Chapter 9. Resident Homeownership Program

Section A. General

9-1. Purpose. This chapter describes the requirements of the Resident Homeownership Program.

A. General. A tenant group may form a Resident Council (RC) which may acquire a project under a Resident Homeownership Program. In accordance with Paragraphs 9-2.A., B., and C. below, as applicable, the RC will organize a Homeowners Association or Condominium Association, to be in effect at the time the RC purchases the project, or a Cooperative Association which will be the actual purchaser of the project. The RC will make the units available for purchase by residents who wish to become homeowners. RCs intending to purchase the project as rental housing may not acquire the project under a Resident Homeownership Program, but instead, should follow the guidelines in Chapter 8, Sections C and E.

B. Organization of the Chapter. This Chapter is organized into Sections A through F as follows:

1. Section A covers:

   a. The formation of a Resident Council;

   b. The forms of homeownership a RC may use.

   c. The procedures a RC must follow in its attempt to purchase the project.

2. Section B describes the requirements for Resident Homeownership Plans (RHPs) submitted by RCs seeking funds to purchase the project when the mortgage on the project is to be prepaid. The following conditions apply:

a. The RC will purchase the project, initially fund the reserve for replacement and operating cost accounts, and pay for other costs associated with the Resident Homeownership Program, i.e., tenant counseling, RC training, and consultant fees, by means of a grant from HUD. All insured loans remaining on the project will be paid off.

b. The discussion in Section B assumes that the RC is using a condominium or other fee simple form of homeownership. However, the RC also may establish a cooperative form of housing under the Resident Homeownership Program. If the RHP is for cooperative housing, the terminology used in Section C would be the appropriate language and should be substituted, as applicable, in Section B.

3. Section C describes the requirements for establishing a Limited Equity Cooperative (LEC) where the existing mortgage on the property is assumed and the RC receives the same incentives as other purchasers.

4. Section D describes the protection afforded tenants who do not purchase units or become members of a housing cooperative.

5. Section E describes the requirements for resale of units or memberships to subsequent homeowners or members of a housing cooperative and the limits on homeowner or member equity. For LECs that assume the mortgages, this information is contained in Section C.

6. Section F describes the requirements HUD staff must follow to monitor projects with Resident Homeownership Programs.

9-2. Forms of Homeownership. There are several forms of homeownership available to RCs. In addition, RCs may establish several types of financing to assist residents to buy their units including the option of using HUD single-family insurance programs for homeownership, if available. If the RC plans to use HUD single-family mortgage insurance to finance the sale of units, the guidelines for the RHP shown be low must be supplemented by requirements in HUD Handbook 4135.1, Appendix 9. The RC must be certain that the RHP meets the provisions required by any source of mortgage financing sought for homeowners' purchases. Following are descriptions of the major eligible forms of homeownership that RCs may use:

A. Fee simple ownership of units (non-condominium) is most commonly used for detached properties. Usually, title to the unit, all of its walls, and the land underlying the unit are conveyed to the individual. For many multifamily properties, condominium ownership is the most feasible form of fee simple ownership because of unit configurations and shared spaces involved. However, other fee simple arrangements are possible for multifamily properties, and the other arrangements may be preferable when the units take the form of attached units, e.g., townhouses.

1. Planned Unit Development (PUD). In one common form of fee simple ownership (known as a PUD) which is suitable both for attached and detached units, homeowners hold title to the individual units and the land under the units. However, the shared common space (such as grounds, parking, recreation facilities, and possibly stairways and elevators in multifamily buildings) is owned by a Homeowners Association in which the homeowners are members. Ordinarily there may be no need for a PUD with a Homeowners Association where there is little or no shared common space. For example, the interest of townhouse owners

sharing a wall may be governed by a recorded party wall agreement, and other forms of recorded mutual easements may govern the interests of owners if there are shared driveways or entryways. However, projects purchased under LIHPRHA which will be operated as fee simple homeownership must establish a PUD with a Homeowners Association. Establishment of a PUD with a Homeowners' Association ensures that there will be a long-term organization controlled by the owners and capable of compliance with ongoing responsibilities, including control of any units not purchased by homeowners.

2. Homeowners Association. The RC must establish the Homeowners Association prior to or at the time of purchasing the project, so that it can own common property and eventually take over remaining functions of the RC when units have been sold. Legal documents establishing and governing the Homeowners Association must be executed and recorded.

3. Organization of Homeowners Association. It is important that the RC establish the Homeowners Association in a form that will be acceptable under the programs of major organizations involved in home purchase financing; e.g., the Federal Housing Administration (FHA), the Veterans Administration (VA), the Federal National Mortgage Association (FNMA), the Federal Home Loan Mortgage Corporation (FHLMC) and the Farmers Home Administration (FmHA). Because of the special involvement of the RC, it is probable that some changes must be made to standard PUD documentation and the RC should obtain the necessary approval for these changes from potential financing organizations before documents are recorded. The RC should anticipate the future needs of subsequent homeowners when the documents are written; not just those of initial homeowners.

4. Control of Units. HUD requires that the RC establish the Homeowners Association so that the RC has authority to exercise the special powers of control vis-a-vis unit purchasers that would normally be exercised by a developer in a for-profit environment. Under such an arrangement, the RC would control and provide the financing for the operations of the Homeowners Association, given through a HUD grant and other sources, until most of the units (typically 75 percent) have been sold. Once 75 percent of the units are sold, the unit owners would take control of the Homeowners Association. The RC can retain a voice in the Homeowners Association, proportionate to the number of units it still owns, or it can choose to transfer the remaining unsold units to the Homeowners Association if the Association is authorized and capable of exercising the remaining responsibilities of the RC under the RHP, Use and Grant Agreements and this Handbook.

5. Requirements of a Homeowners Association. The Homeowners Association established by the RC must meet the following general requirements, local law (many states now have legislation governing the establishment and operation of Homeowner Associations), and any special requirements necessary to preserve the eligibility of the units for home purchase financing:

   a. It must be organized and operated to provide for the acquisition, construction, management, maintenance and care of association property.

   b. The gross income of the Homeowners Association must come from contributions, membership dues, fees or assessments from owners of residential units, including the RC as long as it remains as an owner of units.

c. The expenditures of the Homeowners Association must be for the acquisition, construction, management, maintenance and care of association property and other incidental functions.

d. No part of any net earnings of the Homeowners Association may inure to the benefit of any private individual.

e. Every homeowner must be a member of the Homeowners Association and is entitled to voting representation regarding its operations. No tenants or non-residents of the project may be members of the Homeowners Association.

B. Ownership of a condominium unit is a form of fee simple ownership. Condominiums are established under state law, but a common understanding of the interests of a condominium unit owner is set forth in Section 234(c) of the National Housing Act. These interests include fee simple title (or long-term leasehold interest in fee simple title) in a one-family unit in a multifamily project, including a project in which the dwelling units are attached, semi-detached or detached, and an undivided interest in the common areas and facilities which serve the project.

1. Condominium Association. The condominium owners are members of a Condominium Association which operates much like a Homeowners Association in a PUD. When a for-profit developer establishes a Condominium Association it has control at the start and passes control to the homeowners when most of the units (typically 75 percent) have been sold. The RC should proceed in the same manner by establishing a Condominium Association that will eventually be controlled directly by the unit owners. The RC can

retain a voice in the Condominium Association, proportionate to the number of units it still owns, or it can choose to transfer the remaining unsold units to the Condominium Association if the Association is authorized and capable of exercising the remaining responsibilities of the RC under the RHP, Use and Grant Agreements and this Handbook.

2. Organization of Condominium Association. The Condominium Association established by the RC must meet the general requirements listed above for a Homeowners Association for a PUD. As with a Homeowners Association, the legal documents establishing and governing the Condominium Association must be executed and recorded by the time of project transfer, and the documents should be in a form acceptable under the programs of major financing organizations such as FHA, VA, FNMA and FHLMC. In a properly structured project, if it chooses and is qualified, a family may purchase its unit by way of a HUD/FHA insured mortgage made by a private lender under Section 234(c) of the National Housing Act.

C. Ownership of cooperative housing shares means stock ownership in a corporation that owns the property. Stock ownership gives a member the right to occupy a unit in the cooperative. Stockholders are cooperative housing members. For purposes of this Handbook, stockholders will be referred to as "members." Members occupy units under a proprietary lease. This financing approach is advantageous to low-income homeownership because the low-income homebuyers do not have to qualify individually for much of the mortgage debt carried by the cooperative.

1. Conversion to Cooperative Status. Generally, the project is converted to cooperative status when 70 percent of the memberships have either been purchased or have commitments to purchase from

prospective members. In LIHPRHA projects, this number of commitments would have been made by the prospective members prior to the RC making the purchase offer because earnest money deposits representing a commitment to purchase shares has been received from 75 percent of current tenants.

2. Project Purchased by Cooperative. Subscription Agreements from a minimum of 70 percent of tenants must be signed and the Cooperative must be formed prior to the Grant closing and project transfer, if allowed by State and local law. Therefore, although the RC makes application to purchase the project, in most cases, the grant will be made and the project will be sold to a Cooperative Association.

D. A Limited Equity Cooperative will have, in its by-laws, a limited equity formula that ensures long-term low-income affordability. The formula restricts the profits that members can receive when they resell their interests in the cooperative. There are two types of LECs that may be developed under the Resident Homeownership Program:

1. Those that acquire the project with a grant from HUD, prepay the mortgage, and carry out its housing cooperative program exclusively in compliance with the requirements of the Resident Homeownership Program; or

2. Those that acquire the project by assuming the FHA-insured mortgage and implement its housing cooperative program as a priority purchaser in compliance with the requirements for a POA in accordance with a combination of Chapter 8 and certain elements of the Resident Homeownership Program. This form of LEC may receive Section 8 rental assistance for its members. All information specific to this type of LEC is in Section C.

9-3. The Role of the Resident Initiatives Specialist (RIS). The RIS, located in the Loan Management Branch of the local HUD Field Office, is responsible for providing the expertise to RCs and nonprofit organizations working with RCs to achieve the objectives of the Resident Homeownership Program. Prior to working with RCs and nonprofit organizations to develop Resident Homeownership Programs, the RIS will:

A. Conduct special outreach activities to inform tenants and tenant representatives about the Title VI Resident Homeownership Program. This outreach effort will include providing tenants with information about:

1. The goals and objectives of the Resident Homeownership Program;

2. The technical and financial assistance available from HUD to assist in the formation of a RC;

3. The available forms of homeownership;

4. HUD assistance available for paying costs (see Paragraph 9-9.D.) necessary to implement a Resident Homeownership Program; and

5. Funding from other sources such as State and local governments, corporations and private foundations

B. Carry out the tasks in Paragraph A:

1. Through written communication;

2. By holding meetings with tenant groups at HUD or the project site (where the Field Office travel budget permits); and

3. By sending the organizations any HUD publications on resident homeownership.

C. Assist Loan Management staff with the development and maintenance of a list of priority/qualified purchasers who will be notified when purchasing opportunities are available in accordance with Paragraph 7-3.

9-4. Organization of and Assistance to Resident Councils. Tenants interested in homeownership must establish a RC, which is a tenant-controlled nonprofit group organized, in this case, to develop a Resident Homeownership Program or LEC. They must also organize a Homeowners Association, Condominium Association, or Cooperative to take responsibility for the project after sufficient units or memberships have been sold. To ensure that tenant groups have the capacity and experience necessary to organize a RC and a Homeowners Association, Condominium Association, or Cooperative, as appropriate, and to own and manage the project, the statute requires that they work with a public or private nonprofit organization. Such organizations must have sufficient experience to help the tenants organize, write the RHP, and then purchase and manage the project. The tenants may also seek assistance from HUD during their initial efforts to organize as a RC.

A. Organization of a Resident Council. The RC must meet the requirements defined in Paragraph 1-15. A suggested method for organizing is described below:

1. Organize a Petition Drive to Incorporate. While this step is not necessarily required, it encourages the involvement of residents in the process. The petition also can authorize a committee of residents to work with an attorney to draft a corporate charter and by-laws.

2. Retain an Attorney. Obtaining professional legal advice is an essential early step toward incorporation. Residents can hire an attorney, or possibly find one willing to help free of charge. In either case, the attorney should be familiar with low-income housing, sympathetic to resident homeownership goals, and able to devote sufficient attention to the needs of the project. Community Legal Services agencies are a possible source of such

assistance.

3. Draft By-Laws and a Corporate Charter. By-laws and a corporate charter define the purpose of the organization, identify its name and address, list the officers, and state the rules by which the organization will be governed. Most practicing attorneys can provide standard language for these documents or model documents prepared by National Associations or other organizations could be adapted for RCs in the Preservation program. Even if RCs obtain model documents, however, residents should work with an attorney to shape these model documents to meet their particular needs.

4. Elect Board Members and Officers. A Board of Directors governs the RC and represents the interests of residents. The Preservation Program requires that board members be democratically elected to their positions by the residents and that all these positions be held by residents. The board serves on a voluntary basis and watches over the paid manager of the organization (if one exists). The number of board members must be defined in the by-laws and typically ranges from four to eight persons. The by-laws must also contain written procedures for electing RC officers on a regular basis.

5. Form Committees. Committees can play a very important role in getting full participation and cooperation from the organization membership. Some committees, such as the finance committee, may be required under the corporate by-laws. Others may be formed or dissolved in response to the changing needs or desires of the organization membership. Once the governing body is assembled and officers appointed, the process of forming committees can begin.

6. Meet other needs of the RC during and immediately after incorporation. First, a room large enough to accommodate an audience of residents must be found for

board meetings. Second, office space and office equipment may be needed in order for the RC to perform its administrative functions. Also, the RC will need a corporate identity, which can be created by designing a logo, printing letterhead stationery, and fabricating plaques or banners to post in offices or the board room. Together, the physical setting, functional supports, and graphic symbols of the new organization signify its ambitions, both to those involved and to others in the residential community.

B. The nonprofit organization working with the RC must:

1. Be a public agency or a public or private nonprofit organization;

2. Be incorporated or sanctioned under State or local law;

3. Have sufficient experience to help the tenants consider their options. Such organizations must demonstrate their capacity to help tenants organize, acquire and manage the project, and develop a viable Resident Homeownership Program.

4. Demonstrate Its Ability to Manage the Project, if Necessary.

   a. HUD may approve either the nonprofit organization or the RC to manage the project if one or the other can demonstrate that it has effectively managed an eligible property for at least three years;

   b. If the nonprofit organization manages the project, it must:

i. Meet the requirements for experience cited in HUD Handbook 4381.5, Management Documents, Agents and Fees, Chapter 2, Section I; and

ii. In accordance with HUD Handbook 4381.5, Chapter 2, Paragraph 2-4, certify in the Management Certification that it has obtained fidelity bond or employee dishonesty coverage; and

c. Nonprofit organizations or the RC are not precluded from arms length subcontracting with for-profit organizations to provide management services.

C. If the nonprofit organization is to be paid for its activities, the Loan Management Branch must determine that the nonprofit organization working with tenants, meets the requirements specified in Paragraph B. above. The tenants involved with the establishment of the RC should submit information about the nonprofit organization or public agency to the Chief, Loan Management Branch, as early in the prepayment process as possible so that the RC and the nonprofit organization will not incur expenses that HUD later determines are not eligible for reimbursement under an approved RHP. Log when information is received from the RC about the nonprofit organization

D. GRANTS

1. Technical assistance planning grants are available to qualified Community Based Nonprofit Organizations (CBOs) or RCs under Notices of Fund Availability (NOFAs). The Preservation Division will provide guidance and information to Field Office staff by way of HUD Notices that provide instructions for processing grant applications received in response to the NOFA. The Preservation Division will

also work directly with the Resident Initiatives Specialist (RIS) to make grant information available to eligible applicants. The planning grants provide

funding to facilitate the: (1) organization of a RC or CBO, (2) acquisition of a project, or (3) preparation of an RHP, Plan of Action (POA), or Limited Equity Cooperative Plan of Action (LEP). The operative NOFAs for these grants will vary each year. In general, if the owner of an eligible project has submitted an Initial Notice of Intent (NOI) to sell the project, or if the Initial NOI is to extend affordability but the owner has been working with a resident group which wishes to purchase the project, a qualified applicant may be able to apply for a planning grant under the NOFA. The specific qualifications for receiving a grant may differ in each NOFA. In some cases, intermediaries will be selected by HUD to administer the grants. Potential applicants may obtain copies of NOFAs and application packages from either the RIS in the local HUD Field Office or from the administering intermediary. The RIS will make available names of those intermediaries.

2. Other Grants will be made available through NOFA publication to State and local government agencies, nonprofit intermediaries (as defined in Paragraph 1-15), community-based nonprofit housing developers, and experienced resident organizations and CBOs to carry out resident capacity building, predevelopment activity, community outreach, training programs, and organizational activities.

E. Ineligibility of Grants under the Homeownership and Opportunity for People Everywhere (HOPE 2) Programs. HOPE 2 Planning Grants are not available to RCs of any project for which an owner has submitted an Initial Notice of Intent (NOI). If Loan Management staff receives an Initial NOI for a project that has a HOPE 2 grant in process, the loan servicer must return the Initial NOI in

accordance with HUD Notice 92-32, Processing Instructions for the Fiscal Year 1992 for Homeownership of Multifamily Units Program (HOPE 2) - Applications for Grants, Paragraph 9.

9-5. The RC is responsible for:

A. Electing a Board of Directors and/or creating a Homeowners Association, Condominium Association, or Cooperative to exercise the legal control over the project. The organization of this entity must be done in accordance with State and local laws. The decision must be made whether the entity will operate in conjunction with the RC or will assume all responsibilities of the RC after the required number of units are sold. If the entity is to manage the project, the determinations specified in Paragraph 9-4.B.4. must also be made;

B. Submitting an expression of interest (EOI) and bona fide offer to purchase the project in accordance with Chapter 7, and executing all other agreements;

C. Developing and submitting the RHP in accordance with Section B or a LEP in accordance with Section C;

D. Executing a grant agreement and/or other agreements with HUD;

E. Providing, or contracting for, counseling services that will help residents gain the skill, build the organizational capacity, and acquire the confidence to carry out the Resident Homeownership Program, including developing the ability to identify and obtain the financial resources needed to purchase and manage the project;

F. Administering the Resident-Homeownership Program by:

1. Maintaining or contracting for maintenance of the project in accordance with the housing standards in Chapter 11, Paragraph 11-13.

2. Managing or contracting for the management of the Resident Homeownership Program in accordance with the RHP. This responsibility includes submitting all forms and reports required by the RHP to HUD in a timely manner;

G. The overall administration and policy making decisions for the project regardless of whether it contracts with a nonprofit organization to manage it;

H. Arranging for financing of units by individual homeowners and maintaining relations with lenders and other entities who may provide grant funds. In some jurisdictions participating in locally administered HOME Investment Partnerships programs, the RC may be able to negotiate to "recycle" homeownership funds paid in accordance with Paragraph 9-36. Current homeowners may then use these funds to finance rehabilitation of units. Subsequent homeowners may use the funds to purchase units; and

I. Submitting required reports in accordance with a RHP or LEP.

9-6. Offer to Purchase. Tenants who wish to form or have already formed a RC to purchase the project in which they live must follow the process outlined below. This process describes the timeframe in which an owner may accept a bona fide offer from a RC, the requirements for submission of an Expression of Interest (EOI), the components of a bona fide offer, acceptance or rejection of the offer, and what actions must be taken next. For additional guidance, please refer to Paragraphs 7-4 through 7-12.

A. For the first six-month period beginning on the date that HUD receives a complete and accurate Second NOI reflecting the owner's intention to sell the project, the tenants and RC control the selection of the purchaser. This situation exists because the purchaser must have the RC and tenant support in order to purchase the project.

1. Residents should understand that if they sign a statement signifying that they wish to form a RC to purchase the project, they should not also sign a statement giving support to another organization to purchase the project. Since CBOs may also purchase the project during this period if they can demonstrate support of a majority of the tenants, a tenant who signs more than one statement could create competition for the purchase.

2. Although a RC may offer to buy a project at any time during the 15-month offering period, it should proceed as quickly as possible, to preclude the possibility of the owner accepting another offer after the initial six-month period.

B. Expression of Interest (EOI). As soon as the owner submits a Second Notice of Intent (NOI) to HUD, a RC may begin the purchase process by submitting a written EOI to the Chief, Loan Management Branch, in accordance with Paragraph 7-5.

C. Information from HUD and the Owner. Within 30 days of receipt of an EOI, Loan Management staff will determine the eligibility of the RC to purchase the project under a Resident Homeownership Program, notify it in writing of its eligibility and provide the information identified in Paragraph 7-6. Upon notification from HUD of the RC's EOI, the owner also will provide the RC with any relevant information necessary to complete the sale.

D. Bona Fide Offer. An eligible RC may submit a bona fide offer to the owner with a copy to the Chief, Loan Management Branch. The components of a bona fide offer are identified in Paragraph 7-7. The requirements include the following provisions:

1. The RC must demonstrate that tenants representing at least 50 percent of all units and 75 percent of the occupied units have expressed an interest in

participating in the Resident Homeownership Program to be developed by the RC; and

2. While an owner may not waive an earnest money deposit for a RC, it may, if the tenants agree, and if allowed by State and local law, accept an assignment of any portion of the tenants' security deposits in lieu of the earnest money deposit. The amount of the earnest money or assigned security deposit must be at least $200 from each prospective purchasing tenant representing at least 75 percent of the occupied units. This deposit will represent a firm commitment on the part of the tenant to purchase (unless released from the commitment by the RC for emergency reasons) and must be applied to the tenant's downpayment for the unit or membership.

E. Acceptance or Rejection of Offer. The owner must accept or reject the offer within 30 days of receipt. If an owner rejects the offer, it must return any cash earnest money deposit to the RC. Where pledges of security deposits were used as the earnest money deposit, they must be returned to the tenants' security deposit accounts. Any acceptance must be contingent upon HUD's approval of the offer and of a RHP. Within ten days of notification from HUD that the offer is acceptable, the owner must issue a final acceptance to the RC contingent upon satisfactory completion of a RHP.

F. Additional Conditions. Guidance provided in Paragraphs 7-9, 7-10, 7-12, and 7-13, dealing with acceptance of the offer and procedures to follow if the sale is not consummated also apply to the implementation of a Resident Homeownership Program.

G. Submission of a Resident Homeownership Plan or Limited Equity Plan of Action. The requirements and the conditions for approval for a RHP and LEP are in Sections B and C, respectively. The RC must submit a RHP or LEP to the Loan Management Branch within the following timeframes LOG date POA received :

1. In the case of a voluntary sale, within six months of the owner's acceptance of an offer which contains a contingency clause requiring HUD's approval; and

2. In the case of a mandatory sale, within six months of the owner's receipt of the offer.

9-7. Seller Financing is permitted for RCs on a case by case basis. The Loan Management staff must check with the Preservation Division to determine the acceptability of a specific proposal.

9-8. Notification to New Tenants. Any tenant who moves into the project after the submission of the RHP must sign a certification, before occupancy, indicating that it has been informed by the owner of the pending change in ownership of the project and is aware that a Resident Homeownership Program is being established. The notification should further indicate:

A. The tenant's option to purchase its unit;

B. The length of time that the tenant will likely be allowed to remain in the project as a renter and that the tenant must move at the end of a period clearly specified in the lease if it does not purchase the unit;

C. The possibility of rent increases;

D. That the tenant may be eligible for Section 8 rental assistance if it remains in the project as a tenant after approval of the RHP; and

E. That relocation assistance will not be available.

9-9. Financial Assistance.

A. From HUD. A RC may receive financial assistance to pay for the expenses shown in Paragraph D. below if the Loan Management staff determines that the RHP submission meets the requirements of Section B of this Chapter and Appendix 9-2, Evaluation of a Resident Homeownership Plan. The financial assistance

provided by HUD must be the least costly alternative to the Federal government consistent with establishing a viable Resident Homeownership Program. In most cases, this financial assistance will take the form of a grant from HUD.

B. From State or Local Government Agencies or Other Sources. This assistance may come in whole or in part from these sources as described in Paragraph 8-17.E.

C. Total Maximum Assistance. HUD will subtract any funds that the RC, or the nonprofit organization working with the RC, receives from other sources if it duplicates HUD funding for the same purpose.

D. Types of Assistance.

1. The purchase price, not to exceed Transfer Preservation Value;

2. Transaction expenses as outlined in Paragraph 8-21(A)(1)(c);

3. Reimbursement for the costs of all items listed in Paragraph a. through c. below. The expenses and amount of funds requested for such items must be necessary and documented. The funding level will be limited to the lower of $500 per unit or $200,000 per project.

a. Training for the RC;

b. Homeownership counseling and training; and

c. Fees for the HUD-approved nonprofit organization or public agency working with the RC;

4. Eligible relocation expenses for tenants who elect to move, rather than lease or purchase a unit, as described in Paragraph 9-34.E.;

5. The documented cost of rehabilitation identified by the Capital Needs Assessment plus any other rehabilitation costs justified and documented in the RHP;

6. The establishment of an adequate initial reserve for replacement account; and

7. The establishment of an operating reserve escrow account, including contingencies against unexpected increases in expenses or shortfalls in homeowners' payments, if the RC documents the need.

Section B. Resident Homeownership Plan of Action

9-10. Submission of the Resident Homeownership Plan of Action (RHP). The RHP serves the same purpose as the Plan of Action (POA) submitted by other types of purchasers and must contain all of the elements, documentation, and information required by this Section and the checklist contained in Appendix 9-1, Resident Homeownership Plan Checklist. The

Loan Management staff should follow the guidance in Paragraphs 8-3 through 8-5 when processing the submission of a RHP.   NOTE: The required conditions of a POA for a Limited Equity Cooperative (LEC) which assumes the mortgage are described in Section C and will be called a Limited Equity Plan of Action (LEP).   While any Cooperative which is not an LEC which assumes the mortgage submits an RHP in accordance with this Section, terminology for such RHPs will be in accordance with that specified in Section C. The Resident Council (RC) must submit six copies of a complete RHP to the Chief, Loan Management Branch within the following time frames: LOG date received whether complete or not

A.   Under the voluntary sales process, within six months of acceptance of a bona fide offer by the owner; and

B.   Under the mandatory sales process, within six months of the owner receiving an offer from the RC.

9-11.   Required Review of the RHP. The Loan Management staff must review the RHP and respond to the owner and RC in the same manner and within the same time frames as required for reviewing POAs in Paragraphs 8-6 through 8-10. The staff should use Form HUD-91110, Evaluation of a Resident Homeownership Plan, Form HUD 91110-A, Worksheet for Individual Resident Homeownership Feasibility, and Form HUD 91l10-B, Summary Worksheet for Resident Homeownership Feasibility to evaluate the RHP.

9-12.   Required Conditions of a Resident Homeownership Plan. The RHP must spell out all the duties and responsibilities of the RC and the Homeowners or Condominium Association, meet all of the conditions

listed in this Paragraph and fully address all of the elements listed in Paragraph 9-13. This chapter assumes that the RC will continue to operate in conjunction with a Homeowners or Condominium Association. However, the RHP must specify whether these duties will be retained by the RC or will be turned over to the successor entity at a certain time.

A. Unit values.

1. At the time of sale of the unit to the initial homeowner, the RC should determine the unit values so that the total of all values equals the project's Transfer Preservation Value (TPV) or purchase price, if lower than the TPV. The RC must develop the unit values proportionately and describe the method in the RHP.

2. At the time of sale of the unit to a subsequent homeowner:

   a. If the promissory note that the homeowner signs with HUD is still in effect in accordance with Paragraph 9-37, the RC must determine the value of the unit by means of an appraisal. If an appraisal is required by the lender for mortgage purposes, the subsequent homeowner must submit a copy of the appraisal to the RC. If the lender does not require an appraisal or the RC is the lender, the RC must contract for it.

   b. If the promissory note that the homeowner signs with HUD is no longer in effect and if resale restrictions still exist, the RC will determine the value of the unit using the method described in its RHP.

B. Limits on Homeowner Expenses.

1. An initial homeowner's monthly expenses must not exceed 35 percent of its adjusted monthly income.

   a. An initial homeowner will not qualify to purchase a unit if, during the first year of homeownership, it must spend more than 35 percent of its adjusted monthly income (AMI) on debt service (principal and interest), utility costs, taxes, insurance and homeownership fees.

b. Depending on the RHP and the form of homeownership desired, these costs may be allocated in different ways between those expenses paid directly by the homeowner and those paid by the RC from project funds. At a minimum, the total homeownership fees must be sufficient to cover all operating and administrative costs of the Resident Homeownership Program and maintenance of the common areas. However, a homeowner's maximum total out-of-pocket monthly payments may not exceed 35 percent of its AMI, regardless of how the costs are allocated between those paid by the homeowner and those paid by the RC.

2. For subsequent homeowners, the RC, at its option, may limit the amount of monthly income which can be used to cover housing expenses. The RC also, at its option, may use funds from the general operating reserve account (GOR), established in accordance with Paragraph 9-26.I., to provide subsidies to subsequent homeowners to reduce housing costs. Use of funds from the GOR account, must meet the guidelines developed in the RHP.

C. Unit purchase price.

1. For Initial Homeowners.

a. The unit purchase price must never exceed the unit value. The unit purchase price, established individually for each initial homeowner, must be set so that the debt service on the mortgage for the

unit can be supported by the difference between 35 percent of the homeowner's AMI and all other ongoing expenses connected with homeownership in accordance with Paragraph B. above.

b. For purposes of determining the unit purchase price, the RC must determine both 35 percent of the homeowners AMI and the expenses connected with homeownership as of the date it transfers the unit to the homeowner. However, for purposes of RHP approval, the RC should use information concerning prospective homeowners as of the date it submits the RHP.

c. The minimum purchase price for initial homeowners may never be less than the down payment made in the form of the earnest money deposit paid in cash or pledge of security deposit by the tenant. The RHP may set a higher minimum purchase price, and apply it to other initial purchasers, based on unit type, thus limiting eligibility of some prospective initial homeowners. However, the total number of initial homeowners must meet the criteria set forth in the RHP in accordance with Paragraphs D.2. and E. below.

2. For Subsequent Homeowners.

a. When the Unit Purchase Price and the Unit Selling Price are the Same. The unit purchase price is the amount the subsequent homeowner pays for the unit. Ordinarily, the selling price for which the current homeowner sells the unit and the purchase price for which the subsequent homeowner buys the unit will be the same.

b. When the Unit Purchase Price and the Unit Selling Price Differ. When the unit selling price and the unit purchase price differ, (e.g., when the current homeowner sells the unit to the RC for one amount but the subsequent homeowner purchases the unit from the RC for another amount or if the RHP requires that the selling price be set at the unit value for the current homeowner and the purchase price be computed as 35 percent of the AMI for the subsequent homeowner), the Handbook will use the term selling price when referring to the seller and purchase price when referring to the purchaser.

D. The RC must transfer ownership of all units which are to be sold to the initial homeowners no later than four years from the date of its purchase of the project. However, the transfer of ownership will begin when the RC purchases the project. It is anticipated that only units to be sold to non-residents and to residents who need time to escrow down payments prior to purchase, will require the maximum allowable time for transfer. The RC must ensure, to the greatest extent practicable, that a sufficient number of tenants residing in the project on the date it submitted its RHP, intend and can afford to purchase their unit by:

1. Performing a financial analysis of each prospective tenant's income and assets to ensure that the tenant can afford to purchase the unit and meet the applicable required conditions of the RHP.

2. Seeking and using financing programs that enable a sufficient percentage of current tenants who reside in the project at RHP submission to purchase their units within that four-year period.

a. We recommend that the RHP contain documentation that a minimum of 65 percent of current tenants, in the

same proportion of very low-, low- and moderate-income families that resided in the project at the time of RHP submission, are purchasing their units.

b. For example, if on the date of submission of the RHP, a fully occupied 100-unit project contains 50 very low-income, 40 low-income, and 10 moderate-income tenants, the RHP would contain evidence that at least 33 very-low income, 26 additional very low- or low-income, and at least six additional current tenants will be able to purchase their units. There would be no restrictions on the income category of the additional six or more current tenants who will purchase. Suggestions for ensuring the tenant's ability to meet this requirement are in Paragraphs I. and J. below.

3. Requiring a written expression of interest, from all tenants who are potential homeowners in at least the proportions required by the RHP, certifying the tenants' intent to purchase their units and not rent it to another family for 15 years.

E. Tenant Income Profile. The RHP must include tenant income profiles submitted in accordance with Paragraph 8-17.F. Initial purchasers who do not reside at the project on the date the RC submitted its RHP must be selected in a manner that ensures that the total number of initial homeowners that are very low-, low-, and moderate-income meets the requirements for tenant selection described in Paragraph 8-18.A.3. The RHP should specify any restrictions on above moderate-income purchasers with the following limitations:

1. Above moderate-income tenants who live at the project at the time of RHP approval may purchase a unit and become initial

homeowners, if allowed by the RHP. (PLEASE NOTE: They may also continue to rent a unit at the project as tenants.)

2. Non-resident above moderate-income families may not become initial homeowners.

3. However, above moderate-income families may purchase units and become subsequent homeowners if allowed by the RHP.

F. Use of Project Income.

1. Immediately upon receipt or annually, at the RC's option, the RC must remit to HUD 50 percent of the proceeds from the sale of units to initial homeowners. Depending upon the method of financing used, this will be paid in different stages:

a. If the RC receives cash from the sale of a unit because the homebuyer received a loan from a conventional lender, the RC must return half the purchase price to HUD at the time of sale.

b. If the RC carries back the mortgage, it must remit half the principal to HUD as it is collected.

c. If a unit is sold by the initial homeowner and the initial homeowner pays the RC the total debt, the RC must pay HUD 50 percent of the amount received. (NOTE: If a subsequent homeowner assumes the initial homeowner's remaining debt, the RC would have to continue to remit to HUD 50 percent of all amount it receives in payment of principal, as it is collected.)

2. The RC may use any initial sales proceeds not required to be paid to HUD, along with any interest charged for financing the debt on the units, for costs of the homeownership program, including

improvements to the project, operating and replacement reserves, additional homeownership opportunities in the project, and other project related activities approved by HUD. Other project related activities will include expenses other than normal operating expenses for the project. For example, the RC may use such funds for purchasing units which homeowners are selling, subsidizing homeowner interest payments, or training subsequent purchasers.

3. The RC should use proceeds retained from any subsequent sales proceeds, for costs of the homeownership program, including purchasing units which homeowners are selling, subsidizing homeowner interest payments, training subsequent purchasers, or other HUD approved project-related activities.

4. Monthly homeowners fees should be used for expenses for project maintenance, operating and replacement reserves, and RC-paid taxes, insurance, and utility bills, and other expenses typical of all rental and homeownership projects.

G. Promissory Note.

1. Each initial homeowner must sign a promissory note, payable to HUD, agreeing to repay the difference between the value of the unit and the purchase price. These values are established in accordance with Paragraphs A. and C. above. Subsequent homeowners may have to sign a promissory note in accordance with Paragraph 9-37.

2. The promissory note bears no interest, is not amortized, is non-recourse, and must be secured by a mortgage.

3. The requirements of a promissory note, including the requirements for repayment by both the initial and any subsequent purchasers, are contained in Paragraphs 9-36 and 9-37, respectively.

H. Restrictions on Equity and Resale.

1. RCs should specify in contracts with homeowners and in the RHP whether they have the first right to purchase the unit from the initial homeowner for a specified amount before any other prospective buyer. The RHP must specify the maximum length of time the RC may own the units prior to their sale to an eligible family. The period established must be reasonable, e.g., a period of two years.

2. The RC may place reasonable restrictions, beyond those required by statute and approved by HUD, on the amount of equity appreciation a homeowner may retain. If restrictions are placed, the RC must, at the time of initial sale, enter into an agreement with the family to establish such a maximum.

I. RCs may develop and offer any method or combination of methods of loan repayment to homeowners to purchase their units. At the RC's option, these methods may differ for initial and subsequent homeowners. The RC should ensure, however, that the financing method selected by the purchasers does not result in violation of the requirements of Paragraphs B. through E. Possible methods of financing include but are not limited to:

1. Arranging with a bank or other lending institution for mortgage financing for individual tenants;

2. Helping tenants qualify for State and local homeownership programs;

3. Arranging for State-supported mortgages for the potential homeowners;

4. Arranging with a bank to finance all units through the RC with the RC collecting payments from individual homeowners and then making the bank payments;

5. Using proceeds and interest payments from previous sale of units to provide RC financing of all homeowner mortgages;

6. Use of Federal Agency programs for which the homeowner and property are eligible, such as HUD mortgage insurance, the Department of Veterans Affairs loan guarantees, or Farmers Home Administration financing. If the RC plans to use any of these programs, it should be certain that the discretionary aspects of their RHP do not conflict with the requirements for the specific program. For instance, if any homeowner's mortgage is to be insured by HUD under Section 203 or Section 234, the RHP must state that legal restrictions on conveyance (e.g. prohibition against the homeowner renting the unit, restrictions on sales proceeds retained by the owner, and the right of first refusal by the RC) may have to be terminated if:

   a. The mortgage is transferred by foreclosure;

   b. The mortgage is transferred by deed in lieu of foreclosure; or

   c. The mortgage to the property is assigned to HUD.

7. Using other methods of financing depending upon the income level of the tenant or other financial criteria.

J. RCs may use any homeowner loan repayment method or combination of methods to enable as many residents as possible to purchase units. At the RC's option, these methods may also be used for subsequent purchasers. Some suggested methods include but are not limited to:

1. Subsidizing the lending institution's interest rate. The amount of subsidy would be based on the amount the homeowner may spend in accordance with Paragraph B. above. The RC should

specify whether there is a floor (e.g. one percent) below which it would not subsidize the interest rate.

2. Determining rates and terms for loans payable to the RC to bring the homeowner's payments to the level determined in accordance with Paragraph B. above. It is advisable that the RC not reduce the interest rate that the homeowner pays on the loan to less than one percent nor extend the amortization period beyond 40 years.

3. While the purchase price is determined at the time of closing the sale on the unit, the RC may, at its option, adjust interest rates based on certifications of the homeowner's income at periods specified in the RHP. If the RHP allows it, the RC may also accelerate an extended payment period if the homeowner's income increases.

4. The RC may provide for homeowner repayment of interest subsidized in accordance with Paragraphs 1. through 3., upon sale of the unit, if there are any funds remaining after repayment of the promissory note to HUD.

5. It is advisable that the RHP not allow mortgages which contain negative amortizations, balloon payments, or any other requirement which could act to the homeowner's long-term financial detriment.

K. In the case of loans made by the RC to initial homeowners, it is recommended that the RHP establish the down payment and closing cost requirements so that they do not exceed ten percent of the homeowner's adjusted annual income, with a minimum of the $200 earnest money deposit for initial homeowners who are current tenants. The homeowner should have the option to contribute a greater downpayment in order to increase its equity. The RC, at its option, may set the down payment and closing cost guidelines for subsequent purchasers.

L. All initial homeowners must sign a certified statement that the unit will be used as their principal residence. At the RCs option, the RHP may require a similar certification from subsequent purchasers.

M. Restrictions on Renting the Unit.

1. Initial Homeowner. The property must be occupied by the initial homeowner for at least 15 years from the date of purchase or until the initial homeowner sells the unit, whichever comes first. The unit may not be leased or otherwise made available to other families during this period. A family is exempted from this rule if it temporarily moves outside the market area for employment or because of an emergency. The exemption will end when the emergency ceases to exist. The RC has the option to extend the 15-year period by establishing such a policy in the RHP.

2. Subsequent Homeowners. At its option, the RC may restrict the rental of units by subsequent homeowners in the RHP.

N. The RC must develop a method to keep residents informed of their rights and to make sure that they have the opportunity to participate in the decision making process.

O. The RC must determine whether they will pay moving expenses for tenants who choose to move rather than purchase or continue to lease a unit. If they do, the RHP should specify whether they will pay actual and reasonable expenses for such tenants or develop a schedule of relocation allowances in accordance with Paragraph 9-34.E.

P. The RC must comply with any State and local government laws about cooperative housing or Resident Homeownership Programs. This includes any requirement that a minimum number of residents participate in the housing program where the requirement is more stringent than HUD's.

Q. The RC must specify whether all responsibilities for the project will be turned over to a successor entity, and if so, the sales conditions which must be met prior to this event, or if the RC will continue to operate in conjunction with the Homeowners Association or other applicable entity.

9-13. Required Elements of a Resident Homeownership Plan (RHP). The RC must use the RHP to describe the major elements of and schedules for the development of the Resident Homeownership Program and show how each criteria will be met. Loan Management staff may use Appendix 9-1, Resident Homeownership Plan Checklist, to ensure that the RHP submission is complete and Appendices 9-2, 9-2A, and 9-2B, Forms HUD-91110, 91110-A, and 91110-B to evaluate it. The RHP must include, at a minimum:

A. Information About the Sale of Units to Tenants Who Reside in the Project at the Time the RC Submits Its RHP. All issues described below must be addressed:

1. The type of homeownership contemplated (e.g., condominium or fee simple) along with methods and a schedule for conversion to homeownership;

2. The financing arrangements for the units, including the underwriting standards and rates and terms for loans available for tenants in the various income categories;

3. The methods by which eligibility for purchase and credit, other than income, will be determined;

4. The down payment (with a minimum of the earnest money deposit paid by initial homeowners) and other costs to be paid by the homeowner at closing, including whether sweat equity may be used for all or part of the downpayment and how the sweat equity would be valued;

5. A statement describing the monthly homeownership fees and estimates of utility costs, taxes, and insurance for each unit size;

6. An analysis of the unit purchase price for each potential initial homeowner, given anticipated fees in accordance with Paragraph 5. above and methods of financing, underwriting standards, and other considerations, in accordance with Paragraphs 2. through 4. above;

7. The number of existing residents who wish and are eligible to purchase;

8. Documentation that current tenants who wish to purchase units will be able to purchase in the proportions required by the RHP in accordance with Paragraph 9-12.D.2.; and

9. Identification of the actual proportions of initial homeowners in the three income categories intending to purchase units consistent with Paragraph 9-12.E.

B. Information about Marketing Unsold Units.

1. How vacant units will be marketed to achieve the required tenant income profile in accordance with Paragraph 9-12.E.;

2. A workable sales schedule;

3. An Affirmative Fair Housing Marketing Plan;

4. Credit and income requirements potential purchasers must meet in order to qualify for a loan;

5. Any preferences other than those required by Paragraph 9-12.D.2. and E.; and

6. Whether financing and other factors described in Paragraph A. above will be

the same or different for non-resident initial purchasers.

C. Considerations for Non-purchasing tenants.

1. Anticipated number of tenants requesting relocation assistance;

2. What relocation expenses will be provided in accordance with Paragraph 9-34.E.;

3. Determination of rents in the project if non-purchasing tenants do not relocate in accordance with Paragraph 9-34.C. and D.;

4. Developing phased-in rents for non-purchasing tenants in accordance with guidelines in Chapter 8, Paragraph 8-18.A.7.;

5. Eligibility of non-purchasing tenants for Section 8 rental assistance, whether they remain or relocate; and

6. Nondiscrimination counseling to familiarize non-purchasing tenants with opportunities to select replacement dwellings from a full range of neighborhoods within the housing market area; their rights under the Fair Housing Act and other applicable Civil Rights laws; and how to search for suitable replacement housing.

D. Financial Considerations:

1. The amount of grant funds requested from HUD;

2. The amount of funds requested from State and local governments or other sources;

3. The anticipated waivers or abatements in taxes or other charges;

4. The provision of free or reduced price services to be provided by local organizations or other anticipated means of saving expenses. All such funding,

abated expenses or the provision of free services, must be documented and guaranteed for a minimum of five years;

5. Funds, received as technical assistance grants by either the RC or nonprofit organization, which may be used to offset eligible expenses;

6. The anticipated use of:

   a. HUD grant funds;

   b. Funds from State and local governments;

   c. Proceeds from the sales price and interest payments of units to initial purchasers consistent with Paragraph 9-12.F.;

   d. Technical assistance grants; and

   e. Any other funds received pursuant to Paragraphs 3, 4, and 5 above.

7. Organizational costs;

8. Documented costs for training and other technical assistance;

9. The RC's acquisition costs for the project;

10. A summary of cost estimates for major rehabilitation activities to be carried out, including repairs, replacements and improvements as well as any costs for temporary relocation activities;

11. Anticipated homeownership fees, what the fees pay for, a description of how they are allocated to various unit types, and estimates, with documentation, of other costs to be paid by homeowners;

12. A statement as to responsibility for payment of taxes, insurance, and utility bills for the individual units; and

13. Proforma cash flow analyses for the four years after RHP approval. This proforma must reflect the financial feasibility and viability of the Resident Homeownership Program, taking into account any rental activity resulting from non-purchasing tenants of the project.

a. Homeownership Activities.

i. Project Operation.

(a) Income from homeownership fees, laundry and any other sources;

(b) Expenses for operating the project including maintenance, administrative costs, utilities, taxes, insurance, deposits to a reserve for replacement account;

ii. Unit Purchases and Sales.

(a) Income from the sale of units;

(b) Payment to HUD of 50 percent of the net proceeds from the sale of units to initial purchasers, in accordance with Paragraph 9-12.F.1.; and

(c) Expenses for purchase of units, homebuyer interest subsidies, orientation of new homeowners, and other expenses which are unique to a Resident Homeownership Program;

b. Rental Income and Expenses.

i. Proportionate share of income and expenses from the rental portions of the operating budget. The budgets should show decreases in the rental portion and increases in the homeownership portion over the four-year period in accordance with the anticipated sales schedule; and

c. Any anticipated relocation costs for non-purchasing tenants.

E. Relocation Information.

1. An estimate of the number of tenants who plan to relocate and, if the RHP provides for relocation assistance, the estimated cost for such relocation determined in accordance with Paragraph 9-34.

2. An estimate of the number of nonpurchasing tenants who plan to remain as renters but who must temporarily relocate during the rehabilitation work, the estimated cost of temporary relocation, and the availability of temporary relocation resources.

F. Rehabilitation Information.

1. Expected scope of rehabilitation with justification for any rehabilitation over and above that required by the Preservation Capital Needs Assessment; and

2. Details on how the rehabilitation will be accomplished.

G. The expected scope of technical assistance, training and counseling for the RCs, homebuyers, and nonpurchasing tenants.

H. Requirements for Resale of Units.

1. Any restrictions on resale by homeowners over and above those specified in Paragraph 9-35 and any restrictions on homeowners' equity, over and above those specified for the first six years of homeownership in Paragraph 9-36.A.1.c.

2. Any differences in other parameters between those established for initial homeowners and subsequent homeowners, e.g., establishment of purchase price, downpayments, and financing. If the RC is not establishing a condition for any of the parameters for subsequent homeowners, that fact must be stated.

I. A tenant income profile representing the tenants who resided in the project on the date of RHP submission and pursuant to Paragraph 9-12.E. This profile will be used for two purposes:

1. To designate the percentage of initial homeowners who must fall into each income category;

2. To designate the percentage of tenants who must fall into each income category in accordance with the requirements of Paragraph 8-18.A.3. For the remaining useful life of the project, any new tenants must be selected to fulfill the tenant profile requirements.

J. Copies of all forms, guidelines, worksheets, and contracts developed to implement the Resident Homeownership Program and all other documents required to justify elements of the RHP.

K. A proposed method for submitting any applicable forms, annual reports, and audits to HUD to demonstrate compliance with Federal regulations.

L. Information about the Management of the Project.

1. A Management Plan detailing all aspects of management including:

a. Whether the project will have a resident manager and, if so, the resident manager's duties and remuneration; and

b. The different methods that will be used to manage the homeownership and rental components of the project;

2. Management Agent

a. If the RC is the management agent, the RHP must contain evidence that it has managed the property effectively and efficiently for at least three years; or

b. If a nonprofit organization is the management agent, the RHP must contain:

i. The name and address of the nonprofit organization or public agent selected to manage the property and support documents that reflect the qualifying experience it has to meet the standards in HUD Handbook 4381.5, Management Documents, Agent and Fees, Chapter 2, Section I;

ii. An executed contract between the RC and the management agent, contingent upon HUD's approval; and

iii. A statement confirming that the RC will retain primary responsibility to handle and resolve problems such as regaining control of a unit if the homeowner moves or if the unit becomes uninhabitable.

c. If the nonprofit organization contracts with a profit-motivated management agent, the RHP must contain:

i. The name and address of the profit-motivated management agent selected to manage the property and support documents that reflect the qualifying experience it has to meet the standards in HUD Handbook 4381.5, Management Documents, Agent and Fees, Chapter 2, Section I;

ii. An executed contract between the nonprofit organization, RC and the profit-motivated management agent, contingent upon HUD's approval; and

iii. A statement confirming that the RC will retain primary responsibility to handle and resolve problems such as regaining control of a unit if the homeowner moves or if the unit becomes uninhabitable.

M. The Policy for Repurchasing and Sale of Units.

1. The RC may pursue several options when purchasing units from homeowners who wish to sell, including purchasing all units and reselling them, serving as the buyer of last resort for unsold units, or maintaining the right of first refusal for the purchase of units. If the last option is chosen, the RC must describe the guidelines it will use to make the decision to purchase or not.

2. The RC must describe the method by which it will establish the purchase and selling price for units which it purchases.

3. The RC must describe guidelines for future marketing of such units to ensure that any units it buys are resold to an eligible family, in accordance with the RHP.

N. Information about any limitations on subsequent purchasers, including income and other requirements. This information should include an underwriting analysis showing that restrictions on eligible subsequent purchasers, as defined in Paragraph 9-35, would not jeopardize the operating feasibility of the project.

O. A certification that the RC will comply with the provisions of:

1. The Fair Housing Act;

2. Title VI of the Civil Rights Act of 1964;

3. Executive Order 11063;

4. Age Discrimination Act of 1975;

5. Section 504 of the Rehabilitation Act of 1973;

6. Section 3 of the Housing and Urban Development Act of 1968, as amended;

7. All regulations promulgated under such statutes and authorities cited in Paragraphs 1 through 6 above; and

P. A Complete Transfer of Physical Assets (TPA) package.

Q. A description of the interaction of the RC and other entity formed by the homeowners and/or the schedule by which the RC will be supplanted by the successor entity.

9-14. Approval of a Resident Homeownership Plan. In order to approve the RHP, Loan Management staff must determine that it meets all of the requirements contained in this Section and on Form HUD-91110, 91110-A, and 91110-B, is financially feasible and is the least costly alternative to HUD that is consistent with establishing a viable Resident Homeownership Program.

9-15. Headquarter's Review of the Required Conditions of a RHP. Within 30 days of their approval of the

RHP, the Loan Management Branch must submit to the Preservation Division a request for grant funds, Section 8, and the preparation of required documents.   LOG date request made   The request should include the information and certifications shown below, along with a copy of the approved RHP, to ensure that the RHP meets all required conditions. Any conditions clearly specified in the RHP need not be repeated.

A.   RC name, project name, number and location and amount of grant required;

B.   The projected number of initial homeowners that are very low-, low-, and moderate-income families to meet the requirements outlined in Paragraph 9-12.D. and E.;

C.   An analysis showing that projected debt service payments, occupancy charges (taxes, insurance, homeownership fees) and utilities

payable by the initial homeowners will not exceed 35 percent of their AMI;

D.   An analysis showing that the aggregate incomes of initial homeowners and other sources of funds are sufficient to allow occupancy charges that cover the full operating costs of the project and any debt service while permitting the RC to comply with all requirements of this Chapter and the RHP;

E.   Certifications showing that homeowners will occupy their projects for a minimum of fifteen years or such longer period as required by the RHP;

F.   Evidence that potential homeowners are aware that at closing of their individual loans, they must execute a nonrecourse promissory note for a term of 20 years in accordance with Paragraph 9-36;

G.   All other elements and conditions required for a Resident Homeownership Program including minimum purchase price of units, period of transfer and financing method for the potential initial and subsequent homeowners;

H. The proposed schedule and methodology for release of grant funds and methods for monitoring the release;

I. The proposed method of monitoring the Use and Grant Agreements for their full term along with all reporting requirements with which the project must comply;

J. Any terms or conditions unique to the project or RHP or Special Conditions which Loan Management staff believer should be met which should be included in the Grant Agreement; and

K. Other relevant required conditions for POAs as prescribed in Chapter 8, Sections C and E.

9-16. Grant and Use Agreements. Within 15 days of receipt of the request, the Preservation Division must examine the information for accuracy and completeness and, if acceptable, forward the documents to the Office of General Counsel (OGC). LOG

A. Within 30 days of receipt of the request to prepare documents, the OGC will prepare and send the Grant and Use Agreements to the Preservation Division, which will forward them to the Chief, Loan Management Branch. LOG date received The agreements will cover:

1. The funding described in Paragraph 9-9.D.;

2. The RHP conditions cited in Paragraph 9-15;

3. Procedures governing the drawdown of funds and remedies for noncompliance with the requirements of the program; and

4. Remedies for noncompliance with the requirements of the program including possible cancellation of the Grant Agreement, withholding of further disbursements, repayment of Grant amounts already disbursed including those held in escrow accounts funded through the Grant.

B. Within 30 days of receipt of the grant agreement, Loan Management staff must meet with the RC LOG date of meeting to review the grant agreement, including repayment penalties for noncompliance, and any other issues relevant to the conversion to and operation of the Resident Homeownership Program.

C. Relinquishing Duties to the Successor Entity. The Homeowners Association, Condominium Association, or Cooperative must be established by receipt of the Grant and transfer of the project. The duties of the RC must be transferred to the successor entity in accordance with the approved RHP.

9-17. Phase-In Period for Sales.

A. Timely Homeownership.

1. Transfer to RC. The RC must acquire ownership of the project no later than 90 days after approval of the RHP unless the RC and the owner agree to extend this

date and the owner waives its right, in writing, to prepay during this extension. LOG date transferred

2. Sale of Units. The RC must transfer ownership of all designated units in the project (other than units occupied by nonpurchasing tenants) to the initial homeowners within a reasonable time thereafter. This will be an on-going process, but in no event may take longer than four years from the date of transfer of the project to the RC. LOG number of units transferred quarterly HUD may seek contractual remedies, in accordance with the grant agreement, against any RC which fails to appropriately transfer ownership of all designated units within the four-year period.

B. Tenant Selection.

1. The RC must submit a written tenant

selection plan in accordance with Chapter 2 of HUD Handbook 4350.3, Occupancy Requirements of Subsidized Multifamily Housing Programs, and the tenant profile requirements in accordance with Paragraph 8-17.F. It also must submit a statement of the rules it will use for tenant selection and occupancy during the sales period when it continues to operate and manage the project partially as rental housing. Tenant selection procedures, rental payments, and other occupancy requirements must conform to those for preservation projects in accordance with Chapter 11. The RC must meet all Affirmative Fair Housing Marketing standards and must inform rejected tenants, in writing, of the reasons for rejection.

2. Loan Management staff must evaluate, or send to other appropriate Divisions to evaluate, these criteria for approval based on the RCs ability to continue to provide housing for very low-income families during this interim period.

3. Before occupancy, the RC must advise all new tenants, by a signed statement, of its policy for new tenants as prescribed in Paragraph 9-8.

Section C. Limited Equity Cooperatives

9-18. Introduction. This Section addresses the requirements for a Resident Council (RC) which acquires a project under a Resident Homeownership Program by assuming the federally-insured mortgage and converts the form of homeownership to a Limited

Equity Cooperative (LEC). A LEC is a cooperative form of housing as described in Paragraph 9-2.C., with a limited equity formula in its by-laws which restricts the profits the members can receive when they resell their interests. Model Forms of Articles of Incorporation, By-Laws, Subscription Agreements, and Occupancy Agreements are in HUD Handbook 4550.1, Basic Cooperative Housing Insurance Handbook, and should be modified as appropriate.

A. A LEC is established as a nonprofit corporation whose specific purpose is to provide low-income housing for its residents, referred to as members, who are stockholders in the corporation.

B. A LEC will be required to follow the procedures and requirements applicable to the purchase and operation of projects with mortgages insured under the applicable HUD program with continued low-income affordability restrictions.

9-19. The Resident Initiatives Specialist (RIS) will provide assistance to LECs in the same manner as it does to other RCs in accordance with Paragraph 9-3.

9-20. Organization and Responsibilities of a LEC. Tenants interested in organizing a RC and forming a LEC form of homeownership are subject to the requirements of the Resident Homeownership Program specified in Paragraphs 9-2 C and D, 9-4, and 9-5, with the following exceptions and suggestions:

A. A LEC must:

1. Develop a Limited Equity Plan of Action (LEP) which will include applicable elements of a Resident Homeownership Plan (RHP) and Plan of Action (POA) in accordance with Chapter 8, Sections C and E;

2. Administer the Cooperative Housing Program through a Board of Directors in accordance with the legal documents specified in Paragraph B.4. below; and

3. Establish the minimum number or percentage of participants for the pre-sale threshold. In accordance with HUD Handbook 4350.1, Paragraph 29-4 D, we recommend this participation be set at a minimum of 90 percent of units, but it may be as low as the 75 percent of current tenants who contributed to the Earnest Money Deposit. The 90 percent threshold helps to ensure that the IRS Code requirement of 80 percent of project income be derived from members' carrying charges be met. Initial participation must be in proportion to the current tenant profile.

B. Formation of a LEC.

1. Members of the LEC will buy a share of the housing corporation, usually called a membership certificate, which entitles the purchaser to occupy the unit through an occupancy agreement;

2. The Members will elect a Board of Directors which has the major responsibility to administer the LEC.

3. Membership Agreements. These are legally binding documents that establish the rights and obligations of the members of the LEC and of the Board of Directors:

a. A subscription agreement is the document that allows prospective members to demonstrate their intent to join the LEC and requires a membership fee.

b. An occupancy agreement that lasts as long as the member owns its stock in the LEC, describes the terms and conditions and gives the purchaser the exclusive right to occupy a unit in the project and participate as a member in the operation of the LEC.

c. State and local requirements may supplant or supplement the agreements shown in Paragraphs a.

and b. above. In these cases, State and local requirements should be followed, unless they have been preempted by HUD requirements.

4. Other Principal Legal Documents include:

a. The Articles of Incorporation which sets forth the authority for the LEC to operate the corporation;

b. The By-Laws which establishes the method of operation of the LEC;

c. The HUD Use Agreement which restrict the operation of the LEC to certain FHA requirements; and

d. The Limited Equity Cooperative Plan of Action.

C. Other questions and issues suggested by HUD Handbook 4350.1, Chapter 29 should be reviewed.

9-21. Offer to Purchase. A LEC is subject to the process outlined in Paragraph 9-6 which includes information about the time frames in which an owner may accept a bona fide offer from a RC, the requirements for submission of an expression of interest (EOI) and the components of a bona fide offer.

9-22. Receipt and Acceptance of an Offer. Loan Management staff should follow the guidance in Paragraph 7-8 in making a determination about the owner's receipt and acceptance of an offer from a LEC and about how to determine the level of incentives. The term Preservation Project Income will be substituted for the term Preservation Project Rent referred to in Paragraph 7-8.

A. Acceptance of Offer. In the case of a LEC, the owner may issue an acceptance of a bona fide offer contingent upon the satisfactory completion of a LEP.

B. Guidance provided in Paragraphs 7-9, 7-10, 7-12, 7-13, and 7-15 for RCs also apply to

LECs implementing a cooperative housing program.

9-23. Notification to New Tenants. New tenants must be notified by the LEC of its intention to purchase the project in the same manner required of other RCs in Paragraph 9-8.

9-24. Submission and Review of a Limited Equity Cooperative Plan of Action (LEP). In the case of a voluntary sale, the LEC will submit a LEP within six months of acceptance of an offer by the owner. In the case of a mandatory sale, the LEC must submit a LEP within six months of the owner's receipt of the offer. The LEC must submit six copies of the LEP to the Loan Management Branch in the same manner described in Paragraphs 8-3 and 8-4. Log date received whether complete or not A checklist of items required for a complete LEP is in Appendix 9-3, Checklist for a Complete Limited Equity Cooperative Plan of Action. Because a LEP is a combination of an RHP and POA, Loan Management staff should follow guidance in this Chapter and Chapter 8, Sections C and, E when reviewing a LEP submission. Loan Management staff will use Form HUD-50007, Appendix 9-4, Evaluation of a Limited Equity Plan of Action, to review a LEP.

9-25. Requests for Incentives. The LEC must submit requests for incentives as part of the LEP. Requirements for the requests are the same as those for priority purchasers submitting a POA in accordance with Chapter 8, Sections C and E except:

A. A LEC may not budget an annual authorized return which is provided to other purchasers in Paragraph 8-21.A.1.b. except to pay debt service on a non-Federal loan to acquire the project;

B. LECs may receive a grant for specific Resident Homeownership purposes pursuant to Paragraph 8-21.D. and as outlined in Paragraphs 9-9.C. and D.2. through 4.;

C. An organization receiving Low-income Housing Tax Credits (LIHTC) is not eligible to be a LEC because it is not eligible to become a priority purchaser;

D. The LEC may request project oversight charges but the charges must be based solely on the project's Gross Income Potential. The oversight charges may not be based on income that is unique to the operation of a LEC which is placed in the Cooperative Reserve Account as defined in Paragraph 9-26.I. below.

E. The following changes in terminology will apply:

1. "Member" will be used in lieu of "tenant."

2. "Carrying charges" will be used in lieu of "rent."

3. "Aggregate Basic Carrying Charge" and "Aggregate Market Carrying Charge" will be used in lieu of "Aggregate Basic Rent" and "Aggregate Market Rent.

4. "Minimum carrying charge" will be used in lieu of "minimum rent."

5. Total Member Payment (TMP) will be used in lieu of Total tenant payments (TTPs) for those who purchase memberships. TMPs are the monthly carrying charges paid by members to meet the financial and operating costs of the LEC plus the utility allowance, if any. They will be phased in the same way as TTPs.

6. "Section 8 Contract Payments" will be used in lieu of "Section 8 Contract Rents." They will be established in proportion to the established FMR for the unit.

7. "Preservation Project Income" (PPI) will be used in lieu of "Preservation Project Rent" (PPR). The PPI is the amount of income the LEC needs to fund all approved assistance. The PPI may not exceed the Federal Cost Limit (FCL). The PPI will not include income unique to a LEC such as membership fees. Further, it may not be used to pay expenses unique to a LEC such as the repurchase of memberships.

8. "Gross Income Potential" (GIP) will be used in lieu of "Gross Rent Potential" (GRP). It will include member carrying charges and all other project income including the rental payments from non-members. The GIP may not include income nor be used to pay expenses unique to a LEC, such as repurchasing of memberships.

9. Increases in PPI will be calculated via an Operating Cost Adjustment Factor (OCAF) in the same manner as described in Paragraph 11-7.

9-26. Components of a Resident Homeownership Program which are relevant to LECs pursuant to Paragraphs 9-12 and 9-13, must be submitted as part of the LEP. The following list identifies exceptions and requirements for LECs.

A. The following terms will be used for LECs in lieu of those used for other Resident Homeownership Programs:

1. The term "member" will be used in lieu of "homeowner."

2. The term "occupancy agreement" will be used in lieu of "lease."

3. The term "membership fee" will be used in lieu of "downpayment."

B. Section 8 subsidies are available for LECs. Therefore, TMP will be set in accordance with Paragraph 8-18.A.6. Phase-in of TMP will be done in accordance with Paragraphs 8-18.A.7. and A.8.

C. The units in a LEC project are not sold. Instead, "memberships" are sold for an amount which represents the purchase price. The amount of the membership fee is established in accordance with Paragraph 9-27 for initial members and Paragraph 9-30 for subsequent members.

D. Memberships.

1. There is no requirement that all memberships be sold within any specific timeframe. However, the LEP should specify a period of time in which all initial sales are anticipated to be complete.

2. The requirements for proportionality of initial members, established in Paragraph 9-12.E., are applicable to members of LECs.

3. Current tenants who are prospective members but can not pay the membership fee in cash, may pay it in a variety of ways, such as through loans and/or by assigning a portion of their security deposits, subject to State and local law. If the RC makes the loan for the downpayment, a non-amortizing promissory note specifying the requirements contained in Paragraph 9-27 should be signed by the prospective member.

4. All prospective members must sign a Subscription Agreement or similar document in accordance with State and local law.

5. The tenant income profile requirements established in Paragraph 8-18.A.3. is applicable for all initial and subsequent members.

E. The LEC holds title to the property and executes the mortgage. The individual member does not sign a note nor mortgage and does not have a personal obligation thereunder. Therefore, individual financing is not necessary for members of a LEC.

F. (Reserved)

G. The transfer value of memberships is established in Paragraph 9-29 and the equity limitation requirements specified therein apply to members of LECs.

H. A LEC must specify in its By-Laws whether it will purchase memberships and resell them. A suggested method for handling this is described in Paragraph 9-28.

I. It is advisable that the LEC establish a Cooperative Reserve account to which it will deposit all membership fees and credit any interest or equity accrued. This account should be used to accrue enough funds to allow the LEC to purchase and resell memberships.

J. The LEC occupancy agreement must restrict the ability of members to rent, lease, or sublet their units without written permission of the Board of Directors.

K. A four-year cash flow analysis must be submitted instead of a three-year analysis as required for rental projects. If a Cooperative Account has been established in accordance with Paragraph I, the LEC must include a four year projection of income and expenses for the account.

L. All considerations of Paragraph 9-13.C. for nonpurchasing tenants apply, including provision for payment of relocation expenses.

M. All requirements of Paragraph 9-12.E. for tenant selection and tenant profiles are applicable.

N. All State and local laws regarding LECs are applicable, except those which have been preempted by HUD.

O. Copies of all forms, guidelines, worksheets, and contracts developed to implement the LEC Program and all other documents required to justify elements of the LEP.

9-27. Membership Fees from Initial Members will be required in order to obtain a commitment from tenants to participate in the LEC.

A. The amount of the membership fees will be set in accordance with the approved budget for the Cooperative Reserve Account and the need to identify sufficient numbers of residents who will become members of the LEC. The following guidelines apply:

1. The minimum membership fees will be allocated to unit size and type in proportion to the FMR for the unit.

2. The LEP must specify how membership fees will be established. They should be high enough to show tenant commitment to purchase the membership and low enough to allow all interested members to purchase memberships. For instance, the membership fees for individual units may be set so that each member pays a minimum of the higher of 25 percent of FMR or 60 percent of Adjusted Monthly Income (AMI). However, no LEC should set the membership fee for any unit lower than the amount of the earnest money deposit required by Paragraph 7-7.C.2. The RC, at its option, may also set membership fee and closing cost guidelines for subsequent purchasers.

B. Method of Payment. Where the membership fee is paid through a loan from the LEC, the LEC must establish guidelines to determine how a prospective member will pay its membership fee. This method must be clearly specified in the Subscription Agreement. The following method is recommended:

1. The prospective member's existing security deposit minus any charges against it should be assigned to the membership fee if permitted by State and local law.

2. It is generally desirable that no more than half the membership fee be financed by the LEC. The prospective member may pay the financed portion of the membership fee in installments.

3. The prospective member remains a tenant throughout the period when the membership fee is being paid. It becomes a member at whatever time the total membership fee has been paid.

9-28. Resale of Memberships. The LEP must specify whether the LEC will purchase all memberships sold by members and resell them to new members. If this option is chosen, it is recommended that the LEC purchase all memberships for its Transfer Value, as determined in Paragraph 9-29. The LEC would then either resell the units using Transfer Value as the required membership fee or another method, approved with the LEP, to determine the membership fee. If the LEC resells the membership for less than its Transfer Value (or the purchase price), then the residual equity must accrue to the LEC. The appreciation will be credited to the Cooperative Reserve Account. Membership fees for subsequent members would be financed in accordance with Paragraph 9-30.

9-29. Transfer Value is the amount of equity a member has accrued as its share of the cooperative. Memberships may be sold at no more than the transfer value which will be calculated as the sum of:

A. The membership fee paid by the initial member;

B. The value of any improvements installed at the family's expense during its tenure as owner. The LEC will make this determination using documentation of the amounts the family spent on the improvements, including records that reflect the cost of materials and labor, and estimates of the value the improvement added to the unit;

C. The amount of amortized principal paid by the selling member in the following manner:

1. The unit's proportionate share of the project mortgage payment will be determined by the same ratio method as the Section 8 Contract Payment is determined. An amortization schedule based on the proportionate share will be established;

2. First, each member's TMP will be used to pay for member-paid utilities to the extent of the utility allowance. Then, the remainder of the payment will be

credited to the amortized interest and principal, in that order, regardless of whether or not the member receives Section 8 subsidy.

3. Examples: The amortization schedule for a specific month shows the amortized principal payment as $50 and interest as $150. The utility allowance for the unit is $45 for a total of $245. Under the Section 8 formula:

   a. Member A has a TMP of $250. $45 is applied to the utility allowance and $150 is applied to interest. $50 is credited toward the principal payment. The remaining $5 is credited toward the carrying charge.

   b. Member B has a TMP of $200. $195 is applied to the utility allowance and interest payment and $5 is credited toward the principal payment.

   c. Other members have TMPs of $195 or below. The first $45 for each member is to the utility allowance. The remaining is paid as interest. Nothing is credited to the principal payment; and

D. If approved as part of the LEP, an amount corresponding to the appreciated value, determined by applying the Consumer Price Index (urban consumers) to the contribution to equity under Paragraphs A, B and C. Be certain the Consumer Price Index, for any year, is only applied to the portion of equity already established in that year.

9-30. Subsequent Members Payment of Membership Fees. The LEC should indicate in the LEP how membership fees will be assessed for subsequent members. The Subscription Agreement must clearly specify the method for determining the amount and payment schedule of the membership fee. Following is one possible method the LEC may use to assess membership fees:

A. Require a subsequent member to pay cash or finance up to three months of TMP (90 percent of AMI) prior to becoming a member.

B. Require the member to initially pay a minimum of five percent of its AMI toward the membership fee, or more if the member chooses.

C. The remainder of the membership fee, if any, would be made in monthly payments of a maximum of five percent of AMI.

D. As the membership fee is paid, it will be used as the beginning equity for the subsequent member with additional amortized principal added, as in Paragraph 9-29.C., to determine such member's Transfer Value upon sale of its membership.

9-31. Final Actions and Implementation of a LEP. LECs are subject to all of the provisions of Chapter 8, Sections F and G for the determination of final actions and the implementation of a LEP.

9-32. Other Requirements. The Loan Management staff must review the LEC's compliance with any sales phase-in schedule established in the LEP. The Relocation staff in the Office of Community Planning and Development (CPD) is responsible for monitoring compliance with certain tenant assistance, relocation, and real property acquisition requirements. The Loan Management staff will consult with the Relocation staff with respect to technical assistance needs and monitoring to ensure that there is no duplication of effort.

9-33. Monitoring. A LEC is subject to the housing standards, audit, and reporting requirements of the HUD program under which it is insured. Loan Management staff must follow the guidance in applicable sections of Chapter 11 when monitoring a project owned by a LEC in addition to the applicable portions of Section F of this Chapter.

Section D. Nonpurchasing Tenants

9-34. Protection of Nonpurchasing Families. Nonpurchasing families who continue to reside in a project subject to a Resident Homeownership Program must be protected as follows:

A. Notification to Tenants by Loan Management Staff. Upon approval of a bona fide offer from a Resident Council (RC), the Loan Management staff must send each tenant in the project a letter in the form of Appendix 9-5, Notification to Non-Purchasing Tenants of Available Protections. The Loan Management staff also must send this letter to the RC and owner instructing the owner to post a copy in the project. The letter advises the tenants that the owner is transferring the project to the RC or LEC which will develop a Resident Homeownership Program. It further advises tenants of the percentage of the units which must be transferred to current tenants in accordance with the RHP, in at least the same proportions of very low- and low-income as are currently residing at the project.

B. Displacement prohibited. Tenants residing in a project may not be displaced (forced to move permanently) as a result of a Resident Homeownership Program. The tenants who do not purchase their units may reside at the project for as long as they choose. This does not, however, preclude termination of tenancy for serious or repeated violation of the terms and conditions of the lease, violation of applicable Federal, State or local law, or other good cause. Displacement of any tenant in violation of this policy will trigger the Uniform Relocation Assistance and Real Property Acquisitions Act of 1970, as amended, because Federal financial assistance is used in the project.

C. Section 8 Rental Assistance.

1. HUD will make Section 8 certificates or vouchers available to each Section 8 eligible tenant who does not purchase a unit. Eligible tenants may use the Section 8 rental assistance to rent its current unit or a unit elsewhere.

2. HUD will provide Section 8 LMSA to the LEC for each very low- and low-income tenant living at the project at LEP approval who does not purchase a membership.

3. Federal Preference. The requirement for giving Federal preference to certain categories of eligible families does not apply in the provision of Section 8 rental assistance to protected tenants living in a project operating under a Resident Homeownership Program.

D. Rent Increases for Nonpurchasing Tenants. Total tenant payment (TTP) for tenants living in the project at RHP approval, who do not purchase a unit and are ineligible for Section 8 rental assistance under Paragraph 9-34.C. may be increased to a level consistent with Paragraph 8-18.A.6. Rent increases must be phased-in in accordance with Paragraph 8-18.A.7. and form HUD-90010, Owner's Calculation of Tenant Rent Phase-In Due to Approval of POA. These rent limitations would continue in effect until the tenant moves. Therefore, nonpurchasing tenants will receive the same level of protection against rent increases as those provided to tenants residing in a project at POA approval that is not transferred under a Resident Homeownership Program.

E. Relocation Assistance. The LEP or RHP must specify the amount of relocation assistance it will grant to non-purchasing tenants who move. At the RC's option, this assistance may be up to 100 percent of relocation costs. The RC or LEC must inform each tenant who resided in the project at RHP or LEP submission, how much it, as owner of the project, will pay for relocation expenses for any tenant who chooses to move. This protection does not apply to new tenants who were told of the Resident Homeownership or Limited Equity Program. The RCs and LECs must inform new tenants at the time they apply for occupancy in the project, that they will not be eligible for relocation assistance. The RC or LEC may limit payment of moving expenses to the cost of moving a reasonable distance, based on the availability of other suitable housing in the area. Disabilities and other special needs must be considered when determining if suitable housing is available. The RC or LEC may determine payment in either of the following ways, and must specify the method in the RHP or LEP.

1. Payment of Actual Reasonable and Related Expenses. A tenant who elects to relocate may receive payment based on actual moving and related costs for up to four years after the RC or LEC purchases the project. The RC or LEC has the authority to determine which relocation costs are reasonable and necessary, including expenses for:

    a. Transportation of the person and personal property for a reasonable distance;

    b. Packing, crating, uncrating and unpacking of the personal property;

    c. Disconnecting, dismantling, removing, reassembling, and reinstalling relocated household appliances, and other personal property;

    d. Utility hook-ups, including reinstallation of telephone and cable television service;

    e. Insurance for the replacement value of the property in connection with the move and necessary storage;

    f. Credit checks; and

    g. Other moving-related expenses, as the RC or LEC determines to be reasonable and necessary.

2. Moving Expense and Dislocation Allowance. The RC may offer tenants who elect to relocate a moving expense and dislocation allowance as an alternative to a payment for actual reasonable moving and related expenses described in Paragraph 1 above. The amount of the allowance will be determined in accordance with a schedule of allowances, established by the RC, which takes into account the number of rooms in the person's present dwelling unit and whether the person owns and must move the furniture.

Section E. Resale of Units

9-35. Restrictions on Resale by Homeowners. A member of a LEC is bound by the rules restricting the transfer of membership under the LEC program in Section C. Homeowners under other types of homeownership programs may sell their interests in a unit. The RC may limit the homeowner's right by placing certain restrictions on such a resale. If the RC imposes resale restrictions, the restrictions must be specified in the RHP.

A. Permitted Transfers. A homeowner may transfer its ownership interest in the unit subject to the right of the RC to purchase the unit in accordance with the RHP. If the RC exercises this option:

1. It must determine the purchase price and conditions for purchase by the subsequent purchaser in accordance with the method established in the RHP and specified in a firm contract at initial sale between the RC and the homeowner. The price at which the RC purchases the unit may never be less than the amount specified in a firm contract between the homeowner and a prospective buyer;

2. It must resell the unit to an eligible family within the timeframe established in the RHP or LEP in accordance with Paragraph 9-13.M.

B. Execution and Repayment of a Promissory Note.

1. An initial homeowner is required to execute a promissory note and mortgage in accordance with Paragraph 9-36.

2. A subsequent homeowner may be required to execute a promissory note and mortgage, as specified in Paragraph 9-37, if it purchases the unit during the initial 20-year period of homeownership.

3. The repayment of the promissory note must be made in accordance with either Paragraph 9-36 or 9-37.

C. Resale restrictions established by the RC should not jeopardize the operating feasibility of the project nor unreasonably restrict the sellers by limiting the pool of purchasers or the resale prices.

9-36. Initial Homeowner's Promissory Note. At closing, the RC will require the initial homeowner to execute a nonrecourse promissory note for a term of 20 years with no interest. This promissory note, made payable to HUD, must equal the difference between the value of the unit as established in Paragraph 9-12.A. and the purchase price established for the purchaser in accordance with Paragraph 9-12.C. The promissory note will accompany the mortgage securing the obligation of the note. When the initial homeowner sells the unit, whether to the RC or a subsequent homeowner, it will repay the promissory note to the extent determined in Paragraphs B.1. and B.2. below. The initial homeowner will use the net sales proceeds, calculated in the manner described in Paragraphs A.1. and A.2. below, to repay the promissory note. If there are insufficient net sales proceeds to repay the amount due on the promissory note, the subsequent purchaser may be required to execute a promissory note in accordance with Paragraph 9-37.

Any residual proceeds remaining after the amount due on the promissory note is repaid, will be handled in accordance with Paragraph C. below. (PLEASE NOTE: For FHA single-family insurance purposes, the Department has determined that LIHPRHA's calculation of homeowner's equity is acceptable.)

A. Net Sales Proceeds. The net sales proceeds is the amount of money available to the homeowner to repay the promissory note. It is determined by subtracting from the owner's gross sales proceeds (or the selling price), the owner's retained proceeds calculated in accordance with Paragraph 1. below.

1. Initial Homeowner Sells Unit Within First Six Years. When an initial homeowner sells its unit during the first six years after acquisition, it must pay the amounts computed in accordance with Paragraphs a. and b. below and may keep

the owner's retained proceeds which the RC computes in accordance with Paragraph c. below. The homeowner must repay the entire amount of its net sales proceeds in accordance with Paragraphs B and C below. To calculate the net sales proceeds, the RC must subtract from gross sales proceeds:

a. Any outstanding debt which was incurred in connection with the purchase of the property and which must be repaid at closing as shown on Line 101 of Form HUD-1, Settlement Statement;

b. Any other costs incurred in connection with the sale, including closing costs and transfer taxes, which must be repaid at closing as shown on Line 103 of Form HUD-1, Settlement Statement; and

c. The homeowner's share of the equity, or retained proceeds, computed as the sum of the following:

i. The contribution to equity paid by the family, if any, including any down payment and any amount paid towards principal on a mortgage loan during the period of ownership. This will be calculated as the original purchase price minus the outstanding debt;

ii. The cost of any improvements installed at the family's expense during its tenure as owner. The RC will make this determination using documentation of the amounts the family spent on the improvements, including records that reflect the cost of materials and labor. If the homeowner does not have a mortgage insured by HUD under

Section 203 or 234 of the National Housing Act, the RHP may specify that the value of any improvements will be substituted for cost;

iii. The lower of the results obtained in Paragraph (a) or (b) below:

(a) The appreciated value, determined by applying the Consumer Price Index (urban consumers) against the contribution to equity determined in Paragraphs i and ii, excluding the value of any sweat equity or volunteer labor used to make improvements to the unit. (Be certain the CPI is only applied to the portion of equity established in any one year. That is, if additional equity is paid in the form of principal payments in any one year, the CPI would be applied to increasing amounts for each year).

(b) Any limits on equity appreciation the RC established in the RHP. In order to use the RHP to limit equity at the time of initial sale, the RC must have entered into a written agreement with the family to limit the amount of appreciation at the time of purchase.

2. Initial Homeowner Sells Unit Between the Seventh and Twentieth Year. When the initial homeowner sells its unit seven to 20 years after acquisition, there are no retained proceeds calculated. The homeowner must pay the amounts which the

RC computes in accordance with Paragraphs 1.a. and 1.b. above. The amounts determined in accordance with Paragraph 1.c. are not applicable. The homeowner must repay the amount of the net sales proceeds but no more than the amount required by the promissory note in accordance with Paragraph B. below.

3. Initial Homeowner Sells Unit After the Twentieth Year. When the initial homeowner sells its unit after the twentieth year of acquisition, it must pay all costs in accordance with Paragraphs 1 a. and 1 b. above, and may retain all net sales proceeds.

B. Payment Due Under the Promissory Note. The homeowner must repay the amount of the net sales proceeds in the amounts shown below. To the extent the amount due on the promissory note exceeds the net sales proceeds, the subsequent homeowner may be required to sign a

Promissory Note in accordance with Paragraph 9-37.

1. Initial Homeowner Sells Unit Within First Six Years. When an initial homeowner sells its unit during the first six years after acquisition, the entire amount of the Promissory Note is due and payable to HUD.

2. Initial Homeowner Sells Unit Between Seventh and Twentieth Year. When an initial homeowner sells its unit seven to 20 years after acquisition, the amount payable under the promissory note will be reduced by 1/168th of the principal amount for each month before the subsequent homeowner sells the unit. That is, for each of the 168 months remaining in the 14-year period, the promissory note will be reduced proportionate to the length of time before the homeowner sells the unit.

3. Initial Homeowner Sells Unit After Twentieth Year. When the initial homeowner sells its unit after the twentieth year of ownership, the

promissory note will have been satisfied, and no payment is required.

C. Residual Proceeds. If residual proceeds remain after the amount due under the promissory note is repaid, it will be distributed as follows:

1. Initial Homeowner Sells Unit Within the First Six Years. All residual proceeds must be paid to the HOME Investment Trust Fund in accordance with Paragraph 9-38.A. The homeowner may not retain any residual proceeds.

2. Initial Homeowner Sells Unit Between the Seventh and Twentieth Year. The initial homeowner retains all residual proceeds.

D. Examples:

1. Initial Homeowner Sells Unit Within First Six Years: Assume the initial homeowner purchases a unit valued at $50,000. The purchase price to the homeowner is $25,000. The homeowner, therefore, signs a $25,000 promissory note. The homeowner sells the unit in the fifth year of homeownership for $40,000. First, the owner's costs and retained proceeds would be determined as in Paragraph A.l.a. through c. and would be subtracted from the gross sales proceeds to yield net sales proceeds.

   a. For this example, we will assume that the amount needed to repay debt and any closing costs is $9,000 and retained proceeds is $1,000 for a total of $10,000. Therefore $30,000 ($40,000 - $10,000) is available to repay the promissory note.

   b. The homeowner must use the $30,000 in net sales proceeds to repay the entire amount of the $25,000 promissory note to HUD and the remaining $5,000 to pay the HOME Investment Trust Fund. The subsequent purchaser of the unit

would not have to sign a promissory note since the entire promissory note was repaid.

   c. If the net sales proceeds was under $25,000, the initial homeowner would only repay the amount of the net sales proceeds and the subsequent homeowner may be required to sign a promissory note as described in Paragraph 9-37.

2. Initial Homeowner Sells Unit Between Seventh and Twentieth Year: In the example in Paragraph 1. above, assume the homeowner sells the unit at the end of the 14th year of homeownership. This is exactly 8 years or 96 months after the end of the sixth year.

a. The RC would first determine the homeowner's net sales proceeds as in Paragraph B.2. above. Using the same amounts as in the above example, this amount is $31,000 ($1,000 greater than in the example in Paragraph 1. above, since there are no retained proceeds).

b. 96/168 = 57 percent. This percentage is applied to the amount of the promissory note to determine the amount by which it is to be reduced. $25,000 x .57 = $15,750. $25,000 - $15,750 = $9250.

c. The homeowner would repay $9,250 from the net sales proceeds. The homeowner could retain all remaining $21,750 in proceeds and the subsequent homeowner would not have to sign a Promissory Note.

d. If the net sales proceeds was under $9,250, the initial homeowner would only repay that amount and the subsequent homeowner may be required to sign a promissory note as described in Paragraph 9-37.

E. If the initial homeowner retains ownership for 20 or more years, the entire amount of the note will be satisfied.

9-37. Subsequent Homeowner's Promissory Note.

A. If a subsequent purchase is made during the 20-year period specified in the initial promissory note, whether from the initial purchaser or from the RC, a copy of the appraisal of the unit must be submitted by the purchaser to the RC, unless the RC contracts for the appraisal. At closing, the subsequent purchaser must execute a promissory note under the conditions specified in Paragraph 1. below and for the amounts specified in Paragraph 2. below. The term of the subsequent promissory note must be for the period remaining on the original 20-year promissory note. The term on the subsequent note ends on the date specified in the original note.

1. The subsequent purchaser must execute a promissory note under the following conditions:

   a. The appraised value of the unit exceeds the purchase price; and

   b. The initial homeowner did not repay the total or discounted amount due on the promissory note.

2. The promissory note signed by the subsequent purchaser will be for the lower of:

   a. The outstanding balance, if any, on the original or discounted promissory note; or

   b. The difference between the appraised value of the unit and the purchase price at the time the subsequent homeowner purchases the unit.

B. When a subsequent homeowner sells its unit in less than 20 years from the date of the initial purchase, the RC will calculate the owner's net sales proceeds in the same manner

as for the initial homeowner, in accordance with:

1. Paragraph 9-36.A.1., if the subsequent homeowner sells the unit within the first six years after the initial homeowner purchased the unit; or

2. Paragraph 9-36.A.2., if the subsequent homeowner sells the unit between the seventh and twentieth year after the initial homeowner purchased the unit. Please note that the date on which the subsequent homeowner purchased the unit is not relevant to this calculation.

C. When a subsequent homeowner sells its unit in less than twenty years from the date of the initial purchase, the amount due on the promissory note will be calculated as follows:

1. If the subsequent homeowner purchased the unit within six years after the initial homeowner purchased it, the amount due on the promissory note and the distribution of residual proceeds will be calculated in the same manner as for the initial homeowner, in accordance with:

a. Paragraph 9-36.B.1. and C.1., if the subsequent homeowner sold the unit within six years after the initial homeowner purchased the unit; or

b. Paragraph 9-36.B.2. and C.2., if the subsequent homeowner sold the unit between seven and twenty years after the initial homeowner purchased it.

2. If the subsequent homeowner purchased the unit between the seventh and twentieth year after the initial homeowner purchased it, the amount due will be calculated in accordance with Paragraph 9-36.B., except that the RC will reduce the

amount payable on the subsequent promissory note by a percentage of the principal amount of the subsequent promissory note for each full month of homeownership by the subsequent homeowner. The RC will compute the percentage to be discounted by determining the proportion of the term of the subsequent promissory note that the subsequent homeowner has owned the property. The subsequent homeowner may retain any residual proceeds not payable to HUD under the promissory note.

D. A similar process will be used for all subsequent purchases until:

1. The initial 20-year period has expired;

2. The total amount due on the promissory note has been paid; or

3. A subsequent homeowner purchases the unit for its full appraised value.

E. Examples:

1. Subsequent Homeowner Does Not Sign a Promissory Note. If the conditions described in Paragraph a. or b. below are applicable, the subsequent homeowner and all additional subsequent homeowners of the unit, need not sign a Promissory Note.

a. In the examples given in Paragraphs 9-36.D.1.a. and b. and 9-36.D.2.a., b., and c., the subsequent homeowner would not sign a promissory note because either the total promissory note or the amount due on the discounted promissory note was repaid.

b. In the examples given in Paragraphs 9-36.D.1.c. and 9-36.D.2.d., if the unit is appraised for $40,000 at the time of sale, even though the

initial homeowner did not repay the total amount due on the promissory note, the subsequent homeowner need not sign a promissory note. This is because the subsequent homeowner purchased the unit for its full appraised value.

2. Subsequent homeowner purchases unit in first six years after the original promissory note was signed and signs a promissory note. Assume that the unit

sold at the end of the fifth year after purchase in accordance with Paragraph 9-36.D.1., has a purchase price of $27,000, and the owner's costs at closing plus the retained proceeds are $15,000. Therefore only $12,000 ($27,000 - $15,000) in net sales proceeds will be used to repay the $25,000 promissory note and $13,000 remains due on the Promissory Note. We also will assume that the appraised value of the unit has decreased from $40,000 to $38,000. The appraised value is therefore $11,000 greater than the purchase price.

a. The subsequent homeowner must therefore sign a promissory note for $11,000 (the difference between the unit value and the purchase price) because this is lower than the $13,000 remaining on the initial homeowner's promissory note. The term of the promissory note is the 15 years remaining on the original promissory note.

b. If the purchaser sells the unit within one year (within six years from the date of the initial purchase), the full amount of the promissory note must be repaid if sufficient funds remain in the net sales proceeds. If any additional residual proceeds remain, it must be paid to the HOME Investment Trust Fund.

c. If the unit is sold at any time between the seventh and twentieth year after the initial promissory note was signed, the amount due under the subsequent promissory note is reduced in accordance with Paragraph C.1.b. above. Any residual proceeds may be retained by the homeowner.

d. No amount is due if any conditions specified in Paragraph D. above are operative.

3. Subsequent Homeowner Purchases Unit Between the Seventh and Twentieth Year after Initial Promissory Note was Signed and Signs a Promissory Note.

   a. Assume the initial homeowner who sold the unit in Paragraph 2. above for $27,000 (it appraised at $38,000) sold the unit to the subsequent purchaser eight years after the initial purchase.

      i. The homeowner's original $25,000 promissory note is reduced by 24/168 (14 percent) or 1/168 for each month past 6 years. $25,000 x 14 percent = $3500. $25,000-$3500 = $21,500. $21,500 is due on the Promissory Note. However, the net sales proceeds only total $12,000. Therefore, the initial homeowner pays $12,000 of the $21,500 remaining due.

      ii. The subsequent homeowner signs a promissory note for $9500 ($21,500 - $12,000) because it is lower than the $11,000 difference between the purchase price and the appraised value. The promissory note is for the 12 years or 144 months remaining on the original 20-year promissory note.

   b. The subsequent homeowner sells the unit to a second subsequent homeowner at the end of the 18th year. The value of the unit is $60,000 and the purchase price is $40,000 with $18,000 calculated as costs to be paid at closing, leaving $22,000 in net sales proceeds, in accordance with Paragraph 9-36.A.2.

   c. Since the subsequent homeowner owned

the unit for 10 years or 120 months, the $9,500 promissory note would be reduced by 120/144 = 83 percent of its original amount. The amount due is therefore reduced by $9500 x .83 = $7885 and $9500 - $7885 = $1615 remains due. The homeowner repays $1615 from the $22,000 net sales proceeds and keeps the $20,385 remaining.

d. In this case, the second subsequent homeowner need not sign a promissory note even though it purchased the unit for less than its appraised value. This is because the discounted promissory note has been completely repaid.

F. Resident Council Purchases and Sells the Unit. When a homeowner sells the unit to the RC and the RC sells the unit to a subsequent homeowner, the purchase price to the RC and to the subsequent homeowner may differ. In these cases:

1. The net sales proceeds, amount paid on the promissory note by the selling homeowner, and residual proceeds will be calculated based on the purchase price to the RC.

2. The amount of the promissory note for the purchasing homeowner will be the lower of the amount remaining due on the promissory note of the selling homeowner or the difference between the Purchase price to the purchasing homeowner and the appraised value of the unit.

3. No promissory note will be signed if one of the conditions specified in Paragraph D. above are met.

9-38. Payment of Residual Proceeds.

A. Any residual proceeds remaining after the homeowner pays the promissory note to HUD (within six-years of initial purchase) must be paid to the HOME Investment Trust Fund for the unit of general local government in which the project is located. If the project is located in a unit of general local government that is not a participating jurisdiction, then the residual proceeds must be paid to the HOME Investment Trust Fund for the State in which the project is located.

B. With respect to any proceeds transferred to a HOME Investment Trust Fund under this Paragraph, HUD must ensure that the proceeds are immediately available for eligible activities to expand the supply of affordable housing under the HOME Program. These activities may include funding of activities under the Resident Homeownership Program. Loan Management staff will monitor the payments made to the HOME Investment Trust Fund for each State and unit of local government and will require units of government to maintain any records necessary to calculate accurate payments due under this Paragraph.

Section F. Monitoring

9-39. Housing Standards: Inspections.

A. Until the Resident Council (RC) has transferred all units or shares in the project (other than those occupied by nonpurchasing current tenants) to the initial purchasers or members, the Loan Management staff must monitor the project to ensure that it is being maintained in accordance with the housing standards set forth in Paragraph 11-9.

B. Loan Management staff must inspect the project at least annually in order to determine compliance with the Housing Standards.

9-40. Section 8 Rental Assistance. Loan Management staff has the responsibility to continue monitoring existing Section 8 Housing Assistance Payment contracts.

9-41. Promissory Note. The RC must keep, and make available to HUD, all records and source documents necessary to calculate that the payments due HUD are accurate.

9-42. Audits.

A. Each RC will be subject to HUD audit requirements in accordance with Part 45 and must submit an annual audit to HUD in the form prescribed by the Department in HUD Handbook 2000.4, Investigator General Audit Handbook. The RC must keep records that are necessary to fully disclose the amount and disposition of the proceeds from assistance it receives from HUD. This record keeping requirement includes information about:

1. Any proceeds from sales to eligible families and/or from recaptured funds;

2. The total cost of the Resident Homeownership Program for which such assistance is given or used;

3. The amount and nature of that portion of funds for the Resident Homeownership Program supplied by other sources;

4. Compliance with all financial requirements of the grant agreement and the approved Resident Homeownership Plan (RHP) to confirm that the requirements have been met;

5. Any other aspects of the financial assistance received that would facilitate an effective audit; and

6. The income and expense amounts for the rental and the Resident Homeownership components of the project in each year. Such rental and homeownership accounts must be maintained in separate and distinct accounts.

B. For the purpose of an audit and examination of records:

1. HUD or its authorized representative will have access to any books, documents, papers, and records of the RC that are pertinent to the assistance it receives under the Resident Homeownership Program; and

2. The Comptroller General of the United States, or any of its authorized representatives, will also have access to any books, documents, papers, and records of the Resident Council that are pertinent to the assistance it receives under this program.

9-43. Reports. The RC must submit reports to HUD to demonstrate continued compliance with the requirements of the Resident Homeownership Program. The RC may use forms from the existing HUD programs for these reporting requirements. However, if such HUD forms do not exist because the RC has unique requirements, then the RC will describe the method of reporting it intends to use and will develop and provide samples of such forms. Loan Management staff will review reports submitted to determine

compliance with the approved RHP or LEP. The areas of the Resident Homeownership Program that require reports are:

A. Annual compliance with proportionality during the initial sales which end in four years;

B. Annual status of Section 8 eligible tenants;

C. Annual report on training and technical assistance provided to homeowners;

D. Annual reports on the extent of participation of minorities and women in the program (e.g. homeownership, employment opportunities, etc.);

E. Annual review of the operating budget, separated into homeownership and rental components, where applicable;

F. Semi-annual report on vacancies;

G. Semi-annual report survey of non-purchasing tenants;

H. Semi-annual status of rehabilitation activities;

I. Quarterly review of grant expenditures for the term of the grant;

J. Monthly status of resales;

K. Monthly status of relocation activities, while applicable;

L. Monthly status of sales activity until all units have been initially sold;

M. Changes in closing costs as needed;

N. All records necessary to accurately calculate payments due HUD pursuant to repayment of the Promissory Note;

O. All records necessary to accurately calculate payments due the HOME Investment Trust Fund in repayment of homeowners' residual proceeds; and

P. Documentation that the amount turned over to HUD or the Home Investment Trust Fund are the amounts required; and

Q. Any other reports that Loan Management Branch or the RC determine necessary to demonstrate compliance with the Grant Agreement and RHP.

9-44. Tenant Selection Procedures. Tenant selection during the period when units are being sold or for units which are not sold must follow approved tenant selection procedures in accordance with the RHP or LEP. Loan Management staff should monitor this in accordance with HUD 4350.6.