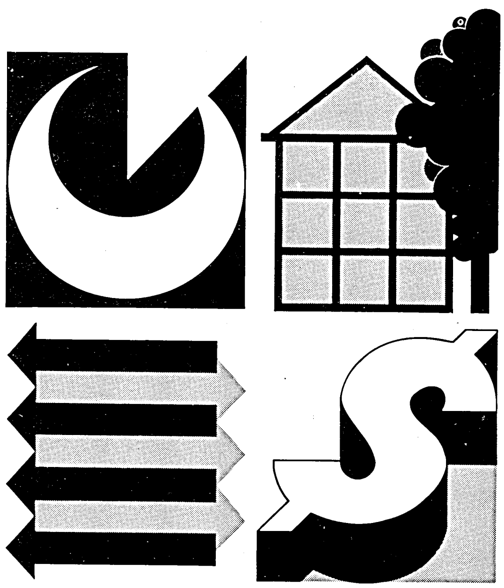
TWIN CITY CONVERSIONS OF THE REAL ESTATE KIND

Barbara Lukermann and others



TWIN CITIES CONVERSIONS
OF THE REAL ESTATE KIND

by
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Graduate students in the Humphrey Institute's Planning Program collectively were responsible for completing the buyer survey of condominium and cooperative households and in addition completed independent papers on topics of their choice. Lukermann has drawn freely on their respective papers, with their permission, and wishes to acknowledge the contribution of Laurie Thompson in the sampling methodology and procedures, Steve Cramer and Keith Krueger in their analysis of St. Paul's Historic Hill area condominium development, Jennifer Abeln's analysis of demographic profiles of condominium buyers, Mihailo Temali's contribution in researching cooperative housing financing mechanisms, and to Jane Maracek for her summary of existing regulation of the conversion market in this metropolitan area. The research product is therefore a collective effort of all of the above cited persons. Authors of individual chapters in this publication are indebted to them and applaud their interviewing skills!

PREFACE

This publication summarizes a larger research effort covering various aspects of condominium and cooperative conversions in the Twin Cities metropolitan area between 1970 and 1980. Many contributed to the effort, including the Center for Urban and Regional Affairs (CURA) at the University of Minnesota and graduate students at the Humphrey Institute of Public Affairs. The conversion studies were directed by Barbara Lukermann. Milo Pinkerton, a graduate student in architecture, worked with her as project assistant. Graduate students in the Humphrey Institute of Public Affairs conducted most of the survey work in conjunction with a workshop in the Institute's Planning Program during the spring of 1980. Louise Brown and Nancy Homans were both workshop participants whose papers expanded on particularly relevant special topics. Thomas Anding, CURA Associate Director, and Rebecca Smith, graduate student in geography, conducted the study on displacement. More detailed reports on several of the substantive topics are available under the following titles:

<u>The Condominium Market: Surveys of Activity, Developers, and Buyers</u>. Barbara Lukermann and Milo Pinkerton. CURA 81-6.

<u>The Displacement Factor: A Survey of Outmovers</u>. Thomas L. Anding and Rebecca Lou Smith. CURA 81-7.

<u>The Case Studies: How the Finances Work</u>. Milo Pinkerton. CURA 81-8.

<u>The Complete Inventory: 1970-1980</u>. Milo Pinkerton. CURA 81-9.

INTRODUCTION

Conversion activity in the housing market has aroused significant interest at all levels of government. As a mechanism for recycling obsolete structures it has received ringing endorsement. As a means of shifting rental housing into home ownership the response has been much more ambivalent, depending on who benefitted and who was harmed. A spurt of conversion activity in the last three years of the 1970s increased the voices of those who saw more harm than good, with the debate moving beyond professional journals or city council meetings and into the daily press.

In the Twin Cities, news clippings from mid-1979 on show increasing pressure on local governments in this area to respond to perceived housing inequities through additional regulation of the marketplace. Initially the issues were directed toward tenants rights and displacement, but more recently the concern has included protection of housing resources for low and moderate income households caught in a housing crunch. The housing crisis is extremely significant in the public debate since alternatives for those required to move out of rental housing to another building are still severely limited. The conversion spurt in 1979 coincided with an increasingly tight rental market. Sources differ as to the actual vacancy rates, but estimate them as between 5 percent and 2 percent depending on the apartment price ranges being considered. 1979 also brought a demographic bulge of young people in their 20s and 30s seeking moderate cost housing at the same time that conditions in the real estate market made new capital investment in market rate rental housing virtually impossible without some type of public subsidy. Today, even subsidy programs are running into difficulties in the struggle to create new rental units at today's interest rates and construction cost levels and still stay within the HUD definition of fair market rents. The resultant fear that the community will suffer a net loss of moderately priced rental units is probably of equal importance to the social injustice of a forced displacement.

Tales of enormous profits to be gained by developers converting in other markets, and fears that buyers are buying a pig in a poke, fuel the flames of public debate. Added to condominium conversion regulations, which provide for adequate tenant notice and right to purchase, have recently come more extensive proposals for rent control, code compliance, tenant relocation payments, requirements that losses of moderately priced rental units be replaced by the developer on a one to one basis (or by cash payments in lieu), all of which could have a major impact on the conversion process and how much activity takes place in the future.

We hope that the following description of the Twin Cities experience to date will shed light on the process and provide a useful data base for considering appropriate public policy options relative to this segment of the housing market. The report is divided into three sections. The first focuses on condominium conversion and summarizes the results of three surveys: a developer survey, a buyer survey, and a survey of outmovers from the buildings being converted. The second section discusses cooperative conversion and again covers a survey of buyers into converted buildings. The third section considers the financial aspects of conversion from both the private market and public intervention perspectives. The study concludes with a discussion of the policy options and regulatory alternatives available to the Twin Cities metropolitan area - more to raise questions than to offer definitive answers.

PART ONE. CONDOMINIUM CONVERSION

by

Barbara Lukermann and Milo Pinkerton

DATA SOURCES

Four primary information sources were developed during our survey of conversions. First, we prepared an inventory from County Recorder offices of all condominium (condo) and cooperative (coop) housing recorded between January 1, 1970 and December 31, 1979. The condo inventory covered the seven county metropolitan area, while the coop survey covered only Hennepin and Ramsey counties. This inventory was supplemented from County Assessor records and individual city Building Inspection Departments to confirm that a project was indeed a conversion and not a new construction activity, that the structure was a previous residential property, that the number of units recorded was correct, and to determine the date of construction of the building itself in addition to the date of its being recorded as a condo or a coop. During this same period, the Metropolitan Council's Housing Program developed a computer inventory of all condominium and cooperative housing from County Assessor sources covering the seven-county area. This inventory was cross-checked with our own, but the two sources resulted in different totals. This report uses the Recorder Office data, except where specifically referenced.

Second, we conducted a survey of Twin City developers. An open-ended questionnaire was used in a series of personal interviews with developers. Interviews were completed with twenty-seven individuals whose collective experience covers approximately 70 percent of all condominium conversions in the past ten years. Developers of cooperative conversions were contacted primarily via telephone interviews without use of a structured questionnaire.

Third, we carried out an attitudinal survey of households purchasing converted units. A structured questionnaire for telephone interviews with buyers of both condominium and cooperative units was developed by the graduate workshop at the Humphrey Institute of Public Affairs, with a subsampling of five groups identified as having potentially distinct characteristics. A total of 264 completed interviews (approximately 50 for each subsample) provided a data base for extensive analysis.

And fourth, a survey of outmovers was conducted by the Center for Urban and Regional Affairs. Telephone interviews were completed with a total of 207 persons who had moved from their apartments in Minneapolis or St. Paul because the building was being converted to condominiums. Questions were structured so that those who bought condos could be compared with those who moved.

Individual city planning department staff members supplemented our information base from their records and gave us special help with the developments that were eligible for city financial assistance. The Metropolitan Council housing unit estimates and building permit data were a further important secondary data source.

A 1980 U.S. Department of Housing and Urban Development (HUD) study on condominium and cooperative conversion activity in all major United States metropolitan markets was being completed at the same time as this study. Data from the HUD report are referenced, so that we may comment on the congruence of final tallies, but the report was not used as a data source for specific conclusions. Copies of the final HUD report are now available.

THE INVENTORY

By January of 1980 the Twin Cities had a total of 6,643 recorded converted condominiums - just under 1 percent of the total housing stock and 2.6 percent of all multifamily units. While this does not appear to be a very large share, it is sufficient to place the Minneapolis-St. Paul area as the fifth most highly impacted market in the United States, according to the 1980 HUD study.* Looking only at gross numbers, however, the Twin Cities fall back into tenth place and the above number appears miniscule in comparison to Chicago's 79,000 or Washington D.C.'s 39,000.

As illustrated in Table 1, almost 6 out of every 10 condominium units are converted units with a heavy concentration in Hennepin and Ramsey counties, containing the two central cities.

Table 1. CONDOMINIUM HOUSING IN THE TWIN CITIES METROPOLITAN AREA, January 1980.

County	Converted Units	New Units	Total Units
Anoka	0	0	0
Carver	0	143	143
Dakota	756	456	1,212
Hennepin	4,169	2,939	7,108
Minneapolis	1,153		
Ramsey	1,712	837	2,549
St. Paul	549		
Scott	6	11	17
Washington	0	487	487
TOTALS	6,643	4,873	11,516
Percent Total	57.7%	42.3%	100.0%

Source: County Recorder Offices, County Assessor Offices, and Municipal Planning Offices.

*U.S. Department of Housing and Urban Development, The Conversion of Rental Housing to Condominiums and Cooperatives. Washington, D.C.: U.S. Government Printing Office, June 1980, page IV-7, Table IV-2.

Locations of converted buildings are identified in Figure 1, where some interesting patterns emerge. A high proportion of conversions occur in the suburbs (74 percent), a pattern corroborated in other metropolitan areas. Quite distinct patterns can be seen in the two central cities. In St. Paul condo conversions are highly localized within the Historic Hill area, but in Minneapolis they are dispersed in peripheral neighborhoods around the downtown. One large project (the Towers, 500 units) was initially built in the 1960s in a downtown redevelopment area (the Gateway) and converted in 1973. It accounts for over 40 percent of all the converted units in Minneapolis.

Conversions in the suburbs are unequally distributed with no strong correlation between the number of multifamily housing units and the amount of conversion. Seven suburbs contain 62 percent of the total converted units for the entire metro area. Four suburbs have had over 20 percent of their multifamily housing stock converted (see Table 2). Most suburbs with major conversion activity may be described as higher income suburbs. This corresponds with findings in the HUD study. Nationally more conversions occur in areas where household incomes average $25,000 and up (1979 dollars).

Table 2. SUBURBAN CONDOMINIUM CONVERSION AND IMPACT ON RENTAL HOUSING, January 1980.

Community in Ranked Order	Number of Projects	Number of Units	Multifamily Units in Community	Percent of Total Units Converted	Percent of Multifamily Units Converted
Edina	15	1,233	6,145	25.0%	20.1%
Burnsville	6	756	3,769	15.3	20.1
Roseville	7	608	4,374	12.3	13.9
Minnetonka	2	522	1,826	10.6	28.6
St. Louis Park	5	411	5,566	8.3	7.4
Little Canada	2	353	1,534	7.1	23.0
Plymouth	2	262	2,358	5.3	11.1
All other suburbs	12	796	21,932	16.1	3.6
TOTALS	51	4,941	47,504	100.0%	10.4%

Source for multifamily units: Metropolitan Council estimate of total housing units by type. January 1980.

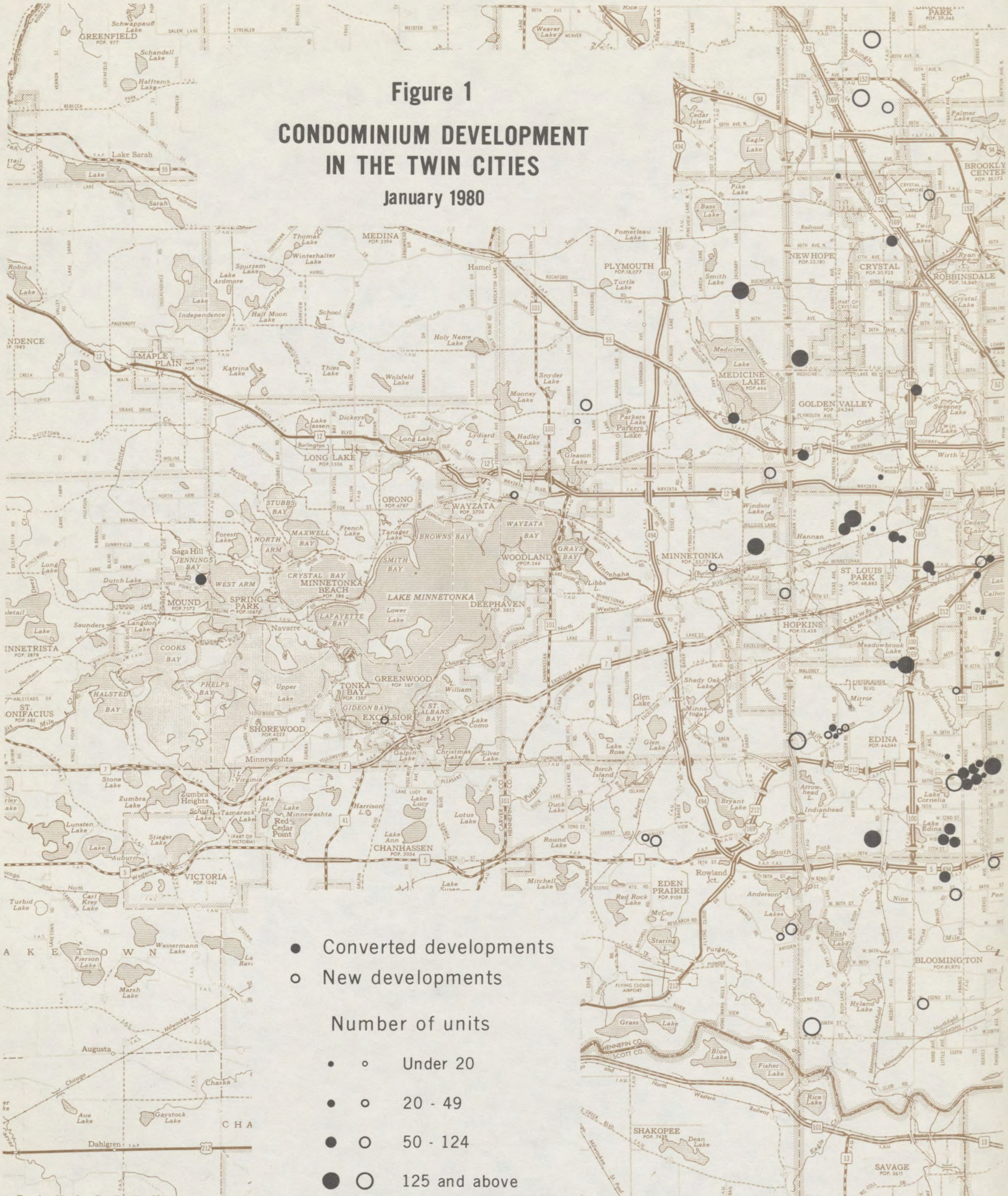
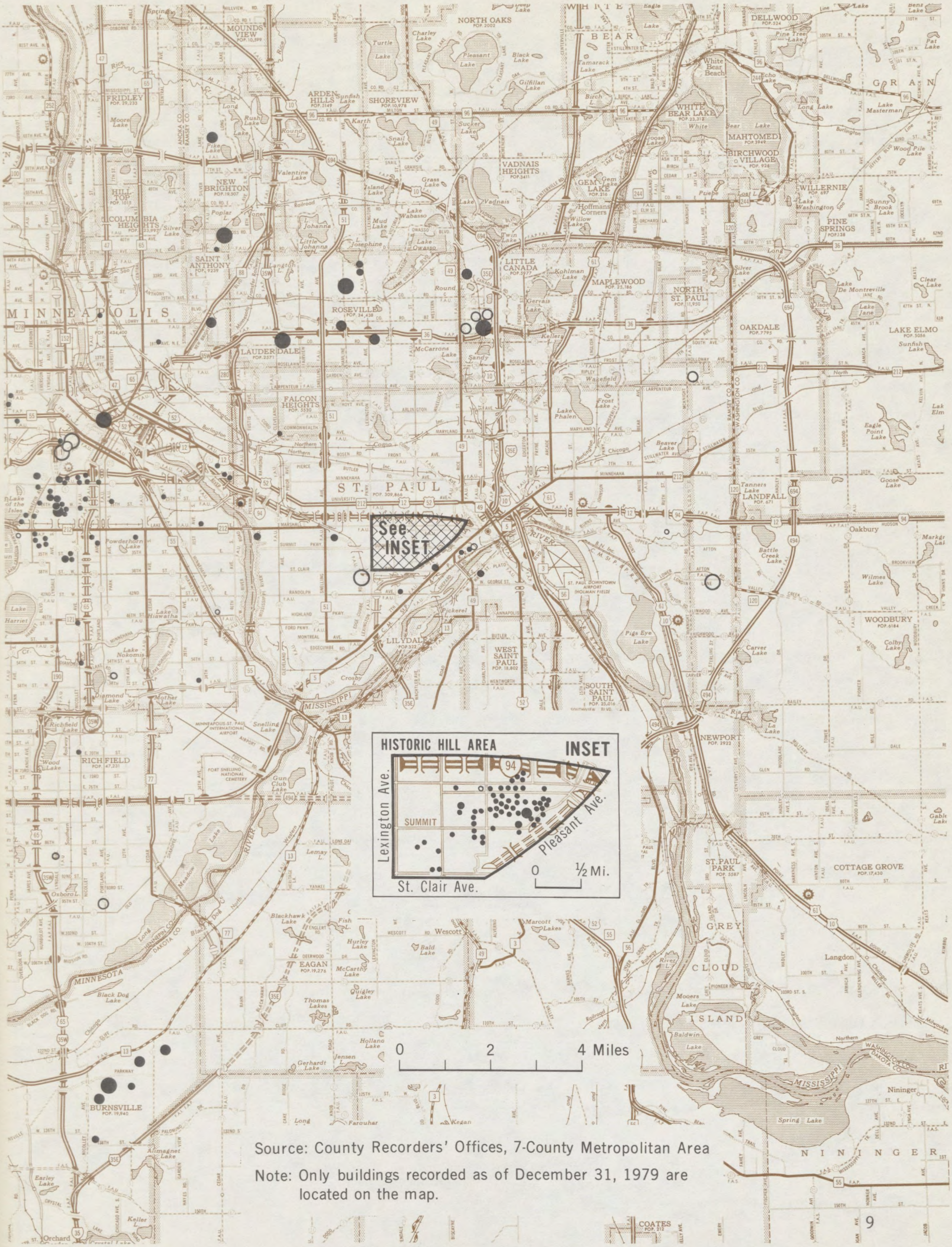


Figure 1

CONDOMINIUM DEVELOPMENT IN THE TWIN CITIES

January 1980



Source: County Recorders' Offices, 7-County Metropolitan Area

Note: Only buildings recorded as of December 31, 1979 are located on the map.

Except for the Towers, conversions have generally been in small structures, averaging only 11 units per project in the central cities but increasing to an average of 93 units in the suburbs. Several suburban projects contain more than one building and were converted in phases. Converted structures in the central cities are broadening housing choices for people looking at condominium alternatives since almost all new condo construction is high cost housing built in larger, high rise structures. Converted condos are available at lower costs. Conversions using the below market rate interest financing of the City of Minneapolis (the HOP IV program) have brought a wider price range and building type into the market.

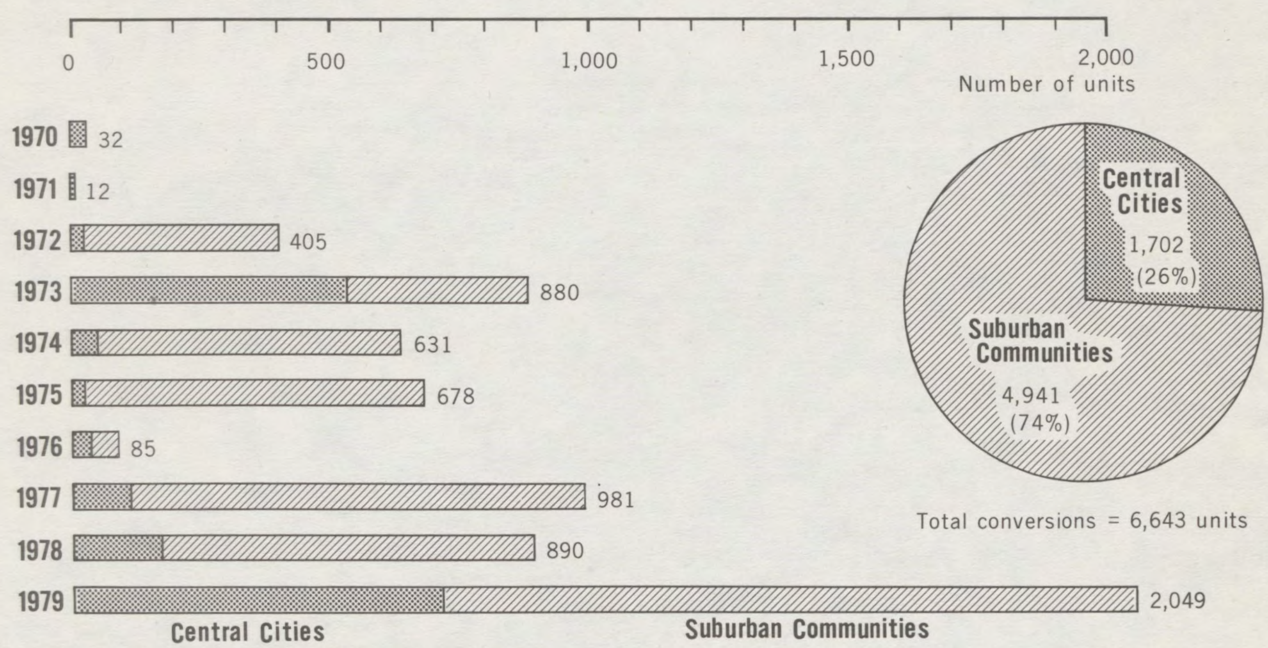
It was initially speculated that if one could profile the type of building undergoing conversion (its age, construction materials, number of units, and location) this might become a good indicator for predicting the future rate of conversions, depending on how large a housing stock existed within this profile. We found that the converted stock could be categorized into three major subtypes. 1) Small buildings that require either major renovation under an historic preservation program or that can be converted fairly rapidly (without major renovation expense) in areas outside of designated historic districts. 2) Large, higher priced rental properties that can be converted rapidly and with a minimum of improvements. This category includes luxury class high rise structures (like the Towers) and a wide range of walk-up apartments, several including multiple structures in one project (like Edina West, Chelsea Woods in Plymouth, and Greenbriar in Minnetonka). 3) Medium sized, post World War II buildings at moderate rentals. This category includes a large number of HOP IV buildings in Minneapolis, but does not necessarily require below market rate interest financing. The market is generally targeted here for the younger, singles group.

We concluded, however, that typing buildings does not produce a good indicator for predicting future conversion levels. The potential choice is so wide that it is the developer's motivation and the financing sources that finally determine the structures actually selected. In Burnsville, overbuilding of the apartment market in the early 1970s strongly influenced the amount of conversion, but elsewhere location, price of acquisition, and time needed to complete a conversion have been much more important factors propelling the industry.

The accelerating pace of conversion in the late 1970s was one of the reasons the HUD conversion study was authorized. HUD found that 71 percent of the decade's total conversions occurred in the last three years (1977 through 1979). For the Twin Cities, our study showed that total conversions during those years were 59 percent; 52 percent in Minneapolis, 72 percent in St. Paul, and 59 percent in the suburbs. Almost a third of all Twin Cities conversions actually took place in a single year--1979, thus creating serious concern as to future decimation of the rental stock (See Figure 2). One reason for this concentration was the increased interest of single persons and young persons in home ownership. Rising interest rates during 1980, however, have dampened the market and the 1979 pace has not been sustained.

Figure 2

CONDOMINIUM CONVERSIONS BY YEAR AND LOCATION



The extent to which rental units have been lost to condominium ownership without replacement is only partially documented in this study. Table 3 lists new multifamily construction matched against losses to conversion each year during the 1970s. During this period, over 59,000 new multifamily units have far exceeded the loss of 6,643 to conversion.* The central cities did not suffer disproportionately in the loss of rental stock according to these figures. The data, however, does not document the extent to which low and moderately priced rental units underwent conversion. Data from our buyer survey (see pages 21-25), provides some greater insight into this aspect of the conversion impact.

Table 3. IMPACT OF CONDOMINIUM CONVERSION ON THE MULTIFAMILY HOUSING STOCK, 1970 to 1980.

	Central Cities			Suburban Communities		
Year	New Units Built	Converted Units	Net Increment	New Units Built	Converted Units	Net Increment
1970	4,681	32	4,649	6,620	0	6,620
1971	2,779	12	2,767	10,764	0	10,764
1972	4,210	18	4,192	9,212	387	8,825
1973	1,068	534	534	2,142	346	1,796
1974	1,033	42	991	1,961	589	1,372
1975	442	28	414	463	650	(-187)
1976	913	37	876	1,079	48	1,031
1977	1,166	120	1,046	3,859	861	2,998
1978	581	171	410	2,221	719	1,502
1979	1,382	708	674	2,526	1,341	1,185
TOTALS	18,225	1,702	16,553	40,847	4,941	35,906
Share of new units built	31%			69%		
Share of conversions		26%			74%	

Source of new units built: Metropolitan Council, Annual Building Permit Records

*Rate of loss due to conversion based on 1970 stock = 3.4 percent; on 1980 stock = 2.6 percent.

CREATION OF THE SUPPLY - RESULTS OF A DEVELOPER SURVEY

It has been claimed that all three parties to a conversion perceive benefits.* The previous building owner wins by getting a higher sales price from the converter than another landlord would have paid for the building, and avoids extra tax burdens by having someone else carry out the conversion process. The converter captures a substantial profit from the process because buyers in the market are willing to purchase at prices above sales price plus conversion expenses. The buyer wins by becoming a homeowner and joining those who enjoy substantial tax subsidies provided by federal and state governments. So far it has been a win/win/win game. Most recently, buyer gains have been fanned by rapid inflationary increases in the housing market in general and in resales in particular. There has been no evidence to suggest that the condominium buyer will gain less from this windfall increase in home values than will any other home buyer. Demand for purchase has in fact been strengthened, with more persons seeking to become owners than to remain renters.

A key link in this chain is the developer, the person who creates the supply and takes on whatever market risks there may be. During late 1979 and early 1980 we conducted a series of personal interviews with Twin Cities' developers with the objective of finding out who they were, what motivated them to enter (and remain) in this market, how they went about the process of conversion, what types of buildings they looked for, and how satisfied they were with their experience to date. We also sought to define developer's attitudes toward a series of public policy issues centering on conversion. A better understanding of how the private marketplace operates in the Twin Cities area can provide a firmer basis for considering the appropriate public sector response to issues involving conversion. We interviewed a total of twenty-seven developers, who were together responsible for carrying out 69 percent of all conversions.

WHO ARE THE DEVELOPERS?

Based on the interviews, we have characterized the developers into three types.

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*Donald H. Haider, Economics, Housing and Condominium Development. Evanston, Illinois: Center for Urban Affairs, Northwestern University, January 1980, p. 9.

Type A. Experienced Investors

For the most part these developers are incorporated entities, with a demonstrated track record in the housing market, either in condo conversions from other parts of the United States or in other types of housing in this local market. They are developers and investors in the real estate market on a continuing basis.

Type A developers are interested primarily in larger buildings of at least seventy-five units and deliberately seek out a "good buy;" they do not convert buildings they already own. Motivation for their projects is clearly a profit motive from short term investment, with the intent to continue in this market if they are successful in realizing anticipated profits. They tend to seek out projects that can be converted quickly and with a minimum of improvements. (Eleven of the developers interviewed fell into this category).

Type B. Contractors and Developers

People in this category have very different motivations, although profit is still important. They seek out buildings with special characteristics that will allow restoration and historic preservation and will tie in with neighborhood revitalization.

Type B developers have a more complex set of interests in conversion. Their efforts are directed toward extensive remodeling and major construction to create final units. For them, the business of conversion is not just a matter of investment, but involves a contracting business as well, so that their livelihood comes from two sources. Small projects are sought out, generally in the range of five to ten units. Conversion takes a long time and thus creates higher financial risks.

To date, this type of developer has concentrated in the Historic Hill and Irvine Park areas of St. Paul. The potential interest, however, could be in any buildings that offer special architectural resources. For-profit and nonprofit organizations are both included in this category. Type B developers can just as easily shift to non-residential conversion since it is not the housing market per se that stimulates their initial involvement. (Eight of the developers interviewed fell into this category).

Type C. Owners and Investors

These individuals are relatively inexperienced in the housing market as developers, although they are very likely to be owners of apartment buildings.

Their motivation to enter the conversion market is opportunistic, in response to specific favorable financing mechanisms. Below market interest rate financing, for example, reduces their risk during a long sell-out period when there is no income. Generally, their projects are small to moderate in size (ten to twenty units), although one developer in this category converted an apartment building with more than fifty units.

Type C developers are likely to be in and out of the condominium market, as financing terms dictate. Conversion risk is high for them in relation to the stoppages in monthly rental cash flow initiated either by remodeling requirements or their inability to retain tenants as buyers.

To date, a large number of these developers have been active in Minneapolis because of the home ownership programs and tax exempt bonding resources that the city offers. There is no reason why other communities could not become equally appealing to Type C developers if similar circumstances for buyer financing were made available. (Eight of the developers interviewed fell into this category.)

HOW DOES THE CONVERSION PROCESS WORK?

There is considerable danger in simplifying the information collected on the conversion process since each project described in the interview had unique conditions attached, but it appears that each of the above types of developers follow somewhat different processes, work with different time lines, and emphasize different phases because of their experience and/or motivations.

1. Selecting the Building to Convert

Type A seeks out buildings from owners on the basis of personal knowledge of the metropolitan real estate market, looking at the location as well as the selling price and tax benefits.

Type B seeks out buildings on the basis of their architectural features and location. Neighborhood is equally as important as structure. The building may be vacant, ready for demolition or moving, or it may be occupied at low rent.

Type C owns or can quickly use contacts to identify a specific building that will qualify for a market created by new financing conditions available to buyers. A new entity will be created for the conversion so as to evade ordinary income gains.

2. Time Taken to Convert a Building

Type A normally plans to complete the entire process in a twelve month time period, plus closings for individual units. Time is allocated equally between securing financing, making improvements, marketing at least half of the units, and final sales.

Type B takes an extended time for conversion, even up to three years. Major construction will not begin until construction financing and legal/architectural documents are finished. Delays run from four to eight months. Construction can take a year or more. Because buildings are small and there is neighborhood interaction throughout the process, actual marketing/sell-out times are cut down significantly.

Type C generally makes the quickest form of conversion, sometimes as little as six months if there is a high retention of tenants as buyers and no major rehabilitation work. Front-end time to complete documents of sale (or creation of a new entity to carry out the conversion) and secure financing is also done swiftly. This rapid pace of conversion has often resulted in favorable and highly competitive prices for buyers.

3. Tenant Relationships

It is impossible to generalize as to the way developers approach and inform tenants in buildings they plan to convert. It would be fair to state from our interviews that early projects started off with the developers not perceptive to tenants' needs. They did not take into account the hardships of forced moves and did not see any direct incentive to pay greater attention to tenants' needs.

According to several of the more experienced developers, second projects were handled differently for several reasons. First, it benefits the developer to retain tenants as buyers in many types of projects and also to maintain a minimum of public controversy if time-lines and sell-out periods are to return expected profits. Second, many developers are in the real estate market for the long pull and their reputation is important. Developers' sensitivity to their tenants' needs tends to increase in proportion to their demographic similarity to prospective buyers.

In response to the question, What would you do differently if you could do it over? - most responded with regard to their tenant relationships, and not to such matters as the type of building, purchase price, or legal entity.

4. Marketing and Contacting Buyers

Here differences between types of developers again surface. Type A uses newspapers, radio media, and realtor referrals. Word of mouth advertising is minimal. Signs are generally rated as only moderately important. Where current renters are a targeted market, major efforts are directed toward providing incentives to them.

Type B conducts marketing in a more informal fashion, using word of mouth, flyers in the neighborhood, and a limited amount of newspaper advertising. Realtors are not seen as major sources. Personal friendship networks are important sources of referrals and result in a high proportion of final sales.

Type C again uses traditional marketing efforts through newspapers but uses the neighborhood "weeklies" more frequently. Flyers are also distributed in the neighborhood in some instances. There is the same general resistance to using realtor referrals as for Type B.

DEPARTURE FROM THE CONVERSION MARKET

Responses to the question, What would have to happen to make you leave the conversion market? - stressed profit squeezes, the opportunity to increase rents so that it becomes profitable to own rental properties, lack of financing for buyers, increased government regulation, over-saturation of the market, and a refreshing comment of "boredom"! Probably the most interesting of the above responses is the prospect of returning to or moving into apartment rental buildings if profit levels and rent levels could get back in line with costs. Some of these factors are already operating to depress the conversion market (high interest rates), while others are a long way from reality (ability to build new apartment units at affordable rent structures).

DEVELOPER ATTITUDES TOWARD PUBLIC POLICY ISSUES

Developers were asked to respond to a series of policy statements centering around tenant rights, buyer protection, protection of the rental stock, management responsibilities and the role of cooperatives in meeting housing needs for low and moderate income households. Responses to twelve of the twenty statements showed enough clustering to indicate a clear developer's point of view (at least 66 percent were all either in agreement or all in disagreement with the statement read). Eight statements did not distinguish any specific developer viewpoint. The statements addressed five areas of public policy and one statement dealt with the developers' future plans.

<u>On Tenant Rights</u>

The developers gave strong support to providing tenants with the exclusive right to purchase for at least sixty days (25 in favor out of 27 total). They also strongly supported not discriminating against tenants on purchase price (21 agreed that lower prices could not be offered to non-tenants). There was strong disagreement with the idea of giving tenant associations legal rights to negotiate purchase of the building (19 disagreed). And developers rejected the notion that relocation payments to tenants would help the conversion process rather than hurt the developer (only 4 supported the concept).

<u>On Buyer Protection</u>

Reactions here showed that developers would give greater support to providing warranties on major appliances than on structural condition and on heating, air conditioning and ventilation systems (19 agreed on appliances, 15 on structural conditions). The greatest support for escrowing funds to cover warranties on structural condition came from developers involved with major rehabilitations (7 out of 8); the least support from developers in programs such as HOP IV (2 out of 8). Experienced developers and investors split down the middle (6 to 5) on this question. There was strong opposition to escrowing funds so that the condominium association could tap the fund, even under appropriate legal constraints (17 disagreed, 8 agreed with the escrow policy). Less than half (11) agreed that it is a good idea to pass over control of the condo association to the new buyers once 50 percent of the units are sold. This attitude may be affected by developer belief that new buyers do not understand property management responsibilities well. No one agreed that buyers understand these responsibilities well and only 9 tended to agree that they do. Developers do not see their obligations to the buyer as their single most important responsibility (none agreed with this statement though 11 tended to agree). The group placing highest priority on buyer interests was developers involved in major rehabilitation and historic preservation. Many of the buildings they converted were vacant or had limited tenant displacement and thus tenant rights had not been an issue.

On Rental Stock Protection

Defining a tight rental market as one with a 4 percent rental vacancy will undoubtedly provoke argument among developers (12 agreed and 12 disagreed with this definition). Only lukewarm agreement was evident for the statement that cities have an obligation to protect the size of the rental stock for low and moderate income households (12 agreed and 14 disagreed). Only the developer group working with major rehabilitation agreed strongly with this statement (6 out of 8). Greatest disagreement came from experienced developers in larger projects (3 agreed while 8 disagreed that the stock should be protected). There was strong agreement that home ownership is a better personal investment today than renting (18 agreed).

On Public Intervention in the Conversion Market

The developers showed strong support for Minnesota's legislative action in 1980 to adopt the Uniform Condominium Act (19 agreed it was needed). They uniformly disagreed with the statement that tenant relocation payments should be required (22 disagreed). They had a tendency to agree that public restrictions on conversions would increase the rate at which rents will rise in the future (4 strongly agreed and an additional 12 tended to agree while 11 disagreed). The developers seemed unwilling to look at rent control and condo conversion as related in a cause and effect way. More experienced developers tended to refuse to answer the question as not relevant. For those who answered the question, twice as many believed controlling conversion was preferable to rent control (12 agreed and 5 disagreed).

On the Alternative of Cooperatives

None of the developers were involved in cooperative conversions but all took a strong position that coop conversions do not provide better protection to tenants as compared to condos (22 felt this way). They strongly disagreed with the statement that coops make a better investment for low and moderate income households (25 disagreed).

On Future Involvement in Conversion

Despite the fact that the preponderance of conversions these developers had made were in the suburbs, they all showed more interest in conversions in the central cities in the future (24 responses). There was strong agreement that conversions have bid up the sales prices of apartment buildings in the last two years (20 agreed, with 10 of them agreeing strongly).

SUMMARY OF DEVELOPER SURVEY FINDINGS

Diversity among developers makes it difficult to either promulgate a specific "industry viewpoint" or to predict where the industry may go in the immediate future. Categorizing developer interests in our three sub-groups should be useful in looking at public policy issues and deciding what might be in the best public interest when regulating or intervening in the private marketplace. It is evident that the public sector has strongly motivated the private sector through financial incentives at the local level; it is even more apparent that state and federal financial incentives propel developer interest into different parts of the housing market wherever profit margins and risk levels are to their best advantage. Incentives to return to the rental market would most likely diminish conversion activity although there will be some segments of the industry which will remain, particularly those involved in major rehabilitation and neighborhood reinvestment activities.

It is generally acknowledged by those in the industry that buyer and tenant protection are legitimate public interest questions, but they disagree on how far the protection should go. There is far less acknowledgement that the public interest is served by preserving rental housing for low and moderate income households. It is probably fair to state that there is a philosophical opposition to the concept of "preserving" a market (for whatever reasons) as an artificial and unneeded constraint over supply.

If local financial incentives dry up and acquisition prices of apartment buildings continue to escalate, it is quite likely that little conversion will take place in the immediate future, despite availability of a large suburban rental supply. Developer interest in the central city rental stock seems at odds with experience to date, but perhaps can be explained by anticipation that central city local governments are more likely to provide the financial incentives, as compared with suburban governments.

SOURCES OF DEMAND - RESULTS OF A BUYER SURVEY

During spring of 1980 a questionnaire was developed for telephone interviewing of approximately 250 households, randomly selected from the total group of converted units throughout the metropolitan area.

Based on the findings of the conversion inventory it was decided to stratify the sample into five subgroups. This would allow us to isolate relatively homogeneous submarkets in the conversion market and thus be able to draw conclusions for each of these submarkets. Cooperatives constituted one group. Condominiums were further subdivided into central cities and suburban. The central cities sample was finally subdivided into three: St. Paul, Minneapolis non-subsidized, and Minneapolis subsidized (HOP IV). Data on the HOP IV subgroup could be used to evaluate the success of that program in meeting its stated objectives.

The sampling methodology required that eighty-eight names be drawn initially for each subgroup in a random sampling process. Because of a large number of unoccupied buildings in St. Paul and difficulties in verifying directory listed households in the suburbs as owners rather than former tenants, additional names had to be drawn. In total 501 "verified" households resulted in 264 completed interviews. From the large suburban pool, the sampling process resulted in twenty-three out of the fifty-two converted projects being included in final interviews. The objective, however, was not to be representative within each community but to gain an overall randomness throughout the metropolitan area for the five subgroups within the conversion market.

GENERAL OVERVIEW OF SURVEY FINDINGS

Comments here refer to all the survey responses (N = 264) and thus include households living in cooperatives in addition to condominiums.

The Buyers

- Seventy-one percent of the households were headed by a single individual. Single women accounted for 45 percent of all households.
- Household size was small: 1.41 persons. Only 5 percent had children and the median age of respondents was 44 years.
- The median household income was $17,900, with 21 percent of all households having a second income contributing to that figure.

- Eighty-seven percent had some postsecondary education; median years completed were 3.4.
- Three-quarters of the moves into the converted unit involved no change in the number of persons in the household, but 25 percent moved at a time when this number decreased either as a move out of a family home by a young adult, as an empty nester when the last child left home, or as a change in marital status.
- A high proportion of buyers had moved in quite recently. Forty percent had lived in their present home for a year or less.
- Buyers came primarily from the two central cities (65 percent), although only 32 percent of all converted units were located in the core cities. Almost half of all buyers had lived in Minneapolis before moving to their condominium or cooperative.
- One out of five had lived in a single family home prior to buying, with 60 percent of these former single family owners coming from the central cities. Former single family owners were older, with a median age of around 60.
- Conversion has shifted renters into ownership status, rather than providing new options for owners. Two-thirds had been renting prior to buying their present unit. Thus to date, conversion has not released a large number of single family homes for occupancy by younger families.
- Twenty-three percent of all owners had earlier rented in the same building. For condominium owners only, the percent is 16.
- Over half (54 percent) of the respondents were in professional/technical or administrative/management occupations, 12 percent were retired, and the remainder were primarily in clerical and sales occupations. A similar occupational distribution was noted for second wage earners in a family.
- While single males occupied 26 percent of all units, they were clustered in the younger age groups (40 percent of households under the age of 30 were headed by single men). Only 6 percent of the 60 and over age group were single men. In total, 21 percent of all households were under the age of 30 and 31 percent were over the age of 60.

The Costs

- Median price of the home (at time of purchase) was $33,000. Median monthly housing cost (current) was $340 which included association fees and heating in addition to repayment on mortgage obligations and insurance.
- A move into a condominium or cooperative resulted in many more households decreasing their monthly housing costs rather than increasing them. (The HUD study arrived at the opposite conclusion in their 1980 report on trends across the United States.) Our survey showed the breakdown on housing costs as follows:

  59 percent decreased monthly costs....median decrease of $90

  23 percent increased monthly costs...median increase of $75

  14 percent incurred no change

  4 percent no data

The Purchase

- Reasons for buying either a condo or a coop were strongly related to investment prospects from a future resale (33 percent) and affordable price and maintenance considerations (33 percent). A variety of reasons were given by the remaining third, including "precipitated purchase" for those who were previously renting in the same building.
- The single most important factor in selecting a specific building was location (45 percent), with characteristics of the building (16 percent) and financing sources (10 percent) falling into second and third ranks.
- Relatively little major reinvestment appears to have resulted from conversions as a whole: 40 percent said no improvements were made to the unit while 11 percent stated that their building was essentially gutted and remodeled.

Satisfaction

- A large proportion of owners believed that developers provided all or most of the information they needed at the time of purchase (70 percent). Fourteen percent said they were misled by the developer: but this seems to have had no lasting impact on overall satisfaction with the decision to buy. Ninety-three percent say they would do it over again.
- Satisfaction levels with association management also were high (76 percent stated that they were very satisfied). Satisfaction may be related

to the fact that 60 percent were doing the management themselves (as a volunteer association). Only 5 percent said that the developer was still in charge of management.

- The general expectation was that present owners would remain for a long time (56 percent indicated ten or more years). Approximately 15 percent saw this as their home for two years or less.
- Over a third said they knew other people in their building very well and this number increased in buildings with twenty or fewer units. A quarter said they had very little contact with other people in the building.

In summary, the survey results showed buyers were generally satisfied with their personal experiences in buying a converted unit, with their current situation vis-a-vis management, and with their expectations for investment gains. Units have attracted a large proportion of single person households and provided ownership opportunities at relatively low monthly costs for people earning somewhat below the metropolitan average. Conversions have not been as attractive to former single family owners as they have been to renters. Since 35 percent of new owners had previously lived in the same neighborhood, conversions have provided an alternative form of owner occupied housing for neighborhood residents.

MAJOR DIFFERENCES BETWEEN SUBGROUPS

Survey totals, however, tend to mask important differences within the market. The market is in fact segmented and our decision to work with five separate subsamples was justified on the basis of the survey results. Cooperative buyers are discussed in Part Two. HOP IV buyers, we found, were much younger than the average buyer and included an even larger number of single persons but with more male owners than average. They earned less income but had extensive postsecondary education. An above average proportion held professional or technical jobs. Almost 60 percent worked in the City of Minneapolis and a third worked in the downtown area of the city. One may characterize these households as potentially upwardly mobile, people who entered the home ownership market earlier than normally expected. Except for age and income, however, they are very similar in profile to the other Minneapolis buyers.

In contrast, St. Paul buyers are much more affluent, more are employed in administrative and management positions and many more households have two adults. They mirror the profile of a larger group of newcomers to the Historic Hill area and part of what has been termed the "gentrification" of an older neighborhood, where higher income households are replacing lower income households.

Suburban buyers tend to be older, with above average income for condo buyers as a whole. Half are husband and wife families and, interestingly, this is the group with the least amount of education after high school.

Table 4 shows the more important differences we found among the four subgroups of condominium buyers.

Table 4. COMPARISON OF CONDOMINIUM BUYERS AMONG SUBGROUPS

	HOP IV N = 56	Other Minneapolis N = 48	St. Paul N = 50	Suburban N = 47	Total N = 201
Previously renting in same building	14%	29%	14%	20%	19%
Living in single family home prior to purchase	7%	8%	22%	26%	15%
Remaining in same neighborhood	40%	33%	38%	35%	37%
Expecting to stay more than 10 years	19%	67%	62%	48%	56%
Median household income	$16,400	$20,225	$27,150	$21,400	$18,650
Median monthly housing costs	$340	$364	$428	$370	$370
Median years living in unit	0.33	3.0	1.75	1.6	1.4
Dissatisfaction with information given by developer ("little or no information given")	13%	6%	10%	13%	10%

It is quite evident that the condominium market is far from homogeneous. Different financing programs, neighborhood revitalization trends, and general shifts in lifestyle preferences have provided a wide range of options. It would be a grave mistake, our survey indicates, to treat conversion as a single faceted phenomenon.

DISPLACEMENT - RESULTS OF AN OUTMOVERS SURVEY

by

Thomas L. Anding and Rebecca Smith

What happened to the renters who chose to move rather than buy when their building was converted to condominiums? To fill this gap in our survey of the impact of conversions, the Center for Urban and Regional Affairs followed up with an outmovers survey conducted within the central cities area. The converted buildings in Minneapolis and St. Paul where successful buyer interviews had been completed (thirty-three buildings) were examined again in an attempt to find out what happened to those who moved. In this way, mover and buyer household profiles could be compared and useful information obtained on the displacement (or involuntary move) question.

Using the Polk Directory and the telephone company's reverse directory for the year immediately prior to conversion, a list of tenants was compiled and the process of "tracking down" initiated. The objective was to complete as many telephone interviews as possible from this group by contacting them at their current address. Over a two-month period (summer of 1980), 207 interviews were completed: 137 interviews in Minneapolis (77 in the HOP IV buildings) and 70 interviews in St. Paul. The questionnaire for this survey of outmovers paralleled that of the buyer survey.

GENERAL OVERVIEW OF SURVEY FINDINGS

Comments here refer to all the survey responses (N = 207).

The Move

- Seventy-two percent stated that conversion of their unit to a condominium was their reason for moving, but only 54 percent reported this as an involuntary move on their part.
- Most (86 percent) found a satisfactory neighborhood in which to live, with convenience of location (40 percent), characteristics of the specific home (10 percent) and neighborhood (14 percent) being primary reasons for their choice.
- Two-thirds liked their current home better and thought it was in better condition than their former home.

- One-third became homeowners after leaving; two-thirds have remained as renters.
- For those buying homes, 77 percent paid higher monthly housing costs; for those remaining as renters, 49 percent found their monthly housing costs higher than before, while costs remained unchanged for 42 percent.

The Movers

- Half of the movers had lived in the converted building for two years or less, while 10 percent had lived there for more than 10 years.
- Forty-two percent of the moving households were single individuals; 41 percent included both a male and female adult; the remaining 17 percent included children.
- Median age was 37.

COMPARISON OF OUTMOVERS AND CONDOMINIUM BUYERS

Table 5 compares demographic profiles of the group moving out and the group buying into the converted condominium units, with some interesting differences appearing. The overall effect was to produce a greater degree of homogeneity among the population residing in the converted buildings. Extremes of age and income were reduced, and a mixture of household types was replaced with predominantly single person households. This means fewer people are housed in these same buildings, with the average size of a household decreasing from 1.7 persons among the former tenants (outmovers) to 1.4 persons among the new buyers.

In the submarkets studied, specific elements of population changeover are highlighted. Among the St. Paul buildings, the elderly and retired residents have been replaced by a younger population. Buyers in the HOP IV program tended to have higher income and employment status than the movers from these buildings. The conversion to condominiums substantially reduced the proportion of residents in the lowest income range in all three submarkets.

Table 5. COMPARISON OF OUTMOVERS AND BUYERS

	TOTAL		HOP IV		OTHER MINNEAPOLIS		ST. PAUL	
	Buyers	Movers	Buyers	Movers	Buyers	Movers	Buyers	Movers
N =	200	207	56	77	48	60	50	70
Household								
Singles	71%	44%	89%	46%	89%	52%	52%	33%
female	42	26	48	30	54	26	30	21
male	29	18	41	16	35	26	22	12
Households with children	5	17	4	22	0	8	7	20
Persons/households	1.4	1.7						
Age								
Under 30	26%	29%	45%	61%	2%	0%	25%	18%
30-39	28	25	34	23	38	26	29	28
40-49	13	11	11	5	11	24	15	8
50-59	15	11	5	5	18	17	15	14
60-69	11	10	3	3	20	21	10	11
70 and over	7	11	2	3	11	12	6	21
Median age	37 years	37 years						
Household Income								
Under $10,000	4%	19%	5%	22%	3%	10%	5%	21%
$10-19,999	48	31	71	40	46	26	21	24
$20-29,999	27	22	22	18	22	16	35	32
$30-39,999	10	16	2	18	14	18	19	13
$40,000 and over	12	11	0	1	16	28	21	10
Median Income	$17,900	$20,000						
Occupation								
Professional/ Technical	34%	33%	45%	36%	35%	32%	43%	32%
Administrative/ Managerial	20	15	9	14	9	24	30	9
Sales/Clerical	24	19	29	26	26	18	6	13
Crafts/Operative/ Service	7	7	14	12	7	0	4	7
Retired	12	21	2	4	22	26	11	29
Student/Homemaker	3	5	2	7	2	0	6	7

There is clear evidence of a population change, resulting from the conversion of rental apartments to condominiums, of a sort that could be labelled "displacement." However, classic displacement--the replacement of blue-collar and lower income households by white collar and higher income households--is absent. Rather, population turnover in these surveyed buildings has resulted in a homogenizing of the resident population along the socio-economic dimension. Population displacement in these buildings has been of a limited and specific nature, affecting only certain types of households: the single-adult household has replaced the two adult household, a younger population has replaced an elderly segment, and a childless household has tended to replace those with children.

Households with children account for 17 percent of the mover sample. They bought homes more frequently when they moved than did the childless movers (54 percent v. 29 percent became owners after the move), suggesting that at the time of the move, they were in the market to buy a housing unit but the condominium did not suit them. This supposition is supported by the additional fact that households with children were less likely than childless households to find a satisfactory neighborhood, yet more often found their new unit better than the one they had left.

The experience of the elderly who moved was quite different from younger movers. They were predominantly retired, living on low income, and far more commonly rated the move as an involuntary one due solely to the conversion of the unit to a condominium.* Upon moving, the elderly nearly all remained renters (90 percent) and the impact of the move appeared to be more severe since more of the elderly had lived a longer time in the apartment building before it was converted (56 percent had lived there for more than six years, compared with 8 percent of those under 60).

The decision by one-third of the outmovers to become homeowners elsewhere corresponds directly with increased housing costs following the move. Table 6 compares median monthly housing costs for condominium buyers and outmovers who became homeowners or remained renters. In all instances the costs for outmovers who became homeowners were higher than for the condominium buyers.

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*Median income of persons over 60 = $14,400; median of persons under 60 = $23,000. Eighty-six percent of those over 60 moved because of conversion, with 68 percent stating this was an involuntary move.

Table 6. COMPARISON OF MEDIAN MONTHLY HOUSING COSTS FOR OUTMOVERS AND CONDOMINIUM BUYERS

	Total	HOP IV	Other Minneapolis	St. Paul
Outmovers				
Owners	$408	$460	$370	$450
Renters	285	272	325	285
Condo Buyers	370	340	364	428

WHO FEELS DISPLACED?

By their own definition, over half of the respondents (54 percent) felt they had been displaced from their former residence. Some 97 percent who said they moved involuntarily cited "condominium conversion" as the reason. Table 7 compares attitudes of those in the mover group who identified themselves as voluntary and involuntary movers. Those whose move was voluntary appear to have had greater mobility and a wider choice in their housing situation. They were younger, more often single, and with a higher income on the average. Despite their decision not to buy a condominium unit in the building where they previously rented, many did purchase a home elsewhere. The ability to pay the higher costs of homeownership was another aspect of their mobility.

Respondents whose move was forced appear to have had fewer options available. On the average, they lived at their previous residence longer than voluntary movers, and generally they remained as renters. The decision to move was quite likely precipitated by limitations of age and income. On the whole, they were less likely to be satisfied with their current home.

The question "Did you move voluntarily?" provides a direct measure of displacement by allowing respondents to define themselves. This was important since the total survey results provided a generally positive outlook toward moving while significant nuances appeared when this self-definition appeared in the tabulations. It seems clear that the catalyst for moves was the conversion process, but the response was unique to the circumstances of each household. Income, age, and length of residence appear to have been critical factors in determining how the move was perceived.

Table 7. ATTITUDES OF VOLUNTARY AND INVOLUNTARY MOVERS

	Voluntary N = 95	Involuntary N = 112
Reason for moving		
Condo conversion	43%	97%
Change in family status	14	0
Other	43	3
Locate satisfactory neighborhood		
Yes	93%	84%
No	7	16
Relation to prior home		
Better	93%	58%
Poorer	5	30
Current tenure		
Own	48%	19%
Rent	51	81
Median current rent	$265	$290
Percent over 60 years old	16%	28%
Median household income	$23,300	$18,000

PART TWO. COOPERATIVE CONVERSION

by

Louise Brown

A 1975 HUD study of cooperatives and condominiums concluded that coops are declining as a factor in new housing, due to the ascendency of the condominium.* In the Twin Cities, however, coops appear to be making a comeback, with over 50 percent of the Twin Cities' coop stock being produced in the last two and a half years. The following analysis discusses characteristics of both long term coop owners and newcomers to coops, comparing both to condominium buyers. In addition it addresses the role of coops in the Twin Cities housing market, emerging coop forms, and related public policy considerations.

*U.S. Department of Housing and Urban Development, HUD Condominium Cooperative Study. Washington D.C.: U.S. Government Printing Office, July 1975, Volume 1, Part IV, p. 7.

THE EXISTING SUPPLY

Our study of cooperative housing was confined to Hennepin and Ramsey counties, containing the central cities of Minneapolis and St. Paul, but Table 8 below includes all metropolitan counties and lists both newly constructed and converted units. Total coop units in Minneapolis (new and converted) were 889; St. Paul had 205 units and the suburbs another 571.

Table 8. COOPERATIVE HOUSING IN THE TWIN CITIES METROPOLITAN AREA, January 1980.

County	Converted Units (projects)	New Units (projects)	Total Units
Anoka	0	0	0
Carver	0	0	0
Dakota	0	219*	219
Hennepin	784 (32)	509 (4)	1,293
Ramsey	209 (7)	163 (1)	372
Scott	0	0	0
Washington	0	504*	504
TOTALS	993	1,395	2,388

*County Assessors Offices

Source: County Recorders Offices; Metropolitan Council Inventory, 1979.

Slightly over 40 percent of all cooperative housing has thus been created by conversion, and well over half the total stock has been produced since 1968 (1,217 units added after 1968 included: 493 in Minneapolis, 171 in St. Paul, and 553 units in the suburbs). In 1978 and 1979 alone, 891 units were added to the total supply, 62 percent of them conversions (see Figure 3). In addition to this inventory, it is estimated that another 400 units are in the process of being converted in Minneapolis at this time.* Figure 4 locates all new and converted cooperative housing projects in Hennepin and Ramsey counties.

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*Minneapolis Housing and Redevelopment Agency 1979 estimate.

Figure 3

GROWTH OF COOPERATIVE HOUSING IN THE TWIN CITIES

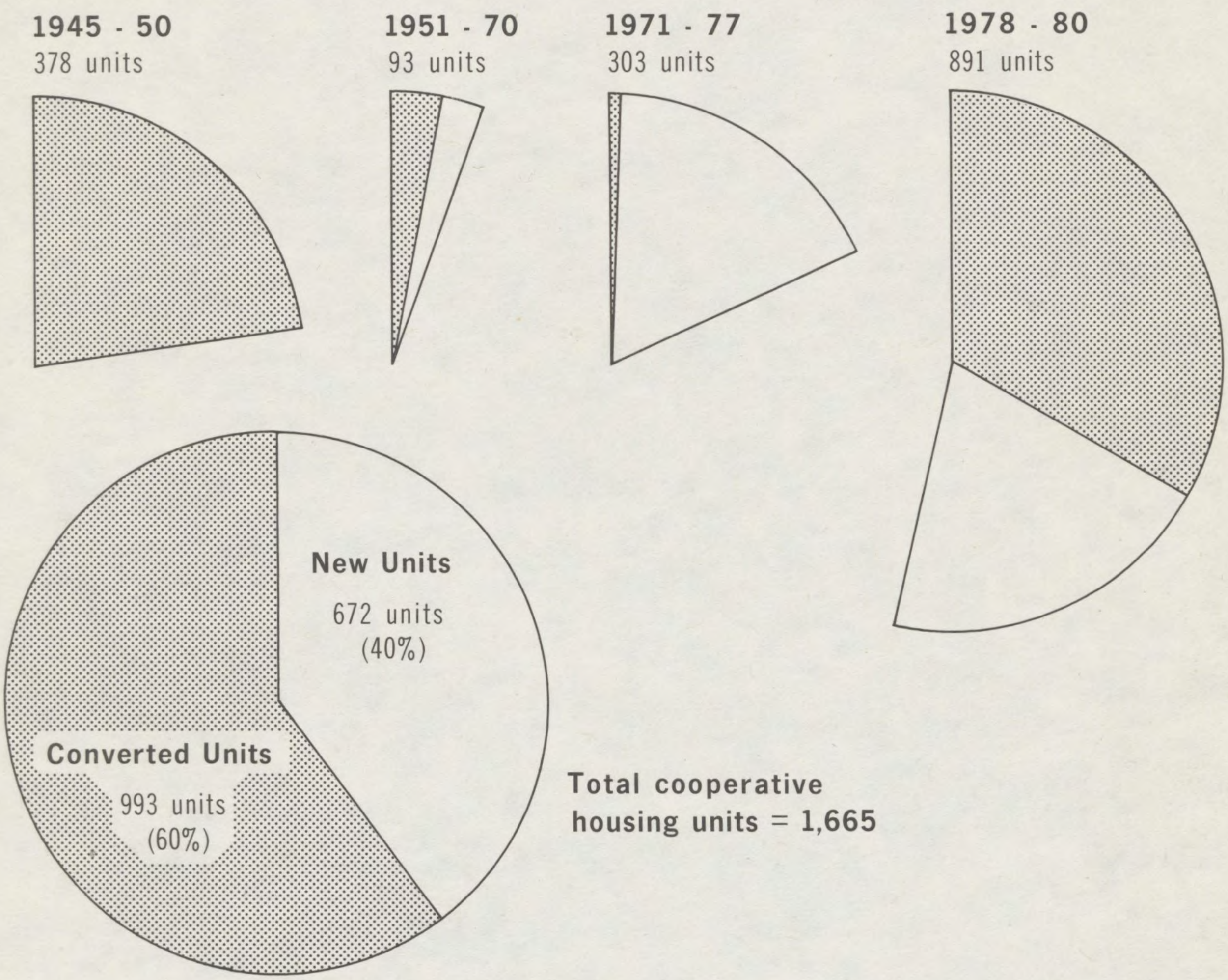
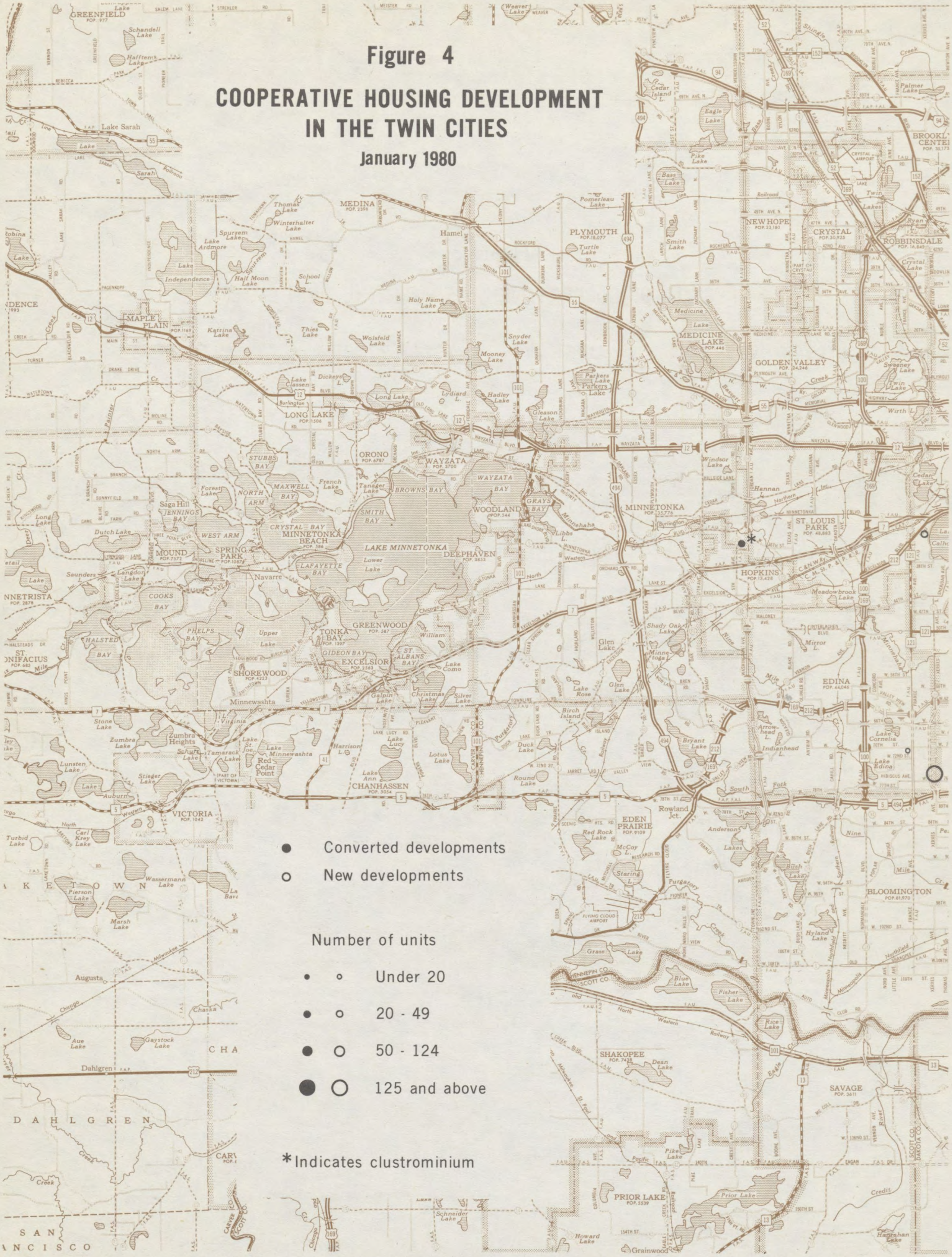


Figure 4
COOPERATIVE HOUSING DEVELOPMENT IN THE TWIN CITIES
January 1980



Source: County Recorders' Offices, 7-County Metropolitan Area

Note: Earliest recording date is 1951. Evidence is that cooperatives were formed before this date, but not recorded.

TYPES OF COOPERATIVE HOUSING

Cooperative housing differs from condominium housing in that residents do not own their individual unit, but rather own a share of the total development. Title is held by the cooperative association and purchase of a share or stock in the association entitles a buyer to use of a particular housing unit, shared use of common facilities, and to a vote in association matters. Where coop units differ in market value the cost of a share may vary, or alternatively all shares may cost the same but a person having a more expensive unit may purchase more shares. However this is arranged, coop by-laws generally prohibit individuals from holding stock in more than one unit and stipulate that all members be given equal voting power, regardless of their investment.* Voting power is used to elect a board of directors from among the membership. Boards may delegate responsibilities to members or hire management, but ultimately they are responsible for maintaining rules and for discharging the financial responsibilities of the association.

Within the Twin Cities, coops have taken a variety of forms and some do not exactly fit every aspect of the above definition. This is due in part to the rather spontaneous evolution of some of these coops. Between 1945 and 1950, twenty-three coop housing associations (378 units) were formed. All but one were located in South Minneapolis in an area between the lakes and close to downtown. All were formed in converted apartment buildings, the majority of which were between twenty and forty years old at the time of conversion. These coops share many elements in common, and for discussion purposes will be grouped and termed "Old-Style Coops."

Since 1950, market factors have occasionally contributed to the production of additional old-style coops, but recently new forms have appeared so that a more complex typology has emerged (Figure 5).

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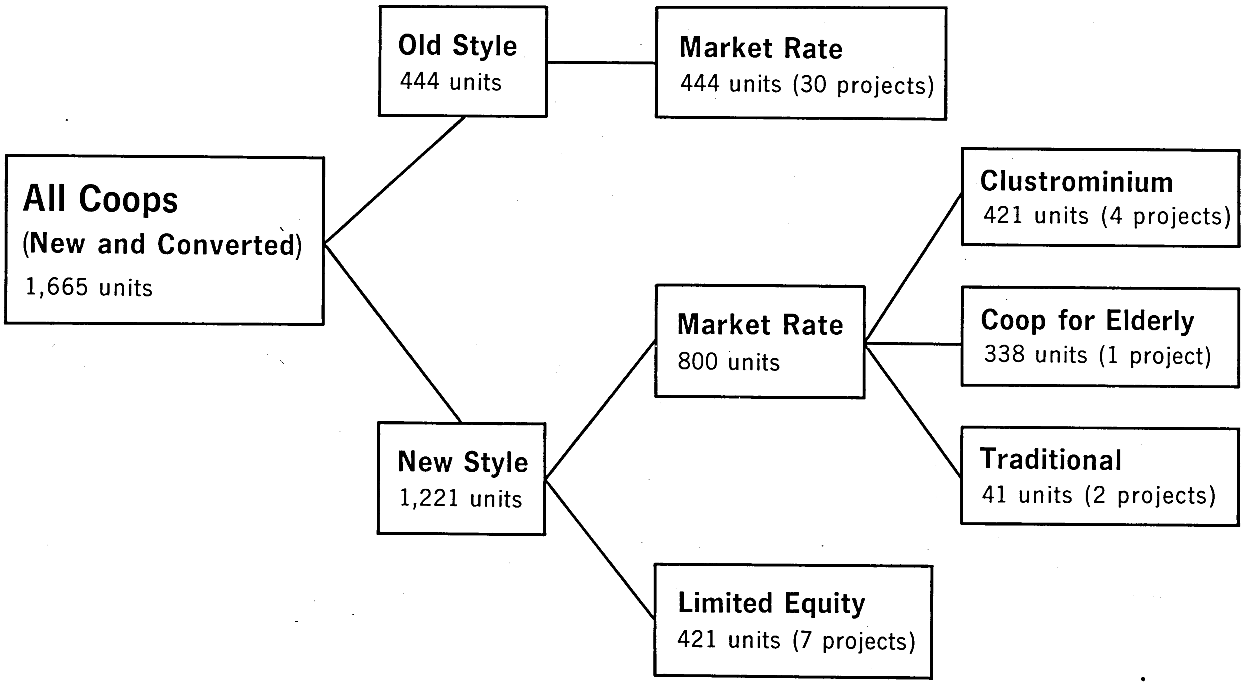
*Jonathan E. Zimmer, From Rental to Cooperative: Improving Low and Moderate Income Housing. Sage Professional Papers: Administrative and Policy Study Series, Vol. IV. Beverly Hills/London: Sage Publications, 1977.

Figure 5
THE VARIETY OF COOPERATIVE HOUSING IN THE TWIN CITIES
JANUARY 1980



OLD-STYLE COOPS

One of the distinguishing characteristics of this type of coop is that the impetus for development came about through tenant initiative or through landlord initiative. The project never included a professional developer or public agency. Old-style coops continue to be formed in the same way today. Currently all are at market rate even though buy in costs are often low. Most were created in response to housing shortages after World War II, when rising prices, coupled with wartime rent controls, made conversion attractive. Displacement was not uncommon, as not all tenants were able to buy in and not all buildings were felt to be worth buying. One displacee recalls... "..housing was so scarce, real estate people would get rich quick buying a building, chopping it up, and selling apartments. They particularly liked beat-up buildings because they could buy them cheap." How many coop attempts failed is not known. The survivors are a tribute to the determination and skill of the residents.

Difficulties encountered by these old-style coops are significant in that they illustrate problems which contemporary coops may be able to avoid or minimize with sufficient planning. The problem areas are in financing, organization and management.

Financing

Most banks were unwilling to finance coops, so many buyers bought on contract for share. In some instances buildings went from coop to rental and back again as sellers repossessed the building when units were not sold quickly enough. In other instances coops faced financial straits when individuals were unable to meet their payments.

Organization

Setting up and managing a coop apparently was easy for some and very difficult for others. Some coops were able to afford outside advice while others relied on their skilled or far-sighted members. Some evolved complex by-laws, though one reports having no by-laws at all and managing very well.

Some coop problems of today are a legacy of these early organizational decisions. For example, most coops have by-laws limiting the amount of time a unit can be rented out to a year or less. Where this is not the case, coops have had difficulty with investors buying in and renting out their units. In one unfortunate coop, even though by-laws prohibit persons from holding more than one share, one individual has bought shares as they became available under different names, and rented out the units. The consequences for owners and renters alike have been unfortunate: deterioration and rapid turnover.

It should be noted that the majority of coops are not used for rental purposes. In 1979, 76 percent of the coops in Hennepin County were homesteaded as compared to 57 percent of the condominiums. But, coops can be successfully rented out. One coop is currently 50 percent rented, and well maintained. Most renters are reportedly long-term (15 years or more) and equally interested in building upkeep. A board member attributed their success to the fact that owners allow the board to screen potential renters.

Thus, another organizational question is how much power the association should have over who buys or rents. Screening can be the occasion for discrimination, but residents who commented on the process felt that it was extremely important. Coops lacking such power report more problems with investors and speculators and distress due to noise or other habits of newcomers.

Management

Though management is often alleged to be one of the biggest problems facing coops, few respondents reported management problems. Difficulties arose in one four-unit coop with rotating responsibilities as members became elderly. Others were not timely in applying for homestead credit. But most proudly reported "doing it themselves" with or without some hired help.

NEW-STYLE COOPS

The key factor distinguishing new-style from old-style coops is the involvement of a professional developer.

Four distinctly different new-style coop forms have appeared in the Twin Cities: traditional, clustrominium, coops for the elderly, and limited equity coops.

Traditional

Coops which appear to be similar to old-style coops but which are known to have been developed for profit by a professional developer are termed "traditional." Only two coops fell into this category, both of which were built new.

Clustrominiums

The term "clustrominium" was copyrighted by a Twin Cities developer who felt the word "coop" might not be popularly received. He had experience in condominium conversion but switched to coops for financing advantages. In coop conversion the developer can assume the mortgage on the building set for conversion (the Minnesota Condominium Act prohibits blanket mortgages on buildings containing condominiums.) Thus the strategy is to locate an apartment building on which a mortgage can be assumed, set up a limited partnership to buy the building and finally establish a homeowners association for each building, selling shares in the association to buyers who will live there. The limited partnership retains ultimate responsibility for the mortgage until paid off by the homeowners association. An added advantage is that the developer receives the profit over a period of years rather than as a lump sum.

This scheme offers multiple advantages: a tax shelter for the investor; reduction in costs for refinancing, points, and closing; and more attractive resale to buyers, since second buyers can also assume the mortgage terms. In marketing these units, the developer plays a role for which there was no counterpart in old-style coops. A key objective is to retain tenants as buyers (3 1/2 percent downpayment in lieu of 10 percent to others). It is estimated that between 15 percent and 35 percent of all tenants have bought. This is higher than the average for tenant purchase in condominiums (16 percent).

Coops for the Elderly

Less of a departure from old-style coops than either clustrominiums or limited equity coops, these are nonetheless distinctive in their exclusive design and marketing for the elderly. The only completed project has a waiting list of one to one and one-half years. A $2,000 deposit is required to be placed on the waiting list.

One example of a building under conversion for the elderly is sponsored by a not-for-profit organization associated with a strong neighborhood church in South Minneapolis. They had been looking for ways to provide alternative housing for long-term neighborhood residents who could no longer maintain their own homes. The coop form was chosen only after serious consideration of other forms of housing. The advantages they found in coops were: home ownership without personal liability; simplified initial purchase procedures and resale procedures; ability of the association to assume maintenance for individual units, if necessary; eligibility for government subsidies similar to rent subsidies; and ability to provide extensive support services in the building (laundry, maid, guest room, central dining). The project is converting an abandoned school in the neighborhood. Downpayments are expected to range from $7,000 to $17,000 and monthly payments will likely be high ($425 to $1,000, depending on use of services). Some residents may be eligible for assistance.

Limited Equity Coops

This type of coop can be designed for either low or moderate income buyers, or both. Initial downpayments range from $350 to $2,600 for a one-bedroom unit. A formula is established for limiting equity build up and thereby future selling price for each unit. Formulae vary significantly. The simplest, limits equity build-up to the share downpayment increased at some predetermined interest rate (ranging from 5.25 percent to the Consumer Price Index). More complicated formulae incorporate the equity portion of monthly housing costs.

In addition to the 421 units of limited equity coop housing now in the Twin Cities market, 186 units (in seven projects) are in the process of being converted to limited equity coops in Minneapolis and St. Paul.

Like old-style coops, the limited equity coop is often tenant initiated. The catalyst may be rent increases, poor management, proposed sale of the apartment building, neighborhood vitalization efforts or a threat of condo conversion. One advantage for today's renter and potential buyer is the existence of organizations such as Common Space, a non-profit developer that will provide assistance only when tenants request it and no tenants will be displaced.

Thus far, limited equity coops have further resembled old-style coops in their relatively small size. The largest is fifty-five units in five buildings. Like old-style coops, all are located in the center city. They do, however, differ from old-style coops in several ways. They are developed in conjunction with neighborhood organizations and are designed to serve the needs of family housing. They involve substantial rehabilitation or use of abandoned buildings, thereby increasing the supply of multifamily housing. They minimize displacement. They discourage speculation by limiting the equity build up and thus maintain the housing as a long term resource at low or moderate cost. And, public and non-profit organizations play a major role in creating limited equity coops and in providing long term support services.

BUYER CHARACTERISTICS AND ATTITUDES

Buyers of converted cooperative units constituted a stratified subsample of the previously discussed buyer survey. Sixty-three interviews were completed. These have been further divided into three categories: newcomers (persons who have moved into any type of coop in the past two years), old-timers (persons living in their coop for nine years or longer), and the in-betweens. One-third of the sample fell into each of these groups.

WHO LIVES IN COOPS?

Coop buyers range from a woman who moved at age sixty-eight from a rooming house with fourteen rooms and one bathroom (where she lived for three years to save money for "something better"), to a couple who moved at age seventy-eight from their single family home and bought a share for $65,000 in order to reduce maintenance, to a young couple instrumental in forming their own coop when the landlord of their apartment building moved out of town. Caretaking responsibilities range from four ladies in their eighties who do all the painting and some of the grounds-keeping themselves, to buildings in which almost everything is contracted out.

Age, Family Size and Length of Residence

One of the most distinctive characteristics of coop residents is their age and length of residence. Some 72 percent of coop residents are single (56 percent single females and 16 percent single males). Almost three-fourths are over 60 years. A third are between ages 70 and 80 and 10 percent are over 80 years. These percentages would be further increased if clustrominium buyers were eliminated from the sample.

The age distribution is explained in part by coop dwellers' length of residence: about a third of the sample had lived in their units for over ten years, some for twenty years or longer. All in all, survey findings documented a high level of satisfaction with this type of environment and housing.

Looking at trends over the past two years, clustrominium buyers tend to resemble condo buyers more than other coop buyers. For instance, only 37 percent of this group are over 50, as compared to 81 percent of newcomers to old-style coops.

Satisfaction

Eighty-five percent of the sample believe they will continue to live in their coop unit for more than ten years or "until I die" - the rate was 56 percent for condo buyers. This high degree of planned permanancy might be predicted from age characteristics since studies indicate that persons tend to move less with age. However, comments by respondents suggest that it also reflects high satisfaction: "It's the smartest thing I've every done." "It's wonderful. You're in your own home, but your neighbors and friends are close by." "It's my home and I love it." "Half of my income goes to housing, but I love this place."

Perhaps another factor promoting satisfaction rests with the style of management and direct involvement. Almost nine out of ten say they run the coop association themselves. Ironically, one of the biggest problems facing old-style coops today is the direct outgrowth of that satisfaction. Most bought when young and have aged with the building. In one fourplex all residents are in their eighties and decided to sell the building to a realtor because it was getting too difficult to climb the steps. This building has reverted to a rental. Deaths and moves into a nursing home from another small building could have caused serious economic disruption had there not been such a ready market for the coop units.

Reasons for Buying

Old-timers tended not to distinguish between the two questions of reasons for buying the unit and choosing the specific building. The majority spoke of difficulties in finding a place to live after the war, desire to own, or desire to be with friends or relatives who had already moved into the cooperative.

Responses given by in-betweens and newcomers tended to reflect the reputation of coops in general and of specific buildings in particular. It became apparent that certain buildings enjoy a reputation for being well-managed, quiet, and well-built which extends far beyond their immediate neighborhood. Friendship patterns are also a strong factor in building selection. The percent who claim to know other residents very well is not significantly different from condo buyers. What is different is that most coop respondents said they have "long waiting lists of interested applicants" and when a unit does become vacant it is more likely to be sold by word of mouth.

Costs

Data from the buyer survey clearly supports the contention that converted coops provide lower cost housing than converted condominiums. Though monthly costs for some coop dwellers exceed $500 a month, 48 percent pay less than $150 a month. This compares with 10 percent of suburban condo owners paying this same amount, 7 percent for "other Minneapolis," and 2 percent for St. Paul and HOP IV samples. The percents for those paying under $250 a month are as follows: coops, 64 percent; suburban condos, 20 percent; other Minneapolis, 16 percent; St. Paul, 7 percent; and HOP IV, 8 percent.

One-quarter of the coop buyers who moved within the past nine years say they paid less than $10,000 for their purchase of shares, 56 percent paid less than $25,000. Sixty percent of the newcomers to old-style coops paid $20,000 or less, although some of the most expensive units are also in old-style coops (over $50,000).

Income and Occupation

Despite lower costs to purchase and lower monthly housing costs, it is not necessarily true that coops in the Twin Cities are the "poor man's condo." Income data was difficult to analyze because over half the sample was retired (12 percent for the buyer survey as a whole), and thus it was not surprising to find 25 percent saying their current income was under $10,000. However, while coops have more persons at this very low income level and fewer with incomes over $40,000, the percent of owners with middle income ranges is roughly comparable with other subgroups.

Of those coop residents who are employed, the proportion in professional, technical and administrative positions is roughly comparable to all other groups. Differences in the amount of formal education after high school are not as great as one might expect in view of the fact that many more are of an earlier generation (only 22 percent of coop residents had no postsecondary education while for condo owners the percent was 10).

NEWCOMERS TO COOPS

Newcomers were studied in greater detail since they may offer clues to future trends. There are two special characteristics of this group when compared with the total sample: they are older than newcomers to condos and are more likely to come from single family homes. Given the lack of promotion of cooperatives as an alternative to single family ownership one asks why this is occuring. Based on reasons offered by movers from single family homes to converted coops, the following are seen as the important advantages of coops over condominiums for this type of household:

- Coops offer more stable operating costs than condos.
- Control is possible over who is admitted.
- Coops are smaller, friendlier, and more secure environments.
- Coops are more closely tied to the neighborhood.
- One has more control over one's housing situation.

Finally, some persons (not all from single family units) were quite specific about their reason for preferring a cooperative: "In coops, we're in control, not some outside firm." "In condominiums someone's out to make a profit and it always costs more. Here no one is out to get rich." Though it is unlikely that there will be a stampede from condos to coops, it is interesting to note that 10 percent of the coop newcomers are movers from condominiums.

POLICY ISSUES

In the last two years of the 1970s the supply of coops increased quite rapidly and new forms appeared. Several of these forms raise particular issues for planners and decision makers.

OLD-STYLE COOPS

Given the advanced age of many residents, there is some question about the future. Will vacancies be filled by younger retirees, thus continuing the coops' role in providing an affordable retirement option? Or will coops collapse with the aging of current residents? If coops turn over gradually to another generation of young singles and couples this may create difficulties for those who tend to rely on "understandings" which are not spelled out in the by-laws. Old-style coops need support during this time of transition and protection from investor/speculator buy-ins so as to preserve them as a housing option.

CLUSTROMINIUMS

Clustrominiums have been produced in a greater variety of locations than other coop types. However, they have not contributed to the multifamily rehabilitation of housing, but have taken some of the more desirable rental properties and made cosmetic improvements. If it is assumed that ownership results in better maintenance, clustrominiums might result in an improved housing stock but at the expense of a diminished rental stock. Despite relatively low costs and financing advantages offered by the developer, few renters have bought in. Government efforts to actively encourage coop development should note the differing impacts of for-profit and limited equity conversion. In addition, cities may wish to consider the potential effects of for-profit coop conversion when they are designing buyer protection laws and condominium conversion ordinances.

LIMITED EQUITY COOPS

Of the 394 coop units known to be pending, half are limited equity. All of these are located in south Minneapolis, close to the downtown area in neighborhoods currently experiencing high population turnover and considered among the poorer areas. Sizes range from two to eighty units and all involve bringing buildings, some of which are totally abandoned, up to code. The result will be an increase in the supply and quality of low and moderate income housing. In addition, limited equity coops may be useful in helping suburban areas meet their housing assistance goals.

One reason for choosing the coop form has been the availability of public funds for underwriting. This raises the question of whether public funds should be used to convert occupied buildings, thus diminishing the supply of rental housing, or whether conversion should be permitted only if all tenants are able and willing to buy into the coop. What proportion of tenants, if any, should constitute the approval threshold?

Questions needing additional exploration are whether there is an ideal size of limited equity coop, especially for family housing, and how best to provide on-going technical support, for instance in budgeting.

IN CONCLUSION

On balance, there appear to be more benefits accruing from cooperative conversions than hardships, but some of the more recent forms contain the same seeds of discontent associated with displacement and buyer protection in converted condominiums. An important first step in an analysis of the appropriateness of this type of housing for a given purpose is to recognize the wide variety of coop forms and the strengths and drawbacks of each.

PART THREE. PUBLIC SECTOR PERSPECTIVES

by

Milo Pinkerton and Nancy Parkman Homans

THE FINANCIAL CASE STUDIES

by

Milo Pinkerton

Three conversion projects were analyzed with the purpose of describing the conversion process, identifying benefits accruing to different participants, and describing how public tax policy influences choices to own rather than rent. Projects A, B, and C are real and financial data supplied by converters are assumed to be accurate. Each project was chosen to represent a "class" of conversions (see also the three types of developers described under the developer survey, pp. 13-15). In order to maintain the developers' confidentiality, the property descriptions have been somewhat generalized and photographs of comparable properties in the same neighborhoods are shown to give the reader some idea of the character of the buildings. Figure 6 shows the location of the three case studies.

DESCRIPTION OF PROPERTIES

Project A

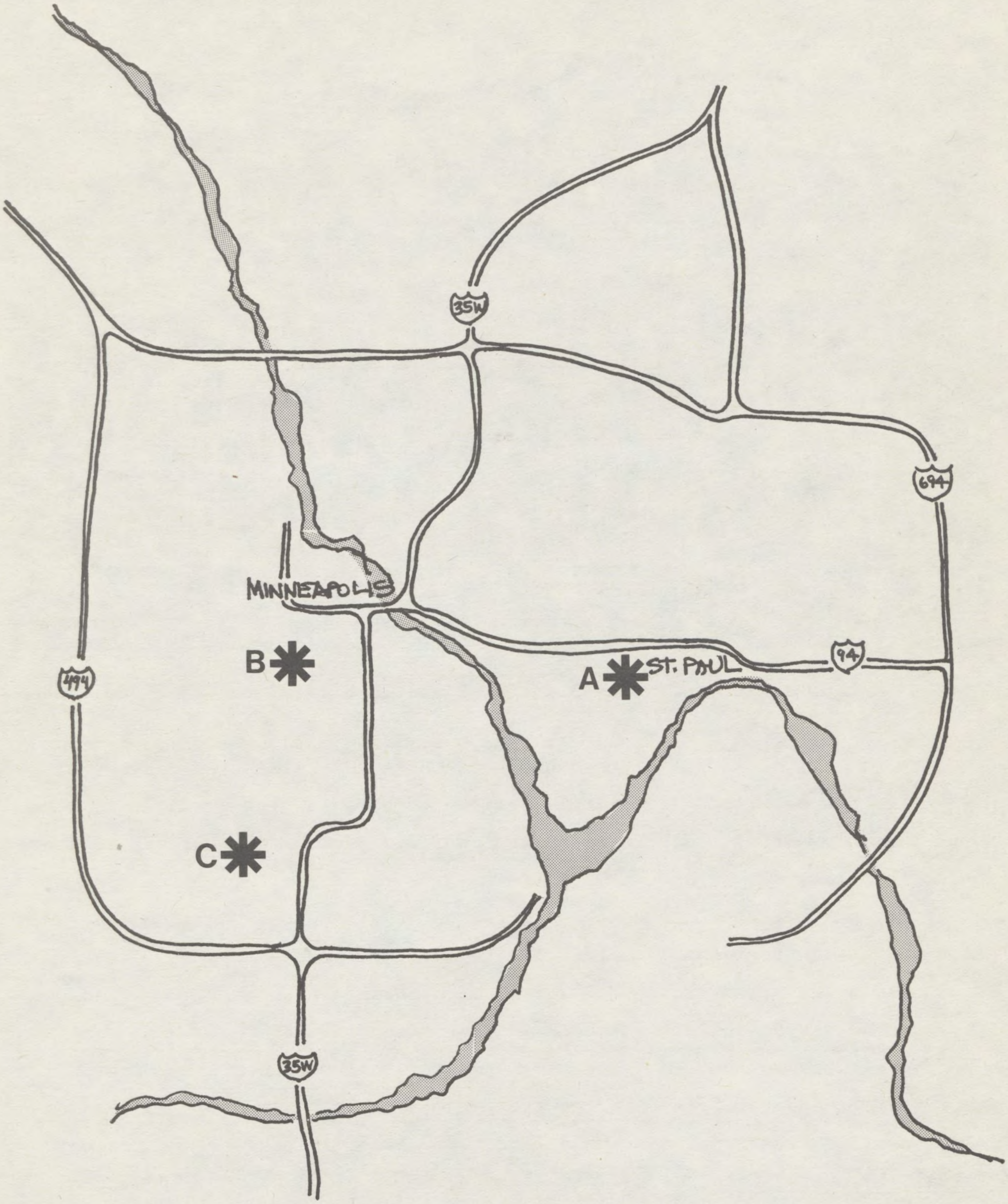
An 1880's vacant side-by-side duplex was moved to a different lot in the Historic Hill area of St. Paul and converted to four one-bedroom condominium units. No cost was incurred in building purchase, but renovation required total gutting of the interior and an extensive facelift of the exterior with care paid to architectural detailing. Off-street parking, laundry facilities, and security entrances comprise the amenity package.

The developer (Type B) was a non-profit organization, among the first to halt neighborhood deterioration by supplying housing for those wishing to remain in the city in rehabilitated homes. This project supplied 8 1/4 percent financing for first-time, single, moderate income buyers.

Project B

Built in the 1920s, this three-story brick apartment building was bought by first-time landlords in 1976, and converted to condominiums. It has a modest number of units (ten to twenty). One efficiency unit was added to an even mix of one- and two-bedroom apartments. Major improvements were made to electrical and plumbing systems, high grade carpeting was laid, and new kitchens and a security system were added.

Figure 6. LOCATION OF FINANCIAL CASE STUDIES



A building comparable to Project A in the Historic Hill Area of St. Paul.

The project is sited in a neighborhood where relatively few conversions have taken place. It is immediately surrounded by a few large single family homes and three-story red brick apartment buildings with generally above average monthly rents.

Fifty percent of those renting, purchased their units. Only one and a half month's rental income was lost per unit. The targeted market consisted of young singles or marrieds, childless, with incomes between $14,000 and $22,500 annually to qualify for below-market financing under the Minneapolis HOP IV program. The developer (Type C) was typical of inner city Minneapolis smaller project developers. This represented a first real estate conversion experience. Motivation to pursue a long term career in real estate was not typical, however. Great care was paid to having a high quality, successful project.

A building comparable to Project B, adjacent to downtown Minneapolis.

Project C

Built within the last ten years, this soundly constructed three-story apartment complex holds a large number of units (over 100). Ninety percent are one-bedroom. The complex offers an extensive list of amenities aimed at young "swingles" with moderate to high incomes who are "activity" oriented. The developer (Type A) had extensive experience in suburban condominium development both in the Twin Cities and elsewhere. Newer buildings, prestige neighborhoods, and large projects are always sought by this developer to capitalize on the in-house appraisers, attorneys, and feasibility analysts.

Acquisition cost of a convertible apartment is calculated by these professionals on the following rule of thumb: total sell out price minus estimated expense to convert at 30 percent (may be as low as 25 percent), minus a 15 percent developer's profit in order to leave 55 percent of sellout price for acquisition. Assumptions in the financial analysis include a 10-20 percent downpayment on three to five year purchase money mortgages; $5,000 minimum

A building comparable to Project C in suburban Minneapolis.

developer profit per unit; developer overhead at 5 percent; and an acquisition cost that is higher than the value the property would have as a rental building.

THE CONVERSION PROCESS

Conversion involved a common set of phrases for each project:

1) Estimating expenses or professional feasibility report.
2) Securing necessary fees, permits, and gap-loan and end-loan financing.
3) Rehabilitation.
4) Marketing and sales.

The length of time taken to complete these steps varied enormously. Project C took twenty-four months, with five months for renovation and sixteen months allocated to sell out; Project A required fourteen months, with one weekend only spent on sales but over eight months spent on renovation; Project B took only seven months, with one month for sales effort, and four months for renovation.

Sales occurred at different times in each development. Project B began sales before any renovation took place. Project C completed all common area renovation before any sales began so that the visual change to ownership could be used as a marketing tool. Sales effort for Project A consisted of one newspaper advertisement and word-of-mouth, which resulted in a complete sell-out in one weekend midway through the renovation process.

Each developer started the process with differing considerations. Project A started when purchase agreements on the lot and building were signed. Project B commenced with a paper transaction transferring ownership to a new entity in order to avoid double capital gains tax. The experienced developer in Project C had a purchase agreement written up, secured by a note allowing ninety days to find gap-loan financing, end-loan commitments, and feasibility reports and all with no cash "tied up" in the project.

Recurring themes in all three projects stressed the importance of using skilled construction workers to speed up the conversion process and doing a complete renovation since bulk purchases reduce costs and are very marketable. In projects A and B sales occurred faster than expected which led developers to believe a higher unit price could have been achieved. Despite this, the developers found it a better use of funds to offer lower than market prices to achieve a fast turnover and then reinvest in their next project. A closer look at each project's income and expense statements follows to help in understanding how the private market place assesses risks and opportunities.

COMPONENTS OF INCOME AND EXPENSE

Project A incurred a small loss (-2.7 percent while projects B and C returned almost 16 percent on gross income (Table 9). All the projects satisfied their initial developer objectives, including Project A where a small net loss was incurred. Higher sales prices, a shorter development period, or changes in reconstruction for Project A could have turned a profit. Extremely fast sell-out plus below market financing helped Project B to keep gap-financing charges low and overhead low. Project C's "rule of thumb" guidelines referred to previously were closely met. Although sales costs were greater than estimated, lower acquisition costs enabled the 15 percent minimum profit level to be realized as well as the $5,000 per unit profit.

Table 9. COMPARISON OF INCOME AND EXPENSES FOR EACH PROJECT

	Project A	Project B	Project C
I. Income			
Gross sales income	100%	98.2%	96.7%
Rental and furniture income	0	1.8	3.3
Total income	100%	100%	100%
Average income per unit	$43,000	$33,000	$47,000
II. Expenses			
Sales	under .01%	under .01%	7.4%
Professional service and fees	3.3	4.2	1.7
Financing	7.0	4.2	12.6
Operations	8.9	1.9	6.7
Renovation cost	79.4	23.7	4.8
Costs to convert	98.6%	34.0%	33.2%
III. Land and Buildings	4.1%[a]	50.1%	51.0%
IV. Gross Profit (loss)	(2.7)%[b]	15.9%	15.8%

a) Includes house moving and foundation costs.

b) Includes staff costs which were expensed.

MOTIVATION TO BUY RATHER THAN RENT

To explain the econcmics of condominium ownership versus renting a pre-conversion unit, a cost/benefit analysis of three one-bedroom units is presented in Table 10. Sales prices were as of June 1979, varying between $50 and $60 per square foot. Financing allowed a 5 percent downpayment on all projects. Below-market 8 percent and 8.25 percent interest rates were available for Projects A and B over a 30 year term, and 11.5 percent rates over a 30 year term were used for Project C. Project A was originally vacant.

The increases in monthly housing costs of $122 and $232 in Projects B and C are offset by various hidden costs and benefits itemized in part IV of Table 10. These include the "opportunity cost" or the amount of money the downpayment would have earned if it had instead been invested at a 10 percent interest

Table 10. COMPARISON OF RENTAL COSTS AND OWNERSHIP COSTS FOR THREE ONE-BEDROOM UNITS

	Project A	Project B	Project C
I. Before conversion:			
Unit size[a]	800 sq ft	600 sq ft	760 sq ft
Monthly rent	0	$225[b]	$295
Rent/sq ft	0	$0.38	$0.39
II. After conversion:			
Unit sales prices 6/79	$41,000	$36,500	$41,500
Sales/sq ft	$ 51.25	$ 60.83	$ 54.60
Downpayment[c]	$ 2,050	$ 1,825	$ 2,075
III. Monthly condominium payments:			
Principal & interest[c]	$293	$254	$390
Association fee	$ 60	$ 53	$ 80
Real estate taxes	included	$ 40	$ 57
Total	$353	$347	$527
IV. Hidden monthly costs and benefits:			
Add: opportunity cost of downpayment (10%)	$ 17	$ 15	$ 17
Less: principal build-up	$ 26	$ 24	$ 13
Less: tax savings (30%)[d]	$ 83	$ 75	$120
V. Actual monthly cost (hidden costs and benefits in IV applied to payments in III)	$261	$263	$411
VI. Equity appreciation required to break even with rent[e]	--	1.2%	3.4%

a) Unit size remains unchanged.

b) Rent is low; $260 is estimated as the comparable market rent.

c) Project A - 8 1/4% interest, 30 years, 5% downpayment.
Project B - 8% interest, 30 years, 5% downpayment.
Project C - 11 1/2% interest, 30 years, 5% downpayment.

d) Median gross income, 1979, Twin City condo buyer was c. $19,000 = 30% tax bracket.

e) Twin City condominium appreciation has been 15% from 1975 to 1980.

rate, the principal build-up on the first year's payment, and the tax savings accrued through deductions on federal and state income tax payments for interest paid and real estate taxes paid (calculated at 30 percent on a single person income of $19,000). Totaling these hidden costs and benefits reduces the "actual costs" (part V of Table 10) to $261, $263, and $411 for each unit even before equity appreciation is considered.

Currently, a most attractive benefit in owning is equity appreciation. Projects B and C required only 1.2 and 3.4 percent appreciation for 1979 to break even with pre-conversion rents, while home appreciation in this metropolitan market has averaged around 15 percent in the latter part of the 1970s. Additional homeownership savings can be garnered as capital gains tax is shifted to a higher priced residence upon sale until a one-time exclusion of tax on $100,000 sale is allowed after age 55. Homestead credit tax in Minnesota (maximum of $650 at this time) further favors homeownership over rental status despite available renter credits. For as little as $2,000 down, plus estimated closing costs of $650, households earning between $13,000 and $19,000 a year could have purchased into one of these projects and gained financially by shifting from their renter status.

CONVERSION EFFECTS ON REAL ESTATE TAXES

After conversion 1980 actual taxes due from owners have decreased for two out of the three projects (Table 11) even though full market values have almost doubled. Instrumental in this reduction was a shift from non-homestead assessment rates in the rental building to homestead rates in the converted building, a slight change in mill rates, and a 58 percent state tax credit (maximum $650) on homesteaded property. Minnesota state income taxes pay this credit back to the local units of government, thus shifting the tax burden from the property tax to the income tax and from the individual home owner to the population at large. Note that it is the homeowner receiving the 58 percent homestead credit. The municipality is not penalized but receives the credited taxes from the state.

Table 11. REAL ESTATE TAX ASSESSMENT BY PROJECT

Project	Municipality	Full Market Value 1979 Before	Full Market Value 1980 After[b]	Full Market Value Percent Homestead	Actual Tax Due 1979 Before	Actual Tax Due 1980 After[b]
A	St. Paul	$715[a]	$143,400	100%	$47[a]	$1,030
B	Minneapolis	$159,500	$510,050	100%	$6,387	$3,878
C	Edina	$2,500,000	$4,665,000	73%[c]	$83,708	$63,092

a) $715 land value; building at zero dollar value; property owned by city at time of purchase.

b) Estimated with projected valuations and homestead formulas for 1980; not yet approved by State Board of Equalization.

c) 21 units not yet registered; of those registered 84% homesteaded for 1980.

IN CONCLUSION

The three case studies chosen for this analysis reflect the diversity in the local real estate market. Profit levels of 16 percent achieved, and profit goals of only 15 percent by developers, demonstrate that this market is sensitive to even slight fluctuations in costs - increases in interest rates or a downturn in sales. Risk levels are therefore high, and it is not surprising that financing conditions during 1980 have discouraged the private sector in condominium conversion.

Conversions have resulted in new capital investment and increased assessed valuation of the municipal tax base, but the tax burden to the homeowner is strongly cushioned by assessment procedures mandated by the legislature. the local community benefits by a spillover effect of increased real estate value. Financial benefits to the homeowner more than offset out-of-pocket increases in monthly housing costs and are a powerful stimulus for modest income households to look to condominium housing as an entrée into the benefits of inflationary spirals in housing prices.

THE MINNEAPOLIS HOMEOWNERSHIP PROGRAM (HOP IV)

by

Nancy Parkman Homans

The fourth annual Home Ownership Program for Minneapolis (HOP IV) was approved by the Council in 1978 and administered by the Minneapolis Housing and Redevelopment Authority (MHRA). The program was designed to expand ownership opportunities for low and moderate income households through a subsidized 8 percent interest rate on mortgage loans. Funding came through sale of approximately $55 million dollars in revenue bonds. Blocks of funds, not to exceed $15 million, were allocated to twenty-six of the city's lending institutions on the strenth of prior applications. After being administered by the lending institutions, HOP IV mortgages were then purchased by the MHRA.

Specific provisions set the maximum adjusted income level for those eligible for the program at $22,000 and maximum eligible purchase price for a single family home at $44,000. Two-to-four-unit buildings, with correspondingly higher allowable costs were also included in the program, provided they were to be owner occupied and sold to low or moderate income households.

The city set three goals for the program: 1) an income distribution goal within the $22,000 maximum (see Table 12); 2) an upgrading of the city's housing stock, with loan application approval contingent upon code compliance; and 3) a shift of existing housing stock from rental to home ownership status in order to satisfy the previous two goals. Condominiums were classified for the first time as single family homes, thus widening the market for lower income housholds. In addition, a provision was included to allow lending institutions to commit mortgage funds in advance to developers who proposed to engage in the conversion of a building. Some lenders committed as much as 50 percent of their allotment in this fashion.

EVALUATION MEASURES

During 1979, 435 units out of a total of 520 condominium conversions in Minneapolis used the HOP IV program. There is no question as to the market's receptivity to the program. In evaluating HOP IV we were concerned with the internal consistency of the program and its outcomes for the city's overall goals and housing policies. Did the program achieve what it set out to achieve? It will be suggested that the evidence is rather mixed.

The Planning Context

The central theme of Minneapolis' Plan for the 80s is population stability. Twin goals of maintaining a stable population of around 370,000 and increasing the proportion of middle income individuals and families are directly related to a number of specific policy areas, among which housing is particularly significant. The relationship between population and housing is clearly articulated in the plan:

> The goal for the Housing plan is to assure that the residents of Minneapolis, and particularly the young adults entering the household formation age during the 1980s, have the opportunity to secure decent shelter in a diverse, increasingly owner-occupied, high quality and affordable housing stock.*

Specifically, the plan outlines four objectives:

- Continuous improvement in the quality of Minneapolis housing.
- Construction of new market-rate units -- at least 800 units annually through the mid 1980s and at least 400 units annually thereafter.
- A ten percent increase in the proportion of owner-occupied housing units during the 1980s.
- Adequate housing for all Minneapolis residents, regardless of household income, composition, age, or race.**

Throughout the plan there is a particular emphasis on the use of condominiums to meet the city's housing needs. There are also a number of reasons to support this emphasis, including the high cost of single family home construction, the lack of land for new construction, and an increasing number of single family and duplex units occupied by only one or two persons. It was hoped that the availability of smaller ownership units might entice the elderly or empty nesters out of their larger units, thus freeing them for use by growing families. Since the population group the city hopes to attract is that in the early stages of family formation, the availability of affordable, single family homeownership opportunities is especially critical. Condominiums represent an efficient way to provide a large number of housing units for smaller households, including those currently residing in larger, single family units.

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*City of Minneapolis, Minneapolis: Plan for the 1980s, Hearing Draft. Minneapolis: City Planning Department, 1979, p. 2/2.

**Ibid, pp. 2/9, 2/21, 2/33, and 2/39.

The Data Base for Evaluation

The developer and buyer surveys presented earlier provided the data base for evaluating HOP IV in relation to these stated goals and objectives. One methodological difficulty with focusing exclusively on condominium buyers was the lack of information on the 60 percent of all buyers under HOP IV who purchased single family housing rather than condominiums. Findings on condominium buyers cannot be translated into an evaluation of the program as a whole.

A second methodological problem rests on possible sources of bias in the sampling process which tended to undersample those who had only recently purchased their unit or who were in a newly converted building so that current telephone directories did not list their names. It is considered unlikely, however, that either of these problems so significantly detract from the research design as to jeopardize the value of the data.

RESULTS

Characteristics of the Buyers

Demographic data from the buyer survey indicate that buyers of HOP IV condominiums are generally single persons, young, and upwardly mobile professionals. Few households (11 percent) have more than one person and even fewer (4 percent) have young children. Average household size is 1.1 persons. Average age is 33.9 and average household income is $16,018. In relation to the percentage goals established by MHRA for income distribution, the condominium component of the program came closer to the goals than did the program as a whole (Table 12).

Table 12. INCOME DISTRIBUTION OF HOP IV HOUSEHOLDS

Income	Goal	Condo Buyers	All HOP IV Buyers
Under $12,000	20%	13%	9%
$12,001 - 14,000	20	26	15
$14,001 - 16,000	15	21	20
$16,001 - 18,000	15	14	24
$18,001 - 20,000	15	8	19
$20,001 - 22,000	15	16	13

Source: Minneapolis Housing and Redevelopment Authority (MHRA), 1980.

It seems apparent that the condominium program component did enable young, moderate income households to own a home in the city. Those households, however, were not young families with children as had been planned. Households purchasing non-condominiums did tend to have slightly larger families (an average of 2.2 persons) and also had a much lower average age (20.7 years) than the condo buyers.

When asked about their previous residence, 80 percent of the HOP IV condo buyers indicated that they had been renting, 14 percent had been renting in the same building; two-thirds had been living in Minneapolis and another 25 percent in the suburbs. In contrast to condominium buyers in nonsubsidized units, the HOP IV buyers were much younger and they did not envision remaining in their unit for more than five years. Both groups found purchase of a condominium unit a good investment and the main reason for buying, but the younger HOP IV resident had not made a permanent commitment to either this type of housing unit or the location.

In the final analysis, it will be important to see whether the HOP IV owners remain in the city as they enter the family formation stage - as city officials hope - and what kind of people make up the next generation of owners in these buildings. Inasmuch as MHRA is not able to restrict the resale of units except to say that the 8 percent mortgages cannot be assumed by nonqualifying buyers, the question of whether the program will provide moderate income housing for longer than the very short run cannot be resolved for some time.

Characteristics of the Buildings

One of the benefits to the city of the HOP IV condominium program is that some older housing stock has been upgraded. Virtually all buyers reported that some work had been done on their unit. The building code compliance was mandatory to receive loan approval.

The concern that arose most frequently was the lack of on-going management and/or maintenance. Approximately 40 percent of the respondents mentioned some dissatisfaction with management - either because they felt misled about association costs or the quality of improvements to the building, or felt that needed maintenance was not being handled.

Once again, it seems that the most important data is not yet in. The durability of the improvements made is critical. Will additional sizable investments in those buildings be required in the short term? Will problems of building management be resolved as homeowner associations become more firmly established? Ongoing evaluation will be necessary to more fully measure the impact of the program on the housing stock.

Characteristics of Developers

Since developers of these converted buildings were, almost exclusively, in small operations for whom the conversion was a first or second project, their inexperience may be the source of many of the difficulties with tenant displacement, management services, and misleading sales promotions which have surfaced both in the surveys and in public discussion of the program. This hypothesis is echoed, in a general fashion, in the 1980 HUD study* of conversions throughout the country which suggest that provisions for tenant and buyer protection are among the outstanding needs in the conversion process. Many of the larger developers have included in their conversion process efforts at tenant resettlement and establishing of homeowners' associations. Inasmuch as it appears that HOP IV developers did not include such efforts, the program may not have been well served.

DISCUSSION

Like any effort to effect change, HOP IV was a melange of social and political goals and their antecedent values. Like all other such efforts, the results are a mixed bag of some goals met more fully than others, some values affirmed and others unfortunately left unaddressed. And, as with most programs designed to implement public policies, it is difficult to attach evaluations of success or failure. Rather, the effort should be to sort out what happened and which elements of the program led to those results. The issues of consistency with goals and objectives defined at the outset will be examined in turn.

Consistency of Program Goals With Context of the City Plan

In most respects, the HOP IV program objectives are highly consistent. Where the city plan stresses increased emphasis on attracting young families, HOP IV sought and received younger households. Where the plan suggested a 10 percent increase in homeownership, HOP IV provided for conversion of 435

*Cited on page 6.

rental units to owner-occupied condominiums. Total number of households served by the program was 1,729. The subtlety of the plan, not included in the provisions of the program, was an emphasis on encouraging empty nest households to relocate to condominiums, thus freeing the larger single family homes for households with children. Admittedly, such a strategy is a complex one, given that notions of shelter are intertwined with a person's self identity and quality of life. However, it is a critical issue for which virtually no provision was made in the design of HOP IV.

Consistency of Program Outcomes to Program Goals and Objectives

Again, the results are a mixed bag. The program did attract about 140 households from outside Minneapolis to buy homes in the city. It did provide ownership opportunities for 435 younger households. But we do not yet know if they will remain in the city once they begin to form families. Homeownership opportunities were provided to about 350 renters, 17 percent of whom remained in the same building, 74 percent of whom were residents of Minneapolis.

On the other hand, the condominium component of HOP IV did not serve young families with children, and with just over half of the units having one-bedroom, it can be argued that the stock was not appropriate for families with young children. Upgrading of the housing stock was accompanied by buyer dissatisfaction and concern about long term maintenance. Actual quality of the work done on the buildings could not be determined through our data, but this issue should be examined in subsequent reviews.

Displacement did result from the conversion process, and the results of the outmovers survey demonstrate that the elderly were a particularly disadvantaged group. As in any conversion, the number of involuntary moves is difficult to determine, but the issue remains sensitive and critical and the HOP IV program established no guidelines regulating the developers in the process.

Consistency of Program Outcomes with City Housing Objectives

It seems clear that the extent to which the HOP IV program contributed to the overall city goals of population diversity and stability, plus an improved housing stock will not be known for five to ten years. During that period, researchers will be able to determine the rate of turnover in HOP IV condominiums and the profile of the second generation of owners. Also interesting to note will be the destination of present owners as they move. A number of things could happen. Present owners, as they enter a period of family formation, may choose another home in Minneapolis and sell their condominium to a second moderate income small household. That would represent the best possible case for the city. To the extent, however, that present owners move to a suburban home and/or sell their condominiums to higher income young households, the purposes of the program will not be as well served.

The other critical issue to watch over time is the quality of the housing stock. To the extent that maintenance of the buildings is sustained, thus providing a quality homeownership opportunity to future generations of buyers, the city will have been well served. If the opposite is the case, and the building is able only to serve a limited number of buyer generations, questions as to the value of the public investment legitimately can be raised.

IN CONCLUSION

An analysis of this sort could have taken a number of tacks. The most obvious alternative to that taken would have been to critique the notion of conversion of the rental stock and evaluate the effect of a decreasing moderate income rental stock for the city's population. That is a legitimate issue but in this study the goals were taken as given -- legitimate outcomes of the political priority setting process. In the final analysis, it can be argued that the "failings" of the condominium component of the program are attributable to the fact that particular issues of conversion were not specifically explored in the course of the program's design. With the exception of a maximum sale price and buyer income, the specific provisions for the conversion of rental units were determined by the lending institutions who committed mortgage funds to converting developers. The high percentage of one-bedroom units, on the face of it, does not affirm the goal of providing housing for families with young children, for example.

Other issues, more specific to condominiums, have to do with the displacement of existing tenants, establishment of homeowners' associations, and delineation of association and maintenance costs. Where it may be reasonably assumed that buyers of a detached single family home will make the effort to maintain it, the dynamics of establishing a homeowners' association to work with a management service is more complex. In most of the non-HOP IV conversions, developers played an active role; often in HOP IV conversions, they did not. The city's long term goal of an improved housing stock will only be met if these buildings are adequately maintained on a continuous basis.

In each of these areas, no guidelines were established, in spite of their impact on the success of a conversion project. Perhaps it was because the MHRA anticipated that relatively few condominiums would be brought into the program. It is clear that an evaluation of the HOP IV program must be ongoing, since several of the most crucial issues cannot be examined in the short run. The condominium conversion process has the potential of enabling the city to achieve its goals of population stability and improved housing stock, but in order to do so, the city must more actively guide that process around some of the pitfalls encountered by the HOP IV program to date.

PART FOUR. QUO VADIS?

by

Barbara Lukermann

As this analysis draws to a close the pace of conversion in the Twin Cities metropolitan market has slowed and anxiety that tomorrow may be too late has given way to a less pressurized environment. The housing crunch has not let up and in fact the combination of tighter rental markets, higher interest rates, and absence of mortgage loan money have combined to make a bad situation worse. We are continuing to look at innovative ways to reduce the cost of housing; homeownership continues to be a most attractive option, if the entrée is there; and yet there is a new anticipation (or fear?) that in response to tightened federal and state fiscal belts the local property tax rolls may once again escalate and the advantages of ownership may not look as enticing as before. This may be a most propitious time to review the conversion phenomenon and the public policy issues that surround it.

Certainly, the concerns noted in the first pages of this report are still valid -- consumer protection, affordability of housing, availability of rental housing for lower income households, and real estate speculation profits. Many communities have enacted regulations to guide the private marketplace so that maximum public good may result, yet the Twin Cities metropolitan area has seen almost no new regulation in the past year. This final chapter is designed to summarize what has been learned about these issues in this local setting and look at future implications. Each issue will be discussed in turn.

DISPLACEMENT

It is likely that around 5,500 households throughout the metropolitan area have been displaced through conversions over the past ten years -- that is, around 550 a year, with 136 a year in the central cities. This assumes that 85 percent of all converted units were occupied prior to conversion, and that the 16 percent figure for tenants who become buyers, identified in the survey, is reliable and representative of the market as a whole.

The largest proportion of those displaced were living in the suburbs in moderate to high priced rentals. If persons that decided to purchase were to mirror those displaced, the majority would be single persons without children and with moderate incomes. Data from the outmover survey however indicate that the tenant/buyers are not representative and that displacees include a larger number of families with children, as well as a larger number of elderly who found themselves either without resources to buy or unwilling to do so at this stage in their life. The outmover survey further showed that the persons displaced have very differing perceptions of the nature or consequences of the conversion activity. For some, the move is personally judged "voluntary" -- it was their choice to make a change. For over half, it was an "involuntary move" with significant personal consequences. It was also found that the Minneapolis HOP IV program promoting homeownership in lower price brackets made no specific provision for dealing with the displacement issue. A more comprehensive set of policies covering circumstances with which displacement can occur, who provides for those displaced, and who pays, still needs to be developed.

LOSS OF RENTAL HOUSING

Conversion of slightly over 7,600 units to condos and coops has removed a relatively small proportion of available rentals during a time period when almost 60,000 new units were built. Undoubtedly, it has reduced the total number of moderately priced rental units, particularly in the suburbs, but the impact is moderated by the fact that two-thirds of new buyers were taking themselves out of the rental market in order to purchase and thereby reducing overall demand.

There is little evidence that conversion has drastically reduced the supply of low priced rental stock for central city households. The highest loss has been associated with conversions requiring total gutting and remodeling (mainly in St. Paul's Historic Hill area), but most conversions have involved relatively little major reinvestment in the housing stock. The transition has been from moderate rental to moderately priced home ownership, and it has been mainly a suburban phenomenon.

Recent activity in converting lower priced rental property into low equity coops is reducing the supply of a scarce resource but at the same time creating an entrée for these households to enjoy affordable housing of reasonable quality, using the financial subsidies we give to ownership at all price ranges. This is a trade-off, with more benefits than losses for the community. It raises an important question of the future desirability of assisting more lower income households to become owners rather than remain as renters. A persuasive argument can be developed that the public objective should be to facilitate this shift in tenure because of financial subsidies to owners at all levels of government. If this is pursued, then more conversion of the rental stock into new forms of ownership would become a positive rather than negative feature. Low equity coops are one of two cheap forms of housing that can result in affordable owner-occupancy, the other being mobile homes. The only other option is to direct public policy so that investment in new rental buildings becomes a more attractive venture for private capital. But where any public funds are involved it would behoove us to look at conditions for maintaining at least some units for moderate income households in concert with those units that receive the subsidy.

AFFORDABLE HOME OWNERSHIP

With the median cost of occupying converted condominiums or cooperatives at $340 a month, and with fewer conversion buyers spending over 25 percent of their gross income on shelter than the average home owner, it appears that conversion activity has provided a viable way by which a fairly broad range of income groups and types of household can gain affordable housing. In a period when interest rates were well below the current rates, this form of housing gave a new choice to single person households, people in their late 20s and early 30s, as well as those in retirement years. It offered an opportunity to participate in the "limited benefits" of inflation -- rapid increases in home prices upon resale -- together with relatively low and stable monthly housing costs. These benefits were available to persons with higher income, but also to persons of more moderate means.

BUYER PROTECTION

There is little evidence in the Twin Cities area that developers have been unscrupulous by selling at inflated prices, making false promises to buyers, or failing to provide necessary information to allow buyers to make an informed choice. Instances of abuse are present, but not pervasive. One major problem, however, lies in the infancy of the market and the fact that four out of ten have lived in their current home for a year or less. There is the comfortable belief that all goes well, that the home is escalating in value and this is the "best personal investment every made," but it is too early to tell what the long term real appreciation rate of an 800 square foot two-bedroom unit in a lower income neighborhood will be after the baby-bulge moves through. In most cities, there is no strong "truth in housing" requirement to bring converted buildings into substantial full code compliance. The newly adopted Uniform Condominium Act requires some disclosure of building condition, but this is disclosure, not remedy.

Without doubt, today's buyer of a converted unit views it as an investment rather than as a simple decision about shelter. This is no different than any other home buyer in the present inflationary market. All wish to play a winning game. Bringing inflation down to an 8 percent annual rate might lessen the interest in home purchase, particularly if property taxes increase and renter credits also increase to equalize the situation. A major change in tax policies to provide tax credits for renters comparable to those that presently exist for home owners could be a significant deterrent for the conversion market--more of a deterrent than additional public regulation.

HOW MUCH MORE?

Conclusions from the HUD study (1980) were that conversions would continue at a rapid pace over the next six years (1980-1985), adding 1.1 million units. This is the equivalent of converting four more units for each one existing now (265,200 conversions in the United States by third quarter 1980). Applying this factor to the Twin Cities would mean another 30,000 conversions by the end of 1985. This is a mind-boggling number, particularly since we added only 60,000 new multifamily units in the decade of the 70s and are failing to add any new rental apartment buildings which do not have some sort of public financial subsidy.

What factors might promote or hold back this level of conversion activity?

SUPPLY OF CONVERTABLE BUILDINGS

Developers who indicate that their traditional supply of buildings is running out, are mainly interested in historic preservation. This stock is indeed in limited supply but the type of building converted in the suburbs and in Minneapolis is not. The supply of available buildings is not constrained so much by either structural condition or location as by money market conditions. New financing conditions create new criteria to be applied to any specific building, given that the location is acceptable to a large buyer group.*

CONDITION OF FINANCING SOURCES

These are legion and include the asking price by the seller of an apartment building, bridge loan interest rates, and mortgage interest rates for buyers. Currently financial conditions are depressing the market and there is very little prospect of the Twin Cities undergoing the pace of conversion anticipated by HUD. Profit margins are squeezed in both the rental and conversion markets. There is probably a greater willingness to sell rather than to buy a building for conversion, outside of some types of coops or luxury rental buildings.

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*See Department of City and Regional Planning, Harvard University. Condominiums in Cambridge: Forecasts of Conversion and Alternatives for the City. Urban Planning Policy Analysis and Administration series. Cambridge, Massachusetts: City of Cambridge, May 1980. This study develops a model for forecasting based on reservation and bid prices and an allocation concept for distribution within the city.

RENT CONTROL

At present, rent control is being debated in Minneapolis and advocated by a number of organizations concerned with affordable housing. HUD findings indicate that legislated rent controls are not necessary conditions for or leading causes of conversion. It is argued that controls on rents will diminish investor interest in the rental market, but there are already disincentives for rental property ownership. Returns on other types of investments exceed those of owning and operating rental property in the Twin Cities.

In general, developers would rather accept more regulation of the conversion process than a policy of rent control. But for many experienced developers this is an irrelevant connection. For them, the real problem is how to create incentives for new construction at rental levels that people can afford. It seems likely that controls on rent would increase rather than decrease the pace of conversion and the proposed rent control ordinance for Minneapolis includes an eighteen month simultaneous moratorium on conversions.

Up until 1980, increasesin construction and housing costs were outstripping increases in local market rents (Table 13). Last year, however, rents caught up.

Table 13. INCREASES IN CONSTRUCTION COSTS, HOUSING COSTS, AND RENTAL COSTS

Year	Construction*	Housing**	Rent**
1971-2	5.49%	4.68%	3.17%
1972-3	8.70	1.16	1.25
1973-4	16.74	10.05	2.21
1974-5	9.06	11.90	4.01
1975-6	3.97	8.91	6.10
1976-7	8.76	6.59	6.11
1977-8	12.27	15.56	6.79
1978-9	13.43	12.17	6.87
1979-80	11.07	11.43	11.04

*national
**Twin Cities Five County Metropolitan Area (1970 U.S. Census Definition)

Source: Data for construction from the Bureau of Labor Statistics, Composite Construction Index, Construction Review. Data for housing and rent from the Department of Commerce, Consumer Price Index, Minneapolis/St. Paul SMSA.

FURTHER REGULATION OF THE CONVERSION PROCESS

Certain forms of regulation can significantly reduce the amount of conversion activity even though not prohibiting it under a moratorium. The pace of conversion will slow in relation to the number of regulations that affect availability of projects. For example, requiring full code compliance as part of conversions would reduce interest in converting some types of buildings for lower and moderate income households, including some of the newer buildings. Requiring a building owner to first offer the building for sale to tenants was viewed by most developers as a factor which would remove them from the market because the costs involved in the search for an appropriate building could not be recouped. Requiring certain levels of tenant relocation payments or the replacement of the lost low or moderate income rental housing (as in Oakland) would significantly affect costs and timing in completing conversion projects.

Regulation per se, however, does not necessarily mean inaction in the market. It might in fact stabilize it. Basic tenant rights protection, already in the Uniform Condominium Act (and in Minneapolis and Wayzata) require notification and options to purchase. These should have no serious impact on the pace of conversion once the procedures have been incorporated into front end planning for a project. It is unanticipated events which extend the completion of a conversion, which have major effects on net profits.

PUBLIC INCENTIVES PROMOTING HOME OWNERSHIP

Tax exempt revenue bonds, with a portion reserved for condominium purchase under a home ownership program, have been a powerful inducement in Minneapolis to increase the pace of conversion. If there is a goal under any public financing program to subsidize homeownership, and condominiums and cooperatives are eligible forms, then the result will most likely be an increase in the amount of conversion activity. The market and thereby the sell-out time is improved for the developer.

In some cities, including St. Paul, use of public subsidies (for rehabilitation loans or below market rate interest) is confined to projects not displacing anyone and there is thus an open policy in favor of conversion with this specific caveat. Should major new sources of financial assistance be made available to support conversion in either vacant or non-residential structures undergoing adaptive reuse, then we should expect another surge of conversion activity.

OTHER

A further important factor is the "intervening opportunity" provided to a real estate entrepreneur. Like water finding its own level, there are persons in the housing market who intend to remain there, but who shift from one type of activity to another in response to financing and profit opportunities. As markets tighten up in their traditional roles, many have shifted to conversion. Some have done so simply to gain experience; others because profits from other sources dried up. During 1979, a 15 percent profit margin was sufficient to keep developers in the arena. Risks are higher today and other intervening opportunities have appeared. Developers are not as likely to continue with conversions unless a subsidy program is available.

A matrix of incentives for each participant in the conversion process is presented in Table 14. Financial, market, and public policy incentives are each considered. These are all factors that tend to encourage further activity but they are counteracted by the current condition of high interest rates. The present "mix" of incentives for all three participants fails to portend HUD's predicted quadrupling of conversions. In the Twin Cities, a pace less than that of the last three years of the 1970s is already evident. Nationally, the number of apartments converted to condo ownership during 1980 is estimated at 150,000 -- approximately the same pace as in 1979.*

*Publisher's letter, July 1981; as cited in Land Use Digest (Urban Land Institute), vol. 14, no. 8, August 15, 1981.

Table 14. MATRIX OF INCENTIVES TO CONVERT RENTAL HOUSING

CATEGORY	FOR THE APARTMENT OWNER	FOR THE CONVERTER	FOR THE UNIT BUYER
Financial Incentives	• Rent levels lag behind Consumer Price Index • Rapid increases in operating and maintenance costs without opportunity for matching rent increases • Building worth more if sold for a conversion • Subject to lower capital gains income tax if sold to a converter	• Mortgage pool (targeted) for buyers • Expanded mechanisms for coop financing	• Rapid appreciation under inflation • Below market interest rates available for targeted buyers • Tax subsidies for home ownership • Lowest cost "ownership option" in high density settings • Lower prices per square foot compared to new construction
Market Incentives	• Increasing vacancies • High turn-over rates	• Opportunities to retain renters as buyers • Demographic bulge in the young singles and empty nester age groups • Two income households making condo-coop life-style attractive (low maintenance demands) • Tight rental markets • Unique architectural feature of structure	• Costs of renting a comparable unit • Opportunities for easy resale • Opportunities to remain in same neighborhood when housing needs shift • Unique architectural feature of structure
Public Policy Incentives	• Mandatory housing maintenance regulations on multifamily housing rentals (potentially not on owner occupied units) • Rent controls - in a variety of versions	• Community goals encouraging home ownership for households without children as well as with children • Eligibility for tax exempt revenue bonding for buyers and/or converters • Eligibility for other public subsidy programs in the conversion process • No special permitting procedures governing conversion	• Buyer protection laws

FUTURE RESEARCH

Three important areas were beyond the scope of this study but are ripe for additional research:

1. Further displacement research, with particular attention to impacts on low and moderate income households and families with children, and on the gentrification implications of conversion activity.
2. Fiscal policy impacts, at the local city level of government, and also the implications of state tax policies and tax transfers and effects of policy shifts to benefit renter groups equally with homeowners.
3. Research as to the appreciation (in constant dollars) of converted properties as compared to other types of residential real estate.

The first area is necessary if we are to formulate appropriate policy to reduce unnecessary hardships and find solutions to the larger problem of increasing the supply of affordable rentals for less affluent families.

The second area of research should document how much new investment is being made to older stock as part of conversion, how more qualitative improvements might be encouraged without unduly increasing occupancy costs, and whether there are increases or decreases in the cost of delivering municipal services to this type of owner occupied housing. None of the above have been documented.

The last type of research should monitor the market to determine how the converted stock compares in appreciation to other types of real estate. This will provide needed consumer information and act as a barometer for converters and buyers alike. Certain types of conversions (for example, lower priced, small one-bedroom units in older neighborhoods) may not maintain their long term value as well as other types of buildings or other locations; but, on the other hand, they may be comparably good investments. Evidence to date is that the first time buyer is the primary financial beneficiary. Subsequent buyers do not capture a comparable rate of appreciation.

PUBLIC POLICIES AND FORMS OF INTERVENTION

Findings from this study suggest that the following policy areas are of highest importance and point out where public intervention in the market is appropriate.

REGULATION FOR DISPLACEMENT AND BUYER PROTECTION

In addition to the basic tenant rights covered under the Uniform Condominium Act there is need to provide special assistance to families with children, low income households, and the elderly when they must find alternative housing. One option is to require a tenant relocation payment, a second is to mandate a referral service. Costs for either could be included in calculating sales prices for the finished units. A third option is to provide a lifetime or extended tenancy within the converted building.

Disclosure of building defects is required under the Uniform Condominium Act with a right to cancel on purchase agreement within 15 days. Recent research on how California buyers react to mandatory disclosure on real estate located in earthquake hazard zones reveals that all too often disclosure is provided at the end of an individual's decision to buy and therefore at a time when the consumer is psychologically unprepared to drop the sale or has made other decisions making it difficult to do so.* The timing of disclosure is, therefore, as important as its nature.

There seems no good reason to exclude condo or coop multifamily housing from any regular inspection program of city building departments. Inspection serves as a means of maintaining public safety and early warning of major structural problems. Since a large proportion of these buildings are run by home owner associations without experience in multifamily property management, inspection should be viewed as an additional buyer protection device, rather than as an intrusion on property rights.

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*Risa Palm, Real Estate Agents and Special Study Zones Disclosure. Monograph, No. 32. Boulder: Institute of Behavioral Science, University of Colorado, 1981.

PROMOTION OF HOME OWNERSHIP THROUGH LOCAL FINANCIAL ASSITANCE PROGRAMS

Our traditional concept of promoting home ownership has been equated with a single family or duplex structure. Other forms (including condos, coops, and mobile homes) have generally been excluded. Given recent changes in household composition and the price of single family homes, it is difficult to justify excluding condos and coops from programs designed in a general way to expand home ownership. The HOP IV experience, however, has shown that this form of housing is not appropriate for creating more home ownership options for families with children. Coops in particular have proven to be a very acceptable housing option for the elderly and perhaps they could become equally appealing for younger, first time buyers.

An important caveat to any public subsidy program that includes converted housing would be making below market interest rate mortgages assumable upon resale only to households meeting the same qualifying income. Some mortgages under the HOP IV program carried this restriction, but many did not. Equally important in making local public subsidies available in the open market is to place restrictions so that the subsidies do not create additional displacement.

REGULATION OF THE RENTAL SUPPLY

Insufficient research has been completed to take any firm position on the merits of rent control as a mechanism for maintaining an adequate supply of rental housing at affordable costs. A recent Citizens League report concluded that rent control as proposed for Minneapolis "promises more than it can deliver" and what is needed is a more effective incomes policy, a way of transferring wealth to those with below minimum income. Policies might include negative income tax (Uncle Sam pays you!), housing vouchers, or grants.*

Many are arguing that a better way to regulate the supply of affordable housing is to increase incentives to build more -- primarily through reform of tax policies, adjustments in rent eligibility standards for new buildings as set by HUD, or reduction in local government's zoning and subdivision regulations. Given the tightening of the housing supply, it is important to

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*Citizens League Report on Rent Control, (Special Studies Task Force, Donald Van Hulzen, Chairman), Minneapolis: Citizens League, February 1981.

follow any path to increase the amount of available housing but only as part of an integrated set of policies.

Tax benefits to renter households and tax incentives for retrofitting older structures to make them energy efficient are other ways in which the public sector can "regulate" and help maintain an affordable housing supply.

In the third generation of condominium conversion regulation we have come squarely to grips with the problem of maintaining the supply of rental housing for those who have special difficulties in the market -- the elderly, the low income, and families with children. This is not a local problem. Given our "in place" subsidies and our commitment to the goals of homeownership, it is likely that more can be accomplished in the short run by encouraging more types of households to move into the ownership group. This includes encouraging lower income persons to move into limited equity coops and expanding equity participation of financing institutions, and possibly public agencies, into more forms of owner-occupied housing. Condominiums and cooperatives (and the converted versions of both) have a role to play and there are opportunities for making the benefit-cost ratio come out with a positive rather than a negative rating.

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