

Limited Equity Cooperatives

a

Legal Handbook

By

Barry Mallin, Esq.

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Mario M. Cuomo, Governor
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ABOUT THE AUTHOR

Barry Mallin is an attorney who has specialized for the past ten years in the field of community development law. During that period, Mr. Mallin has worked with more than 200 low income cooperatives and homesteading groups. He served as the Director of the Community Development Legal Assistance Center from 1980-1985, and is a co-author of the **Legal Handbook for Community Development Organizations**.

John Conway, Technical Assistance Program Manager for DHCR, provided editorial assistance and supervised production and distribution of this Handbook.

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INTRODUCTION

The lettering on the bright green awning leading to the entrance of 1500 Boston Road, a six-story apartment house in the heart of the South Bronx, identifies the property as "New Hope Plaza." Twelve years ago, a hand-painted, tattered banner draped from the roof of the building bore the inscription "Last Hope Tenants Association."

The difference today is that the tenants own and operate the property as a low income cooperative. The residents bought the building from the City of New York in 1982 and have struggled to maintain it as affordable housing for its cooperative members. Their experience has been replicated during the past decade by tenants in hundreds of buildings containing thousands of housing units. A variety of public and private programs have evolved in New York in the last ten years to spur efforts to bring cooperative ownership to low income people.

Low income people owning their own apartments is an idea that was virtually unheard of prior to 1980, but it is now a reality that has taken hold. In New York City many buildings have been successfully converted to cooperatives for low income individuals and families. Upstate, the concept is gaining acceptance and there have been a number of successful conversions of not only buildings, but also mobile home parks.

For low and moderate income people with severely limited options in today's housing environment, cooperative ownership has been one of the few positive developments in the effort to provide decent, affordable housing.

The purpose of this manual is to present the legal framework for creating cooperatives owned and operated by low and moderate income people in New York. The term "limited equity" is often used to describe such cooperatives.

Chapter I will provide an overview of cooperative basics and will describe the structure and organization of housing cooperatives and the benefits of cooperative ownership.

Chapter II will explain the process by which a property is converted to cooperative ownership. The

chapter will discuss the types of limited equity cooperatives, the formation of the legal entity, the purchase of the property by the cooperative and the sale of shares to members.

Chapter III will discuss the requirements of New York laws and regulations relating to the sale of cooperative shares and how such laws and regulations impact on the creation of limited equity cooperatives.

Chapter IV will focus on the nature of the limited equity cooperative and how it differs from other types of cooperatives. The chapter will describe the various public and private programs most active in New York in the creation of limited equity cooperatives and the different mechanisms used to maintain the apartments as affordable housing.

Chapter V will explain the operation of a cooperative. The chapter will analyze the rights and obligations of cooperative members under the group's governing documents and the responsibilities of the board of directors in the ongoing operation of the property.

Checklists will be included to guide groups through the steps involved in the process. Model forms directly relevant to limited equity cooperatives are contained in the Appendix.

In New York the common ownership of real estate by residents is most often organized as either a cooperative or condominium. In the creation of luxury housing, condominiums have become the most prevalent form of ownership. In the creation of low income common ownership entities, however, the condominium model is rarely used. (The reasons for this are discussed in Chapter I.) Because of the preferred use of cooperatives for low income ownership, this manual will focus on the cooperative, rather than condominium, form of ownership.

As in any discussion of legal issues within the context of a manual, however, the information provided cannot replace the need to obtain competent legal advice on the specific questions relating to actual cooperative projects. It is recommended that any group undertaking such a project secure as part of the professional team the services of an experienced attorney.

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CHAPTER I

OVERVIEW: COOPERATIVE BASICS

Forms of Ownership of Residential Real Property

Ownership of housing can be divided into three basic types:

1. **Fee Simple** ownership of property,
2. **Condominium** ownership of an individual unit in a multi-unit project, or
3. **Cooperative** ownership of an individual unit in a multi-unit project.

In recent years, neighborhood-based organizations also have developed hybrid forms of ownership, utilizing **mutual housing** or **land trust** models, and, in some cases, have combined these models with cooperative forms of ownership.

In **fee simple** ownership, the purchaser of the property receives a deed, obtains mortgage financing, if needed, for the purchase and pays his taxes and other expenses of maintaining the property.

In a **condominium**, the purchaser of a unit receives a deed to a specific unit and an undivided ownership of the common elements of the project. The purchaser must obtain his own mortgage

financing on the unit and he pays his own real estate taxes. The maintenance of the common elements, however, is covered by the payment of common charges to the condominium's board of governors by each unit holder.

In a **cooperative**, the purchaser does not receive a deed to the unit. He becomes a shareholder in the corporation which owns the deed to the building. The purchaser receives a personal property interest (shares of stock) and the right to a long term lease (typically 99 years), known as an occupancy agreement or proprietary lease, to the unit.

The purchaser may finance the purchase by pledging his stock and proprietary lease as security for re-payment of the loan. The maintenance of the common elements, including real estate taxes, is covered by the payment of maintenance fees to the cooperative corporation by each shareholder. The cooperative corporation may use its ownership interest to secure a mortgage to finance the purchase and/or renovation of the entire building. The payment of this mortgage is then included proportionally in each shareholder's monthly maintenance charge.

In a **mutual housing** model, the property is owned by a not-for-profit corporation typically composed of representatives of the community and residents of the project. Resident-members of the mutual housing organization occupy their units under leases from the not-for-profit owner. The resident-members will have a role in the decisions relating to the operation of the project, but not an ownership interest in the legal sense.

In a **land trust** model, the land beneath the building is owned by a not-for-profit community based entity. The building itself may be organized as a not-for-profit rental or it may be owned by a cooperative. The owner of the building will rent the land from the land trust under an agreement known as a ground lease. The ground lease is the mechanism by which the land trust can enforce long-term affordable use provisions. In the cooperative situation, the cooperative corporation will thus not own the deed to the land, but rather will enter into a ground lease to occupy the land owned by the land trust, giving rise to the term "leasehold cooperative" to describe this form of legal relationship.

Differences Between Cooperative and Condominium Ownership

The cooperative, rather than condominium, form of ownership is the model of choice for limited equity (i.e. moderate and low income) projects for two fundamental reasons, **control** and **funding**.

Control of the Project

Through its corporate by-laws and occupancy agreement, a cooperative is structured with broad powers vested in its board of directors. Elected by the shareholders, the board has centralized control over numerous decisions involving individual units, including the re-sale and subletting of apartments. If the goal of the cooperative is to maintain the affordability of the units for present and future members, the board has the power to enforce and monitor re-sale profit and price limitations. It also bears the responsibility of complying with such restrictions embodied in the governing documents of the cooperative. The condominium format, in contrast, utilizes a board of managers, which usually performs primarily administrative functions on behalf of a federation of property owners. Ownership rests in each individual occupant, rather than in a centralized corporation. The basic function of the Board of Managers is to maintain the common areas of the building. It has limited control in connection with the sale and subletting of units, thus making it more difficult to ensure long-term affordability.

Funding of the Project

In the cooperative model, it is the cooperative corporation which holds the deed to the property. This enables the corporation to use the entire property as security for a "blanket" mortgage to obtain acquisition and rehabilitation funds. The burden of obtaining financing thus falls upon the corporation

rather than on the individual shareholders whose incomes might make obtaining the necessary funds difficult. The sharing of this burden is not possible in a condominium where each individual deed holder bears primary financial responsibility for his or her unit. It is not possible in a condominium to place a "blanket" mortgage on the entire property.

The ability of the cooperative members as a group to use the entire property as collateral for financing the project places them in a far stronger position to achieve their funding goals.

Organization of the Cooperative Corporation

A New York housing cooperative is usually created by forming a corporation pursuant to the Business Corporation Law. Low income cooperatives, however, are generally created under and governed by both the Business Corporation Law and Article XI of the Private Housing Finance Law. (See Chapters II and IV for discussions of Article XI cooperatives.)

A housing cooperative is a corporation organized to buy, own and operate a residential building or property for the purpose of providing housing for its shareholders. A purchase price for the shares of the corporation, also commonly referred to as the apartment purchase price, is set by the sponsoring organization. In low income cooperatives, affordability is the prime concern in determining purchase prices.

The residents of the building become the shareholders of the corporation through the purchase of shares allocated to their individual apartments. It is the ownership of the stock in the corporation that entitles a resident to a long-term lease to a particular apartment.

Shareholder/Tenant.

The shareholder/tenants of a cooperative occupy two legal positions in relation to the corporation: 1) as **part-owners** through the ownership of the stock of the corporation and 2) as **tenants** of the corporation by virtue of being entitled to leases for their respective apartments. A prospective purchaser who buys shares in the cooperative corporation receives a lease, known as a proprietary lease or occupancy agreement, that entitles the purchaser to occupy the apartment for which the shares have been allocated.

Board of Directors.

As in other corporations, the Board of Directors makes policy and management decisions for the organization. The Board is elected annually by the shareholders. The Board, in turn, appoints officers (i.e. president, vice-president, secretary and treasurer) to carry on the day-to-day affairs of the cooperative. In the typical housing cooperative, the officers are selected from the members of the Board of Directors. (See Chapter V for a discussion of the role of the Board and officers).

Cooperative By-Laws.

The procedures by which the corporation calls meetings, holds elections and otherwise conducts the business of the cooperative is governed by the corporate by-laws. (See Chapter V for a discussion of the cooperative by-laws).

Proprietary Lease.

The proprietary lease or occupancy agreement, typically structured for a 99-year term, defines the relationship between the corporation as lessor and the tenant/shareholder as lessee of the particular apartment. The tenant/shareholder receives the right to occupy the apartment and undertakes, among other things, the obligation to pay the monthly maintenance charges for the operation of the building.

(See Chapter V for a discussion of the rights and obligations under the Proprietary Lease). The monthly maintenance charge is paid to the corporation to cover the expenses of operating the building, such as fuel, insurance, taxes, mortgage payments, repairs, salaries and reserves.

Other Governing Documents

Certificate of Incorporation. The legal document used to create the cooperative corporation. The certificate is filed in Albany with the Secretary of State. It sets forth the basic purposes, powers and restrictions of the Corporation.

Deed. The legal document that is evidence of the Corporation's ownership of the property. The deed is filed with the local county registrar's or recording office. In the case of low income cooperatives, the deed typically contains restrictions on the re-sale of individual apartment units. (See Chapter IV for a discussion of re-sale restrictions in limited equity cooperatives).

Benefits of Cooperative Ownership

As the availability of affordable housing remains scarce, the surge of interest in cooperative housing for low and moderate income people can be attributed to the following benefits:

Control by Residents.

By owning, rather than leasing, residents of the property can maintain long-term control over their own housing decisions. This can act as a shield against the whims of the market place.

Fair Rent Structures.

The shareholders of the cooperative, acting through their elected Board of Directors, prepare their own operating budget and set the monthly maintenance costs. Landlord profit is eliminated as a factor in establishing costs. Although the Board cannot control such outside factors as the cost of fuel and insurance, the self-interest of the shareholders serves to maintain monthly charges at an affordable level. In most limited equity cooperatives, the cost of operating the building is pro-rated among the shareholders according to apartment area, whether it is defined in terms of square footage or number of rooms. This creates a fair method of sharing costs. Many cooperatives are members of organizations that buy fuel and insurance at bulk rates, an example of ways in which Boards can seek reduced costs for their shareholders.

Direct Involvement of Residents in Maintaining Decent, Affordable Housing.

As owners, the shareholders can make themselves heard as to how their money should be spent. In well-run cooperatives, the Board will prepare regular reports on the financial health of the property. A Fiscal Management committee can also be established consisting of board members and shareholders to work on fiscal planning. At a minimum, the shareholders are entitled to an annual financial statement issued by the Board.

Democratic Decision Making.

Board members are elected by the shareholders to serve one year terms. In many limited equity cooperatives, each apartment unit can cast one vote for each director to be elected. Although the Board is responsible for operating the property, the ultimate electoral power resides with the shareholders. In situations involving serious dissatisfaction with the performance of the Board, the shareholders can petition to hold a special election to replace the Board members.

Anti-Displacement Strategy — Maintaining Neighborhood Roots.

As an owner, a shareholder cannot be forced to give up his home because of rising market pressures. The shareholder will not be subject to harassment or tactics employed by a landlord seeking to vacate the unit for higher profit. This protection enables the shareholder and his family to feel more secure from outside market forces and makes it easier for him to set down roots in the community. The

stability generated by being a shareholder in the cooperative often manifests itself in a long-term commitment to community stability as well. The shareholder makes the decision when and if to sell his unit. In limited equity cooperatives, sales are controlled through restrictions on sale price and the income level of the purchaser. This is done in an effort to preserve the affordability of the unit over the long term. (See Chapter IV for a more detailed discussion of resale policies).

Legal and Income Tax Benefits.

As an owner, the shareholder has the right to sell his shares, sublet his apartment and undertake alterations in his unit. Before the shareholder can exercise these rights, however, he must obtain the approval of the Board, thus maintaining a balance between the individual rights of the shareholder and the responsibility of the Board to protect the interests of the other tenant/shareholders. In limited equity cooperatives, the individual rights of the shareholder are also subject to restrictions on selling and subletting contained in the cooperative's governing documents. (See Chapters IV and V for further discussions of re-sales and subletting).

Shareholders in general also are entitled to income tax deductions under Section 216 of the Internal Revenue Code. This entitles each shareholder to take as a deduction his pro rata share of any real estate taxes or mortgage interest paid by the cooperative. In the case of low income taxpayers who do not itemize deductions, however, this will not have real benefit.

CHAPTER II

THE CONVERSION PROCESS

Market-Rate Cooperatives

In general, market-rate cooperatives are created when the owner of a property decides to sell his interest to a cooperative corporation. The owner initially forms the cooperative corporation. The owner's goal is to sell the shares of the newly-formed corporation to the tenants in the building or to the general public in the case of vacant or newly-constructed units. The owner, also called the sponsor, seeks to obtain the highest possible price for the sale of the shares. Once he is able to sell a majority of the shares in the cooperative corporation, control of the corporation is taken over by the shareholder-residents of the property.

Limited-Equity Cooperatives

Definition

A limited equity cooperative can be defined as a housing cooperative in which low income eligible members purchase shares at below market prices and are subject to limitations on the amount of equity or profit they can receive on the re-sale of their units. The term "low income" cooperative is often interchangeable with "limited equity."

The creation of a limited equity cooperative, however, can involve a variety of paths.

Private Developer Sponsors.

Private developers have created limited equity cooperatives, for example, under the New York

State Affordable Housing Program. Below market acquisition and financing costs provided by the State and local municipality enable the developer to build new units at a lower price. The units are sold at below market prices. Purchasers, in turn, must agree to restrictions on re-sale profits.

Not-for-Profit Sponsors.

Many not-for-profit groups throughout the State are engaged in purchasing properties, renovating them and then selling the units as low income cooperative housing. Vacant buildings owned by New York City, for example, have been sold to such groups for a price of one dollar. The groups obtain public funds provided by the City and the State (for example, through the State Housing Trust Fund) to rehabilitate the buildings. Once completed, the buildings are transferred to cooperative corporations. Shares in the cooperative are sold to low income members of the general public after an application and screening process.

In upstate New York, for other examples, the City of Rochester worked together with a not-for-profit sponsor, Housing Opportunities, Inc., to convert two vacant city-owned buildings into low income cooperatives. One building was renovated to create 15 apartments using grant and loans funds from the State Urban Initiatives Program, the federal Urban Development Action Grant program and a private bank. Equity funds also were provided by investors who received federal tax credits for rehabilitation of an historic building. The other project was the renovation of an unused school building into 35 low income cooperative units, financed by the New York State Housing Trust Fund and federal section 312 loan funds.

Even mobile home parks in rural areas are being converted into cooperatives. A coalition of church groups in Chautauqua County, for example, working together with the Mobile Home Coalition and the Greater Upstate Law Project, organized a group of 40 tenants in a mobile home park into a cooperative. The tenants each paid \$250 for their sites and the project received funding from the New York State Housing Finance Agency under its Affordable Homeowners Grant program and from the Institute for Community Economics, a non-profit foundation.

Tenant Sponsored Cooperatives.

Tenant groups in occupied buildings have taken the initiative in organizing and negotiating the purchase of properties from either private or public owners. In New York City, hundreds of buildings have entered the City's Tenant Interim Lease Program in which tenant associations have managed their buildings for a number of years before purchasing through a cooperative form of ownership at \$250 per unit. In privately-owned dwellings, the Ownership Transfer Project of the Community Service Society has assisted a number of tenant groups to organize, negotiate and finance the purchase of their buildings from private landlords.

Homesteading Groups.

Many groups have organized themselves to embark on the purchase and rehabilitation of vacant and abandoned properties. New York City's Homesteading Program has sold dozens of City-owned buildings to such groups. The process is long and hard, requiring the groups to devote their own labor, called "sweat equity", to complete parts of the work. Assistance in organizing and financing, as well as training in construction skills and cooperative management, have been provided by such not-for-profit groups as the Lower East Side Catholic Area Conference, the Urban Homesteading Assistance Board and the Banana Kelly Community Improvement Association, Inc. in the South Bronx.

Formation of the Legal Entity

Market-rate housing cooperatives in New York are usually formed as corporations under the Business Corporation Law. Most limited equity cooperatives in New York, however, are created as corporations under the combined provisions of the Business Corporation Law and the Private Housing

Finance Law. Under Article XI of the Private Housing Finance Law, a corporation may be created for the exclusive purpose of developing a housing project for persons of low income and for the benefit of persons and families who are entitled to occupancy in the housing project by reason of ownership of shares in the corporation. These corporations are known as Housing Development Fund Corporations. The incorporation of an Housing Development Fund Corporation (HDFC) must be approved by the government agency having primary supervision over the project. In some cases this may be the State Division of Housing and Community Renewal (DHCR) or in other cases, the local housing agency such as the New York City's Department of Housing Preservation and Development (HPD). Housing Development Fund Corporations (HDFCs) are the preferred legal entity for loans and grants under most New York State and local funding programs for low income cooperatives. Indeed, most of the programs mandate that the cooperative be organized as an HDFC. In addition, HDFC's receive benefits not available to other types of business and cooperative corporations.

Benefits of Housing Development Fund Corporations

1. **Direct Sales.** A Housing Development Fund Corporation (HDFC) is empowered to purchase municipal property through direct negotiations with local government agencies without public bidding or auction.
2. **Mortgage Recording Taxes.** An HDFC is exempt from mortgage recording taxes.
3. **Franchise Taxes.** An HDFC is exempt from New York State corporate franchise taxes.
4. **Corporation Tax — New York City.** An HDFC is exempt from New York City Corporation Tax.
5. **Real Estate Taxes — New York City.** In New York City, an HDFC receives preferential treatment under the City's real estate tax exemption and abatement program (J-51) available for the rehabilitation of buildings. Under this program, HDFC's receive benefits for 32 years (instead of 20) and can be exempted from paying real estate taxes during the construction period.
In New York City, if an HDFC purchases a privately-owned building that is encumbered with real estate tax arrears, the HDFC may enter into a longer term (12 years instead of 8) installment agreement with the City to pay the tax arrearage.
6. **Real Estate Taxes — Statewide.** The local legislative body of any municipality in which a project of an HDFC is located may exempt the project real property from local taxes, including school taxes.
7. **Loans to HDFC's.** Many government loan programs look favorably on HDFC's, for example, the New York State Housing Trust Fund and Housing Development Fund and the New York City Article 8-A loan program, by providing below market financing and interest-free grants to HDFCs.

The Conversion Process in a Nutshell

The process of converting to a cooperative can be summarized in the following checklist:

1. **Agreement to Sell to the Cooperative Corporation**
 - a. Privately-Owned Building — Signing of Contract of Sale
 - b. Government-Owned Property — Commencement of Land Use Review Procedures (the Uniform Land Use Review Procedure (ULURP), for example, in New York City).
2. **Formation of Cooperative Corporation.** Most limited equity cooperatives in New York are formed under the combined provisions of the Business Corporation Law and Article XI of the Private Housing Finance Law.
3. **Agreement by Cooperative Members to Subscribe to the Stock of the New Corporation.**

Execution of subscription or purchase agreements by a sufficient number of prospective shareholders. In projects in which a not-for-profit sponsor is rehabilitating a vacant building or undertaking new construction, the sponsor will form the cooperative corporation and will offer purchase agreements to prospective shareholders generally during the construction period.

4. **Purchase of Shares of Stock by Cooperative Members.** Purchase of shares is subject to laws and regulations governing the sale of cooperative interests in real estate under the General Business Law (for example, the requirement to present an offering plan or prospectus to the tenants of the building).

5. **Acquisition of Property by Cooperative Corporation.** Purchase price paid at closing and deed obtained.

6. **Resident-Shareholders Assume Control and Responsibility for Owning and Operating the Building** — election of directors and selection of officers.

Incorporation of a Housing Development Fund Corporation

Drafting the Certificate of Incorporation

A corporation comes into existence when its certificate of incorporation is accepted and filed in Albany by the New York Department of State. The certificate must contain at a minimum the basic requirements set forth in Section 402 of the Business Corporation Law and, in the case of an HDFC, the requirements of Section 573 of the Private Housing Finance Law. The following is a checklist of those requirements for a HDFC incorporation:

1. **Corporate Name.** The term "housing development fund corporation" or "housing development fund company" must be included as part of the name.

2. **Purposes.** The purpose must state that the corporation has been organized exclusively to develop a housing project for persons of low income and, in addition, in the case of a low income cooperative, that the housing project be operated exclusively for the benefit of persons or families who are entitled to occupancy in such housing project by reason of ownership of shares in the corporation.

3. **Restrictions.** The certificate must state that all income and earnings of the corporation shall be used exclusively for corporate purposes and that no part of the earnings of the corporation shall inure to the benefit or profit of any private individual, firm, corporation or association. (This means that the income of the corporation can only be used to maintain and repair the building and to fund necessary reserves, but may not be distributed as profits or dividends to individual members or any other parties.) In addition, local municipalities may impose additional restrictions that must be included in the certificate. This most often takes the form of provisions governing the re-sale of individual units in the cooperative.

4. **Capital Structure.** The initial value (known as "par value") and the number of shares that the corporation is authorized to issue. (The total number of shares is most often established by adding the total number of rooms or square footage for each apartment and then specifying a price per share.)

5. **Location of Corporation.** The county in which the corporation will operate.

6. **Agent for Process.** The Secretary of State must be designated as agent of the corporation upon whom process against the corporation may be served and the address to which the secretary of state can mail a copy of any process served against the corporation. (This enables a party to serve court papers against the corporation through the Secretary of State in the event that a corporate officer cannot be found.)

7. **Approvals.** Attached to the certificate must be the consent of the Commissioner of DHCR or the local supervising housing agency, as for example, the Department of Housing Preservation and Development (HPD) in New York City. (The certificate must be mailed to the legal department of the agency involved for review and obtaining of the consent.)

8. **Name of Incorporator(s).** The certificate must be signed by the incorporators (only one

required) and must contain the incorporator's full name and address. (The incorporator can be a person connected with the sponsoring organization or one of the members of the cooperative.)

The Appendix contains a model HDFC Certificate of Incorporation.

Purchase of Shares by Cooperative Members

The sale of shares in a residential cooperative is controlled by the General Business Law, section 352-e et seq (the Martin Act) and the Regulations promulgated under it, as administered by the Attorney General of the State of New York. The Martin Act deals with the sale of real estate securities. The creation of a common form of ownership in real property, as in the formation of a cooperative, is deemed by law to involve the sale of real estate securities.

The General Business Law requires that in any instance in which a public offering or sale involves shares in a cooperative, a written statement, known as an "offering plan" or "prospectus" must be filed with the New York State Department of Law prior to such offering. Such offering plan must contain a detailed description of the transaction. The purpose of the offering plan is to afford purchasers an adequate basis upon which to determine whether to buy into the cooperative.

The drafting of an offering plan is expensive and time consuming, requiring the extensive services of an attorney, accountant, engineer and other real estate professionals. In most cases, the cost involved is beyond the capacity of low income cooperatives. To deal with this problem, the Attorney General has formulated regulations and policy guidelines to provide a more streamlined procedure for HDFC cooperatives. The purpose of such procedures is to enable the HDFC cooperative to obtain what is known as a "no action" letter from the Attorney General. The "no action" letter allows the HDFC to sell its shares to members without the filing of an offering plan. (See Chapter III for a discussion of the procedures for the filing of offering plans and applications for no-action letters.)

Once the offering plan has been accepted for filing by the Attorney General or the Attorney General has issued a "no-action" letter, the corporation may offer its shares to prospective members of the cooperative. The usual procedure is for the prospective shareholders to sign purchase or subscription agreements committing themselves to purchasing shares at the prices specified in the plan. (See Appendix for Model Purchase Agreement used in a low income cooperative.) The purchase price is held in escrow by the sponsor's attorney pending the acquisition of the project property by the cooperative corporation. In most programs involving the development of low income cooperatives, purchase prices range from \$250 to \$2500 per apartment. Upon the closing of individual units in the cooperative, each of the purchasers receives a stock certificate and a fully executed proprietary lease for the apartment.

Purchasing the Property by the Cooperative Corporation

Purchase from a Private Owner

If a tenant group has negotiated the purchase of its building from a private owner, the procedure is to enter into a contract of sale setting forth the terms of the transaction. As in any important legal transaction, it is advisable to obtain the services of an experienced lawyer in the early stages and, most certainly, prior to the signing of the contract of sale.

Checklist for Contract of Sale

1. **Name of Parties.** If the contract is initially in the name of individual tenants or the tenants association, the group should obtain the right to assign the contract to a corporation to be formed. (It is advisable for a corporation to buy the property to protect the tenants from individual liability).

2. **Description of Property.** Metes and bounds description from prior deed.
3. **Purchase Price.** It is customary for a purchaser to pay a down payment of ten percent of the price upon execution of the contract of sale. The down payment is held in escrow by the seller's attorney pending the successful completion of the transaction. The balance is due at the closing of title. The amount of the down payment can be negotiable if the tenants need more time to raise funds.
4. **Condition of Property.** Right to inspect the property by termite inspector and purchaser's engineer. In many cases in which tenants have purchased buildings from landlords, the property needed considerable repair. The tenants should be aware of the cost and whether it is feasible to undertake the borrowing of such funds. The inspection of the building condition should take place prior to the signing of the contract of sale.
5. **Satisfaction of Existing Mortgages, Liens and Taxes.** It must be clear in the contract what liabilities the tenants will assume and what items the owner is responsible for removing.
6. **Closing Date and Place.** Contracts specifying that "time is of the essence" generally should be avoided because they restrict flexibility if the tenants need more time to raise funds for the purchase.
7. **Apportionments.** What items, such as fuel on hand, rents, taxes, will be apportioned between the parties as of the closing date.
8. **Compliance with Regulations.** Will the tenants take the building as is, including existing violations, or must the owner be responsible for clearing up such items?
9. **Mortgage Commitments.** If tenants intend to borrow funds to finance the purchase price, the contract should be conditioned on the obtaining of such funds. Otherwise, the tenants could lose their down-payment if they are unable to obtain a mortgage commitment. It also is possible for the owner himself to accept a mortgage for the balance of the sale price. This is commonly known as a "purchase money mortgage".
10. **Closing Costs.** The contract should specify clearly whom is to pay such items as transfer taxes and mortgage recording taxes. It is customary for the seller to pay the transfer tax and for the purchaser to pay the mortgage recording taxes, if any, and fees for title insurance and recording the deed and mortgage.
11. **Form of Deed.** The most prevalent form of deed used in New York is a "bargain and sale deed with covenants against grantor's acts."
12. **Marketable Title.** The seller must convey such title that a reputable title insurance company is willing to insure.

Purchase from a Municipality

Although procedures vary according to jurisdiction, sales of publicly-owned property must be approved by the local governing body.

In New York City, for example, the transaction must follow the requirements of the Uniform Land Use Review Procedures (ULURP) under the City Charter. Under a new New York City Charter enacted in 1989, the Board of Estimate, which formerly had final land review powers, was abolished and a new land use procedure is now in effect. The ULURP process involves reviews and recommendations by the local community boards, the Borough Presidents, and the City Planning Commission and approval by the City Council. However, a sale to a group that has been organized exclusively to develop housing for persons of low income can obtain final approval at the City Planning Commission level.

In the case of low income housing, New York City as well as other municipalities, also have the authority to shorten the review procedures under the powers granted to them by the Urban Development Action Area Act (UDAAP) (Article 16 of the General Municipal Law).

As a condition to approval, the local governing body may impose low income requirements in the deed and other instruments involved in the conveyance of the property. Once approved, the final step is the closing of title to the property.

The Closing

At the closing the parties come together to essentially exchange the purchase price of the project property for a deed to the property. Prior to that meeting, the cooperative and its attorney must take the steps necessary to prepare for the actual conveyance. It is important for all documents to be assembled and reviewed and issues resolved prior to the actual closing. The following is a checklist of the key steps:

1. **Title Report.** All title objections and unanticipated liens on the property must be resolved.
2. **Deed.** Form of deed must be reviewed.
3. **Corporate Seal.** Ordered and affixed to important corporate documents, such as stock certificates and proprietary leases.
4. **Federal Employee Identification Number.** Applied for upon incorporation.
5. **Note and Mortgage.** If bank or government financing is involved in the purchase of the property, the loan documents must be reviewed.
6. **Applicable Taxes and Related Forms.** Depending on the form, these are executed either prior to or at the closing, for example, the New York City Real Property Transfer Tax ("RPT") Return and the New York State Real Property Transfer Gains tax forms and affidavits.
7. **Adjustments.** List of items and amounts to be adjusted between buyer and seller at closing. For example, real estate taxes, water and sewer charges, fuel and rents from tenants.
8. **Insurance.** Obtain fire and liability policies.
9. **Assignment of Rents and Leases.** Any leases or other agreements to be transferred to the cooperative must be reviewed.
10. **Certified Check for Acquisition.** Any cash balance in the purchase price to be paid at closing must be in certified funds. Lender's check at closing for any financed amounts.
11. **Payment of Closing Expenses.** Title Insurance and Recording Fees; Real Estate Taxes; Water and Sewer charges; Insurance Premiums (prior to closing); Legal Fees and disbursements.
12. **Multiple Dwelling Registration Card (New York City).** Registration of New Owner prepared at closing.
13. **Corporate Documents.** Certificate of Incorporation and Filing Receipt from Secretary of State; Corporate By-Laws prepared or reviewed by attorney; Corporate Resolution signed by authorized corporate officer.
14. **Discharge of Tax Arrears.** In the case of a municipality, letter removing all tax arrears and other municipal liens up until the date of closing or proof of payment. In the case of a private owner, proof of payment (if payment required by terms of the contract of sale).

Control and Responsibility for Owning and Operating the Property

Once the closing has occurred, the responsibility for operating and managing the property shifts to the cooperative corporation and its shareholders. The corporation is required to organize its activities to properly manage the operations and funds of the cooperative.

The first step in the formal organization of the cooperative is a meeting of the shareholders to elect its board of directors. The first meeting of shareholders also can serve as a forum for the organization's attorney to explain cooperative operation and procedures and to answer shareholder questions.

Under normal corporate procedures, officers are elected, not by the shareholders, but by the board of directors. Thus, a meeting of the board should occur soon after the election of directors for the board to elect the officers of the corporation (i.e. president, vice-president, secretary and treasurer). The officers are responsible for the day to day operations of the building owned by the corporation. The typical practice is for the officers to be chosen from among the members of the board of directors. (See Chapter V for a detailed discussion of the operation of the Cooperative).

CHAPTER III

THE OFFERING PLAN

Approval by the New York State Department of Law

The sale of an interest or shares in a housing cooperative or condominium falls within the jurisdiction of the New York State Department of Law, an agency headed by the New York Attorney General. The role of the Department of Law is to enforce the provisions of the New York General Business Law, section 352-e et seq. (the Martin Act) and the rules and regulations promulgated by the Attorney General pursuant to the Martin Act.

The Martin Act requires that in any instance in which a public offering or sale of an interest in a real estate venture is contemplated, including cooperative and condominium sales, a written statement, known as an "Offering Plan" or "Prospectus" must be filed with the Department of Law prior to such offering. Such offering plan or prospectus must contain a detailed description of the transaction as well as the information required under the applicable rules and regulations. The basic purpose of the Martin Act is to provide potential purchasers with adequate disclosure of the details of the offering.

The Department of Law is empowered to waive those requirements when it determines that the participants are sufficiently aware of the nature of the transaction and do not require a full-scale offering plan. Such waivers, in the form of "no-action" letters, have been issued by the Department of Law for low income cooperatives that satisfy the eligibility requirements and comply with the application procedures formulated by the Attorney General. (See the section below entitled "No-Action Letters" for a detailed discussion of these requirements and procedures).

Applicable Statutes

Statutes governing cooperative offering plans are contained in different sections of the General Business Law (GBL) depending upon geographic areas within the State.

Real Estate Syndication Offerings — General Business Law, Section 352-e

This section of the General Business Law includes in its coverage those conversions to cooperative ownership not governed specifically by Sections 352-eee and 352-eeee (see below). In general, the section describes what is required to be disclosed in the offering plan, including the detailed terms of the transaction, a description of the property, essential terms of all financing and mortgages, background on the principals involved and their financial interests and restrictions, if any, on the resale of units.

Conversions to Cooperative and Condominium Ownership in Certain Cities, Towns and Villages Located in the Counties of Nassau, Westchester and Rockland — General Business Law, Section 352-eee

This section of the General Business Law governs conversions to cooperative and condominium ownership within those municipalities that have adopted section 352-eee and are located in Nassau, Westchester and Rockland counties. The section describes the minimum disclosure requirements for a cooperative or condominium offering plan, including the rights of tenants under an "eviction" or "non-eviction" plan and protection for senior citizens and disabled persons.

Business Law Section 352-eeee

This section defines the minimum disclosure requirements for conversions to cooperative or condominium ownership in the City of New York. This section also sets forth the rights of tenants and that of senior citizens and disabled persons.

Both GBL Sections 352-eee (Nassau, etc.) and 352-eeee (New York City) contain similar provisions, but are different in two significant aspects:

1. **Eviction Plan Percentage.** In New York City, eviction plans cannot become effective until purchase agreements have been executed by at least 51 percent of the bona fide tenants in occupancy, **excluding** eligible senior citizens and disabled persons. In localities outside of New York City covered by Section 352-eee, a two-prong test is required, (i) purchase by at least 51 percent of the tenants, **excluding** senior citizens and disabled persons **and** (ii) 35 percent of all tenants **including** senior citizens and disabled persons.

2. **Non-Eviction Plan Percentage.** In New York City, a non-eviction plan may be declared effective when purchase agreements have been executed for at least 15 percent of the bona fide tenants in occupancy or by bona fide purchasers who represent that they intend to occupy the unit when it becomes vacant. Therefore, it is possible to implement a non-eviction plan without a single purchase by a tenant in occupancy. In locations outside of New York City governed by Section 352-eee, a non-eviction plan may not be implemented until at least 15 percent of the **bona fide tenants in occupancy** of the building have signed purchase agreements. Thus, the threshold requires purchase by at least the required percentage of tenants residing in the building.

The Condominium Act — Real Property Law, Article 9-B

For those projects selecting the condominium form of ownership, the relevant statute is Real Property Law, Article 9-b, known as the Condominium Act.

The purpose of the Condominium Act is to establish a uniform system for creating and operating condominiums in the State of New York. The Act sets forth the manner in which condominiums are organized and the essential documents and rules under which condominiums operate.

Attorney General Regulations

Occupied Cooperatives (Title 13) New York Code, Rules and Regulations (NYCRR) Part 18

Part 18 of the Regulations applies to offering plans for the conversions of occupied buildings to cooperative ownership. This Part describes the procedures for submission of an offering plan to the Department of Law and the material that should be included in the plan.

Newly Constructed and Vacant Cooperatives (13 NYCRR Part 21)

Part 21 of the Regulations applies to offering plans for the creation of a cooperative in a newly-constructed or vacant building. This Part likewise describes the procedures for submission and the contents of the plan.

Condominium Regulations

13 NYCRR Parts 20 and 23 describe the procedures for submission of, and formats for, offering plans involving newly constructed and vacant condominiums (Part 20) and occupied condominiums (Part 23).

Impact of Rent Laws

Residential housing in many parts of the State is subject to various rent regulation laws. These local

statutes also contain provisions regarding the rights of tenants in buildings undergoing cooperative or condominium conversion. In locations subject to such laws, the offering plan must link together the provisions of the local rent law together with those contained in the Martin Act and applicable regulations of the Attorney General.

It is essential for those involved in the conversion of an occupied building to know if the dwelling is subject to rent regulation laws. Buildings may be subject to the provisions of the Rent Control Law, to the Rent Stabilization Law, to the Emergency Tenant Protection Act and to more than one law (i.e., Rent Control and Rent Stabilization). Under the Omnibus Housing Act (OHA) of 1983, all of the rent regulating statutes throughout the State are now under the jurisdiction of the New York State Division of Housing and Community Renewal (DHCR). Although the administration of the laws has been centralized, local differences still apply in connection with cooperative and condominium conversions.

Types of Conversions

Occupied Buildings

1. Eviction Plans

In an eviction plan, a tenant who chooses not to purchase into the cooperative may be evicted after a certain time period by the purchaser of the shares allocated to his or her apartment. The provisions governing an eviction plan vary according to the location of the building and the rent laws in effect in that area. In New York City, for example, an eviction plan requires the purchase by 51% of the bona fide tenants in occupancy in the building.

Under the Martin Act, eligible Senior Citizens and eligible Disabled Persons are protected against eviction. An **Eligible Senior Citizen** is defined as a tenant who is 62 years or older. An **Eligible Disabled Person** is essentially defined as a tenant having a physical or psychological impairment which is expected to be permanent and prevents him/her from engaging in gainful employment. The definition excludes addictions to alcohol, gambling or any controlled substance.

As a result of changes in the law increasing the required percentage for eviction plans from 35 to 51% in areas where most conversions are occurring (i.e. New York City and Westchester County), combined with increased awareness by tenants of their rights under such offerings, eviction plans are now relatively rare.

2. Non-Eviction Plans

Under a non-eviction plan, non-purchasing tenants may not be evicted for failure to buy the shares allocated to their apartments. They may remain in their apartments as rental tenants, subject to existing rent laws and regulations. In general, an eviction plan can be declared effective when purchase agreements have been signed for 15 percent of the units.

Vacant Buildings

Buildings under construction or renovation which are vacant of any tenants may be sold as cooperatives or condominiums. In this case, the offering is made to the general public. These offering plans are less complex because issues regarding tenants rights do not apply. A sponsor can declare such a plan effective when it has purchase commitments for 15 percent of the apartments.

Tenant-Sponsored Plans

In many cases, low and moderate income tenants have organized and negotiated the purchase of their buildings from their landlord. In most situations, a majority but not all of the tenants have participated in the negotiation process. Not all of the tenants may want to buy into the building. Therefore, to convert the building to a cooperative, the tenants must comply with the provisions of the Martin Act. A tenant-sponsored offering plan is similar to other types of offering plans, except that the tenants set the purchase price of the shares themselves, establish the terms of the cooperative's

governing documents, hire their own engineer to prepare a report for the offering plan and allocate all of the funds received from the sale of the units toward the purchase or rehabilitation of the building (rather than as profit as in the case of a landlord-sponsor). In most cases, tenant-sponsored plans are also non-eviction plans.

New York City Sponsored Plans

The New York City Department of Housing Preservation and Development (HPD) has developed a standard offering plan for the sale of City-owned, occupied, multiple dwellings to the tenants of the buildings. Under HPD's Tenant Interim Lease (TIL) Program, a tenants association will initially manage the property under a lease from the City as the first step toward acquisition of the building under a City-sponsored cooperative offering plan. Several hundred buildings have been sold to tenants in the last ten years at \$250 per unit. The standard HPD Plan is an eviction plan that requires at least 60% of the residents to purchase shares in the cooperative. (See Chapter IV for a more detailed description of the City's low income cooperative program.)

Conversion Timetable

The steps and timing involved in the submission of a plan to the Department of Law are set forth as follows:

1. **Initial Submission of the Plan.** Before an owner, also known as the "sponsor", can convert an occupied, rental building, he must present a draft offering plan to each tenant and to the Department of Law. This plan constitutes only a preliminary prospectus of the proposed conversion. It is referred to as a "**red herring**" because the legend on its cover is printed in bold red lettering. Shares in the cooperative cannot be sold on the basis of a red herring. As the red legend on the cover of each plan indicates, the information contained in the red herring is subject to review and may be supplemented or changed by direction of the Department of Law.

After the red herring is submitted, the Department of Law may issue a list of proposed revisions or deficiencies. In the case of buildings occupied for residential purposes, the Department of Law is required to inform the sponsor within four to six months after the submission of the red herring of any modification or deficiencies. In the case of totally vacant buildings or new construction, a red herring is not required to be distributed and the Department of Law is required to issue its comments within 30 days of the submission of the proposed plan.

Once the Department of Law has reviewed the plan, and the sponsor has complied with any requested changes, the Department of Law will issue a letter indicating that the plan has been accepted for filing.

The revised final version of the plan, known as the "**black book**", is then reprinted and distributed to the tenants in occupied buildings and to prospective purchasers in the case of new construction and vacant buildings. In place of the red legend that appeared on the cover of the red herring, this plan has black lettering stating that the plan constitutes the sponsor's offer to sell cooperative or condominium units on the terms and conditions set forth in the plan.

2. **Presentation or Offering Date.** This is the date upon which the final offering plan or black book is given to the tenants or may be provided to the public in a new construction or vacant building project. From this point, the sponsor may accept signed purchase agreements from purchasers.

3. **Exclusive Purchase Period.** A tenant in occupancy at the time of the offering will have the exclusive right to purchase for 90 days from the presentation date.

4. **Matching Period.** After the expiration of the 90-day exclusive right to purchase, the tenant will be given the exclusive right for six months to match any bona fide offer made between the sponsor and an outside purchaser.

5. **Effective Date.** When the sponsor has received signed purchase agreements from the required

percentage of purchasers, it may declare the plan effective. By declaring the plan effective, the sponsor agrees to transfer the property to the cooperative or condominium. The plan is formally declared effective by notice to the tenants and by submission of an amendment to the plan filed with the Department of Law attesting that the requirements for effectiveness have been met. If a plan is not declared effective within 15 months of the date it was filed with the Department of Law, it will be deemed to be abandoned.

6. **Eviction Period.** Under an eviction plan, a non-purchasing tenant (other than an eligible senior citizen or eligible disabled person) may be evicted after the later of the following:

- a. Expiration of the tenant's lease;
- b. Three years after the date the Offering Plan is deemed effective.

Essential Areas of Disclosure in the Offering Plan

The regulations formulated by the Attorney General describe in detail what information must be disclosed by the sponsor. The following is a checklist of those items:

1. **Special Risk Factors.** Information regarding special risk or unusual circumstances must be highlighted. In a low income cooperative, for example, this would include highlighting that the ownership of shares is subject to income eligibility and restrictions on the re-sale and subletting of units.

2. **Purchase Prices and Share Allocations.** The total cash payment and the number of shares allocated to each apartment must be set forth in a schedule. The price per unit and number of shares is most often calculated proportionally based on the number of rooms or square footage per apartment. The schedules will also include the projected monthly maintenance for each apartment. In most cooperatives, the operating expenses are shared proportionally by the members based on the size of the space they occupy. The maintenance figures are obtained by dividing the total projected operating budget for the building by the number of shares in the cooperative. The per share amount is then multiplied by the number of shares allocated to a particular unit to determine the individual maintenance figures. (An exception to this found in the offering plans of New York City-owned buildings, in which all units are allocated 250 shares. The maintenance per apartment in these buildings is based not on the number of shares owned but by the number of rooms in the unit.)

3. **Projected Budgets.** The projected budget for the first year of operation must be set forth in a schedule that will include the typical expenses associated with operating a multiple dwelling. These are: Fuel, Utilities (for common spaces), Repairs and Supplies, Labor, Management Fee (if applicable), Insurance, Corporate Taxes, Real Estate Taxes, Water and Sewer Charges, Debt Service, Legal and Accounting and Reserve Funds.

4. **Attorney's Income Tax Opinion.** Shareholders of a cooperative are entitled to deduct for income tax purposes their proportional share of the real estate taxes and mortgage interest paid by the cooperative, if certain requirements are met pursuant to section 216 of the Internal Revenue Code. The key requirements under this section are that (1) 80 percent of the gross income of the cooperative must be derived from rent or maintenance received from the shareholders of the cooperative and (2) a reasonable relationship exists between the price paid for the unit and the total value of the Property or between the unit's share of real estate taxes and mortgage interest to the total cost of these items. If the cooperative desires to be covered by the proportion of taxes and interest method, it must do so by written election to the IRS. The offering plan must include an opinion from the Sponsor's attorney regarding whether the cooperative will qualify for section 216 deductions. Low income shareholders who do not itemize deductions will not benefit from this section of the Code.

5. **Opinion of Reasonable Relationship.** If the cooperative expects to utilize the benefits of Section 216 of the Internal Revenue Code, then the plan must include an opinion from a qualified real estate professional (such as a real estate broker) that the reasonable relationship tests will be met.

6. **Accountant's Certified Statement of Operation.** The plan must include certified statements

of income and expenses for the two most recent fiscal years of operation, prepared by the sponsor's accountant.

7. **Rights of Tenants.** The prospectus must include a description of the rights of eligible senior citizens and eligible disabled persons and non-purchasing tenants if it is an eviction plan and, for all plans, an explanation of the 90-day exclusive period for tenants to purchase and the six-month matching period.

8. **Purchase Procedures.** The Plan must contain an explanation of where to submit signed purchase agreements and downpayments and under what circumstances downpayments may be refunded. The downpayments must be held in trust by the sponsor pending the transfer of the property to the cooperative.

9. **Effective Date.** A discussion must be included of the percentage of purchase agreements required to declare the plan effective, whether eviction or non-eviction, and within what specified time period the property will be transferred to the cooperative.

10. **Financial Details of the Transaction.** A schedule must be included, showing the cash amounts to be raised by the offering; the amount of debt in the form of mortgages to be carried by the cooperative; the amount of working capital and reserve funds that will be available to the cooperative after the transfer of title; and the profit to the sponsor. The terms **working capital fund** and **reserve fund** refer to a fund of money left to the cooperative corporation from the proceeds of the offering. The New York City Administrative Code requires a minimum reserve fund of 3 percent of the total cash proceeds of the offering. This **reserve fund** may only be used for capital repairs, replacements and improvements to the property. A **working capital fund** is used to describe a fund that can be used for any proper corporate purpose. There is no legal requirement to establish a working capital fund.

11. **Terms of Mortgage.** Details of mortgages that will be the responsibility of the cooperative corporation must be described, including the amount of the mortgage, term, interest rate, monthly payments and whether the mortgage is completely self-amortizing or will require a "balloon" payment on the due date. A **balloon** mortgage is one in which all or a part of the principal is payable on the due date of the loan.

12. **Low Income Provisions.** Any provisions, covenants or agreements regulating the use and occupancy of the units to maintain long-term affordability must be explained. These may include, for example, covenants in a deed from a municipality; a regulatory agreement with the New York State Housing Trust Fund; and provisions in the cooperative's governing instruments, relating to the re-sale of the property and individual units. (See Chapter IV for a discussion of the various types of provisions found in low income cooperatives).

13. **Identity of the Parties.** Disclosure must be made of the names, business addresses, backgrounds and experience of the sponsor and principals of the sponsor.

14. **Proceeds of the Sale.** The profit, if any, to be made by the sponsor must be disclosed.

15. **Description of Building Condition.** A licensed architect or engineer, hired by the sponsor, must prepare a report describing the physical condition of the property. The report is required to disclose all defective conditions found and those that are hazardous or require immediate repair. The report should describe the use and location of the property; the status of construction; the condition of the structural system, including foundation, walls and roof; the condition of the plumbing, heating and electrical systems; results of inspections of typical units; and an analysis of, and recommendations for, removal of asbestos in the building. The tenants may hire their own professional to inspect the property to obtain an independent opinion.

Documents in the Offering Plan

Copies of essential documents relating to the purchase of shares and to the operation of the cooperative must be reproduced in the offering plan. They are:

1. **Purchase Agreement.** (also known as Subscription Agreement). The agreement between the sponsor and the prospective shareholder specifying the terms and conditions of the purchase of shares in the cooperative. Before a sponsor can declare a plan effective, he must obtain the required percentage of signed purchase agreements. The Purchase Agreement contains the name of the purchaser, the number of shares, the apartment number, the price of the shares and the downpayment required (typically, the downpayment is 10 percent of the purchase price). The Agreement commits the purchaser to complete the transaction by paying the balance due prior to the transfer of the property to the Apartment Corporation and to sign a proprietary lease for the apartment. The Agreement is contingent on the plan being declared effective and the downpayment must be held in escrow by the sponsor's attorney pending the transfer of the building. The Agreement stipulates that the purchaser has inspected the apartment and has accepted the existing, or "as is", condition of the unit. If the sponsor, however, has agreed to made certain repairs, this must be specified in the agreement. Otherwise, the sponsor will not be responsible for repairs within the apartment after the closing date. In the event of default by the purchaser, the Agreement specifies that the damages shall be loss of the downpayment.

2. **By-Laws.** The by-laws set forth the rules under which the cooperative corporation governs itself. The by-laws detail the procedures for holding annual and special meetings of shareholders, including notice, quorum, voting and proxy requirements and the order of business at the meeting. The by-laws contain general rules on the issuance of proprietary leases and shares of stock. The by-laws describe the books and records required to be kept by the corporation, rules involving transactions with directors and officers and the method for amending the by-laws. (See Chapter V, **Operation of the Cooperative** for a further discussion of the role of the by-laws in the operation of the cooperative).

3. **Proprietary Lease.** (also known as **Occupancy Agreement**). The Proprietary Lease is the agreement between the cooperative corporation and each of its shareholders setting forth the rights and obligations of the parties concerning the shareholder's use and occupancy of the apartment. The Proprietary Lease contains provisions relating to the obligation to pay maintenance; responsibility for repairs; use of the premises; sub-letting; alterations; transfer of ownership; and events of default. Annexed to the Lease are House Rules which govern the use of public halls, roofs and common areas; prohibit disturbing noises and the playing of musical instruments or electronic equipment during night-time hours; and regulate the disposal of garbage, the keeping of pets and other details of living in a multiple dwelling.

4. **Election Forms for Senior Citizens and Disabled Persons.** In the case of an eviction plan, the Offering Plan should contain election forms to be submitted to the sponsor by those eligible senior citizens and disabled persons who do not wish to purchase. The forms must be submitted within 60 days after the presentation of the Plan to the tenants. The submission of an election form does not preclude the tenants from later purchasing the unit on the same terms offered to tenants in occupancy during the exclusive purchase period.

5. **Applicable Laws and Regulations.** To the extent that they apply to a particular offering, the Plan should contain reproductions of relevant sections of the General Business Law and local rent laws and regulations.

No Action Letters

General Considerations

Preparation of an Offering Plan entails considerable time and expense. If every potential low income cooperative was required to file an offering plan, many of these projects would be crippled from the outset. In recognition of the need to encourage the development of affordable housing, however, the

Attorney General has formulated regulations and guidelines permitting low income cooperatives to obtain waivers known as **no action letters**.

Upon application made in accordance with Part 18.9 of the Attorney General regulations, the Department of Law may, in its discretion, issue a no action letter stating that it will not take any enforcement action despite the fact that no offering plan has been prepared for the project.

A no action letter may be issued where the Department of Law determines that the potential cooperative members do not require the protection of an offering plan; or that the participants are aware of the condition of the property; or that the filing of an offering plan is not necessary to effectuate the purposes of the Martin Act or to protect the public interest.

Low Income Cooperatives

In situations involving low-income cooperatives, the Department of Law has looked to certain guidelines as conditions for issuing no action letters. These conditions are:

1. The cooperative is organized as a Housing Development Fund Corporation (HDFC);
2. All of the participants in the cooperative agree to join in the application for the no action letter;
3. The purchase price of the individual units is less than \$10,000; and
4. The governing documents of the cooperative contain re-sale restrictions insuring long-term affordability of the apartments.

Application Procedure

The application consists of affidavits from the cooperative members and a transmittal letter from the group's attorney. An Affidavit must be submitted to the Department of Law by each member of the cooperative. The following sets forth the essential information to be included in the affidavits:

1. Name and address of the cooperative member
2. The specific unit being offered and the total number of units in the building
3. A description of the proposed project
4. The purchase price of the unit
5. A statement that the member is aware of the physical condition of the building and the plans for rehabilitation, if any.
6. A statement that the member has read and understood the restrictions on the re-sale of units.
7. A schedule listing the names of the cooperative members, the apartments being offered and the number of shares allocated to each apartment.
8. A statement that the Corporation [or sponsor] shall provide to each member a schedule of the
 - a. amount of money required to purchase shares in the Corporation;
 - b. the estimated maintenance for the apartment and the current or proposed budget for the first year of occupancy;
 - c. a copy of the mortgage encumbering the property;
 - d. a copy of the most recent financial statement of income and expenses for the operation of the property;
 - e. any information which may result in extraordinary expenses for shareholders or for the corporation including, but not limited to, assessments, liabilities, dangerous or hazardous conditions, pending litigation and administrative proceedings;
 - f. such other information as the Department of Law may require to be presented to each member.
9. A statement describing the property's legally permissible use.
10. A statement disclosing whether the Corporation or any of the members have participated in any other applications for no action letters or have made any other offerings regarding the property in the preceding five years.
11. A statement that prior to the closing on any individual units, the corporation will obtain a further affidavit from each member containing representations that
 - a. the member has read the application for a no action letter;
 - b. the member understands that no offering literature other than that required by the no

action letter will be provided and that if the project constituted a public offering within the meaning of the provisions of the General Business Law, he/she would be entitled to protections under the Law; and

c. the member has inspected the property.

Transmittal Letter

A transmittal letter signed by the attorney who prepared the application must be submitted stating:

1. The reasons why the transaction described in the affidavits meets the standards set forth by the Department of Law;
2. That the attorney has no actual knowledge of any omission or untrue statements of a material fact included in the application; and
3. That the attorney has prepared or has reviewed all legal documents necessary to form a cooperative and, in the attorney's opinion, the cooperative is duly organized, validly existing and in good standing.

A filing fee of \$150 must accompany the application. The Appendix includes a sample application for a no action letter.

CHAPTER IV

THE LIMITED EQUITY COOPERATIVE

The critical need of low-income people for affordable housing has required the development of innovative strategies to deal with the overwhelming burden of paying for a decent place to live. One such strategy is the limited equity cooperative, a phenomenon that has undergone a rapid evolution in the last decade.

Definition

A limited equity cooperative can be defined as a housing cooperative in which low income eligible members purchase shares at below market prices and are subject to limitations on the amount of equity or profit they can receive on the re-sale of their units. The term "low income" cooperative is also used to characterize this type of housing organization.

Purpose

The limited equity cooperative is designed to provide and maintain affordable housing for low income people over a long period of time. By building in mechanisms that regulate the price of the apartments, the cost of the units become insulated from market forces. In most cases, the construction or rehabilitation of the cooperative building is subsidized by grants and low interest loans from government agencies and foundations. This enables the purchaser to buy an apartment for a low cash outlay. This initial low price combined with restrictions on the re-sale of the unit, maintains the apartment within the range of affordability for future low income purchasers. A variety of programs, both public and private, have been created in the New York using the limited equity cooperative as its basic model. Although all of the programs incorporate mechanisms for achieving the goal of affordable housing, each has developed its own particular design. Some of these programs are described below, illustrating the different ways in which limited equity cooperatives can operate.

Limited Equity Cooperative Programs

Description of Program

Enacted in 1985 as Article XVIII of the Private Housing Finance Law, the Low-Income Housing Trust Fund provides funds from New York State for the rehabilitation and construction of housing for persons of low income, including low income cooperatives and condominiums.

Eligibility

For cooperative and condominium projects, those eligible to purchase units in the project are persons of low income, defined as persons and families whose incomes do not exceed eighty percent of the area median income for projects in New York City, and ninety percent of median income for most upstate projects. Eligible properties are those that are vacant or underoccupied and are located in blighted areas.

A sponsor, such as a not-for-profit organization, can build the project using Housing Trust Fund monies and then sell the units to eligible individuals and families.

Initial Equity

No specific limit is placed on the purchase price for the initial purchasers, but prices are required to be affordable to low income persons or families and are usually set by sponsors at well below market rates, with typical prices ranging from \$250 to \$1,500 per unit.

Re-Sale Provisions

For a Housing Trust Fund cooperative project, the shares applicable to a cooperative unit may be transferred or sold only to an eligible low income individual or family and the resale price may not exceed the sum of the following items:

1. the **original cash equity** paid by the shareholder, with interest at the rate of six percent per year; plus
2. the cost of **capital improvements** to the unit paid by the shareholder after completion of the original construction or rehabilitation, with interest at the rate of six percent per year; plus
3. the pro-rata portion of any **assessments** for building-wide improvements paid by the shareholder, with interest at the rate of six percent per year; plus
4. the pro-rata portion of actual **amortization** (principal) paid by the shareholder on the project's mortgages, with interest at the rate of six percent per year; plus
5. the actual **amortization** (principal) paid by the shareholder in reduction of his own loans used for the purchase, construction, rehabilitation or improvement of the unit, with interest at the rate of six percent per year; plus
6. the actual outstanding **balance on all loans** used by the shareholder for the purchase, rehabilitation, construction or improvement of the unit which the shareholder is required to satisfy upon resale; plus
7. the **reasonable costs and expenses** incurred in connection with the resale of the shares allocated to the unit. (The allowance of the six percent increments described above was added by the legislature after June, 1988. Resale provisions in projects that received Housing Trust Fund commitments prior to June, 1988 do not contain the six percent increments.)

Under the terms of the Housing Trust Fund Regulatory Agreement, the resale provisions must be complied with generally for a period of thirty years. Similar resale provisions are applicable to condominium projects.

Other Restrictions

Each shareholder must certify that he intends to occupy the unit as his principal and primary place of residence. Sublets of the unit may only be to eligible low income persons and the cooperative may only approve a sublet if the rent on the sub-lease does not exceed the shareholder's actual monthly maintenance and principal and interest payments for loans on the apartment. In addition, the sublease rent may not exceed thirty percent of the income of the subtenant.

New York City Programs

Tenant Interim Lease (TIL) Program

Description of Program

The TIL program provides organized tenant groups in City-owned multiple dwellings the opportunity to lease, manage and then buy their buildings as low income cooperatives. Under the TIL program, the tenants self-manage the building under a lease from the City's Department of Housing Preservation and Development (HPD). After a period of hands-on experience and training provided by the Urban Homesteading Assistance Board (UHAB), a City-wide technical assistance organization, the tenants are presented with a City-sponsored cooperative offering plan.

Eligibility

The cooperative must be organized and operated as a Housing Development Fund Corporation. The Offering Plan requires that at least 60 percent of the tenants sign purchase agreements before the building can be sold to the corporation. The HPD offering plan is an eviction plan, which means that non-purchasing tenants, except for eligible senior citizens and disabled persons, are subject to eviction upon the expiration of the time period specified in the plan.

Initial Equity

Under the HPD plans, the price is set at \$250 per unit. For those tenants on public assistance, lump-sum grants are available from the Department of Social Services for the purchase of the units.

Re-Sale Provisions

The HPD plan contains no formula or cap on the re-sale price of apartments. The only restriction relating to affordability is that units must be sold to low income persons as defined by section 576 of the Private Housing Finance Law. Under the law, the **income** of persons or families seeking to purchase units in the building may not exceed six times the annual maintenance, plus utilities, for the apartment. The ratio is seven times the annual maintenance plus utilities for families with three or more dependents. For example, if the annual maintenance plus utilities for an apartment is \$4,200 per year (\$350 per month), then the income limitation for an eligible purchaser is \$25,200 or \$29,400 for a family with three or more dependents.

The definition of a low income person under section 576 has remained the same for 20 years. Because maintenance costs have escalated faster than incomes, the standard under the law may no longer be an accurate measure of what constitutes low income.

Although there is no ceiling on the re-sale price (other than the unit must be sold to a low income person), the HPD plans do place limits on how much of the profits can be retained by the selling shareholder. Depending upon the appraised value of the building prior to the cooperative conversion, HPD has two types of basic structures regulating the re-sale of apartments.

60-40 Plans. If, prior to the date the building is sold to the cooperative, HPD determines that the appraised value of the building exceeds \$2,000 per dwelling unit, then upon the re-sale of an individual unit, the proceeds for a period of twenty-five years must in most cases be divided as follows:

1. the selling shareholder receives his original purchase price;
2. the City receives 40 percent of the profits of the re-sale. Profits are defined as the sales price minus the initial purchase price paid by the selling shareholder;
3. after crediting the Seller for special assessments for building-wide improvements, the remaining 60 percent of the profits is divided 25 percent to the Seller and 75 percent to the cooperative during the first ten years and 50-50 between the cooperative and the Seller during the remaining 15 years of the restriction period (unless a different distribution is approved by the shareholders pursuant to an amendment to the By-Laws). The cooperative's share is retained by the Corporation as a fund for capital

and operating expenses.

At the time the building is sold by the City to the cooperative, HPD will place a lien on the property in the form of a security agreement to insure payment of its 40 percent share.

The HPD plans also contain restrictions on the sale of the entire building by the cooperative corporation. Most buildings now sold by HPD under the TIL program contain 60-40 provisions.

Standard TIL Plans. Prior to the introduction of the 60-40 structure, HPD sold buildings under the TIL program containing re-sale restrictions effective for a period of ten years from the date of the closing on the building. Under this plan, the City receives no share and the proceeds are divided as follows:

For the first **two** years from the purchase of the building by the cooperative, the selling shareholder receives from the proceeds of the sale:

1. the original purchase price;
2. the amount of special assessments for building-wide capital improvements, if any, that the corporation has levied upon, and collected from, the selling shareholder;
3. the amount spent for capital improvements to the individual unit that the selling shareholder can document to the satisfaction of the corporation; and
4. the remaining balance is retained by the corporation as a reserve for capital and operating expenses, unless three-fourths of the shareholders approve an allocation of up to 30 percent of the balance to the selling shareholder.

For the remainder of the ten year period, a selling shareholder may receive his **original purchase price**, his share of **special assessments, capital improvements** to his unit and **fifty** percent of any profit. The other fifty percent goes to the cooperative. The shareholders may amend the by-laws to further limit the portion and amount allocated to the selling shareholders for capital improvements and profit.

Community Management Buildings (N.Y.C.)

Community Management buildings are those buildings which have been managed, not by tenants, but by a not-for-profit community organization under contract with HPD prior to cooperative conversion. These buildings typically have received greater amounts of City funds for repairs and capital improvements than TIL buildings. The HPD offering plans are similar, except that the re-sale provisions apply for 15 years; the selling shareholder cannot receive any profit for the first three years; reimbursement for capital improvements to individual units is limited to \$1,500 and the allocation of profits after three years is 30 percent to the shareholder and 70 percent to the cooperative.

Homesteading Program (N.Y.C.)

Under the homesteading program, vacant City-owned buildings are sold to organized groups of low income people. Each homesteading association must agree to rehabilitate its building with voluntary labor (known as sweat equity) and funds borrowed usually from a combination of city, state, and private sources, including foundations.

Eligibility

The group must be organized and operated as a cooperative under the Housing Development Fund Corporation statute. All of the members must join with HPD in application for the issuance of a no-action letter from the Department of Law, thus avoiding the requirements of an offering plan.

Initial Equity

The buildings are sold by HPD at \$250 per unit. In addition, the groups usually collect membership dues (also known as license fees) from its members during the planning and construction period. These dues are typically \$50 to \$100 per month and are used to cover basic costs for tools and materials for the

sweat equity work and for other ongoing expenses.

Re-Sale Provisions

Units may only be re-sold to eligible low income people under the same definition previously described under the New York City TIL Program.

The homesteading program mandates a 15 year compliance period regulating the re-sale of units. Within the first three years from the date of the original conveyance by the City to the cooperative, a selling shareholder may receive from the sale of a unit the **original purchase price**; all **license fees (membership dues)** paid by the shareholder to the homesteading association; the amount of **special assessments** for building-wide capital improvements that the cooperative has levied upon and collected from the selling shareholder; and the amount spent by the shareholder for **capital improvements** to the unit. The balance, if any, is retained by the cooperative.

For the remainder of the 15 year compliance period, the selling shareholder may receive from the proceeds of a sale, the **original purchase price; license fees or membership fees; special assessments; capital improvements** to the unit; and 30 percent of the balance. The cooperative will retain the remaining 70 percent of the balance. The shareholders may vote to amend the corporation's by-laws to increase the share to be retained by the cooperative on re-sales.

Many homesteading projects are rehabilitated through monies provided by the Housing Trust Fund (HTF). Since HTF regulations place a limit on the re-sale price, the groups must follow the more restrictive HTF rules in determining the re-sale value of a unit.

Other Government Programs

Other municipalities in New York State, such as the City of Rochester projects described in Chapter II, have played a role in the development of limited equity cooperatives. These projects have combined local, state and federal funds including federal community block grant funds and section 312 loan monies and State Housing Trust Fund monies. Since most of the projects utilize Housing Trust Fund monies, the re-sale provisions follow the Trust Fund statutory mandates described earlier in this chapter.

Private Not-for-Profit Programs

Several not-for-profit organizations in New York City have taken the lead in organizing low income cooperatives. The Lower East Side Catholic Area Conference (LESAC), for example, has negotiated with the City on behalf of many groups seeking to purchase vacant buildings, and has provided assistance in obtaining rehabilitation funds, supervising construction and training homesteaders in cooperative management.

LESAC has developed a re-sale policy for its groups that is different in one key factor not found in most other cooperative models. The usual procedure permits a selling shareholder to obtain his own buyer (subject to cooperative approval) and negotiate his own sale price. In the LESAC model, the selling shareholder must offer his shares back to the cooperative at a price set by a pre-determined formula. The goal is to provide stricter controls to preserve the affordability of the units.

LESAC Re-Sale Provisions

1. **Restrictions on Transfer.** A shareholder must offer his shares back to the cooperative. Only in the event that the cooperative declines the offer can the shareholder seek an outside buyer.

2. **Transfer Value.** The price to be paid by the cooperative for the shares is calculated by a **transfer value** formula. The transfer value is the sum of the following items:

- a. license fees (membership dues) paid by the shareholder;
- b. original purchase price (typically \$250 per unit);
- c. amount of special assessments for building-wide capital improvements levied upon the

selling shareholder; and

d. the amount spent by the selling shareholder for capital improvements to the individual unit, as approved by the cooperative.

3. **Vesting.** A selling shareholder must be a member in good standing of the cooperative for a period of three years to receive the transfer value of his shares.

In practice, the cooperative will obtain a new buyer who will provide the funds at a simultaneous closing to pay the departing shareholder.

Community Service Society

The Community Service Society (CSS) is a not-for-profit organization in New York City providing a wide variety of social services. One such service is the Ownership Transfer Project, a program that works with tenants in privately-owned occupied buildings. The project has worked with low income tenants seeking to buy their buildings from owners.

Many of the buildings assisted by CSS are those that were involved in ongoing landlord-tenant battles which culminated in rent strikes or the appointment of administrators by the court. In such circumstances, the economic value of the property becomes eroded, providing the tenants with the leverage to negotiate a purchase.

The Ownership Transfer Project helps in negotiating the purchase, securing acquisition and rehabilitation funds and assisting in cooperative management training. One goal of the program is to limit the initial apartment prices to no more than \$2500 per unit, the maximum amount that the Department of Social Services will pay a public assistance recipient to buy a cooperative apartment.

CSS Re-Sale Policy

CSS requires that groups assisted by it agree to maintain re-sale restrictions in the cooperative's governing documents. Under the CSS formula, re-sale prices of apartments must be limited to the sum of the

1. original purchase price
2. ten percent of the original price of the apartment for each year from the original purchase (compounded annually);
3. the shareholder's pro rata share of principal paid on building mortgages; and
4. the amount for improvements to the individual unit, approved by the cooperative, and limited by a pre-determined cap on the value of a particular improvement. The standard used to calculate the value of the improvements is the guidelines established under New York City's real estate tax abatement (J-51) program.

Urban Homesteading Assistance Board

The Urban Homesteading Assistance Board (UHAB) is a not-for-profit organization in New York City providing a wide range of services in the development and management of limited equity cooperatives. UHAB provides management training and technical assistance to new homesteading groups as well as to operating cooperatives. UHAB can furnish assistance to cooperatives seeking to develop and understand re-sale policies.

Subletting Policies

Many low income cooperatives are faced with the problem of individual shareholders who wish to sublet their apartments for a profit. In most cooperatives, the maintenance charges are lower than market rent for a similar unit. Unrestricted subletting can undermine the original purpose and philosophy of the limited equity cooperative. At the same time, a shareholder may have a legitimate need to sublet his unit for a period of time. To balance the various interests involved, many cooperatives have adopted

subletting policies to regulate such activity. A model developed by the Lower East Side Catholic Area Conferenc (LESAC) has been used by a number of low income buildings.

LESAC Subletting Provisions

Under this model, all sublet approvals by the cooperative board are subject to the following conditions:

1. the sublease rent must be the same as the maintenance charges for the apartment
2. the subtenant is required to perform all maintenance duties of the prime shareholder
3. the subtenant must pay his rent directly to the cooperative
4. the subtenant must pay a security deposit of one month's maintenance
5. the sublease may not be for a term longer than one year
6. the written lease to be used must be approved by the Board before it can be signed.

CHAPTER V OPERATION OF THE COOPERATIVE

Initial Organization

Planning for the operation of the cooperative must take place well before the formal transfer of ownership to the shareholders. The sponsor should be aware of the critical need to provide training in the operation of a cooperative to the new tenant-owners of the building.

After title to the property has been transferred to the cooperative, the legal organization of the corporation must be structured to insure that:

1. the management of the building will be run on an orderly and fiscally sound basis; and
2. the decision-making process will be based on a democratic foundation.

First Meeting of Shareholders

The initial legal step to achieve these goals is the first annual meeting of shareholders. The primary purpose of this shareholders' meeting is the election of the board of directors. The board serves as the democratically-elected representatives of the shareholders. The board members are chosen for one-year terms, but the shareholders reserve the power to call special meetings to change directors. Each year, the shareholders must come together for a meeting to elect directors for the coming twelve months.

First Meeting of Board of Directors

Under the standard by-laws, the officers of the corporation (president, vice-president, secretary, and treasurer) are elected by the board of directors. For this reason, a meeting of the newly-elected directors should take place immediately or soon after the shareholders' meeting. It is customary for the officers to be selected from among the members of the new board. Thereafter, the officers and directors are responsible for the day-to-day operation of the cooperative.

Responsibilities of the Board

One of the first legal responsibilities of the board is to make certain that all stock certificates and proprietary leases have been properly executed and distributed to the shareholders.

- ✗ preparing the annual budget
- ✗ fixing the monthly maintenance charges
- ✗ maintaining financial and other corporate records
- ✗ providing financial and other reports to shareholders on a regular basis
- ✗ collecting the maintenance charges from shareholders and rent from commercial tenants, if any
- ✗ paying the bills of the corporation
- ✗ hiring maintenance employees, managing agents and professional experts
- ✗ maintaining and repairing the common spaces, building structure and building-wide systems (electrical, plumbing, heating)
- ✗ approving apartment alterations and sub-leases
- ✗ supervising the sale of apartments and approving new members
- ✗ insuring compliance with income limitations and re-sale provisions and governing documents of the cooperative
- ✗ enforcing shareholder obligations under the proprietary lease
- ✗ attending to any litigation involving the cooperative
- ✗ mediating disputes between shareholders

Rights and Obligations of Shareholders

The underlying rationale of a cooperative's legal structure is to achieve a balance between the individual shareholder's rights as the owner of his own home and the need to protect the interests and rights of the rest of the members.

Summary of Rights

As members of the cooperative, shareholders receive the right:

1. to permanent, long-term occupancy of the apartment. The term is typically 99 years and can be renewed by the shareholders residing in the building when the proprietary lease expires.
2. to sell their shares and assign their proprietary leases, subject to compliance with re-sale provisions and procedures and the consent of the board of directors.
3. to make capital improvements and alterations in their apartments, subject to procedures and requirements of the lease and consent of the board.
4. to use the shares and proprietary lease as security for personal loans, subject to the consent of the board.
5. to sublet their apartments, subject to the consent of the board.
6. to participate in the affairs and operation of the cooperative through shareholder meetings and elections and through membership on the board of directors and/or committees.
7. to take a pro rata share of the corporation's real estate taxes and mortgage interest payments as personal income tax deductions, subject to the provisions of section 216 of the Internal Revenue Code.
8. to receive annual financial statements and to inspect the corporation's books and records.

Summary of Obligations

As members of the cooperative, shareholders have the obligation

1. to pay the monthly maintenance or carrying charges as fixed by the board of directors.
2. to abide by the terms and conditions of the proprietary lease and the cooperative's by-laws.

Major breaches of the lease which can result in forfeiture of the shares and eviction from the apartment are:

- a. default in maintenance payments
- b. unauthorized sale, subletting or occupancy of the apartment

- c. objectionable conduct in violation of the house rules (i.e. pattern of excessive noise at late hours which disturbs neighbors)
- 3. to pay the cost of repairs and decorating (i.e. painting) within the apartment.

By-Laws of the Cooperative

The by-laws set forth the rules for governing the cooperative corporation. Except as mandated by law or controlled by provisions in the certificate of incorporation, the by-laws regulate most aspects of the corporation's operation. The by-laws usually track the rules for conducting the affairs of a corporation set forth in the New York Business Corporation Law and may not contradict the provisions of this statute.

The explanations that follow of by-law provisions describe prevailing practices, but by-laws may vary in different buildings.

Specific Provisions of the By-Laws

Meetings of Shareholders

The by-laws will describe procedures and requirements for conducting meetings of shareholders. The key provisions include,

1. **Place of Meeting.** At the cooperative or at such place specified in the notice of meeting.
2. **Annual Meetings.** A meeting of shareholders must be held at least once per year for the election of directors. The by-laws must specify when the annual meeting is to be held.
3. **Special Meetings.** Typically, By-laws will specify when and how special meetings may be called. Special meetings of shareholders may be called by the president, by the board of directors or by a specified percentage of shareholders (usually 25 percent).
4. **Notice of Meetings.** By-Laws will specify how notice of meetings shall be given. For example, written notice of the annual meeting must be given personally or by mail to each shareholder not less than ten nor more than forty days before the meeting. Written notice of a special meeting also must state the purpose of the meeting. The attendance of a shareholder at a meeting without protesting the lack of proper notice shall constitute a waiver of the notice by that shareholder.
5. **Quorum.** The definition of quorum will be specified. Usually, a majority of the shareholders, in person or by proxy, will constitute a quorum.
6. **Voting.** The general rule for cooperatives is to permit shareholders to vote according to the number of shares owned by them. In electing directors, most cooperatives utilize what is known as **cumulative voting** in which each shareholder may cast a cumulative total of the number of shares he owns multiplied by the number of directors to be elected. This total number of votes may be distributed by the shareholder in any manner he chooses among the candidates for election. In an effort toward more democratic representation, many limited equity cooperatives contain provisions in their certificate of incorporation providing for one vote per apartment, regardless of the number of shares owned by the shareholder.
7. **Eligibility to Vote.** Any restrictions on voting eligibility will be included in the By-Laws. Many cooperatives for example, require shareholders to be current in their maintenance charges to be eligible to vote.
8. **Proxies.** Most by-laws will permit a shareholder to appoint another person to vote at a meeting in his/her behalf. This appointment, known as a proxy, must be submitted to the corporation's secretary prior to the start of the meeting and it must be in writing, signed by the shareholder, but need not be notarized or witnessed.
9. **Order of Business.** The order of business at all regularly scheduled shareholder meetings will be specified, generally in the following order:
 - a. call to order; determination of quorum

- b. proof of notice of meeting
- c. reading of minutes of preceding meeting
- d. reports of officers
- e. reports of committees
- f. election of directors (if annual meeting)
- g. unfinished business
- h. new business
- i. adjournment

Directors of the Corporation

The business of the corporation must be managed under the direction of its board of directors. By law, it is improper for the directors to defer corporate decisions to the shareholders. If an issue is particularly controversial, the directors may call a shareholders meeting to hear opposing arguments and to seek a consensus, but the determination of the issue must be made by a vote of the Board.

The key by-law provisions relating to directors are:

1. Number and Qualifications. The number of directors must be specified (usually an odd number to avoid tie votes) and may not be less than three. Directors must be shareholders who are at least 18 years of age. Many cooperative by-laws provide that no more than one director may be elected from any one household or family.

2. Powers and Duties. The Board must determine the cash requirements needed to operate the cooperative and must fix the monthly maintenance charges to be paid by each shareholder. The Board has the power to prescribe the manner of maintaining and operating the building. Every such determination will be final and conclusive as to all shareholders and any expenditures made by authority of the Board will be deemed necessary and proper.

3. House Rules. The Board may adopt and amend such House Rules as it may deem necessary for the health, safety, convenience and enjoyment of the shareholders.

4. Election of Directors. Directors should be elected at the annual meeting of shareholders and serve for a term of one year.

5. Resignation and Removal. Any director may resign by delivering a written resignation to the office of the Corporation. Most by-laws provide that a director may be removed from office at any duly called regular or special meeting of the shareholders and a successor may then be elected to fill the vacancy. Vacancies resulting from the resignation or death of a director generally may be filled by a vote of the remaining directors until the next annual meeting of the shareholders.

6. Regular and Special Meetings of the Board. Regular meetings of the Board may be held at such times as determined by the directors, but no less than four times per year. In most cooperatives, the Board will meet monthly, or more often, depending upon the decisions it must confront. Notice of a regular meeting must be given to each director personally or by mail or telephone at least two days prior to the meeting. Special meetings may be called by the President or by the request of ten percent of the directors on one day's notice. At all meetings, each director shall be entitled to one vote.

7. Quorum. A majority of the directors constitutes a quorum for the transaction of business.

Officers of the Corporation

The individuals responsible for the day-to-day functioning of the cooperative are the officers of the corporation. As is the case for most corporations, the officers of a cooperative are selected by the board of directors, not by the shareholders. They are usually chosen from among those individuals who have been elected to serve on the board. Cooperatives may choose to hire managing agents to perform many of the tasks of operating a building, but the directors and officers are still the chief management officials. The key by-law provisions relating to officers are:

1. Designation. The principal officers of the Corporation are the President, Vice President, Secretary and Treasurer and they must be shareholders of the cooperative.

2. Election of Officers. The officers should be elected by the Board at the first meeting of the Board following the annual meeting of shareholders and hold office for one year terms. Officers may be removed by a majority vote of the Board.

3. Duties of President and Vice President. The President presides at all meetings of the shareholders and of the Board of Directors. The president or vice president must sign all contracts, leases, mortgages and other instruments which are authorized by the Board. The president, subject to the control of the Board, has the general management authority over the affairs of the Corporation. In the event that the president is absent or cannot perform his duties, the vice president shall have the power to exercise the duties of president.

4. Duties of Treasurer. The treasurer is responsible for the funds of the corporation and for depositing such funds in the Corporation's bank account. He is responsible for keeping full and accurate accounts of all receipts and disbursements in the books of the corporation and for furnishing financial reports to the shareholders.

5. Duties of Secretary. The secretary is responsible for maintaining the general files of the Corporation. He must keep the minutes of the meetings of directors and shareholders and is responsible for providing to shareholders and directors notices of meetings. The secretary also must maintain a record book containing the names of shareholders, numbers of shares owned, when acquired, price paid for the shares and other information needed to calculate the distribution of re-sale proceeds.

Fiscal Management of the Corporation

The by-laws contain basic procedures for maintaining the financial records of the Corporation.

1. Books and Accounts. Books and accounts of the Corporation must be kept under the direction of the Treasurer in accordance with generally accepted accounting procedures.

2. Auditing and Annual Reports. At the close of the year, the books and records of the Corporation must be audited by an accountant. (The hiring of a certified public accountant (CPA) for this purpose is recommended, but not required). Based upon the accountant's report, the Corporation must furnish shareholders with an annual financial statement, including the income and expenses of the Corporation. The shareholders also are entitled to a statement showing each member's pro rata share of real estate taxes and mortgage interest paid by the Corporation during the preceding year.

3. Examination of Books. All shareholders have the right to inspect the books, records, documents and accounts of the Corporation, at reasonable times at the office of the Corporation.

4. Signing of Checks. It is advisable for all cooperatives to follow the customary practice of requiring the signatures of at least two officers on all checks, usually the president or vice president and countersigned by either the secretary or treasurer. No officer should sign a check without knowing what expense the check is to cover.

Compensation of Directors and Officers

Most low income cooperatives provide that no compensation be paid to directors or officers for their services as directors and officers. No remuneration may be paid to a director or officer for services performed by them in any other capacity, unless a resolution authorizing such payment is approved by the board before the services are undertaken.

Transactions with Directors and Officers

The directors and officers are elected by the shareholders and owe a duty to act on their behalf. Directors and officers should manage the cooperative in a manner that is free from even the appearance of self-interest. The by-laws should provide rules that must be followed to avoid accusations that directors acted for personal gain rather than for the benefit of the members. Typical provisions are as follows:

1. **Loans to Directors and Officers.** Loans to directors, officers and shareholders are prohibited.
2. **Dividends.** The Corporation may not pay dividends or distribute any of its income or profits to any of its shareholders, directors or officers. **All funds received by the cooperative must be used to pay the expenses of operation, undertake capital improvements or to establish reserves.**

3. **Contracts with Directors and Officers.** Contracts between the Corporation and any director to provide services to the cooperative may only be valid if the board approves the contract without counting the vote of the interested director and full disclosure is made of the director's interest in the transaction. In the alternative, the shareholders may authorize such a contract, if full disclosure is made.

Indemnification of Directors and Officers

In general, directors and officers of a corporation are not personally liable for claims involving the Corporation if the director or officer acted in good faith for a purpose he reasonable believes to be in the best interest of the Corporation. The by-laws may provide for the corporation to indemnify, or reimburse, such director or officer against personal judgments or claims arising out of the performance of his corporate duties. However, a director or officer may be personally liable if he performs his responsibilities in a negligent or unlawful manner. Most such situations involve loose supervision over or improper handling of the corporate funds.

Amendments to the By-Laws

The manner in which by-laws may be amended varies among cooperatives. Some provide that only the shareholders may amend the by-laws, while other buildings permit amendments by either the shareholders or directors, with the percentage of votes needed to approve an amendment ranging from a majority up to 75 percent.

The Proprietary Lease

The proprietary lease (or occupancy agreement) is the basic agreement between the cooperative corporation and each of its shareholders. The lease is long term, typically 99 years, and establishes the rights and obligations of the parties concerning the shareholder's use and occupancy of the apartment. One master form is used for the cooperative, with the corporation and each shareholder signing an individual copy.

The explanations that follow describe the key provisions of a standard proprietary lease (also known as an **occupancy agreement**), but cooperatives may amend these provisions to fit their needs.

Maintenance (Rent)

Each shareholder is obligated to pay the monthly charges, including late payment fees, as fixed by the Board. The Board also possesses the power to levy assessments upon the shareholders to pay for large capital expenses.

Services Provided by the Cooperative Corporation

The Corporation is required to maintain and manage the building and must keep the common areas properly cleaned and lighted. The Corporation is obligated to provide the apartments with basic services, such as heat and hot water.

Repairs

The Corporation is required to keep in good repair the entire building, including the apartments and common areas, except those parts of the building that are stated to be the obligation of the shareholder. Repair responsibilities commonly imposed upon shareholders include the interior walls, floor and ceilings of the apartment (including painting), plumbing, gas and heating fixtures within the apartment, all appliances, such as refrigerators and stoves, and all lighting and electrical equipment in the apartment. The interior of the apartment may be looked upon as the shareholder's own home and he/she is responsible for repairs within that home.

The line between whether the Corporation or the shareholder is responsible for a repair can sometimes lead to disputes. In general, the rule is that if you can see the pipe, equipment or fixture within the apartment, then the shareholder must maintain and repair it; if you cannot see the pipe, equipment or fixture, then the Corporation is responsible.

refuses to do so and to charge the shareholder for the work.

Improvements and Alterations

A shareholder may not undertake major improvements or alterations within the apartment without first obtaining the written consent of the Board. The Board must have a valid reason if it decides not to give its consent. Improvements requiring consent generally include apartment alterations involving the water, gas, electrical and heating systems and pipes. The role of the Board is to insure that the planned project will not disrupt or cause damage to the building's systems or structure.

Use of the Apartment

Most limited equity cooperatives require that the apartment be used as the personal and primary residence of the shareholder. The intention is to provide housing for a low income person or family, not as a vehicle for real estate investment. The shareholder may occupy the apartment with his spouse and other family members (typically defined as children, grandchildren, parents, grandparents, brothers and sisters). Many cooperatives permit the shareholder to live in the apartment with a roommate. Guests are usually permitted for up to one month periods, provided that the shareholder remains in occupancy. Troublesome issues arise when a shareholder moves out, leaving the so-called "guest" behind in the apartment. If the Board has not approved such an arrangement, then the Board may declare this to be an improper sublet and seek to terminate the lease and recover possession of the apartment.

Subletting

If the shareholder desires to sublet his apartment, he must obtain the written consent of the Board (or, if the Board refuses its consent, by approval of shareholders owning typically at least 2/3 of the stock). Any consent to subletting may be subject to such conditions as the Board may impose. In a low income cooperative, a Board might ask to see a copy of the sublease and require income verification to insure that the sublessee qualifies as a low income person. Many limited equity cooperatives prohibit any profit to be made by the shareholder under the sublease, and place limits on the length of time during which an apartment may be sublet.

Assignment

Any assignment, sale or transfer of the lease and shares to the apartment must be approved in writing by the Board (or if the Board refuses, by the holders of typically 2/3 of the stock). The customary procedure is for the Board to interview the prospective buyer and check personal and employment references. The Board may ask for income verification and copies of tax returns to insure that the buyer is income eligible. In general, a cooperative Board has total discretion over whether to consent to a sale (as long as a disapproval does not violate any civil rights laws).

An exception to the general rule regarding Board consents involves what happens upon the death of a shareholder. If the shareholder is survived by a spouse, then no consent is needed for the lease and shares to be transferred to the spouse. (In many cases, the spouse may already be a co-owner of the shares.)

The transfer of the shares and lease to any other person requires the board's approval, with the proviso that the Board may not unreasonably withhold consent to a financially responsible member of the deceased shareholder's immediate family. This means that the Board must have a valid reason for denying approval of such person.

In deciding whether to give approval of a transfer of the stock and lease in the event of a shareholder's death, the Board first must ascertain who is the rightful heir of the deceased. The Board cannot give approval to a member of the immediate family if another heir has the right to inherit the property. The Board should avoid becoming involved in a struggle between competing relatives. For this reason, the Board should request proof as to who may legally inherit the property, such as documentation from the local Surrogate or Probate Court.

Except in the case of a spouse, the right to inherit does not give the heir the right to occupy the apartment. In rejecting occupancy to a member of the deceased's immediate family, the Board must provide a valid reason for its action. Illustrations of such reasons are:

2. a history of disruptive behavior as a tenant
3. the applicant is not financially responsible as evidenced by a poor credit or employment record
4. the applicant does not intend to use the apartment as his/her primary and personal residence.

If the heir does not wish to move into the apartment or is rejected by the Board, he/she is still entitled to benefit from the sale of shares to a third person. The heir has the right to receive from the sale whatever monies would have gone to the deceased shareholder, minus any maintenance arrears or other debts owed to the cooperative.

House Rules

The Board has the power to adopt House Rules regulating various conduct within the cooperative. The House Rules are incorporated in the Proprietary Lease and a breach of the Rules constitute a breach of the Lease. House Rules usually prescribe such matters as the manner in which garbage should be disposed of, restrictions on the playing of music or electronic equipment in a loud manner after 11 p.m., and the use of laundry facilities and public areas of the building.

Pledge of Shares and Lease

The shareholder may use his shares and lease as security for the repayment of a loan, but only with the consent of the Board. The Lender usually requests that the Board execute a Recognition Agreement, acknowledging that the Lender is holding the shares and lease as security until the loan is paid. A shareholder may seek a loan to borrow the funds necessary to purchase the unit.

Amendments to the Proprietary Lease

The terms of the Proprietary Lease may be amended by an affirmative vote of members owning at least two-thirds of the shares of the cooperative. Items which are controlled by agreements with government agencies or by statutory provisions, such as low income re-sale provisions, may not be altered by the shareholders.

Enforcement of the Proprietary Lease

A cooperative Board must sometimes confront the serious issue of how to handle a shareholder who has violated the terms of the lease. This violation may take the form of failing to pay the maintenance on the apartment or non-financial matters such as unauthorized subletting of the unit. Since the defaulting shareholder is a part owner of the cooperative as well as a neighbor, this situation poses difficult problems for the Board. Most Boards will attempt to deal with the default with a letter from the directors, followed by a letter from the Corporation's attorney if no progress is made. The directors may request that the shareholder meet with them to seek a resolution. If all efforts to resolve the issue fail, then the Board may have to turn to litigation. It must be remembered that the directors have a responsibility to protect the interests of all of the members of the cooperative. If a shareholder does not pay his fair share, then this impacts on all of the members. Below is a summary of the litigation options available to a cooperative Board in the case of a shareholder who is in violation of the lease.

1. Non-Payment of Maintenance Charges

The Cooperative possesses two principal methods for enforcing the requirement of shareholders to pay the monthly maintenance.

a. **Non-Payment Proceeding.** If the shareholder has defaulted in the timely payment of maintenance charges, then the cooperative (after service of proper notice to cure the default) can commence a non-payment action to evict the shareholder. The shareholder can terminate the proceeding by paying the past due rent, plus any late charges and legal fees, at any time before the issuance of a warrant of eviction.

b. **Hold-Over Proceeding.** A difficult situation faced by cooperative boards is what to do about the shareholder who consistently pays his maintenance late. Chronic late payment of maintenance undermines the Board's ability to pay its own bills on time. Non-payment actions are often not effective, because the shareholder can stop the proceeding by paying the arrears. An alternative procedure is for the Board to send the shareholder a notice that the lease is being terminated by reason of the

shareholder's history of late payments. The Board could seek to deem this conduct to be "objectionable" justifying a termination of the lease. If the problem is serious enough in a particular building, the shareholders should consider adopting an amendment to the proprietary lease declaring that a pattern of repeated late payments (e.g. five such payments within a 12-month period) constitutes separate grounds for termination of the lease.

If the shareholder refuses to vacate the apartment after receiving a notice of termination of the lease, the Board may commence in court what is known as a hold-over proceeding, in that the shareholder is "holding-over" after the termination date.

2. Other Types of Defaults

Other types of defaults under the proprietary lease include unauthorized assignment, subletting, occupancy or alteration of the unit or objectionable conduct on the part of the shareholder or other occupants of the apartment. Objectionable conduct has been defined by a court as unreasonable or unlawful conduct to the annoyance, inconvenience, discomfort or damage to other shareholders. The lease also prohibits a shareholder from permitting or tolerating a person of "dissolute, loose or immoral character" to enter or remain in the building or in his apartment. To declare that a person's tenancy is undesirable requires a two-thirds vote of the Board or by shareholders owning two-thirds of the stock. Legal enforcement of such defaults include:

a. **Hold-Over Proceeding.** If the shareholder has violated the lease, the Board can seek to evict the member by sending a notice of termination of the lease and then commencing a hold-over proceeding. If successful, the Board may evict the shareholder and then sell the shares to the apartment.

b. **Injunction.** If a less drastic step is called for, when, for example, the Board desires to remedy the breach but does not want to evict the shareholder, an alternative method is a court action for an injunction. This procedure can be effective in preventing an unauthorized alteration, sale or subletting of a unit or to gain entry to an apartment for needed repairs.

Contracts with Outside Parties

One of the responsibilities of the Board is to enter into agreements with outside parties to provide services for the cooperative. The most important of these contracts are agreements with contractors to undertake repairs and improvements and with management agents to provide management services for the building. Every contract entered into by the Board should describe clearly the scope of work to be performed, how much it will cost, how long it will take and the rights of the Board to terminate the agreement. The Board should always check references before it engages the services of an outside professional.

The Board may hire an outside company to manage the building, but it must be remembered that the Board and its officers still bear the primary responsibility for protecting and safeguarding the interest and financial assets of the corporation and its shareholders.

The following is a checklist of items to be covered in a management agreement, in the event the Board decides to engage an outside firm to render such services:

1. Scope of Services.

In general, a Management Company should be responsible for:

- ✍ cleaning and maintenance of the building
- ✍ hiring personnel, subject to the approval of the Board, to perform these services
- ✍ engaging contractors, subject to the approval of the Board, to make necessary repairs
- ✍ collecting and depositing in the corporation's bank account the monthly maintenance charges
- ✍ paying the bills of the cooperative

- ✧ handling shareholder complaints
- ✧ complying with all building codes and clearing violations
- ✧ preparing and filing government, tax and employment forms

2. Records. The Management Company should be required to maintain records in accordance with generally accepted accounting standards and procedures, showing income and expenditures and the assets and liabilities of the cooperative. The Corporation should have full right to inspect all of its records held by the Management Company, including checks, bills, invoices, and statements. The Management Company should provide the Corporation with monthly and yearly financial statements. The monthly statements should be supported by copies of documentation (cancelled checks, bills, etc.).

3. Bank Account. The Management Company should maintain a bank account on behalf of the cooperative and should provide the cooperative with copies of all records relating to the account (statements, cancelled checks, deposit slips, etc.).

4. Insurance Coverage. Subject to the approval of the Board, the Management company should make certain that all insurance policies are current and are in sufficient amounts to properly protect the Corporation. The Management Company should promptly investigate and make a full written report regarding all claims against the Corporation.

5. Compensation. The typical management fee ranges from between six to eight percent of the monthly rents collected. The Corporation should ascertain whether there are hidden fees not anticipated (e.g. the Management Company might seek to allocate building funds to pay the cost of its bookkeeper or other office personnel).

6. Termination. The Corporation should possess the right to terminate the contract (with or without cause) on thirty days notice. Upon termination, the Management Company should be required to turn over all of its records in its possession belonging to the Corporation.

Apartment Sales

One of the Board's responsibilities is the supervision and approval of re-sales of apartments. Below is a checklist of the legal documents involved in the sale of a unit.

1. Contract of Sale. Entered into between the seller and purchaser, the contract of sale specifies the basic agreement between the parties: purchase price, when and where the closing or transfer of ownership will take place, financing arrangements, if any, and whether the contract is contingent on the purchaser obtaining a loan to buy the unit; what personal property and appliances will be included.

2. Consent of Board of Directors. The Board must pass a resolution accepting the new shareholder and consenting to the sale. A written consent to an assignment of the proprietary lease and the shares of stock allocated to the unit is issued by the Board and presented at the closing.

3. Assignment of Proprietary Lease. This document is signed by the seller to transfer his interest in the proprietary lease to the purchaser.

4. Acceptance of Assignment. This document is signed by the purchaser to indicate his assumption of the seller's obligations under the proprietary lease.

5. Stock Power. This document is signed by the seller to transfer the shares allocated to his apartment to the purchaser.

6. Recognition Agreement. If a bank or other institution is lending money to the purchaser to buy the unit, the lender will request the Board to sign a document known as a recognition agreement. Under this agreement, the corporation recognizes that a lending institution will hold a security interest in the shares and proprietary lease. By signing the document, the Board agrees to notify the lender in the event the purchaser defaults under the proprietary lease, affording the lender an opportunity to cure the default to safeguard its security.

7. New Stock and Lease. The Corporation must issue a stock certificate and a proprietary lease in the name of the purchaser to be presented at the closing.

APPENDIX

MODEL FORMS

1. Certificate of Incorporation of a Cooperative Housing Development Fund Corporation
2. Purchase Agreement
3. Application for a No-Action Letter

MODEL FORM 1

CERTIFICATE OF INCORPORATION OF

HOUSING DEVELOPMENT FUND CORPORATION

PURSUANT TO ARTICLE XI OF THE PRIVATE HOUSING FINANCE LAW AND
SECTION 402 OF THE BUSINESS CORPORATIONS LAW

THE UNDERSIGNED, for the purpose of forming a corporation pursuant to Article XI of the Private Housing Finance Law ("PHFL") and the Business Corporations Law, both of the State of New York, hereby certifies:

I

The name of the corporation is **HOUSING DEVELOPMENT FUND CORPORATION** and is hereinafter referred to in this Certificate as the "Corporation".

II

The Corporation is organized exclusively for the purposes of developing a housing project for persons of low income, which property may be aided by a federally-aided mortgage, state-aided

mortgage or municipally-aided mortgage, as defined in Section 572 of the Private Housing Finance Law of the State of New York, as amended. The Corporation is empowered to do and perform all acts necessary to accomplish the above- mentioned corporate purpose, including, but not limited to: (a) the execution of such instruments and undertakings as may be required by any governmental body giving financial assistance to the Corporation, and (b) making available to shareholders of the Corporation apartments, spaces and facilities located in such property for residential purposes under leases commonly known as proprietary leases. Said proprietary leases provide that shareholders of the Corporation shall be entitled, solely by reason of their ownership of shares of the Corporation, to occupy the aforementioned apartments, space and facilities for residential purposes, pursuant to such proprietary leases.

III

The office of the Corporation is to be located in the County of the _____, State of New York.

The housing project is to be located on Lot _____ in Block _____ in the Borough of _____, County of _____, City and State of New York, said site having the following street address: _____, _____, _____.

IV

The Corporation is not organized for pecuniary profit or financial gain. All income and earnings of the Corporation shall be used exclusively for corporate purposes, and no part of the net income or net earnings of the Corporation shall inure to the benefit or profit of any private individual, firm, corporation or association.

V

If the Corporation receives a temporary loan or advance from the Housing Development Fund or a Municipal Housing Development Fund, as established by or pursuant to Article XI of the PHFL, it shall be authorized to enter into an agreement with the Commissioner of Housing and Community Renewal of the State of New York or the New York City Department of Housing Preservation and Development (HPD), providing for regulation with respect to rents, profits, dividends and disposition of the property or franchises.

VI

If the Corporation receives a temporary loan or advance from the Housing Development Fund or a Municipal Housing Development Fund, as established by or pursuant to Article XI of the PHFL, the Commissioner of Housing and Community Renewal of the State of New York or the Supervising Agency shall have the power, if, in his or its discretion, he or it determines either that any such temporary loan or advance is in jeopardy of not being repaid, or that the proposed housing project for

which such a temporary loan or advance was made is in jeopardy of not being constructed, to appoint to the board of directors of the Corporation a number of new directors, which number shall be sufficient to constitute a majority of the board, notwithstanding any other provision of this Certificate of Incorporation, the by-laws of the Corporation or of any other provision of law.

VII

The Corporation may not be dissolved without the written consent of the Commissioner of the New York State Division of Housing and Community Renewal (DHCR). Such consent must be attached to the "Certificate of Dissolution" which the Corporation will file with the Department of State.

VIII

This Certificate may not be altered or amended without the written consent of DHCR; and may not be amended without the written approval of the Secretary of the United States Department of Housing and Urban Development (HUD) so long as a mortgage on any real property of the Corporation is outstanding, unpaid and held by the United States Department of Housing and Urban Development.

IX

The Secretary of State is designated by the Corporation as agent upon whom process against it may be served. The post office address of the Corporation to which the Secretary of State shall mail a copy of any process against the Corporation served upon him or her is:

X

The number of directors of the Corporation shall be not less than three nor more than . The exact number of directors shall be set forth in the By-Laws. Each director shall be at least eighteen years of age. At every meeting of the shareholders, each shareholder present, either in person or by proxy, shall be entitled to cast one vote on each question without regard to the number of shares held by the shareholder. No shareholder shall be eligible to vote or to serve on the Board of Directors who is shown on the books or management accounts of the Corporation to be two months delinquent in payments due the Corporation under the proprietary lease. The directors shall be elected by a majority vote of the shareholders of the Corporation.

XI

The names and residences of the directors of the Corporation until the first annual meeting are:

Name**Address****XII**

The Incorporator(s) whose signature(s) appears below is (are) at least eighteen years of age.

XIII

The Corporation is authorized to issue only one class of stock. The total number of shares which the Corporation shall have the authority to issue is _____, with a par value of \$1.00 per share.

XIV

The housing project of the Corporation shall be operated exclusively for the benefit of persons or families who are entitled to occupancy in the housing project by reason of ownership of shares in the Corporation, and the Corporation may issue shares for home owners' purchase notes if the purchase transaction has received the written endorsement of the Commissioner of Housing and Community Renewal and if at least two hundred dollars in money or property is received by the Corporation toward the issuance of such shares.

XV

Notwithstanding any other provision contained herein, the Corporation is authorized to enter into a contract with the Secretary of the United States Department of Housing and Urban Development (hereinafter referred to as the "Secretary") and shall be bound by the terms thereof to enable the Secretary to carry out the provisions of the National Housing Act and the United States Housing Act of 1937 as amended. Upon execution, the contract shall be binding upon the Corporation, its successors and assigns, so long as a mortgage is outstanding, unpaid, uninsured, or held by the Secretary, or any rent subsidy pursuant to the United States Housing Act of 1937 as amended is payable.

XVI

Notwithstanding any other provision contained herein, the following restrictions upon the transfer of shares allocated to individual units shall apply:

If an individual tenant shareholder sells his or her shares in the cooperative, the following shall apply:

1. the shares to a cooperative unit may only be transferred or sold to an eligible applicant as defined under the regulations of the New York State Housing Trust Fund Corporation.
2. the resale price of shares applicable to a cooperative unit shall not exceed an amount equal to the sum of:
 - i. the funds originally paid by the tenant shareholder to purchase such shares and rehabilitate or construct the unit, plus the lesser of the cost or fair market value of the contribution to the unit of material and of labor, with interest thereon at the rate of six percent per annum, excluding all funds received pursuant to Article XVIII of the Private Housing Finance Law (the "Act") and from such other sources as determined by the Housing Trust Fund Corporation.
 - ii. the payments made by the tenant shareholder after rehabilitation or construction for capital improvements made to such unit, with interest thereon at the rate of six percent per annum, excluding all funds received pursuant to the Act and from such other sources as determined by the Housing Trust Fund Corporation.
 - iii. the pro rata portion of any capital assessment or capital contribution for building-wide improvements paid by such tenant shareholder, with interest thereon at the rate of six percent per annum.
 - iv. the pro rata portion of the reduction in the amount of the outstanding principal of all mortgages on such project paid by the tenant shareholder, with interest thereon at the rate of six percent per annum.
 - v. the reduction in the amount of the outstanding principal on all loans for such unit paid by the tenant shareholder to the extent that the proceeds of the loan were used for the purchase of shares or for the cost of the rehabilitation or construction of, or capital improvement to, such unit, with interest thereon at the rate of six percent per annum.
 - vi. the actual outstanding principal indebtedness on all loans or other obligations for such unit, which the tenant shareholder is required to satisfy, and to the extent that the proceeds of such loans were used for the purchase of shares or for the cost of rehabilitation or rehabilitation of, or the capital improvement to, such unit, provided that if such indebtedness is not paid in full upon the sale of such tenant's shares such tenant shareholder shall not be credited with the amount of such indebtedness.
 - vii. the reasonable costs and expenses incurred in connection with the sale of such shares.
3. For rental, condominium or cooperative projects, resale and occupancy restrictions shall apply for a period of 30 years following the completion of construction, rehabilitation or conversion, or for the period during which any Housing Trust Fund loan or indebtedness remains outstanding, whichever is greater.

XVII

Annexed hereto or endorsed hereon are copies of all approvals and consents required by Article XI of the Private Housing Finance Law for filing this Certificate with the Secretary of State.

XVIII

A copy of this Certificate of Incorporation and a copy of the filing receipt issued by the Department of State, Division of Corporations, shall be delivered to the Commissioner of the Supervising Agency when such filing receipt is received.

In WITNESS WHEREOF, this certificate has been signed and the statements made herein are affirmed as true under the penalties of perjury this _____ day of _____, 1990.

APPROVAL OF SUBSCRIBERS AND CONSENT TO INCORPORATION BY COMMISSIONER OF THE DIVISION OF HOUSING AND COMMUNITY RENEWAL

I, _____, Commissioner of the Division of Housing and Community Renewal of the State of New York, do this _____ day of _____

of _____ hereby approve the subscribers named in the foregoing Certificate of Incorporation of HOUSING DEVELOPMENT FUND CORPORATION for the purpose of and as provided by Article XI of the Private Housing Finance Law of the State of New York, and pursuant to said Article XI hereby certify that I consent to the filing of said Certificate of Incorporation with the Secretary of State of the State of New York.

Commissioner of the Division
Renewal

of Housing and Community

MODEL FORM 2

**PURCHASE AGREEMENT
for shares of**

HOUSING DEVELOPMENT FUND CORPORATION

Purchaser: _____
Apartment: _____
Number of Shares: _____

Total Cash Payment: \$ _____
 Down Payment: (10%) \$ _____
 Balance due after Cooperative is declared effective: \$ _____

1. **Agreement to Purchase.** I agree to buy the number of shares stated above of _____ Housing Development Fund Corporation, Brooklyn, New York (the "Apartment Corporation") allocated to the apartment listed above, and to become the proprietary lessee of the Apartment.

2. **Down Payment and Balance.** Here is my check payable to _____, Attorney-at-Law, for the amount of the initial down payment. I agree that, if and after the Cooperative Project becomes effective, I will pay the balance of the purchase price by my certified check or with an official bank check within 15 days after written notice from the Sponsor of the Closing Date. I will not be required to pay the remaining balance more than 45 days before the Closing Date stated in the notice.

The Sponsor will promptly notify me in writing when the Cooperative either becomes effective or is abandoned.

3. **Re-Sale Provisions.** I have read the attached Re-Sale Provisions regarding the re-sale of units as required by the New York State Housing Trust Fund Regulatory Agreement. I understand that the re-sale of my unit will be governed by these provisions.

4. **Proprietary Lease.** I will sign and return to the Sponsor two copies of the proprietary lease for the Apartment within 7 days from presentation to me. I understand that if I fail to return the proprietary leases within the seven-day period, such failure will be considered a default under this agreement and this agreement shall be cancelled and I shall lose my down payment hereunder. If I pay the Total Cash Purchase Price when due in full and am not in default under this agreement, the Apartment Corporation will deliver the certificate for shares and my signed copy of the proprietary lease to me, promptly when the building is ready for occupancy.

5. **Payments to be Held in Escrow Account.** All money received for the purchase of shares shall be held by the attorney for the Sponsor in a special escrow account at _____. The funds so deposited will be disbursed only at the Closing Date when the building is ready for occupancy or refunded to me if I am entitled to a refund under the terms of this Agreement. A signature of an attorney will be necessary to release funds from the escrow account.

6. **Refund and Limitation on Claims.** If the Project is abandoned or does not become effective within twelve months from the date of this Agreement, this Purchase Agreement shall be deemed cancelled and, not later than forty-five (45) days thereafter, I will receive a full refund of my downpayment and, upon such refund, I shall not have any claim against the Sponsor/Apartment Corporation, and all parties shall be released from all obligations hereunder. The Sponsor also may cancel this Agreement upon seven (7) days written notice if, prior to the Cooperative being declared effective, it determines that I will be unable to meet my financial obligations to the Cooperative, based upon information regarding my employment and credit history. In such event, I shall receive a full refund of my downpayment, and upon receipt of my refund, I shall not have any claims against the Sponsor or the Apartment Corporation, and all parties shall be released from all obligations hereunder.

7. **Default.** I agree that if I fail to pay the Remaining Balance of the Total Cash Purchase Price

when due, the Apartment Corporation may demand it by written notice to me at my address stated below, by registered or certified mail, and if I do not make the required payment within fifteen (15) days after the notice is mailed, all payments made by me hereunder shall be forfeited and the Agreement cancelled. If this Agreement is cancelled, the Apartment Corporation may sell the shares to the Apartment and enter into a proprietary lease with any other person as though this Agreement had never been made.

8. **Identification of Purchaser.** I represent that I am over 18 years of age and am purchasing the subject shares for my own account (beneficial and of record) and that the Sponsor has and will have no interest, direct or indirect, in the shares or the proprietary lease being purchased hereunder. I represent that I am signing this agreement with the intent of occupying the apartment as my primary and personal residence. The representations contained in this paragraph shall survive the Closing Date.

9. **Notices.** Notices hereunder shall be delivered or mailed as follows: to the purchaser(s), at the address stated below; and to the Sponsor at c/o _____ Development Corporation,

10. **No Oral Modifications.** This Agreement may not be changed orally.

11. **Definitions.** The term "I" shall be read as "we" and "purchaser" shall be read as "purchasers" if more than one person are subscribers, in which event the obligations of each subscriber shall be joint and several. The term "Sponsor" shall mean the _____ Development Corporation.

12. **No Assignment.** This Agreement cannot be assigned by the Purchaser.

13. **Successors and Assigns.** This Agreement shall bind and inure to the benefit of the sponsor, its heirs, legal representatives, successors and assigns.

Dated: _____, 1989

Purchaser(s): _____

Apartment Number: _____

APPROVED AND ACCEPTED:

_____, 1990

HOUSING DEVELOPMENT FUND CORPORATION

By: _____

DEVELOPMENT CORPORATION

By: _____

MODEL FORM 3

December , 1989

, Esq.
Assistant Attorney General
Real Estate Financing Bureau
Department of Law
23rd Floor
120 Broadway
New York, NY 10271

Re: No-Action Letter/
Housing Development Fund Corporation

Dear :

As attorney for the Housing Development Fund Corporation, I am submitting this transmittal letter in connection with the corporation's application for a no-action letter pursuant to Part 18.9 of the Department of Law regulations.

As described in the annexed affidavits and in the opinion of the undersigned, the relationship between the parties is such that they do not require the protection of an offering plan and that the filing of an offering plan pursuant to GBL Section 352-e is not necessary to effectuate the purpose of GBL Article 23-A or to protect the public interest.

The undersigned has no actual knowledge of any omission or untrue statements of a material fact included in the application.

The undersigned has prepared or has reviewed all legal documents necessary to form the Housing Development Fund Corporation under Article XI of the Private Housing Finance Law and, in the attorney's opinion, the corporation is duly organized, validly existing and in good standing.

Enclosed are affidavits from all of the tenants in the building and an affidavit from the President of the HDFC.

A check in the amount of \$150.00 as required by GBL Section 352-e(7) is also enclosed and made payable to the Department of Law.

Sincerely yours,

Barry Mallin

Enclosures

State of New York)
): ss:
County of New York)

Application of DEVELOPMENT FUND CORPORATION for a No-Action Letter under Housing Title 13 NYCRR 18.9

, being duly sworn, deposes and says:

1. I am the President of the HOUSING DEVELOPMENT FUND CORPORATION ("HDFC"), and submit this Affidavit in support of an application for the issuance of a no-action letter in connection with a cooperative offering for the building located at , , .
2. It is the intention of the HDFC to issue to its member-offerees shares and proprietary leases for the purpose of creating a residential low income cooperative.
3. The Cooperative, once established, will be subject to the re-sale limitations contained within within its Proprietary Lease and By-Laws in accordance with the restrictions mandated by the Housing Trust Fund Corporation of the State of New York.
4. In connection with the application for a no-action letter, the HDFC shall provide to each offeree the following information and documents:
 - a. the consideration to be used for the purchase of shares in the Corporation;
 - b. the estimated maintenance and the current or proposed budget for the first year of occupancy;
 - c. a copy of the mortgages on the property;
 - d. a copy of the most recent financial statement of the income and expenses for the operation of the property;
 - e. any information known to the offeror which may result in extraordinary expenses for shareholders or for the apartment corporation including, but not limited to, assessments, liabilities, dangerous or hazardous conditions, pending litigation and administrative proceedings;

- f. a copy of the certificate of occupancy for the building, if available;
- g. and such other information as the Department of Law may require to be presented to each offeree.

5. The HDFC will furnish a complete copy of the application for a no-action letter to each offeree and will furnish within five days, after request by the Department of Law, copies of executed offeree affidavits required pursuant to subparagraph (k) of section 18.9 of the Department of Law regulations.

6. The property's legally permissible use is residential housing and such shall continue. The residential use will be in accordance with the building's certificate of occupancy and the Corporation will comply with all applicable zoning, building and housing laws and regulations. At the time the building is occupied there will be no vacancies, nor will there be any sub-tenants.

7. To the best of my knowledge, neither the offeror Corporation nor any of the named individuals herein have participated in any other application for a no-action letter or have made any other offerings regarding the property within the preceding five years.

8. Prior to the closing on a unit that is subject to this application, I understand that the offeror Corporation will obtain from each offeree an affidavit containing the following representations:

- a. the name, residence and business address and legal status of each offeree;
- b. that the offeree has read the affidavit of offeror submitted as part of the application for a no-action letter;
- c. that the offeree understands that no offering literature other than that required by the no-action letter will be provided; that the offeree acknowledges that he/she has been informed that if this transaction constituted a public offering within the meaning of GBL Article 23-A, he/she would be entitled to certain rights and protections pursuant to such Article; and
- d. that the offeree has inspected the subject property.

WHEREFORE, it is respectfully requested that the Department of Law issue a no-action letter in connection with a cooperative offering for shares in the HOUSING DEVELOPMENT FUND CORPORATION.

ACKNOWLEDGEMENT

State of New York)
): ss:

On the _____ day of _____, 1990, before me came to me known to be the individual described herein, and who executed the foregoing instrument, and acknowledged the same.

Notary Public

State of New York)
): ss:
County of New York)

Application of _____ STREET DEVELOPMENT FUND CORPORATION for a No-Action Letter under Title 13 NYCRR 18.9

_____, being duly sworn, deposes and says:

1. I am a member of the _____ STREET HOUSING DEVELOPMENT FUND CORPORATION ("HDFC"), and submit this affidavit in support of an application for the issuance of a no-action letter in connection with a cooperative offering for the building located at _____, _____, _____.

2. The Property was purchased on _____, _____ as a vacant building from the City of New York York by the _____, a not-for-profit, community organization active in developing low income housing in the _____. Construction Financing in the amount of \$ _____ for rehabilitation of the building was provided by the Housing Trust Fund Program of the State of New York. The building is also eligible for New York City's real estate tax abatement program.

3. After the completion of the rehabilitation construction, the title to the property will be transferred to the _____ HOUSING DEVELOPMENT FUND CORPORATION.

4. The Property/Project consists of 8 residential units and all of the members of the HDFC join in this application for the issuance by the Department of Law of a no-action letter. The members of the HDFC will become the tenant-shareholders of the building.

5. The _____ negotiated the acquisition of the property from the City of New York and obtained the financing for the rehabilitation of the building. The _____ has provided construction supervision of the project and is furnishing the tenants with assistance in the conversion of the building into a cooperative.

6. The members of the Corporation are aware of the condition of the property. It is the Corporation's intention to issue to the members shares and proprietary leases for the purpose of creating a residential cooperative.

7. The Cooperative, once established, will be subject to the re-sale limitations contained in its Proprietary Lease and By-Laws in accordance with the restrictions mandated by the Housing Trust Fund Corporation of the State of New York. Annexed hereto and incorporated herein are the provisions regarding the re-sale of units, the limited return on shareholder equity and the maintaining of the units as housing for low income persons. I have read and understand these provisions. I also understand that I shall be required to occupy the apartment as my principal and primary place of residence.

8. The names of the members of the Corporation, the apartments being offered and the number of shares allocated to each apartment is incorporated herein in Schedule A.

9. This offering shall be limited to those offerees named in Schedule A. The consideration for the shares shall be \$ _____ for my unit. All of the offerees have already agreed to pay the purchase price.

10. I understand that the offeror Corporation shall provide to each offeree the following information and documents:

- a. the consideration to be used for the purchase of shares in the Corporation;
- b. the estimated maintenance and the current or proposed budget for the first year of occupancy;
- c. a copy of the mortgages on the property;
- d. a copy of the most recent financial statement of the income and expenses for the operation of the property;
- e. any information known to the offeror which may result in extraordinary expenses for shareholders or for the apartment corporation including, but not limited to, assessments, liabilities, dangerous or hazardous conditions, pending litigation and administrative proceedings;
- f. a copy of the certificate of occupancy for the building, if available;
- g. and such other information as the Department of Law may require to be presented to each offeree.

11. I understand that the offeror Corporation will furnish a complete copy of the application for a no-action letter to each offeree.

12. I understand that the offeror Corporation will furnish within five days, after request by the Department of Law, copies of executed offeree affidavits required pursuant to subparagraph (k) of section 18.9 of the Department of Law regulations.

13. The property's legally permissible use is residential housing and such shall continue. The Corporation will comply with all applicable zoning, building and housing laws and regulations pertaining to its use and shall use the building in accordance to its certificate of occupancy.

14. To the best of my knowledge, neither the offeror Corporation nor any of the named individuals herein have participated in any other application for a no-action letter or have made any other offerings regarding the property within the preceding five years.

15. Prior to the closing on a unit that is subject to this application, I understand that the offeror

Corporation will obtain from each offeree an affidavit containing the following representations:

- a. the name, residence and business address and legal status of each offeree;
- b. that the offeree has read the affidavit of offeror submitted as part of the application for a no-action letter;
- c. that the offeree understands that no offering literature other than that required by the no-action letter will be provided; that the offeree acknowledges that he/she has been informed that if this transaction constituted a public offering within the meaning of GBL Article 23-A, he/she would be entitled to certain rights and protections pursuant to such Article; and
- d. that the offeree has inspected the subject property.

WHEREFORE, it is respectfully requested that the Department of Law issue a no-action letter in connection with a cooperative offering for shares in the HOUSING DEVELOPMENT FUND CORPORATION.

ACKNOWLEDGEMENT

State of New York)
): ss.,
 County of New York)

On the day of , 1990, before me came to me known to be the individual described herein, and who executed the foregoing instrument, and acknowledged the same.

Notary Public

RE-SALE RESTRICTIONS

The following restrictions upon the transfer of shares allocated to individual units shall apply:

If an individual tenant shareholder sells his or her shares in the cooperative, the following shall apply:

1. the shares to a cooperative unit may only be transferred or sold to an eligible applicant as defined under the regulations of the New York State Housing Trust Fund Corporation.
2. the resale price of shares applicable to a cooperative unit shall not exceed an amount equal to the sum of:
 - i. the funds originally paid by the tenant shareholder to purchase such shares and rehabilitate or construct the unit, plus the lesser of the cost or fair market value of the contribution to the unit of material and of labor, with interest thereon at the rate of six percent per annum, excluding all funds received pursuant to Article XVIII of the Private Housing Finance Law (the "Act") and from such other sources as determined by the Housing Trust Fund Corporation.
 - ii. the payments made by the tenant shareholder after rehabilitation or construction for capital improvements made to such unit, with interest thereon at the rate of six percent per annum, excluding all funds received pursuant to the Act and from such other sources as determined by the Housing Trust Fund Corporation.
 - iii. the pro rata portion of any capital assessment or capital contribution for building-wide improvements paid by such tenant shareholder, with interest thereon at the rate of six percent per annum.
 - iv. the pro rata portion of the reduction in the amount of the outstanding principal of all mortgages on such project paid by the tenant shareholder, with interest thereon at the rate of six percent per annum.
 - v. the reduction in the amount of the outstanding principal on all loans for such unit paid by the tenant shareholder to the extent that the proceeds of the loan were used for the purchase of shares or for the cost of the rehabilitation or construction of, or capital improvement to, such unit, with interest thereon at the rate of six percent per annum.
 - vi. the actual outstanding principal indebtedness on all loans or other obligations for such unit, which the tenant shareholder is required to satisfy, and to the extent that the proceeds of such loans were used for the purchase of shares or for the cost of rehabilitation or rehabilitation of, or the capital improvement to, such unit, provided that if such indebtedness is not paid in full upon the sale of such tenant's shares such tenant shareholder shall not be credited with the amount of such indebtedness.
 - vii. the reasonable costs and expenses incurred in connection with the sale of such shares.
3. For rental, condominium or cooperative projects, resale and occupancy restrictions shall apply for a period of 30 years following the completion of construction, rehabilitation or conversion, or for the period during which any Housing Trust Fund loan or indebtedness remains outstanding, whichever is greater.