



**Cooperators United for Mitchell-Lama**

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**Position Statement from Cooperators United for Mitchell-Lama  
on HDC Offer to Convert Mitchell-Lama Cooperatives  
to Article XI HDFC Cooperatives  
May 22, 2012**

*Over the past year, the city agencies HPD and HDC have created and promoted a plan to encourage conversion of Mitchell-Lama (ML) cooperatives to Housing Development Fund Companies (HDFC) through the combination of an HPD rule change and a financing scheme devised by HDC. This paper states the position of Cooperators United for Mitchell-Lama (CU4ML) regarding this plan.*

CU4ML views the proposed conversion of any ML cooperative to HDFC organization through Article XI of the PHFL as detrimental to all the major parties involved, including most importantly: [1] current cooperators who remain in residence; [2] the cooperative as limited-equity housing for a diverse community of residents; [3] would-be cooperators on the waiting lists; and [4] New York City and its taxpayers, who have subsidized and would continue to subsidize the cooperatives by abatement of the municipal real estate tax.

Only a thin slice of New Yorkers would benefit from such a conversion, namely, current shareholders who move out immediately following conversion either by selling their apartments at prices much higher than ML equity or by passing them to their children, who thereby acquire the (now much higher-priced) apartments with no payment to the corporation. A windfall profit for such families is the principal driver of the attempts to privatize ML cooperatives, and it is inescapable that exactly the same people would reap that windfall by conversion through Article XI as through privatization.

On March 29, 2012, the shareholders of Cadman Towers, a moderate- and middle-income ML cooperative in Brooklyn, were offered a “restructuring plan” designed by HDC that would withdraw Cadman Towers from the ML Program and reconstitute it as an HDF Company under PHFL Article XI. In the plan, the lowest post-conversion apartment sale price is projected as three to ten times greater than the highest price of any ML cooperative apartment in New York City. This kind of loss of ML housing does not match the purpose of PHFL Article XI. Article XI establishes Housing Development Funds to enable seriously deteriorating housing to be converted to habitable, well-managed housing affordable for low-income households, families with incomes well below Area Median Income (AMI).

## **[1] Impact on current cooperators who remain in residence**

HPD's Article XI conversion regulation §3-14(i)(15), adopted in December, 2011, indicates that a simple majority of current shareholders would be required to vote approval of restructuring before it can be effected. To be consistent with all other such votes in Mitchell-Lama cooperatives, this conversion would have to require a 2/3 majority vote for shareholder approval.

### **a. Shareholders would not be protected by the Martin Act**

A major deficiency of such "restructuring" conversions would be the failure to require a Martin Act-mandated disclosure review by the State Attorney General's Office (AGO) to protect current shareholders and future purchasers. There is also no provision to ensure that shareholders would be allowed an opportunity to comment on the plan prior to the vote. Relative to privatization, the process of conversion to HDFC is treated casually, even though it is an equally drastic change in the organization of the cooperative and the price of its apartments' shares.

### **b. Shareholders would be misled about income to the cooperative (see also [2], below)**

The shareholders will be told that the conversion will enable the cooperative to afford major capital improvements without burdensome charges (maintenance or assessments) to shareholders or loss of affordability of their homes. In the example plan (for Cadman Towers), a loan and a grant from HDC would provide almost all of the support for Major Capital Improvements (MCIs). Flip taxes paid by new shareholders would also provide funds for that purpose, but actually only a small (see [2], below) and variable fraction of the amounts needed. Other financial needs would be met by a 17.8% increase in maintenance charges, to be borne by continuing (and new) shareholders for the foreseeable future. Most of the increase would be needed to compensate for the elimination of over-income surcharges (ML rule §3-03(b)), which currently account for 11.4% of Cadman's income from shareholders, when cooperators are charged the increased base maintenance regardless of household income.

### **c. Shareholders would be misled about transfer taxes as a cost of conversion**

The City and State tax agencies have ruled repeatedly that conversion of a ML cooperative to a cooperative that allows far higher apartment prices represents a taxable property transfer because it results in a significant change in the benefits of ownership. The Cadman shareholders would not be told that the Real Property and Real Estate Transfer Taxes of NYC and NYS, respectively, would be imposed. No mention of these taxes appears in the plan. These taxes should be disclosed as a sizeable cost of the process of conversion before the shareholders are asked to vote on acceptability of the plan.

## [2] Impact on the cooperative development

The restructuring plan for Cadman Towers is not straightforward. It misrepresents the reason for withdrawal from ML; the true, net value of apartment flip taxes; and the severely reduced affordability of the housing and diversity of the community.

### a. Eligibility for HDC assistance does not require withdrawal from ML

The restructuring plan implies that eligibility for HDC financial assistance requires withdrawal from the ML Program. Through the ML Preservation Program, a ML development may obtain a grant of several million dollars for major capital improvements and/or refinance its mortgages with minimal impact on monthly charges. Withdrawing from ML has not been a condition of eligibility for such help; on the contrary, one condition is that “. . . owners and/or cooperative corporations are required to keep their buildings within the Mitchell-Lama Program.” *See HPD web site, section Mitchell-Lama Preservation Program, Frequently Asked Questions, question 2; see also questions 3 and 4. ]*

### b. The true, net value of flip taxes would provide very little support for the HDC funding of major repairs

The 30% “transfer tax” (better known as “flip tax”) to be levied on apartment sales is purported to benefit the HDFC cooperative by providing funds for major capital improvements (MCI). However, enhancement of the cooperative’s revenues sufficient for this purpose is illusory. The net value of annual flip tax revenue should be calculated as flip tax revenue projected minus revenues lost as a consequence of conversion. For Cadman Towers, the major annual revenue losses would be shareholder surcharges (\$450,221 in 2011) and excess equity paid by purchasers as First Sales Assessments (\$164,149 in 2011), a total of \$614,370 in 2011. Thus:

**net annual flip tax** = gross flip tax (\$858,246) minus lost surcharges minus lost excess equity

**net annual flip tax** = \$858,246 minus \$450,221 minus \$164,149 = \$243,876

This amount would not contribute a significant proportion of the millions needed for MCIs.

Gross revenue would vary from year to year and cooperative to cooperative, depending on the number of sales and the prices of apartments—speculative values that are certain to fluctuate widely. In the example plan for Cadman Towers, the projected net revenue to the coop is only 28.4% of the gross revenue and only 8.5% (30% of 28.4%) of the sale price. As a source of funds for MCI’s, this yield from flip taxes would be so inadequate that the restructuring scheme is pointless.

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**c. Both affordability of the housing and diversity of the resident communities would be greatly reduced**

The generally accepted meaning of “affordable housing” in 2012 is housing that consumes no more than 30% of household income. The annual cost of housing for the vast majority of ML cooperators is base maintenance charges (which include payments on the cooperative’s mortgages) plus utilities if not included in maintenance. Initial ML equity (“apartment price”) is typically five- to seven-fold lower than market rate for comparable housing, and was (and still is) paid off by most of today’s ML cooperators upon or shortly after entry into occupancy.

Today, the annual cost of a two-bedroom+ apartment at Cadman Towers is \$10,092, which is 30% of \$33,640, the annual income needed to afford the apartment. Assuming (as in the plan) that the new shareholder of that apartment after conversion would need to borrow 90% of the equity, the annual cost of that same apartment would become \$11,880 (maintenance) plus \$14,964 (personal mortgage payment) = \$26,844. Consequently, the annual household income needed to afford this same apartment would become \$89,640, an increase of nearly three-fold — a three-fold loss of affordability, for this and every other Cadman apartment.

Narrowing affordability would exclude large sections of working New Yorkers from eligibility for cooperative housing currently in ML. In addition, removing cooperatives from the ML Program would eliminate the mandatory waiting lists organized, under ML rules, by random lotteries. The waiting lists have ensured non-discriminatory sales policies and preserved diversity of the resident communities. Loss of these waiting lists would enable discriminatory sales practices in housing developments that today are the most open, integrated moderate- and middle-income communities in the United States.

We believe that HPD and HDC have a responsibility to protect not just affordability, but also diversity in housing under their supervision. To eliminate ML cooperatives through any path, whether privatization or Article XI HDFC, is to fail to meet that responsibility.

**[3] Impact on would-be cooperators on the waiting lists**

Mitchell-Lama cooperatives are such desirable housing that they have not accommodated the flood of eligible applicants. A lottery system was instituted to place applicants on waiting lists, which have moved slowly for the simple reason that people don’t move out. Consequently, many applicants have waited eight years or more to be allocated a ML apartment in the expectation that secure and affordable ML cooperative apartments would eventually become available.

Conversion to HDFC would eliminate the waiting lists, which would be a regrettable breach of faith with the public.

#### **[4] Impact on the taxpayers of New York**

The Shelter Rent paid by Mitchell-Lama cooperatives in lieu of real estate taxes is 4.5 to 5.5 times lower than ordinary real estate tax in NYC. For a coop such as Cadman Towers, shelter rent is about \$400,000 per year, whereas real estate tax would be more than \$2 million. The difference constitutes a sizeable subsidy that was justifiable as long as Cadman, like the other ML cooperatives, served the “public purpose” for which the Program was established by the PHFL, namely, rehabilitating and rejuvenating neighborhoods by providing housing affordable for moderate- and middle-income New Yorkers, including people with incomes below AMI. Converting a ML cooperative to a development that excludes those people would remove that justification, and profit-taking by ML cooperators upon move-out would be an indefensible and undeserved reward for having enjoyed the subsidy for decades.

According to the HDC plan, Cadman apartments that are today affordable for families whose income is below AMI would become affordable only for households with incomes above AMI. If this proves typical of ML-to-HDFC conversions, then one projected consequence would be a significant loss of housing affordable for current and would-be cooperators, and for all New Yorkers in similar occupations as these people.

#### **CONCLUSION**

It is the considered opinion of CU4ML that the conversion of any Mitchell-Lama cooperative to a Housing Development Fund Company through Article XI would be contrary to the interests of current cooperators and applicants on waiting lists, as well as to almost all the people of New York.

Except for continuing the real estate tax abatement, the scheme proposed for the conversion of ML cooperatives to unaffordable HDFC cooperatives differs very little from privatization of the ML cooperatives. It shares the most undesirable features of privatization: it drastically reduces affordability and diversity, provides only a fraction of the cost of major capital improvements, and is intentionally short-sighted, with a high net flip tax available to the cooperative for only one generation of apartment sales. CU4ML finds that there is no defensible reason to effect such conversions and views them as impractical, pointless, and unfair to New York and New Yorkers.

We also hold that these conversions would be an abuse of Article XI, which serves a different, and valuable, purpose from that which would be accomplished by ML-to-HDFC conversions. We urge that plans for converting ML cooperatives to HDFC cooperatives be abandoned and that the recent amendment to the ML rules [3-14(i)(15)] allowing such conversions be rescinded.