Article XI Conversion:
A New Threat to Mitchell-Lama Cooperatives
Where do we get our information?

Outlined in this pamphlet is an overview of the issues related to converting Mitchell-Lama to Article XI that explains why Cooperators United for Mitchell-Lama (CU4ML) opposes these conversions. This information and analysis is based on a number of meetings with staff from HPD and HDC as well as on the DRAFT financial spreadsheets given to Cadman Towers, a Mitchell-Lama coop in Brooklyn that seems to be the first to be offered this type of conversion. We refer to this draft as the ‘Cadman Towers plan’ although a fully detailed plan has not been provided to shareholders in this development. While we acknowledge that there are still pieces of information that are needed to provide a complete analysis, we believe that there is enough information to conclude that these conversions are unnecessary, unaffordable and bad public policy.

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Background

HPD RULE CHANGE
In August, 2011, the Department of Housing Preservation and Development (HPD) proposed a set of amendments to the Mitchell-Lama Rules which govern HPD’s supervision of all city-supervised Mitchell-Lama (ML) coops. These amendments were distributed, and public input requested at a hearing, as is HPD’s normal practice before rule amendments are adopted. The hearing was held in September, 2011 and CU4ML, among other groups and individuals provided comments and feedback. In December, 2011, the amended rules were released, but they contained a **surprise**—a new amendment that had **not** been presented to the public for comment at the hearing. This amendment—(3-14(i)(15))—allows conversion of Mitchell-Lama coops to Article XI coops with only a majority vote and a minimal disclosure period.

**WHAT IS ARTICLE XI COOPERATIVE HOUSING?**
Article XI refers to the section of the NY State Private Housing Finance Law that contains the statutory provisions (laws) for this type of housing. Also known as HDFC housing (for Housing Development Fund Companies), this program has been very successfully used to convert abandoned buildings and rental properties into ‘affordable’ cooperative housing. Another section of the Private Housing Finance Law—Article II—contains the statutory provisions for Mitchell-Lama housing—so Mitchell-Lama developments are, similarly, sometimes called Article II housing. To see the full law see: [http://codes.lp.findlaw.com/nycode/PVH](http://codes.lp.findlaw.com/nycode/PVH)

**Just to be clear, no one is suggesting that there is anything wrong with Article XI housing or that this is not a good program for rental projects that would benefit by converting to cooperative ownership.** The bad idea is converting Mitchell-Lama coops to Article XI coops because these coops would become unaffordable to the people who want to continue to live in them and to the families on the ML waiting lists (or who would like to be on the waiting list) who will be priced out of these developments.
Why would HPD and HDC want to ENCOURAGE these conversions?

RETURN ON EQUITY?

According to the co-designers of this plan—HPD and the NYC Housing Development Corporation (HDC)—the dubious idea behind this conversion option was to develop a plan that would allow ML shareholders to get a return “on” the equity in their ML apartment when they leave. This would replace the long-standing Mitchell-Lama practice that allows these affordable apartments to be passed to the next generation of moderate-income New Yorkers by giving a return “of” the equity when they move out.

A COMPROMISE!?

HPD has indicated that they enacted the provision allowing conversion to Article XI in order to put an end to privatization efforts, and seems to see the plan as a compromise. In the several years it took to develop this “compromise,” CU4ML, the pro-Mitchell-Lama group, was never consulted or informed, while the plan seems to have been developed in concert with pro-privatization individuals. It is clear that if it is a compromise, it didn’t involve those of us who want to preserve Mitchell Lama housing. And why was it kept out of the public hearing process?
The BIG PICTURE of what is wrong with this plan

Instead of working to preserve affordable ML housing, it defies logic that government agencies would propose a plan that has as its primary goal to give a profit to those who have already received generous housing subsidies/tax exemptions for whatever number of years they lived in a ML development.

It is just plain **Bad Public Policy** to allow those who no longer want to live in ML cooperative housing to walk away with a profit, while:

- **increasing the costs to those who want to continue to live in these developments.**

- **dramatically increasing the costs to new buyers.** (Obviously, if the next person that purchases the apartment has to give the departing owner a big profit, the apartment will no longer be affordable to a moderate-income buyer.)

- **eliminating the current waiting lists, breaking longstanding agreements with those people who have waited for years or decades for affordable ML housing**

- **destroying diversity and impeding equal access to housing for the elderly, single parent families, young people starting their careers, and those on the lower end of the middle income range.**
Unaffordable

WHAT IS AFFORDABLE HOUSING?
There is no house or apartment on the planet that is unaffordable. There is always someone who can afford even the most expensive housing. The term ‘affordable housing’, therefore, tells you nothing unless you specify to whom it is affordable.

Converting Mitchell-Lama coops to Article XI coops would make these developments unaffordable to most of the families who now qualify for ML housing. Instead, the developments would only be affordable to families with much higher incomes.

Purchase price/monthly costs rise substantially
Conversions from ML to article XI would increase costs dramatically to any new purchasers as well as to any current residents who are not currently paying a surcharge.

Projected increases in maintenance in the Cadman Towers plan would also push out some of the current residents who are on fixed incomes or have lower incomes. This is because there would be a maintenance increase of 17.7% at the time of conversion and because there is an automatic rent stabilization guidelines annual increase in maintenance built into the plan.

Loss of surcharge income
At least part of this projected increase is to cover the loss of surcharge income.* So conversion would, essentially, be giving a break to the higher income residents (who would no longer pay a surcharge) at the expense of the lower income families who live in, and want to continue to live in, the development.

Middle income people priced out
Cadman Towers currently has a minimum income of about $21,037 for one person coming into a one-bedroom apartment to about $40,235 for a larger family eligible to move into a 3-bedroom apartment.

Under Article XI, a single person would need a minimum income of about $66,600 to purchase a one bedroom apartment and a family would need a minimum income of $107,000 to purchase a 3-bedroom.

These yearly income minimums go a little bit lower or a little bit higher in other ML developments—but the bottom line is that many, if not most of us who live in ML developments would not have had a high enough income to purchase our apartments if they had been converted to Article XI. Many of us struggled to come up with the purchase price even under ML—but under Article XI the prices would be significantly higher.

* We understand that a Board of Directors could, in an Article XI building, vote to continue the surcharge but would need to replace HPD’s role in the administering of the surcharge.
IN THE CADMAN TOWERS DRAFT PLAN

Again, the reason given for dramatically increasing the costs in these developments is to make sure that people who no longer want to live in them leave with a profit.

The chart, below, extracted from the Cadman Towers draft plan, shows the ESTIMATED costs to new buyers of an Article XI Cadman Towers:

Clearly the income needed to purchase one of these apartments will be much higher than to purchase these apartments if they were Mitchell-Lama. In addition, new buyers would be paying the increased maintenance costs PLUS an apartment mortgage—so monthly costs for the Article XI buyers would be much higher than as a ML.

**Flip tax**

A flip tax of 30% is projected in the Cadman Towers plan with outgoing shareholders giving Cadman Towers 30% of the sale price of the apartment on first sales and 3% on future sales. While this is being touted as producing money for capital improvements, in the case of Cadman Towers it appears that even with a 30% flip tax on apartment sales, there would still be a loss of income because the corporation would have to make up for lost surcharge income ($450,000 in 2011) and lost monies from the first sale assessment ($164,149 in 2011). The Cadman Article XI Plan projects a 3% turnover rate even though Cadman's privatization plan disclosed an actual 2% transfer rate for the prior five years. At the 2% rate, the 30% flip tax would only generate about $571,999 per year, less than necessary to make up for the lost surcharge income and first sales assessment income totalling $614,149 in 2011.

**Loss of unique diversity**

One of the beautiful things about ML housing is the diversity in our developments and, in many of the developments, a true spirit of cooperative living that is not often found in regular, market-rate coops.

<table>
<thead>
<tr>
<th>Bedroom size</th>
<th>Sale price</th>
<th>Down payment</th>
<th>Mortgage</th>
<th>Mortgage payment</th>
<th>Maintenance</th>
<th>TOTAL MONTHLY PAYMENT</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>$209,555</td>
<td>$20,955</td>
<td>$188,599</td>
<td>$1,041</td>
<td>$736</td>
<td>$1,777</td>
</tr>
<tr>
<td>2</td>
<td>$250,964</td>
<td>$25,096</td>
<td>$225,868</td>
<td>$1,247</td>
<td>$990</td>
<td>$2,237</td>
</tr>
<tr>
<td>3</td>
<td>$282,294</td>
<td>$28,229</td>
<td>$254,065</td>
<td>$1,403</td>
<td>$1,272</td>
<td>$2,675</td>
</tr>
</tbody>
</table>
Unnecessary

Mitchell-Lama shareholders are already the beneficiaries of significant government subsidies. There is no reason shareholders should be getting a profit when they leave—thus destroying affordability for those who want to stay and for those on the waiting list.

There is some talk that Article XI is a “good compromise” and might dissuade those who are trying to privatize our developments from continuing privatization efforts. For the most part, when developments look at the huge increases and financial risk that would come with going to market rate, this foolish idea has been voted down. Article XI, like privatization, would destroy affordable housing. Mitchell-Lama is still the best deal in town—both for current residents and for future generations.

CU4ML believes that we should be good stewards for ML housing so that the next generation, our children and grandchildren’s generations, can have the same benefits that we have had. We oppose the idea that it is ok to ‘pull the ladder up behind us’ and deny the next person on line a chance for affordable housing.

Bad Public Policy

Something is terribly wrong when government designs a plan to destroy affordable housing in order to give a profit to subsidized housing recipients. The argument seems to be that this housing would still be “affordable” and that Mitchell-Lama coops are flawed because the higher earners in the ‘middle-class’ make too much money to qualify for ML. So, the public policy seems to be—throw the lower earners in the middle-class under the bus in favor of the upper-earners so that long-subsidized ML shareholders can leave with money in their pockets.

Adding insult to injury, the plan seems to be to allow “safe” ML coops to convert to Article XI: Good public policy was when, in 2004, the Bloomberg administration came up with a brilliant plan to save Mitchell-Lama housing. Called the Mitchell-Lama Refunding Program, ML coops (and rentals) could restructure and refinance their mortgages with the NYC Housing Development Corporation (HDC), get a grant for building repairs, and be eligible for capital repair loans while agreeing to stay in the ML program for at least 15 years of “safety” from privatization. Bad public policy would be to allow the “safe’ ML coops out of their commitment to stay affordable.

When a coop is exempted from paying real estate taxes, and instead pays Shelter Rent Tax, other NY taxpayers have to make up the loss of this income. The public good of giving this tax exemption is that there is housing affordable to moderate-income New Yorkers which increases diversity in our communities. Giving these same tax breaks to much higher earners while shutting out more moderate earners is terrible public policy. It will end up destroying the diversity in our communities when only high income earners will be able to afford to purchase one of these apartments. Further, conversions would discriminate against single-income families in favor of two-income families as the much higher costs would be unaffordable, for example, to a single parent who makes a decent living (say $60,000 a year)—while a two parent family making $120,000 could purchase.
### Why Mitchell-Lama is good for current ML shareholders

Mitchell-Lama cooperatives are limited equity coops. This is the quintessential affordable housing. This means:

<table>
<thead>
<tr>
<th>YOU PAY WELL BELOW MARKET RATE FOR THE EQUITY IN YOUR APARTMENT</th>
<th>MITCHELL-LAMA COOPERATIVE HOUSING IS AFFORDABLE BECAUSE:</th>
<th>OTHER BENEFITS INCLUDE:</th>
</tr>
</thead>
</table>
| When you leave:  
  - you get your ‘limited equity’ back  
  - Plus the amount you have paid over the years toward the building mortgages (amortization)  
  - Plus any additional equity you paid toward repair projects | We are exempted from paying regular real estate taxes and instead pay ‘shelter rent tax’—usually about 10% of market rate real estate taxes  
  Many developments have government subsidized mortgages with better rates and/or terms than available to market-rate coops  
  Developments collect a surcharge from shareholders whose income is higher than the caps which helps support the operating costs of the development | We are eligible for some repair loans not available to market-rate coops  
 Oversight for large expenditures by government supervising agencies who must also give approval for maintenance increases  
 Don’t have to worry about getting a buyer for your apartment—it goes to the next eligible person on the waiting list |

### Why Article XI is bad for current ML shareholders

**LACK OF FLEXIBILITY IN MOVES WITHIN THE BUILDING**

Under Mitchell-Lama, when your family size changes you have the flexibility to move within the building. A single person or couple in a one-bedroom can move to a two-bedroom if they have a child, and can move to a three-bedroom if they have two or more children of opposite genders. Likewise, when the kids are grown a ML shareholder can move down to a smaller apartment to save money. These moves will not be possible under Article XI unless you meet the income guidelines and family size guidelines to purchase the apartment, and can come up with the much higher purchase price.

Similarly, many people take whatever apartment that is offered to them to get into a ML coop and then, after a year, can put their names on the waiting list for a lateral move—e.g. from a small one-bedroom on a low floor to a large one-bedroom on a higher floor. This also will no longer be possible without much higher costs and without the proper family size and income.

**UNCLEAR RULES AND PROCESS FOR CONVERSION AND BEYOND**

Unlike the prescribed process for a ML coop considering privatization, a ML to Article XI conversion is completely uncharted territory. HPD amended its rules related to privatization a number of times as problems in the process arose—so there is now a clearer process with protections in place so that shareholders are not voting to change the nature of their housing without full disclosure of the risks. **NO SUCH PROCESS IS IN PLACE** for this type of conversion. Cadman Towers, or whoever else pioneers this process, may end up with unanticipated problems after it’s too late to turn back.
BOARDS OF DIRECTORS WILL BECOME MUCH MORE POWERFUL UNDER ARTICLE XI

Mitchell-Lama coops are ‘supervised’ by HPD (city) or HCR (state). This supervision is to assure that these taxpayer subsidized developments are run effectively and efficiently and in the best interest of their purpose to provide affordable housing to moderate-income families. If these coops convert to Article XI coops, the Boards of Directors in these building will have more power and less supervision.

Boards of Article XI coops will have MUCH MORE POWER to decide who gets in and who doesn’t. There will no longer be waiting lists as sellers will have to find their own buyers for the apartment.

BOARDS ARE ALLOWED TO ACCEPT OR REJECT YOUR BUYER WITHOUT GIVING YOU A REASON.

ADDED SELLER RESPONSIBILITIES:

- Finding someone with the proper size family for their apartment—with the same rules for occupancy as a Mitchell-Lama apartment (e.g. you cannot sell your 2 or 3 bedroom apartment to a single person)
- Finding someone within the income range for the apartment
- Finding someone who has good credit so that they can get a mortgage
- Being responsible for real estate brokers and lawyer fees, paying real property transfer tax, and paying a transfer fee/flip tax to the coop. This transfer tax/flip tax would be a percentage of the sales price.

A BAD DEAL FOR PURCHASERS?

Our initial analysis is that there are a number of problems for new apartment buyers under Article XI, which could impede sales. These include:

- While they will get a below-market cost for their apartment, they will pay a lot for an apartment that will not be a typical investment property
- They will be governed by resale prices that are below market-rate and will not be able to sell to whomever they want, but only to those who qualify
- They will be burdened with a mortgage in addition to paying the building mortgage as part of their maintenance charge.
- They will not end up getting much of an increase in their equity when they sell.

Below is a chart comparing monthly maintenance payments of current residents with the total payment for new buyers who have to take a mortgage to buy the apartment. It was extracted from the information in the Cadman Towers Draft.

<table>
<thead>
<tr>
<th>Apartment size</th>
<th>Current maintenance</th>
<th>Total monthly payment (new buyers)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1 bedroom</td>
<td>$ 574</td>
<td>$ 1,665</td>
</tr>
<tr>
<td>1 bedroom +</td>
<td>$ 625</td>
<td>$ 1,777</td>
</tr>
<tr>
<td>2 bedroom</td>
<td>$ 788</td>
<td>$ 2,124</td>
</tr>
<tr>
<td>2 bedroom +</td>
<td>$ 841</td>
<td>$ 2,237</td>
</tr>
<tr>
<td>3 bedroom</td>
<td>$ 1,080</td>
<td>$ 2,675</td>
</tr>
<tr>
<td>Simplex</td>
<td>$ 813</td>
<td>$ 2,211</td>
</tr>
<tr>
<td>Simplex +</td>
<td>$ 850</td>
<td>$ 2,306</td>
</tr>
<tr>
<td>Duplex</td>
<td>$ 1,035</td>
<td>$ 3,044</td>
</tr>
</tbody>
</table>
Why Article XI might be tempting to current ML shareholders

Using our example, Cadman Towers would commit to staying in Article XI for 30 years and would be able to continue their tax exemption and be able to restructure and refinance their mortgages with HDC—so it does seem like it would end privatization efforts.

It is unclear if there would be any type of buy-out procedure once cooperatives have dissolved and reconstituted as Article XI developments. Given HDC’s willingness to allow refinanced Mitchell-Lamas with a fifteen-year ML commitment to break that commitment, this scenario seems possible. Even without such a change, those who stay in these Article XI developments will have much higher maintenance charges and new owners will pay prices much closer to market rate—so, in terms of affordability of these apartments, Article XI is more like privatization than it is like Mitchell-Lama.

➤ Flip taxes/transfer fees—a percentage of the profit of leaving shareholders—can be used for capital repairs and improvements. Of course these fees must FIRST be used to cover the loss of surcharge income and the loss of first sales equity income, so no additional income may be realized.

➤ Succession rights seem to change slightly from Mitchell-Lama rules. Many questions about how succession will work remain unanswered, but from initial discussions it seems that an Article XI owner will be able to leave their apartment to whomever they want. HOWEVER, and this is a BIG however, only people who qualify will be able to live in the apartment.

Requirements for your heir to live in the apartment after you die:*

- It would need to be their primary residence.
- They would also need to have the correct family size. Your single adult child could not live in your two-bedroom or three-bedroom apartment. They could inherit it, sell it, pay the flip tax, and pocket the difference.
- An exception, as with ML succession, is that if your child has lived with you for the past 2 years they could continue to live in the apartment—maybe. We do not know, yet, if the Board would be able to disqualify your child or heir from living in the apartment if they deem them unsuitable.

As with privatization, the Board will have an incentive to keep your child from moving in since they would not collect a flip tax. We don’t know, yet, under what parameters the Board could refuse your heir.

Rescind the amendment!

The amendment of the NYC Housing Preservation and Development (HPD) Mitchell-Lama (ML) rules in December 2011 that allows Mitchell-Lama coops to convert to Article XI coops was a mistake and should be rescinded. This change was inserted into the rules without public comment and without a careful consideration of the damaging consequences. Specifically, it allow for a simple majority vote on a radical change to ML coops to occur without full disclosure of the risks of such conversion. If the rule is not rescinded, a full Offering Plan/Black Book and a super majority, affirmative vote should be required as dictated by Section 1001 of the NY Business Corporation.

Mitchell-Lama cooperatives are still the best affordable housing program for the moderate income New Yorker. Converting Mitchell-Lama cooperatives to Article XI cooperatives in UNNECESSARY, makes the housing UNAFFORDABLE and is just BAD PUBLIC POLICY.

* It is unclear whether or not you could give the apartment to someone else and move out or if the apartment can only be inherited after you die.
How to take action

➤ Join CU4ML and get involved
➤ Sign our petition
➤ Visit our website—www.cu4ml.org
➤ Circulate this booklet to your ML neighbors
  (it can also be found in pdf form on our website)

THE HPD RULE CHANGE

This is the HPD amendment to its Mitchell-Lama Rules, adopted 12/06/11 without public comment that we believe should be rescinded. This is 3-14(i)(15) [that is, section 3-14, subsection i, paragraph 15] in the amended rules, which can be found in full at www.nyc.gov/htmlapartment/mitchell-lama.shtml

“(15) Notwithstanding anything to the contrary contained in this subdivision, if a mutual housing company intends to transfer the property to a housing development fund company (organized pursuant to Article XI of the Private Housing Finance Law) that will enter into a thirty-year regulatory agreement with HPD, a vote of the shareholders of such mutual housing company to authorize such transfer shall take place only after such mutual housing company has submitted an exemption application to the office of the Attorney General of the State of New York. Such transfer shall be approved by a majority of the dwelling units in such mutual housing company. Each such dwelling unit shall be entitled to one vote regardless of the number of shares allocated to such dwelling unit, the number of shareholders holding such shares, or the provisions regarding voting in such mutual housing company’s certificate of incorporation or by-laws.”

To allow such a radical change in the nature of these developments with no rules in place that assure full disclosure of risk and only a majority vote is a set-up for disaster.