. Agency concerns about the project surfaced very early. A file note dated March 22, 1982 states "There is a problem with living standards – animals in homes and very low standards of house maintenance. Occupants need guidance" (File notes by Bob H., 1982).

Eleven Mile Corner. The National Council of La Raza (NCLR) was the non-profit developer for this co-op. NCLR received some payment for their development work, but the funding was gone after two years and it took four years to build the project. After completion, NCLR acted as management agent, but this wasn't their primary business and economies of scale are not possible on such a small project. According to Mark Van Brunt of NCLR, NCLR was losing money on the service and eventually advised members to hire the Pinal County Housing Authority for property management services.

In summary, the case studies reveal a number of problems with relying on under-paid non-profit support for development:

> There are relatively few non-profits involved in the development of rural housing, much less rural cooperative housing. It may be very difficult to find a local nonprofit with the expertise necessary to develop a co-op. For example, the construction of Cielo Azul was delayed for ten years because the original developer, Tierra del Sol, withdrew from the project in favor of a local group. The local group lacked the skills to lead a multi-family housing development, and the project languished for ten years after loan approval.
>
> Non-profits don't always have the resources to support the vertically integrated model that is common among for-profit owners. In any case, since they aren't

owners of the co-ops, the non-profits have no assurance that they will be rewarded the maintenance contract after the co-op is built.

If a non-profit developer is underpaid for development work, they may not have the capacity to continue a positive relationship with the co-op after construction. Cooperative boards, members, and managers need ongoing training in co-op principals and operations. Ideally, a non-profit co-op developer would be able to provide this training, or partner with other organizations that specialize in this area.

Evidence of regulatory barriers to the positive operation of the co-ops: the important issues of ownership, membership selection and maintenance

Ownership

One of the key differences between the cooperative model and the more familiar rental model is the concept of "ownership". At all four cooperatives, people talked about the benefits of members taking ownership, but in each case there was either confusion or ignorance about the definition of ownership. This was true for members, property managers, and agency staff.

There is no single definition of ownership in housing cooperatives, but it usually includes the concepts of democratic control, and the opportunity for some financial gain through membership in the co-op. Transfer value, patronage capital, equity appreciation, and membership fees are discussed in the regulations and exhibits, but minimal guidance is offered for handling these important, but possibly unfamiliar concepts.

This is a particularly difficult issue in the context of the low-income member population of these cooperatives. The financial incentives that would give them a sense of ownership in the cooperative are very limited in the current regulations, but it is possible that these limited incentives could be significant if they were applied consistently. This is a subject that deserves additional study.

Transfer value is discussed in §1944-E Exhibit D-1 (Sample Bylaws):

> Article II Section 2.10. Transfer value. Whenever a membership is transferred to the cooperative, the term "transfer value" shall mean the sum of:
> a. The membership fee paid by the member on the books of the cooperative, and
> b. The amount of patronage capital which has accrued to the member during his/her period of membership as shown on the books of the cooperative.

Patronage capital is defined as excess operational costs in §1944-E Exhibit D-1 (Sample Bylaws):

> Article II Section 2.06. Patronage Capital.
> All funds accruing to the cooperative during the year, above and beyond the costs and expenses of operating the cooperative, shall be assigned to each member on the books of the cooperative as patronage capital at the end of each fiscal year….

Capital accounts based on contributions to principal are mentioned in §1944-E Exhibit J (Occupancy Agreement), although there are no directions on distribution of these accounts:

> Section 1.02…That amount of the occupancy charge required for payment on the principal or mortgage of the Cooperative or any other capital expenditures shall be credited upon the books of the Cooperative as a capital contribution by the Members.

Cooperative limited equity is discussed in §1944.215(h):

> (1) RCH loans will only be made to cooperatives which limit the accumulation of equity…
> (2) Inflation equity which accrues on cooperative property is not considered part of members' limited equity and will not be taken from the project when a member vacates the project.

This section also refers to Exhibit H, the "Limited Equity Agreement", which includes additional language on equity, essentially defining it as patronage capital.

> (a) Equity accumulated by the cooperative, other than through the appreciation in value of real estate, furnishings, and equipment of the cooperative, will be assigned on the cooperative's books equally to members at the end of its fiscal year and in accordance with the Internal Revenue Service ruling concerning patronage capital.
>
> (e) Only membership fees and money accrued in the members' patronage capital accounts will be distributed to the members and represents the entire equity payment to which the members are entitled…

Cooperative membership fees are defined in §1944-E (g):

> Cooperative housing is a form of homeownership. In order to promote a commitment from prospective members, cooperatives will require a membership fee. The membership fee established by the board of directors will be equal to one month's occupancy charge.

Hope Village. The definition of transfer value differs at Hope Village from the definition found in the current regulations. The Hope Village Bylaws define transfer value as the sum of the membership fee and "The amount of principal paid by the Corporation on its mortgage indebtedness exclusive of the FHA contribution and attributable to the dwelling unit as paid by the member…" (Bylaws of Hope Village, 1986). This policy was not consistently followed during the early years of the co-op. The current property management company is working with their accountants and RHS staff to prepare proposed bylaw changes so that transfer value can be accurately accounted for and credited to departing members. The cooperative's auditor will not issue final financial reports until these changes are made.

Eleven Mile Corner. The Bylaws define transfer value similarly to Hope Village. The co-op is not following these policies. The membership fee is treated as a security deposit and there is no attempt to calculate the amount of principal paid by departing members.

Cielo Azul. The co-op requires a membership fee in addition to the security deposit, but there are no other additions to the transfer value when a member moves out. Although the RHS's sample bylaws for a cooperative allow for some financial gain for owners through a return on patronage, members of Cielo Azul actually have no hope of receiving a patronage refund, since the co-op's Articles of Incorporation prevent it:

> VIII. …"No part of its net earnings shall inure to the benefit of any member, director or individual. The balance, if any, of all money received by the cooperative from its operations, after payment in full of all operating expenses, debts, and obligations of the cooperative of whatsoever kind and nature as they become due, shall be used to make advance payments on debt service or reserve accounts of the cooperative, to lower the lease-rental charge to occupants of the housing, or for other related purposes". (Restated Articles of Incorporation of Cielo Azul, 1995)

This is identical to the language from §1944-E Exhibit C for rental only. Like the other cooperatives studied, Cielo Azul apparently used the sample Articles and Bylaws from the regulations, but they didn't use the co-op models. They used the rental language in §1944-E Exhibit C (Articles of Incorporation) and the Sample Bylaws for a nonprofit corporation (§1944-E Exhibit D).

Member Selection

Member selection is discussed in §1944-E Exhibit D-1 (Sample Bylaws). Although the language seems to be clear, it provides no guidance for the complexity of handling member selection in an environment of waiting lists, rental assistance, Section 8, and management companies that are much more familiar with rural rentals than cooperatives.

This is the language from §1944-E Exhibit D-1 (Sample Bylaws):

> Article IV, Section 4.01… The powers of the board of directors shall include but not be limited:

a. To accept or reject all applications for membership and admission to occupancy of a dwelling unit in the cooperative housing project, either directly or through an authorized representative.

Each of the co-ops that employed a property management company depended on the company to screen and select applicants. The on-site managers handled member selection as if the co-ops were rental complexes. In Hope Village and Eleven Mile Corner, where the Bylaws include this language, the boards interview members after they've been selected by the on-site manager. They have no role in accepting or rejecting applications for membership, and none of the board members seemed to be aware that they had delegated that authority.

Member Maintenance Responsibilities

Member maintenance is addressed in §1944-E Exhibit J (Sample Occupancy Agreement):

> Article 11 Repairs.
> Section 11.01. By Member. Member agrees to repair and maintain Member's dwelling unit at own expense as follows:
> (a) Any repairs or maintenance necessitated by Member's own negligence or misuse;
> (b) Any redecoration of own dwelling unit authorized, done or contracted for by Member;
> (c) Any repairs, maintenance, or replacements required on the following items: (Insert the items desired, subject to FmHA approval.).

Each of the co-ops that distributed an Occupancy Agreement included the standard language about member maintenance responsibilities in the document. In practice, this differentiation between rural rental and co-op living seems to have been ignored. Although self-maintenance was referred to frequently during interviews, there was substantial confusion about the relative responsibilities of members and management.

Hope Village. The only member maintenance responsibility currently enforced at Hope Village is "maintenance of the yard around his/her home".(Occupancy Agreement) If members don't mow their grass, they're charged a small fee and the property management company takes care of it. Maintenance staff reported that few people fix up their own units beyond decorating. The members basically behave like renters.

Member maintenance was a more important goal in the early years of Hope Village. In a 1981 evaluation of Hope Village, the Monitoring Committee reported that although residents "failed to understand exactly which maintenance responsibilities were theirs", the Maintenance Committee was "conspicuously successful in serving as liaison between the members of the cooperative, the two maintenance employees and the Board of Directors. The committee also succeeded in explaining to the members which repairs and improvements are the members' responsibility and which are the coop's. They did this through frequent informal meetings with small groups."(Hope Village Monitoring Committee, 1981)

Cielo Azul. The Rules and Regulations disallow any "additions or alterations". Residents are instructed "Do not attempt to repair any of this equipment" (refrigerators, stoves, furnaces and hot water heaters). "Cost of labor and materials for repairs of damages caused by resident abuse or neglect will be charged to residents".(Rules, Regulations) At the same time, the Occupancy Agreement is the standard format (Exhibit J), which discusses the right of the member to repair and maintain their unit at their own expense, including "any redecoration of own unit".(Cielo Azul Occupancy Agreement)

How have support systems operated in the development and operations of rural housing cooperatives?

The need for successful management

In the typical cooperative structure, members elect a board of directors to be the governing body of the organization. The board usually hires a manager to handle day-to-day operations, while the board provides guidance through decisions on policies and strategic direction.

Cooperatives must well managed in order to provide good quality housing for their members. A professional management company can be an important part of a cooperative's support system. Although professional property management is recognized as an important component of most multi-family complexes, including many urban cooperatives, the RHS regulations state that self-management is the primary management objective for small housing cooperatives. (§1944.215(d)(1)). The regulations and exhibits provide no guidance for a board that's working with and monitoring a management company.

In the four cooperatives studied, the boards would have benefited from a positive message that they could retain ownership of the co-op while supervising a management company. Several things made this a difficult message to convey:

> None of the management companies had any other experience working with co-ops. They were used to working fairly autonomously for a hands-off owner, or within a vertically integrated structure. They found it difficult to adjust to the cooperative structure, where the residents had decision-making responsibility.
>
> All of the current management companies were hired at times of stress or crisis for the co-op.

> Because the regulations state that self-management is the primary objective for small housing cooperatives, there was an implied sense of failure when the co-op hired a management company. This was particularly evident among agency staff and advisors.

Section 1944.215(d)(1) describes the components of self-management:

> To achieve this, education and training efforts should be an on-going part of their early years of operation. Accordingly, modest educational costs will be permitted in the budget as a subheading under management expenses. It is understood that, in the beginning, it may be necessary to obtain some outside services, such as a bookkeeper. If so, then partial self-management can be considered. It will be necessary for a qualified non-member (individual or organization) to advise the board during the formative years of the cooperative…

Unfortunately, when the section proceeds to describe the alternative forms of management for a cooperative (partial self-management and contract management), there is no recognition of the need for continuing board education and training under these scenarios.

Another problem with this section is that payment to the board advisor is not addressed. The concept of an "Advisor to the Board" is described in §1944-E Exhibit F, "Qualifications of an Advisor to the Board", Exhibit F-1, "Relationship of Advisor to Members", and Exhibit G "Advisor Responsibilities". Although the Exhibits outline an extensive role, there is no reference to payment of the advisor.

Elements of a Support System

"The logic of co-operatives is simple and straightforward. The users of the services should be the owners and the organization should run to meet the needs of the users. This implies that the organization needs to keep in touch with its members and learn from them; how else but through participation and democracy." (International Joint Project on Co-operative Democracy, 1995)

The logic may be simple and straightforward, but all cooperatives struggle with issues of ownership and democracy. Based on the experience of successful cooperatives in housing and other sectors, these are several elements of a support system that would help rural housing cooperatives build ownership among their members:

- Regular training for the board
- Good member orientation and communication
- User friendly documents and knowledgeable staff
- Management companies that understand co-ops and can interface effectively

The following section discusses these components in relationship to the case studies.

Elements of a Support System: Regular training for the board

A 1998/99 survey of agricultural cooperative boards in the Midwest found that co-op boards receive an average of three days of training per year, with some co-ops devoting as much as 18 days to training. Survey respondents rated board training as "very important" to the co-op's performance. The average co-op in Wisconsin invested $6,172 in training last year. (Assessment of Cooperative Board Training Programs, in progress 1999)

Training must be offered on a regular basis in order to reach new and veteran board members. Although Section 1944.215(f), on cooperative management, discusses training needs as part of a co-op's "early years" of operation, all cooperatives elect new board members regularly. In fact, the Sample Bylaws (§1944-E Exhibit D-1) recommend staggered terms of one and two years for board members.

In general, the co-ops reported very limited and irregular access to training.

Cielo Azul. Although the board president was elected in September 1997, the other officers have been on the board for one year or less. The co-op's only board training was held in November 1996. The board president attended one session of the "Spectrum" training offered for owners and managers of RHS financed projects. She found it useful, but didn't think that the management company had included expenses for her training in the 1999 budget.

Eleven Mile Corner and Happy Acres. NCLR offered training to the early boards at Eleven Mile Corner Co-op, but, since then, the only board training for these co-ops has come from RHS staff. They occasionally attend meetings to answer questions and discuss board roles and responsibilities. At Happy Acres, which is self-managed, RHS staff assisted the board president directly by helping her set up accounts, developing financial worksheets, handling contractors, and making effective purchasing decisions. They have also offered to train other board members.

Hope Village. During the long development period of this project, future members were trained on governance and FmHA requirements. In its early years of operation, the co-op received educational support from three individuals:

> Chloe Wacenske, Regional Specialist in Community Resource Development for the Cooperative Extension Service of Cornell University. She attended each of the board meetings for 18 months and trained the Board of Directors on setting priorities and effective governance through policies.
>
> Richard Howard, District Director, FmHA He met regularly with the board and members to discuss FmHA regulations.
>
> Maudie Weeks, the project champion. In her advisory capacity, she provided on-going operational training to the Treasurer, the Board and the Finance Committee.

> She wrote guidelines for Board responsibilities and procedures., and brought in community resource people to discuss legal issues, zoning laws, household repairs, and budgeting.

In the co-op's third year of operation, an evaluation by a HUD/FmHA-appointed Monitoring Committee recognized the benefits of the board's current training and support system, and recommended that the Board receive additional training in basic financial analysis and accounting. "Funds should be made available in the permanent loan itself for modest training at least for Board members, if not all of the members of the cooperative". (Hope Village Monitoring Committee, 1981)

There are no reports of recent training at Hope Village.

Elements of a Support System: Good member orientation and communication

Member orientation

At Hope Village, Happy Acres and Eleven Mile Corner, new members meet with at least one board member for orientation. The system is more haphazard at Cielo Azul.

Hope Village. The site manager processes new applicants and gives them copies of the articles and bylaws, in addition to other documents. She then contacts the Selection Committee to set up a meeting with the new members. The Committee introduces new members to Hope Village and discusses the rules and regulations.

Cielo Azul. The site manager gives new members an orientation packet which includes grievance procedures, bylaws, the occupancy agreement, rules and regulations and other documents. Several of the members reported that they were unaware that they were moving into a co-op. They eventually heard about it from other residents or the board president.

Happy Acres. Since this co-op is self-managed, the Board president meets with all perspective members, does the paperwork, and explains the organization of the co-op.

Eleven Mile Corner. The site manager processes new applicants and then arranges a meeting between the new member and the board president. The board president then explains how the co-op operates.

This procedure contrasts sharply with the co-op's early days, when the selection process at Eleven Mile Corner was described in a letter to FmHA, dated December 20, 1983:

> "Essentially, the cooperative wants the right to interview any perspective resident whom the management agent has screened as being eligible under FmHA guidelines. The cooperative reserves the right to make the final decision based on the FmHA criteria in Section D-7 of the Plan. [i.e. the co-op's Management Plan]

> The management agent assists in all these processing steps and is even used as a personal and credit reference. However, the final decision rests with the cooperative as guided by FmHA regulations." (Letter from Mark Van Brunt, 1983)

Cielo Azul and Eleven Mile Corner. The lack of Spanish-language documents was mentioned at both Eleven Mile Corner and Cielo Azul. Some of the members are Spanish-speaking, with very little English. At Eleven Mile Corner, the site manager is able to explain things in Spanish, but the documents members take home are all in English, which limits their usefulness.

Member communication

Cooperatives must communicate regularly with their members in order to solidify a sense of ownership. All co-ops need to find ways to solicit member input, as well as distribute information and build community spirit.

Here are few comments that illustrate the range of issues and opinions on communications within the cooperatives:

- There were member meetings during the rehab process. People got to decide about paint colors and other things. (Eleven Mile Corner member)

- During the rehab process, members took an active role in decisions, in a group setting. It wasn't just a question of making individual decisions about your own unit – the co-op members worked as a group to make decisions that affected all the residents. (USDA-RD architect talking about Happy Acres and Eleven Mile Corner).

- We don't get enough notice on meeting times and dates. (Cielo Azul member)

- The board reserves thirty minutes at the beginning of each monthly board meeting for members' comments. In the past, more people showed up to talk. (Hope Village board president)

- It's difficult to know what you can and can't fix in your unit. (Eleven Mile Corner member)

- Members arrange holiday parties for the children, and are planning an all-member picnic this summer. (Hope Village member).

Hope Village. This is the only co-op currently producing a newsletter for members. "Newsy Notes for Hope Village Folks" has a long history. It was started by members in 1980, but it's currently produced by the management company. The four to six page newsletter lists monthly birthdays, reminders about rules, meeting announcements, recipes, and messages from the office and maintenance staff.

Eleven Mile Corner. Membership meetings are held every two months. Ten to twelve people from the 18 units usually attend.

The Family Resource Center provides another avenue of communication at Eleven Mile Corner. Although the Center wasn't created as part of the co-op, it is conveniently located nearby. The Center is open every day, with a full-time director and several part-time employees. Co-op members go to the Center daily for bottled water (the drinking water on the site is contaminated), and the Center offers programs for children, adult tutoring, immunizations, free clothing, and jobs training. Both the Housing Authority staff and the co-op board president referred to Center's important role in member communications. Center staff help publicize co-op meetings, and act as informal liaisons between the site manager and co-op members.

Happy Acres. This is a small community where most people have connections through family or friendship. Although there weren't any reports of formal member communications, membership meetings are held to discuss important issues, such as the major rehabilitation planned for 1999. Members were originally resistant to the rehab, but frequent communication by RHS staff, through meetings with members and the board president, have helped to reconcile them to the idea.

Elements of a Support System: User friendly documents and knowledgeable agency staff

User friendly documents

Bylaws should be understandable by co-op members, since they serve as one of the important vehicles for understanding the fundamental organization of the cooperative. A guide that focuses on the key points could accompany the bylaws to make them more accessible.

Documents for members should be clear and consistent. Most of the co-ops used the sample documents provided in §1944-E, along with forms used by the management companies at other sites. For instance, at Cielo Azul, the Occupancy Agreement (which is based directly on §1944-E-Addendum J), contradicts the "Rules, Regulations, Occupancy Policy and Paying Procedure" in several significant areas. The procedures on repairs and alterations differ substantially. Making things even more confusing, the first document refers to an "Occupancy Charge" and the second refers to "Rent".

Required compliance is challenging. There is a small industry of companies that are skilled in managing program 515 projects and adhering to the necessary reporting requirements. Despite the regulations' expressed vision of self-management, it's difficult to imagine a co-op member voluntarily undertaking to complete all the required reports. At Happy Village, the only self-managed co-op, RHS files include frequent reports of missing budgets and other documents.

Knowledgeable agency staff

In all of the co-ops, there is evidence of a substantial role played by agency staff to educate members, work with the co-op's advisors, and help the cooperative solve problems in its dealings with the agency and management companies. This is a drain on RHS staff time and makes the cooperatives seem uniquely burdensome. In the majority of their portfolio, staff expect to have very little contact with owners. As staff resources have diminished, the offices have relied increasingly on professional management companies. It is more efficient for them to work directly with a small number of management companies, who have multiple contracts, experience with the regulations, and access to resources.

At each of the co-ops, there is evidence of agency staff's personal involvement at times of crisis. They attended membership meetings and worked proactively to find permanent solutions to problems. For example, at Happy Acres, Johnna Vargas and Steve Langstaff helped the co-op deal with neighbor complaints by working with members to devise a rehabilitation plan that fixed up the units and removed some of the animals and out-buildings that were the source of complaints. At Hope Village, Richard Howard worked with the board to hire a professional management company during a time of financial crisis and embezzlement.

Although RHS staff has shown a willingness to work hard to help these cooperatives, their job has been made more difficult because they've operated in relative isolation. Although Steve Langstaff in Arizona knew about Cielo Azul in New Mexico, there seemed to be almost no exchange of information between offices, and no reports of contact with the rest of the cooperative community. Local cooperatives in other sectors are a potential source of support. They might be willing to work with the housing co-op board, sponsor training sessions, or recommend advisors.

Another potential resource are the cooperative specialists, which were recently designated in each state. The role of the specialists varies from state to state, and they often have substantial additional assignments. In New York, though, the cooperative specialist is described as "a source of management advice to all rural cooperatives" (USDA Rural Development New York, 1999). Although he is a potential source of advice on the co-op model, the local RHS staff didn't know him, and he indicated in an interview that he was unaware that there was a RHS-financed housing cooperative in New York.

In spite of the challenges of isolation, lack of training and the lack of good written guidelines, RHS staff have played an important role in the continuing viability of the co-ops in their states. This is clearly demonstrated in the case studies.

Happy Acres and Eleven Mile Corner. Agency staff helped to initiate substantial rehabilitation projects at both of these cooperatives, and they also worked with the cooperative members to make decisions on how the money would be spent, the plan for implementing the rehab., and elements of design. The RHS architect reported that decisions were made at member meetings, as part of a group process which often involved differences of opinion and conflict. In each case, members reported that they had a role in the decision-making.

Happy Acres. Agency staff helped the board president set up a chart of accounts, record keeping system and purchasing procedures. They also talked frequently about aspects of cooperative governance, such as member involvement, use of selection committees, etc.

Cielo Azul. Although current agency staff have an appreciation for the cooperative nature of the project, they aren't knowledgeable enough to provide guidance in the differences between operating a cooperative and a rural rental project. They are trying to do a good job, but they operate in the environment where they're comfortable: rural rental housing. According to the owner of the property management company, a "leadership vacuum" at the co-op makes this possible. Without any cooperative-related training, co-op members have trouble understanding the difference between living in a rental unit and a co-op. This is especially true for new members. The co-op structure has become increasingly marginalized, and the potential benefits of living in a cooperative are less evident.

Hope Village. There is a long history of agency staff involvement at Hope Village, although this has been substantially diminished since a professional management company was hired.

Elements of a support system: Management companies that understand co-ops and can interface effectively with the board and members.

Three of the cooperatives have contracted with a professional management company. In each case, they are the only co-op in the management company's portfolio. Some of the implications of this situation have been discussed previously. This section includes more examples of the interaction between the management companies and the co-ops.

Eleven Mile Corner, Hope Village and Happy Acres. In all cases, member selection is handled exactly like rental. On-site managers believe that they cannot deviate from the rural rental system. In Hope Village and Eleven Mile Corner, the manager selects new members, and then refers them to the board president or the selection committee for orientation. Since even that step is missing at Cielo Azul, several members reported that they didn't realize they'd moved into a co-op until they were invited to their first meeting.

Cielo Azul. The packet distributed to members by the management company includes contradictory information. The Occupancy Agreement was copied directly from §1944-E Exhibit J, which includes some very co-op specific language. The instructions in this document vary significantly from the "Rules, Regulations, Occupancy Policy and Paying Procedure", which is also given to new members. For example, the Occupancy Agreement refers to a three year term, renewable for successive three-periods. The Rules and Regulations refer to giving a 30-day written notice before vacating the unit.

Cielo Azul contracts with Monarch Properties for management services. During an interview, Monarch's property supervisor emphasized the complexity of the RHS regulations. He emphasized his belief that the co-op structure requires a lot of time from residents, without returning any tangible benefits. In a presentation prepared for our interview, he listed a number of reasons why he thinks co-ops should not attempt to self-manage:

- A co-op requires all of the responsibilities, skills and knowledge mentioned [technical knowledge mentioned earlier in the discussion]
- The person responsible knows every other residents' "business" due to program requirements
- Amounts to a full time job
- Tendency to develop "cliques" (Monarch Properties presentation 1999)

Although the board president expressed concern about the amount of work required by her position, some of it was related to the time required to monitor the management company. Board members expressed a general concern that the management company did not always communicate with the board on important issues. For example, they appeared to have unilaterally hired a resident manager, without informing the co-op board or members. The board had no idea how this affected the budget, and maintenance was still a problem. In fact, none of the members that we spoke to knew how or when to contact the resident manager.

Hope Village. As discussed previously in this section, equity and ownership issues are confusing to many members. The opportunity for financial gain from cooperative membership is not readily apparent. Hope Village's management company, Baldwin Real Estate, is addressing the confusion about equity and transfer value by requesting bylaw changes from the co-op and approval for the changes from RHS. Because records from the 1970s and 1980s are so poor, they are requesting that the calculations of transfer value, as described in the Bylaws, commence three years ago. Although this means that long-time members will lose part of their remuneration, it also means that the system will be standardized and applied consistently in the future.

For most residents, the on-site manager is their closest contact with the property management company. At Hope Village, the on-site manager seems to be supportive of the concept of cooperative organization, although she is inexperienced. Her predecessor, also a management company employee, was a long-time resident of the co-op who worked closely with residents and understood the co-op tradition of Hope Village. The present manager discussed her responsibilities in this area knowledgeably, while acknowledging that she was still learning. She talked about making sure that there were board elections, and working to get the board back on track with monthly meetings. She also has revived production of the co-op newsletter. This is a valuable vehicle for communicating with members, and the format reflects an informal and community-minded attitude.

Eleven Mile Corner. The Pinal County Housing Authority doesn't appear to significantly differentiate between management of the cooperative and their rental units. They attend meetings with the residents, but they basically apply the same policies. This sometimes creates tension, because members expect the co-op to be different from a regular rental. For example, the board president has requested regular financial reports, but the site manager does not provide them. Instead, RHS staff send the reports to the board.

The board president would like to encourage more residents to do their own maintenance, which would encourage a sense of pride and ownership, but the Housing Authority has made it clear that there are penalties if the maintenance is not done correctly. This is strong deterrent for most people.

The site manager believes that co-op members relate ownership to two things: clear title to the property after the mortgage is paid off, and the ability to transfer their apartment to a family member. The former cooperative president wanted a family member to move into her unit after she moved, but the Housing Authority insisted on adhering to the waiting list procedures that they use for their rental units. Although the site manager reported that this problem caused families to feel that the co-op is similar to rental, she seemed unaware of the transfer policies in the co-op's Bylaws. They allow a member to "sell his membership to any person who has been duly approved by the Corporation as a member and occupant", as long as the co-op has not exercised its option to repurchase the vacant unit. Alternately, the unit can be transferred as part of the member's estate.

Although the site manger was aware that there were references to patronage accounts in the USDA regulations, she said that the co-op has never actually made any money for a patronage account.

Happy Acres – self-managed

Are cooperatives a viable alternative to rural rental and/or homeownership?

Every member of a housing cooperative brings their own experiences, attitudes and expectations to their living situation. For most of the low and very low-income people in the case studies, the co-op is an alternative to rental housing. For people like the Board President at Eleven Mile Corner, who is saving to buy his own home, the co-op's subsidized rents offer a financial benefit, but his concept of co-op ownership relates to member control more than wealth-building. Although it's possible for limited equity co-ops to more closely resemble homeownership financially, (e.g. by requiring a substantial membership fee and allowing an appreciation of equity) these four cooperatives basically operate on a rental financial model. Membership fees are similar to a security deposit, and members are unaware that the co-op offers opportunities for financial rewards, even when they're included in their membership documents.

In order to offer a positive alternative to other forms of housing, co-ops must have sound finances and be in relatively good physical condition. One important indicator of problems is excessive turnover, which is low in all these co-ops. Vacancies are rare. Except for Happy Acres, which is in the midst of a rehab. project, the physical condition of the co-ops is fine. Hope Village and Eleven Mile Corner recently completed major renovations and Cielo Azul is only 3 years old. Cielo Azul is still affected by problems related to construction, but a recent interview with USDA-RD staff confirmed that they've finally completed a costly erosion control project. At Hope Village, they are planning to fund $100,000 worth of rehabilitation from cash flow annually. Reports were not available for Happy Acres, but project budgets for Eleven Mile Corner, Hope Village and Cielo Azul are attached in the Appendix.

Each of these cooperatives was started because a group of people had a need for better housing and were attracted to the co-op model. During the period of organization, planning and building, families were remarkably tenacious in retaining their involvement in the cooperative. Development work started at Eleven Mile Corner in 1979 and Cielo Azul in 1980; Eleven Mile Corner was built in 1983 and Cielo Azul opened in 1996. Hope Village members began organizing in 1970, and it was built in 1980; the pre-application for Happy Acres was written in 1978, and it was built in 1980.

In each case, members believed that the co-op model offered a positive alternative for meeting their housing needs. Although each of the cooperatives has faced significant challenges over the years, interviews with current members demonstrated that the cooperative model, as it exists in these four co-ops, has many positive elements:

- Members' satisfaction is reasonably high
- Board members showed leadership on issues
- Limited financial gain for members is possible within the co-op structure (although not realized in practice).
- The co-ops help to build social capital

Cielo Azul. Although Cielo Azul faces significant challenges in maintaining a sense of ownership among members, there is also evidence that the co-op structure contributes to a positive experience for its members**.** Residents reported meeting their neighbors through meetings and committees. The board president is proud of the fact that she is able to act as an advocate for members when dealing with the management company. The community room is available for meetings, and the co-op president has investigated grant funding for a computer lab.

Eleven Mile Corner. Many of the members of Eleven Mile Corner are connected through family ties or friendship. Co-op members participate in Hispanic cultural activities, volunteer in the neighborhood school, and help out at the near-by Family Resource Center. The board president knew many of the members through work, and was elected president of the co-op very soon after he moved in. He believes that the co-op model offers many opportunities for members to improve themselves and the place they live. He encourages them to take more responsibility, and would like co-op members raise funds so that they could offer ESL or GED classes in the Family Resource Center.

Members feel that the cooperative is peaceful and safe. They were part of the planning process for the renovation, and many of them attend membership meetings. Maintenance is sometimes an issue, but at least they can go to the co-op president if they have a problem.

Happy Acres. This site gives ample evidence of a sense of ownership. Each family has their own unit, and the yards and out-buildings are highly individualized. We were only able to interview the board president, but Happy Acres was clearly her home and her community. RHS staff felt that this was true for the rest of the members.

Hope Village. Most of Hope Village is a community of single family homes. The houses are well maintained, with plantings and flowers in front of some of them. Two of the members that we interviewed have adult children living in the co-op. The board president grew up in Hope Village, and certainly feels it's home. Although she complained about a lack of privacy at times, there are a lot of rewards in the way that people watch out for each other. Members also feel that individual involvement can make improvements in the community. One member joined the board because he was concerned about maintenance issues and had ideas for changes. Another organized a summer recreation program for children in the Community Center. Residents were working on a summer picnic, and planned to revive the tradition of inviting local officials.

Six families have lived in Hope Village since it was built. Although many people would see this as a positive indication of stability and commitment to the Hope Village community, Richard Howard, the retired FmHA specialist who worked closely with the co-op, saw it as a failure. During his interview, he made it clear that he hoped that the co-op's emphasis on self-management would give people the skills they needed to move into home ownership. He shared this vision of the co-op as a stepping-stone to homeownership with Maudie Weeks, the co-op champion. This may be a problematic vision, since it relegates co-op ownership to a secondary status, but it's important to be aware that this vision may be shared by many of the people involved in housing co-ops.

REVIEW OF SECTION 1944 OF THE USDA MULTIFAMILY HOUSING REGULATIONS

Below is a review of the Part 1944, Subpart E and recommended changes to improve the current regulations and guidelines. However, thought should be given to revamping the programs under new regulations that are based on applicable HUD insurance and direct lending programs. The focus should be on project economics, not management of the design and development process.

Definitions

Accessible – Use of common language with HUD and other federal agencies is recommended. There is no need to "re-invent the wheel" on this issue.

Congregate Care – Language should be changed to reflect states adopting Medicaid waivers that enable healthcare services to be provided in a variety of residential settings. Last sentence could be eliminated.

Elderly – Should be 55 years in accordance with the standards set by HUD. There should be a separate category for disabled.

Elderly family – This is very similar to the definition of elderly and elderly household. It seems as though there is some room to consolidate here.

Elderly household – Could be removed and combined with Elderly family, it is essentially the same definition.

Individual with disability - Make sure definition is consistent with generally accepted definition. Age limit of 22 seems arbitrary and should be eliminated.

Individual with handicap – Definition should conform to generally accepted definition for individuals with handicap.

Limited equity – This definition is somewhat confusing. Limited equity generally refers to limited equity cooperatives that limit the amount a share price can increase over time. This is typically done by allowing increases that are a certain percentage of CPI or inflation.

Loans to build or acquire new units – It should be evaluated whether or not it would be acceptable to allow prepayment of these loans under certain conditions. Prepayment should be at the State Director's discretion.

Low-income household – Ensure consistency with HUD guidelines.

Manufactured Homes – No need for FmHA standards. Industry standards should suffice.

Manufactured Home projects – Why is it necessary to have a clustered configuration? It should be sufficient to say that homes are contiguous to each other.

Moderate-income household – This should be consistent with HUD definition.

Owner-builder – This should read "demonstrated the ability and capability to build a multifamily project. Stipulating RRH is too limiting.

Very low income – This should be consistent with HUD definition

<u>1944.211 Eligibility Requirements</u>

Section (a) (2) – Eligibility of applicant – Programs should be geared to enhancing development opportunities and providing low rates and beneficial terms to the borrower. This would be similar to HUD insurance programs and direct lending programs. It should not be stipulated that the applicant could not obtain the necessary credit elsewhere. Program should represent an option (if not the best option) for applicant. This section should be eliminated.

Section (a) (10) – Stipulations for Non-profit entity – These are generally too restrictive and very limiting. There are a number of non-profit developers that consist of less than the required number of members who would present good options for developments. Also, non-profit developers may tend to work in a variety of locations. These developers should be evaluated based on their mission and experience. It should not be stipulated exactly what their organization should look like. This section should be removed and replaced with much looser guidelines.

Section (a) (13) (ii) - general partnerships 5% interest requirement should not apply for projects financed using low income tax credits. Projects using LIHTC should be considered for financing. Once again, these programs, as the HUD insurance and direct lending program, should represent an option for applicants, whether or not they could get adequate financing elsewhere.

Section (a) (14) - Long term commitment clause is not necessary because transfer not allowed without approval of State Director. This presents in an overly negative fashion and should be removed.

<u>1944.212 Loan and Grant Purposes</u>

Section (b) – Project economics should dictate whether or not to do a rehabilitation or not. The 5% rule may be too restrictive and difficult to determine. In some instance, there may be compelling reasons to keep existing structures other than cost. This should be changed to allow for more interpretation. One general comment concerning this entire section, it presents rehabilitation in a negative fashion and could act to discourage development. The section should be reworked to be more general and allow local offices greater latitude in the decision making process.

Section (b) (2) – Current safety language is unnecessary. It should be stipulated that the project must comply with local building standards and comply with local and federal safety standards.

Section (b) (6) – The cost of retail space should be allowed if it is not excessive and serves the interests of the residents. The current regulations call for a difficult calculation of the cost of such space and how to remove it from the loan. This can be eliminated or alleviated by allowing some retail to be included to benefit residents.

Section (c) (1) – Land purchase value should reflect value as improved. Otherwise, loan funds will never be sufficient to cover actual cost of the land.

Section (g) – Central laundry facilities should not be required. Washers and dryers can be included in units relatively inexpensively and should be allowed if project economics warrant. Laundry facilities can be required, either in each unit or centrally.

Section (i) – In many instances, costs associated with the start up of sponsor organizations and housing cooperatives are legitimate development costs associated with doing a project. These should be allowed under the loan.

Section (j) – Technical assistance should be allowed to be provided by for-profit entities in addition to non-profit entities. In many cases, for-profit groups may be the only ones with the capacity to provide such services in certain areas. Increase the amount allowed to be paid for technical assistance to consistent with HUD programs.

1944.213 Limitations

Section (b) (8) – This seems to be a cost that would normally be covered under private real estate loans and should be allowed under USDA programs.

Section (d) – Obligations before the loan – this should allow loan proceeds to be used to pay for all reasonable predevelopment costs incurred by borrower that are customary and required for project start up.

Section (e) - Cost increases that are normal and required to complete project and do not substantially change the economics of the project should be allowed . Again, this section has a very negative tone and should be worded to show more flexibility.

Section (f) – This section is very confusing and difficult to understand. Its context at this point in the regulations does not make sense. Effort should be made to clarify this section.

Applicability should be determined based on market need. It should not limited to whether other housing has been built using federal subsidy or FMHA or HUD programs.

1944. 215 Special Conditions

Section (a) - Remove limitation on development process, allow for choices and value engineering of the applicant. Project design and amenities should only be limited by affordability and the debt that cash flow can support.

Section (a) (1) - Remove cost maintenance data and allow for flexibility. Don't destroy creative element of the development. Project design and amenities should only be limited by affordability and the debt that cash flow can support.

Section (a) (5) – Site development – Costs should be allowed that are reasonable and if project economics dictate.

Section (a) (6) - The only limits placed on site density should be those allowed by local zoning requirements. There is no need to further limit the building capacity. Development of any size parcel should be allowed as long as it is reasonable.

Section (a) (8) – This is very limiting and negative in presentation. Design should be limited by project economics only. This paragraph dilutes the creative process of development and is too restrictive. It should be removed.

Section (a) (9) – Roof slope limitations do not need to be dictated by USDA. This section should be removed and project economics should dictate design features.

Section (a) (10) – Repeat designs clause is should not be required. This restricts the creative process and is indicative of burdensome oversight on the government's part. This clause should be removed.

Section (a) (11) &(12)&(13) – USDA should not restrict design or amenities. Once again, this needs to be driven by project economics. Maximum discretion should be allowed to the developer as long as project is within overall cost limitations. For cooperatives, this comes across as extremely restrictive and negative. USDA can and should set certain minimum requirements. Look at HUD's 202 program for guidance, there is tremendous variety in these projects because the development process is not restricted.

Section (a) (14) – Parking should be dictated by local zoning requirements. Minimum is understandable, however a maximum is not necessary.

Section (a) (15) – Too negative, need to remove. Allow developer to do what they can within cost guidelines.

Section (b) (1) – Type of Housing – This section should be removed, it is not necessary. Allow what can be done within cost limitations. Do not restrict unit size. This may vary greatly, especially with a rehabilitation of existing projects.

Section (b) (4) – Should be used as a standard for number of bathrooms, however, should not be used as a disqualifying measure for a project. Once again, projects should be governed by affordability and overall project costs. Need to allow maximum flexibility for local director and developer.

Section (b) (6) – Instead of having there own standard, number of handicap units should be consistent with local building standards/federal housing regulations unless property has a specific use for disabled or handicapped individuals.

Section (b) (7) – Handicap accessibility should be consistent with other federal and local standards.

Section (f) (1) – Cooperative Management - self management - Training and education should be included in the budget for every year. New cooperative members will need training as units turnover. The training needs to extend for the life of the project.

Section (g) – Cooperative membership fee – Membership fee should actually be termed as "share price". The share price is paid by members for a share of the cooperative corporation. Share price is typically, even for limited equity cooperatives, somewhat higher than one months rent or carrying charges. It is necessary to differentiate cooperatives from rental projects. Market should dictate share price except in limited equity cooperatives where is should be based on potential members income scenario, market and project economics.

Section (h) (2) – Limited equity cooperatives typically limit equity increased to a percentage of inflation increase plus capital improvements made to individual units. Therefore, inflation increases should be allowed based on equity increase formulas in the cooperatives' by-laws.

Section (i.) (4) – Interest Credits and rental assistance - Management reserve charge should be included as part of the carrying charge. Therefore, Rental Assistance should be allowed for this charge.

Section (n) – Establishing profit base on initial investment – This is too complicated and unnecessary. Profit base should be established based on accepted standards for real estate investment.

Section (p) – Guidelines for preparing environmental assessments and environmental impact statements – guidelines should be consistent with HUD guidelines.

Section (r) (4) (iii) (iv) – These sections should be removed. There is no need to limit the ability of developer/borrower to develop a quality project. Costs should be lower, but should not be stipulated as such. Additional amenities should be allowed if land costs are lower. Project economics should dictate what can be accomplished.

Section (r) (6) – Consideration of downtown business areas for housing – This is very limiting. Most downtown communities in rural areas will not have comprehensive revitalization plans. Housing should be allowed if it makes economic sense and common sense.

1944.222 Technical, legal, and other services

Section (a) – Appraisals – Guidelines should be consistent with HUD requirements.

Section (c) – Construction and development policies – Should be consistent with AIA standards. Can remove otherwise, as additional requirements are unnecessary.

Section (e) – Contracts for legal services – Fees in most cases can not easily be estimated at this point in time. Based on experience, a cap on fees may be established, however, should not limit too much this early in the process. Legal fees should be considered as part of overall cost.

Section (h) – Title clearance and legal services – It seems to make sense to do what is prudent and reasonable rather than create an elaborate system to deal with it. This section should be simplified.

1944.223 Supplemental Requirements for manufactured home project development

Section (a) (1) through (a) (5) – Provisions do not allow for tenant purchase of existing manufactured home parks using the cooperative model. Home ownership could be a goal through allowing refinances of this type. New housing units should not be the goal, but quality housing units should.

Section (b) - Maximum loan limits – This should be determined based on project economics and as developed value. Some consideration may be given to adopting the HUD per unit loan limits, however, these are often not in accordance with local and current market conditions.

Section (c) – Loan Terms - Some consideration should be given to a longer term to allow greater project feasibility. Newer parks with strong maintenance schedules and reserves may have an economic life in excess of 30 years.

Section (d) - Security - In the case of cooperatives, homes can be owned by the individuals and the land by the cooperative. In this instance the security for the loan would be a first lien on the land only. Paragraph needs to be more flexible to allow for a variety of circumstances.

Section (e) - Property requirements – This should be based on local zoning and industry standards. Allow for the maximum amount of flexibility.

Section (e) (3) - This should be deleted. For new parks, it may be necessary to have a model for some time to help the marketing efforts.

Section (e) (4) - This should state that projects must meet or exceed local zoning requirements and industry standards. A lot of this is repetitive. Perhaps, simply leaving section (iv) would suffice.

1944.224 Supplemental requirements for congregate housing and group homes

Section (a) (2) (ii) - Design criteria – FmHA loan should be sufficient to pay extra costs of oversized units for congregate care facilities. There should not be a need for other sources of funds and references to this should be removed.

Section (a) (2) (vii) - Consideration should be given to removing the requirement for a kitchen in some instances.

Section (a) (3) - Limitation on use of loan funds – Section 232 loans at HUD allow loan funds to be used to purchase major movables and specialized equipment. FmHA 515 should allow similar provisions.

1944.235 – Actions subsequent to loan approval

Section (c) (iii) – Acceptable performance of contractor and payment of all construction bills – This entire paragraph is unnecessary. It is overly negative and should be changed to say that all construction and bills should be paid in accordance with generally accepted standards.

Section (c) (viii) – Use of excess funds – Along with the theme of basing decisions of design and amenities on project economics, excess funds should be allowed to be utilized in the project if the application of such funds improves the marketability and appeal of the project.

1944.238 Prohibition against repayment

Along the same lines as recent developments in HUD's 202 direct loan program for senior housing, prepayments should be allowed for refinancing that benefit the residents of the project. This can be accomplished by providing money for additional amenities or services, enhancing the project, or lowering rents/carrying charges.

RECOMMENDATIONS AND CONCLUSIONS

The results of the case study research support the hypothesis that regulations have posed a barrier to rural cooperative development and operations. One of the key problems is the general theme in the regulations that cooperatives will be developed and operated on a low-cost basis. Compensation for non-profit sponsors during the development phase is limited, and in all of the cases the non-profit sponsors and volunteers donated significant amounts of time to building the cooperative. Once the cooperatives were operational, it became clear that the regulations were difficult to follow and occasionally contradictory. Some of the key elements of cooperative ownership, like equity and transfer value, offer limited incentives as currently written and were poorly understood by members. The regulations offered minimal guidance, and agency staff were unable to work with them effectively.

The central conclusion from the regulatory review is that the USDA Multifamily Housing programs in their current state do not provide the necessary framework to allow for adequate development and operation of affordable cooperative housing in the rural areas of the country. Generally, the regulations are confusing and burdensome. In addition, they are written in a negative tone, which implies a heavy-handed approach to approving and administering loans. Especially for cooperative housing, the regulations do not allow for significant creativity from the sponsor or the residents.

Promote democratic decision making and resident control

The keystone to any cooperative is democratic control by members to achieve an agreed common objective. For housing cooperatives, this means creating a “home” for individual members and a community for the cooperative as a whole. Cooperatives are autonomous, self-help organizations controlled by their members. If they enter into agreements with other organizations, including governments, they should do so only on terms that would ensure democratic control by their members and maintain their autonomy. In this sense, cooperatives need autonomy and decision-making ability to exist at all. For that reason, regulations such as those of the USDA multifamily housing programs, in the their current state, infringe upon the sovereignty of a housing cooperative by severely restricting the creative process of establishing a home. In order to make them useable, the focus of these regulations needs to uphold the idea of empowerment to individual owners, allowing them to make the most important decisions for themselves and to create the home that they desire.

One particular area highlighted in the regulations is the idea of "self management" for cooperatives. The regulations imply that "self management" as a primary goal of cooperative housing. In addition, the regulations imply that cooperatives that are not able to obtain "self management" are in some ways unsuccessful. Interviews with members and agency staff at each of the cooperatives confirmed this impression. It was considered a failing when the co-op contracted with a property manager, and the role of the co-op in managing that relationship was not well understood.

"Self management" should not be a primary objective for co-ops. Instead, the primary objective should be "member control". Few individuals living in cooperative have the time, experience or expertise to manage a property. When needed, professional management should be utilized. The idea of the "management reserve" highlighted in the exhibits allows for cooperative members to be financially rewarded only through self-management. This seems controlling as well as unnecessary. Cooperative members should be rewarded through proper management. If that means hiring a professional management company, then that should be allowed. The idea of the management reserve should be eliminated from the regulations. Although residents may not manage the property, they are still in control through their ability to choose and manage the property manager. Critical decisions concerning the way the property is run, organized, and the community at large continue to rest with the members, without the day-to-day burden of property management.

Cooperatives need a strong support system

In order to be successful, housing cooperatives need a strong support system. The cooperatives in the case studies all operate in relative isolation. This isolation applies to the members, the USDA-RD staff and the management companies. Board training is extremely rare or non-existent. USDA-RD staff have no formal or informal networks for supporting their work with co-ops. The management companies are familiar with rural rental, and tend to apply similar policies. There are many examples of good support systems in the housing and cooperative sectors. Partnerships could be formed with cooperative development centers, the university – based cooperative centers, cooperative housing associations, and some of the new groups working in the area of senior co-op housing. These partnerships could form the basis of a strong support system for successful cooperative development and operations.

Education and training are an important part of a good support system for cooperative housing, and critical to their long term success. The regulations and guidelines should give greater significance and importance to the idea of training both at the front end of the development process and ongoing. For example, the regulations require a marketing survey for larger projects. It would be very difficult for an individual to answer a short questionnaire on cooperative housing and determine whether or not cooperative housing would be good for them without some significant training on cooperative housing. Training dollars need to be expended in the beginning of the process to allow an accurate determination of demand. In addition, continued and on-going training dollars need to be included in the budget every year for a cooperative to be successful. As residents turn over and new board members are elected, these individuals will need training on cooperative living as well as the responsibilities of leadership. The importance of training should not be under-estimated.

Co-ops should have a self-contained set of guidelines and regulations

Cooperative development and operations would benefit greatly by having a complete set of separate guidelines and program regulations. The case studies demonstrated that the cooperatives and their advisors struggle with the fact that the regulations make it difficult to clearly recognize the significant differences between cooperative home ownership and multifamily rental housing. The few areas where differences are highlighted are not tremendously helpful in recognizing the unique advantages of cooperative housing. Most individuals are not familiar with these advantages and need to be educated prior to being able to determine whether or not cooperative housing is for them. Separate regulations can help in this process as well as address the uniqueness of this type of homeownership. Exhibits to the existing guidelines could also be improved. Generally, these exhibits should provide the minimum requirements and allow each sponsor/borrower room to create and "fill in the blanks" to match their situation. The exact form and wording need not be provided, as each circumstance is unique. Exhibits should generally allow flexibility while providing minimum acceptable standards.

Regulations should be geared to project economics

In addition to the recommendations outlined above, a fundamental change in focus is required if the USDA housing program hopes to be more effective in developing new cooperatives. The regulations should be looser and geared to project economics rather than being based on functionality of the property. Sponsors should be allowed to leverage their resources and relationships to provide the greatest benefit to the owners at their projects.

Even a quick read of the regulations identifies significant weaknesses. They attempt to regulate every aspect and phase of the development process. This results in projects that are similar in architectural style, unit type, and configuration. For cooperative housing, this is particularly stifling to development. Cooperative principles call for a significantly different approach to development. These principles are shared by all housing cooperatives and promote the balance of individual family privacy, while enriching neighborhood relationships in a unique way.

HUD insurance and direct lending programs are good models

The direct loan program, 515, would best be based on HUD's 202 program for senior rental housing. The simple idea evident in this program is that if project economics dictate that you can afford a unique design or certain amenities at given rent levels, then you can build it.

In addition, insurance programs should be modeled after HUD insurance programs, primarily 213, 221 (d) (3), 221 (d) (4), and perhaps 223 (f). These HUD programs set financial parameters for projects and allow the development process to fall into place around those parameters. All of these programs focus on project economics, using underwriting criteria such as loan to value, debt service coverage, rent/carrying charge levels, per unit loan limits and market conditions as the limiting factors in their project feasibility analysis. The creative aspect of development is left up to the sponsor to decide. For instance, the 221 (d) (3) program, which provided mortgage insurance for new construction and significant rehabilitation for housing cooperatives, sets forth the following program parameters:

Eligible Properties:	To be built or projects requiring substantial rehabilitation that are greater than 5 units. Projects must comply with specified HUD and local standards.
Eligible Borrowers:	Non-profit or For-profit sponsors of cooperative housing projects. Non-profit sponsors may finance up to 100% of the project cost.
Term:	Up to 40 years or 75% of the remaining economic life of the asset.
Prepayment:	Negotiable.

General Program parameters:

1. Debt is non-recourse.
2. Debt Service Coverage Ratio of 1.056x
3. 100 percent of project cost can be financed.
4. Loans are limited by per unit statutory limits. These vary based on the area, however the program limit starts at a range of $48M to $70M per unit depending on the number of bedrooms.
5. Prevailing wage requirements under Davis-Bacon Act apply.
6. Owner must sign a regulatory agreement with HUD governing project operations.

Other than the basic economic parameters outlined above, there are very few significant restrictions on what you can build as long project economics allow your target market to afford it. Once again the concept of "if you can afford, you can build it" is present in the programs structure. Unit size, amenities, and design are not limited in any way. As stated above, this is particularly important for cooperative development.

HUD's 223 (f) program is a refinance program for existing projects. It can be utilized in a number of ways. One way is to allow tenant groups to purchase existing rental projects and convert to cooperative home ownership. This type of transaction could exist in some circumstances in a rural setting and it should be considered under USDA programs. The programs should foster the idea of homeownership.

In summary, one of the most important lessons from the case studies is that five rural cooperatives have survived for 20 years and are doing well. This is in spite of the significant obstacles, including the regulatory issues outlined in this review, isolation from other cooperatives, and challenges ranging from poor physical designs to budget problems. The fact that these cooperatives are providing good housing, using the resident ownership model, is a testament to the hard work and tenacity of many people. RHS staff, cooperative members, and their advisors have devoted extraordinary energy to the success of these cooperatives. The fact that people were willing to devote this energy to overcome multiple hurdles is evidence of the strength of this model.

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<u>Documents from the Cooperatives</u>

Many documents were reviewed for this study.   These are the documents that are referenced directly in the report.

Cielo Azul Cooperative

Amended Bylaws of Cielo Azul, filed 1995

Cielo Azul Apartments – Occupancy Agreement (used currently)

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APPENDIX I

1999 Operating Budgets for:

Cielo Azul Cooperative – Taos, NM

Eleven Mile Corner Cooperative – Casa Grande, NM

Hope Village Cooperative – Wolcott, NY

Appendix II

Photographs

Cielo Azul Cooperative – Taos, NM, April 1999

Eleven Mile Corner Cooperative, Casa Grande, AZ, May 1999

Happy Acres Cooperative, Queen Creek, AZ, May 1999

Hope Village, Wolcott, NY, July 1999