IV. Policy

The Role of State and Local Government in Supporting or Impeding the Expansion of Shared Equity Homeownership

Public policy has been a key factor in determining where alternative models of homeownership will thrive. Below the federal level, the three policies most favorable to the growth of shared equity homeownership are durable affordability, subsidy retention, and equitable taxation. Where these policies are lacking, resale-restricted housing tends to be in short supply.

Shared equity homeownership, in its many permutations, would barely exist in the United States without the commitment of hundreds of nonprofit, community-based organizations that persisted in championing these alternative models of tenure during years of little understanding and less support from major institutions of the market and the state. Most of the heavy lifting of developing, marketing, and managing resale-restricted, owner-occupied housing is still being done by nonprofits today, although more of the burden has been slowly shifting to the shoulders – and pocketbooks – of the public sector. Indeed, much of the growth in shared equity homeownership in recent years is due to the increasing number of city, county, and state officials who are incorporating these models into their own policies, programs, and plans. Especially in jurisdictions with inclusionary housing programs, where regulatory mandates or financial incentives have induced private developers to create affordably priced housing for lower-income homebuyers, these models have become a widely used administrative tool for preserving homeownership gains that government has worked so hard to create.

Despite the recent growth in governmental support for shared equity homeownership, there are still many cities and states where public policy remains more a hindrance than a help. The density allowed for residential development is too low to produce low-cost housing of any kind, or the regulatory burden is too high. The subsidies provided by a city or state are too meager to bring homeownership within the reach of low-income households. The political will of local officials is too feeble to resist the battle cry of "not in my backyard" when neighbors oppose low-cost housing or insist on affordability concessions when developers propose high-cost housing.

Impediments like these are not peculiar to shared equity homeownership, however. They discourage the development of any housing intended for persons of modest means, regardless of tenure or type. They shall not concern us here, therefore, despite the impact they can obviously have on how much (or how little) resale-restricted, owner-occupied housing will be produced in a particular locale. Our focus, instead, shall be on a trio of public policies at the state and local levels that systematically support – or, in their absence, systematically impede – the expansion of shared equity housing: durable affordability; subsidy retention; and equitable taxation.

In jurisdictions where these policies are present, the number of resale-restricted, owner-occupied homes tends to be large – and growing. In jurisdictions where these policies are lacking, usually because they have been preempted by policies far less favorable to shared equity homeownership, the number of resale-restricted homes tends to be small or nonexistent. Absent a policy of durable affordability, cities and states either impose temporary restrictions on the use and resale of publicly assisted housing – or require none at all. Absent a policy of subsidy retention, cities and states either steer their support for affordable housing away from nonmarket models of homeownership or structure their support in ways that cripple the performance of these models. Absent a policy of equitable taxation, cities and states force the owners of resale-restricted homes to pay property taxes not only on the equity they own, but also on equity they can never claim for themselves, eroding the hard-won affordability created by the jurisdiction's own subsidies, incentives, or mandates.[124]

Durable affordability, subsidy retention, and equitable taxation are treated as separate policies in the present chapter, despite their definitional and operational interdependency. Durable affordability is dependent on public subsidies that remain in place across multiple transfers of owner-occupied property and on public taxes that take into account multiple restrictions on a property's use and resale. Subsidy retention is dependent on models of tenure that perpetuate the affordability of housing assisted with public dollars and on methods of taxation that do not grab back with one hand what government has given with the other. The equitable taxation of resale-restricted housing depends, in most jurisdictions, on convincing a local assessor that the affordability purchased with public dollars will contractually endure for many years. These policies should be inseparable. Too often, they are not, making the production and preservation of shared equity housing for persons excluded from the conventional homeownership market a pair of tasks that are seldom easy and sometimes impossible.

Durable Affordability

Whether in cities and regions with housing markets that have long been strong or in areas where real estate prices have been historically stagnant but are now soaring, low-cost housing left completely exposed to market forces can quickly become unaffordable for persons of modest means. Confronting this market reality, a growing number of cities and states are now insisting on a quid pro quo for their support. They will use their dollars or powers to promote the production of housing that low-income or moderate-income homebuyers can afford, but the eligibility, occupancy, and affordability of that housing must be contractually preserved for a number of years. The most pressing policy issue then becomes how long these contractual controls should be made to last.

"Forever" has been the policy of some cities and states. These jurisdictions require permanent affordability for any low-cost housing created through the investment of public resources, the provision of regulatory incentives, or the imposition of inclusionary mandates.[125] Such a policy virtually guarantees the expansion of shared equity homeownership because deed-restricted homes, community land trusts, and limited equity (or zero equity) cooperatives become priority recipients of a jurisdiction's investment in affordable housing. The only places where the amount of shared equity housing has not dramatically increased under a policy of permanent affordability have been jurisdictions in which public subsidies for affordable housing have been reserved primarily for rental housing, or where public intervention has been ineffective in encouraging the production of low-cost housing of any kind.[126]

Many cities and states that have made a commitment to lasting affordability, however, have been reluctant to declare their allegiance to permanent affordability. They want contractual controls over the eligibility, occupancy, and affordability of any publicly assisted, owner-occupied housing to extend across multiple resales, enduring for a period of time, but they consider 40 years, 30 years, 20 years, or even 10 years to be "long enough." Once that period is over, all controls are lifted and the housing is pushed into the stream of commerce.[127] Some jurisdictions with time-limited controls, on the other hand, manage to achieve something close to "forever" by restarting the clock every time a home is resold. Since many homeowners are likely to put their resale-restricted property up for sale sometime before the contractual controls are due to lapse, even a control period lasting less than the 30-year standard we have adopted here in defining shared equity homeownership may permanently preserve most of a jurisdiction's publicly assisted owner-occupied housing.

Depending on the length of this mandated period of affordability and depending on how decontrol is handled, a policy that falls short of permanent affordability can still support the expansion of shared equity homeownership. The locality's pool of resale-restricted housing may eventually start leaking units into the market, but any policy that nudges public resources toward housing with affordability controls that endure across multiple resales is going to favor the development of alternative models of tenure.

Far less favorable is a policy of short-lived controls or, as still happens in many cities and states, a policy of no controls at all. Affordable housing for low-income homebuyers is created through the dollars or powers of government, but its affordability is quickly lost, disappearing at the first resale. Within such a policy regime, deed-restricted housing, community land trusts, and limited equity cooperatives may be eligible for public support, but they are at an enormous disadvantage. They must compete for scarce public resources against for-profit (or nonprofit) developers of market-rate housing who do not need to concern themselves with the durability of the materials they are using or the sustainability of the administrative structure they have put in place to oversee the eligibility, occupancy, and affordability of the housing they have produced. They must compete for attention and funding from public officials who may be biased against any controls over housing that is owner-occupied, no matter how much assistance these homes may have received from public coffers.

This bias runs wide and deep. The longer controls are made to last, moreover, and the closer they come to being permanent, as they are in models like the CLT and LEC, the stiffer the resistance among many public officials to offering them sanction or support. Their resistance is sometimes an expression of personal prejudice or political ideology, where any government-imposed encumbrance on private property is considered unacceptably "un-American." But the reluctance to insist on long-term controls over the resale of publicly assisted, owner-occupied housing may also be rooted in more practical concerns. Three tend to trouble public officials the most: the economic impact, the administrative burden, and the legal enforceability of resale restrictions that endure for many years.[128]

The economic impact feared by some public officials is that long-term controls over the use and resale of owner-occupied housing may prevent the improvement of low-income neighborhoods and impede the advancement of low-income people. Although limited equity cooperatives and community land trusts have been effectively used in a number of cities to revitalize neighborhoods with a history of disinvestment,[129] durable affordability is sometimes seen as a policy that is incompatible with community building in distressed inner-city areas. Similarly, although shared equity housing not only expands access to homeownership for low-income households and allows homeowners to increase their equity, under most resale formulas, durable affordability is sometimes seen as a policy that is incompatible with wealth building among impoverished households.

Those who advocate for durable controls have taken several different tacks in attempting to address these economic concerns. Some have focused on persuading public officials to take a longer view of neighborhood change, urging them to plan for the day when public and private reinvestment eventually succeeds in turning a neighborhood around, unleashing market forces that can threaten lower-income residents with displacement. Others have focused on persuading public officials to take a wider view of wealth creation. While conceding that resale controls impose a cap on the equity windfalls that individuals can sometimes reap in a rapidly rising real estate market, advocates for durable affordability point out that the amount of wealth actually accumulated by the low-income owners of most market-rate housing is usually less abundant and less secure than is commonly supposed. They argue, too, that boosting many households into homeownership via shared equity housing, allowing each an opportunity for a modest gain in wealth, is a wiser policy than helping fewer households to accumulate more. Some wealth is better than no wealth, in other words, and community wealth is as important as individual wealth in bringing prosperity to lower-income communities.[130]

Another way of addressing the economic impact that resale controls are feared to have on market building and wealth building has been to peg the duration or restrictiveness of these controls to market conditions prevailing in different areas of a city or state. In New Jersey, for example, the state's housing trust fund has often required resale controls to last longer on assisted projects located in hot-market suburbs than in cold-market inner cities. In Chicago, municipal officials have backed the development of a citywide community land trust that will monitor and enforce long-term affordability restrictions on publicly assisted, owner-occupied housing in dozens of neighborhoods. Different neighborhoods will have different resale formulas, however. The ground leases or deed covenants used in hot-market neighborhoods will contain a resale formula that heavily caps the amount of equity which a homeowner may remove on resale. The leases or covenants used in cold-market neighborhoods will contain a resale formula that lightly caps a homeowner's equity – or imposes no cap at all until the real estate market turns upward in that particular locale.

Other public officials have been less concerned about the economic impact of durable controls than about the administrative burden of monitoring and enforcing these controls over a long period of time.[131] Unwilling to have government bear that burden, they impose short-term controls or none at all. To their credit, they acknowledge a reality too often ignored by public officials who readily attach long-term affordability covenants to the deeds of publicly assisted, privately owned housing and then blithely assume them to be self-enforcing. To be worried about the stewardship of occupancy, eligibility, and affordability restrictions that endure for many years is to admit, at least, that somebody must monitor these durable controls if they are to have much effect. The question is who that "somebody" should be. As noted in the previous chapter, the party that imposes these contractual controls does not need to be the same one that monitors and enforces them; nor does that party need to bear unilaterally all the costs of monitoring and enforcement. These responsibilities can be shared, so they do not fall on government alone. It is reasonable, therefore, for public officials to concern themselves with how long-term compliance with publicly mandated controls over hundreds or thousands of units of privately owned housing is to be assured – and how the cost of compliance is to be covered. It is less reasonable to reject durable controls out of hand simply because somebody must watch over them for 30 years or more.

Finally, some public officials have been reluctant to embrace a policy of durable affordability because of an expressed concern for the legal enforceability of long-term controls. Their concern has a basis in two common law principles known as the "rule against perpetuities" and the "rule against unreasonable restraints." These doctrines, established in England during the 16th and 17th centuries, were adopted because of public sentiment against the concentration of land in the hands of an entrenched aristocracy.[132] They were intended to prevent the "dead hand of the past" from reaching too far into the future, constraining what later generations could do with their property. Simply stated, the rule against perpetuities says that controls over a property's future disposition, including its use and resale, may not extend longer than the lifespan of someone who is alive at the time the controls are imposed (a "life in being"), plus 21 years. The rule against restraints says that controls that unreasonably impede or discourage a property's owner from conveying his or her ownership interest are prohibited.[133]

Ironically, the motivation for encumbering shared equity housing with durable use and resale restrictions is rooted in the same sentiments that gave rise to the rule against perpetuities and the rule against unreasonable restraints over three centuries ago. Thus:

> The purpose of long-term affordability restrictions is similar to the purpose behind these old real estate doctrines. The restrictions retain housing affordability for low-income persons so that housing opportunities will be available to a wider income range of the population. They also tend to avoid concentration of housing ownership. It is therefore perverse that the very doctrines that were intended to undo concentration of land in the hands of a few are now possible barriers to expanding housing opportunities. (CHAPA, 1989: 3)

On the face of it, these barriers look rather formidable, since shared equity homeownership would seem to run afoul of both doctrines. After all, the disposition of privately owned housing is controlled for a very long period of time. These controls determine not only how private property may be used, now and in the future, but also to whom that property may be conveyed, how it may be conveyed, and how much the seller may charge. Some forms of shared equity housing try to limit forever the price for which an ownership interest may change hands, as well as the pool of income-eligible households who may purchase that ownership interest.

There is no question, therefore, that shared equity housing imposes restraints on the conveyance ("alienation") of residential property, restraints which endure across successive generations of homeowners. Nevertheless, the critical legal issue here is not whether such restraints exist, but whether they are reasonable. If the imposition and enforcement of these durable controls over the use and resale of privately owned housing can be shown to accomplish a worthwhile purpose – serving, in particular, a broader public interest – they can withstand legal challenge. As Debbie Bell concluded several years ago, when reviewing the relevant case law on this subject, "Limited-price preemptive rights are generally upheld when they serve a legitimate purpose or promote significant public policies, and when the person giving the option received some benefit in return."[134]

To buttress the argument that resale-restricted, owner-occupied housing does indeed serve a public purpose, supporters of shared equity homeownership have sometimes pursued an administrative agenda, persuading a state or municipal agency to make a public commitment to durable affordability – and to models that achieve it – through its comprehensive housing plan, its housing trust fund, or other homeownership assistance programs. For example, the policy of "forever housing" that was instituted by Connecticut's Department of Housing in the late 1980s (but later dismantled by a more conservative administration) declared that "state-assisted housing should be permanently removed from the speculative market" and proceeded to prioritize funding for limited equity housing cooperatives, community land trusts, mutual housing associations, and other nonmarket models designed to preserve "the long-term affordability of housing generated by public funds."[135] Affordability requirements lasting anywhere from 40 years to the useful life of the assisted property can also be found in selected housing programs of the City of Boston and the Boston Redevelopment Authority (Collins and White, 1994), in the municipal housing trust funds of Ann Arbor, Cambridge, Berkeley, San Francisco, Los Angeles, and Washington, DC, and in the state housing trust funds of Ohio, Oregon, Rhode Island, and Vermont (Brooks, 2002, 1994).

Supporters of shared equity homeownership have also pursued a legislative agenda in several states, aimed at removing common law barriers to the expansion of housing encumbered with long-term restrictions over its use and resale. They have won statutory sanction either for durable affordability controls in general or for specific models of shared equity housing that incorporate a commitment to durable affordability into their purpose and structure. The affordable housing covenants allowed by state law in Maine, the "housing subsidy covenants" allowed in Vermont, and the affordable housing restrictions allowed in Massachusetts are examples of the first.[136] Cooperative housing statutes enacted by Minnesota, Massachusetts, California, and Vermont are examples of the second.[137]

Legislative support for durable affordability and for models that achieve it has taken other forms, as well.

Since 1979, for example, California's Redevelopment Law has required the state's 400-plus community redevelopment agencies to set aside at least 20% of their tax-increment funds for low- and moderate-income housing. In addition, redevelopment agencies are required to ensure that 15% of all new housing produced within redevelopment areas is affordable to low- or moderate-income households. Long-term affordability restrictions must accompany all housing that is assisted with these set-aside funds or that is counted towards an agency's housing production goals. Rental housing must remain affordable to targeted income groups (very low, low or moderate income) for a period of at least 55 years. Homeownership housing must remain affordable for at least 45 years.[138]

Even in states where public policy, legislative action, or judicial opinion has tended to run in favor of durable controls over the use and resale of residential property, the common-law bias against long-term restraints has led attorneys for the sponsors of shared equity housing to be extra-cautious in crafting the covenants, ground leases, and corporate documents that contain such controls. They have also been careful in fashioning procedures for the sale of shared equity homes that ensure full disclosure and full acceptance of these controls by prospective homebuyers.[139] Documenting the voluntary nature of this contractual arrangement, in which all parties are fully aware of what they are getting into and what they are giving up, may be the simplest way of answering questions about the enforceability of the durable controls imposed by CLTs, LECs, and other sponsors of shared equity housing. A number of courts have upheld durable, fixed-price options, as Debbie Bell has pointed out, "simply because it was clear that the party granting the option intended to create it, understood the agreement, and received something in return."[140]

All of these administrative, legislative, and lawyerly contrivances are designed to increase the defensibility of durable controls should they ever be challenged. In point of fact, no cases have been found where durable controls over the use and resale of publicly assisted, privately owned housing have been invalidated by a state or federal court. Attorneys advising the sponsors of deed-restricted housing, community land trusts, and limited equity cooperatives have become increasingly confident that, with proper precautions, the longevity of contractual controls encumbering these homes can be legally sustained.

In the end, it is not the law that poses the greatest barrier to a policy of durable affordability. Nor, for that matter, is it the economic impact or administrative burden of durable controls. These practical concerns can usually be addressed. Much harder to address are personal, political, or ideological biases that have little to do with the practicality or impracticality of shared equity homeownership. In too many jurisdictions, the main impediment to a policy of durable affordability is the animus of key individuals toward any publicly mandated controls over private property lasting longer than a handful of years. They may reluctantly endorse short-term controls to prevent the quick turnover of publicly assisted, owner-occupied housing, but stubbornly resist more lengthy controls that preserve the availability and affordability of such housing for successive generations of lower-income homebuyers. They are morally convinced that durable affordability is bad.

Subsidy Retention

Durable affordability and subsidy retention are two sides of the same coin. Both policies preserve the public's stake in affordable housing. Both policies rely on nonmarket models of homeownership to make preservation a reality. They differ only in their emphasis. Durable affordability is focused on the way that private property is used and priced, demanding that homes assisted by government in the present remain affordable for lower-income homebuyers in the future. Subsidy retention is focused on the way that public money is invested, demanding that resources provided by government in the present remain available to lower-income homebuyers in the future. Since neither can be fully realized without the other, these policies should be inseparable. In many places, they are not. There are many jurisdictions in which a public commitment to durable affordability is not accompanied by a parallel commitment to subsidy retention. Because the latter is often treated as a separate policy, it must be discussed that way.

The high rate of homeownership in the United States is a product, in large measure, of public policy. For decades, prospective homeowners have feasted on a veritable banquet of public largess designed to lower the land costs, construction costs, rehabilitation costs, mortgage rates, downpayments, infrastructure, insurance costs, and property taxes for this favored form of tenure. Indeed, in any given year, the total amount of governmental subsidies made available to homeowners, across a broad spectrum of household incomes, usually exceeds by a wide margin everything that is spent by all levels of government in producing and assisting rental housing for lower-income people.[141]

What happens to these homeowner subsides when an assisted property is resold? To the extent they are identifiable, quantifiable, and recoverable, they are treated in three different ways by the public or quasi-public agencies that provided them; that is, they are subject to three different policies determining their disposition. Subsidies are either given away to the homeowner (subsidy removal), taken back by the agency (subsidy recapture), or locked into the home, stabilizing its price for future generations of lower-income homebuyers (subsidy retention). Only the last is entirely compatible with shared equity homeownership. It is also the policy least commonly found among the homeownership programs of most cities and states.

Under a policy of subsidy retention, subsidies are granted or loaned to a sponsoring organization to reduce the purchase price of houses, townhouses, condominiums, or cooperative apartments to a point where they are affordable to homebuyers of modest means.[142] A house that costs a nonprofit organization $150,000 to build, for example, might be subsidized with a $50,000 grant that the organization has received from the local municipality, allowing the nonprofit to sell the completed house for $100,000 to a low-income homebuyer. In exchange for this public assistance, the homebuyer agrees to limit the home's resale price, limiting the amount of equity that he or she will receive from the sale. The subsidies invested in making homeownership affordable for one generation of low-income homebuyers are thus retained in the housing itself, keeping it affordable for the next generation of low-income homebuyers. A new infusion of public dollars will not be needed every time a publicly assisted home is resold. The subsidy is preserved, along with the affordability of the assisted property. Since deed-restricted homes, community land trusts, and cooperative housing are the vehicles by which such a policy can be implemented, these models become priority recipients of public largess whenever and wherever the disbursement of homeownership assistance is guided by a concern for retaining subsidies and maintaining the affordability these subsidies buy.

Subsidy retention, however, is either completely omitted from the housing assistance programs of many cities and states or only applied to the public's investment in rental housing. Even in cities and states where subsidy retention is a key ingredient of the jurisdiction's homeownership programs, the policy is often applied only to monies disbursed through an isolated program, like a housing trust fund. All other subsidies for the acquisition or rehabilitation of owner-occupied property are subject to a very different policy – either subsidy removal or subsidy recapture (see Figure 4.1 on next page).

Prior to the 1970s, the prevailing policy governing the public's subsidization of homeownership in the United States was subsidy removal. For many cities and states, it remains the dominant policy today.[143] Typically structured as a grant or non-amortizing loan to an individual homeowner, such subsidies enable lower-income homebuyers to purchase market-priced homes that would otherwise be beyond their means. When these publicly assisted, owner-occupied homes are resold, they are priced and purchased for whatever the market will bear. If the property has held its value or increased in value, the seller may claim whatever public subsidies were put into the home, along with any appreciation that occurred between the home's initial purchase and later resale. Removed by the seller, these subsidies are no longer available to the next buyer. Another investment of public funds will usually be needed, if a subsequent homebuyer of modest means is to be able to buy the same home or one like it.

Subsidy removal may be reasonable in weak-market neighborhoods, cities, and regions where the affordability gap between housing costs and household incomes is either small or shrinking. It may be sustainable – or, at least, acceptable – in jurisdictions where an abundant stream of public dollars is available to replenish the pool of subsidies being lost as assisted homes are resold for market

Figure 4.1
Removal, Recapture, or Retention: Three Policies for the Subsidization of Owner-Occupied Housing

	SUBSIDY REMOVAL	SUBSIDY RECAPTURE	SUBSIDY RETENTION
Recipient of the subsidy	Individual homeowner	Individual homeowner	Corporate sponsor, usually a community development corporation, CLT, or LEC
Form of the subsidy	Grant or non-amortizing loan to the homeowner	Loan to the homeowner	Grant or loan to the corporate sponsor
Price paid by homeowner at initial purchase	Total development cost or appraised value of the home	Total development cost or appraised value of the home	Total development cost, minus the amount of the subsidy
Price paid to homeowner when home is resold	Market value of the property	Market value of the property	Price determined by a resale formula contained in a deed covenant, ground lease, or an LEC's bylaws and shares
Disposition of subsidy at resale	Subsidy pocketed by the seller	Subsidy recaptured by the lender (in whole or in part) and then re-loaned to next low-income homebuyer	Subsidy retained in the property, lowering its purchase price for the next low-income homebuyer
Price paid by next homebuyer	Market value of the property	Market value of the property	Formula-determined price paid by the corporate sponsor in repurchasing the home from the first owner
Need for additional investment of public funds (in a rising market) to assist the next low-income homebuyer	More public investment is always needed, since none of the original subsidy is available to close the gap between the buyer's income and the property's increased market value	More public investment is usually needed, since recaptured funds are seldom sufficient to close the gap between the buyer's income and the property's increased market value	More public investment is not needed, if the resale formula has performed as expected in maintaining an affordable price for the next low-income homebuyer

prices, or where an abundant supply of low-cost land and newly constructed starter homes are available to replenish the pool of assisted homes being lost to the market.

These are not the circumstances of most localities, however. The affordability gap, for them, has been growing greater, not smaller. The per-unit subsidy required to boost a lower-income household into homeownership has been growing larger, while the budgets of the public agencies charged with providing such assistance have become tighter. Buildable land has become less plentiful and more expensive, pushing the price of even the smallest starter home far beyond what a lower-income household can afford.

In the face of these harsh realities, an increasing number of cities and states have come to regard subsidy removal as a wasteful, unsustainable policy that cannot be justified either fiscally or politically. Subsidy recapture has been steadily taking its place. Public subsidies, under this latter policy, are loaned to lower-income homebuyers, helping them to purchase market-priced homes that would otherwise be beyond their means. These loans are structured in a variety of ways. They may be short-term or long-term. They may be interest-bearing or not. If interest is charged, the rate may be as low as 1% per annum or nearly as high as a market-priced mortgage. The payment of the loan's interest and principal may occur on a monthly basis or both may be deferred until the home is resold. The lender may require not only repayment of principal at the time of resale, but payment of a share of the property's appreciation as well. The loan itself, under many subsidy recapture schemes, may be gradually forgiven, reducing the homeowner's indebtedness by a specified percentage each year of occupancy until the loan eventually disappears. What is true in every case, however, is that the homes receiving such assistance are priced and purchased at resale for whatever the market will bear. The original subsidy, if not forgiven by the time of resale, is wholly or partially recaptured by the public agency that provided it. Recaptured funds are then re-loaned to another lower-income homebuyer, assisting in the purchase of another market-priced home within the agency's service area.[144]

Subsidy recapture is widely considered an improvement over subsidy removal. It does in fact go further in protecting and recycling the public's investment. Less money is needed from government coffers to subsidize future homebuyers, since some funds are recaptured from previously assisted homeowners when they eventually resell their subsidized homes. But subsidy recapture suffers from some of the same problems as the policy it replaced. In a rising market, the affordability purchased by the public's investment is immediately lost when an assisted home is resold. Its price rises instantly to a market value that few low-income households may be able to pay. To purchase that home, or another like it, a low-income homebuyer will need the same sort of subsidy that boosted the first low-income household into that home. Funds recaptured from the first homeowner can be used for part of that subsidy, but they will seldom be enough to bring homeownership within the financial reach of another low-income homebuyer in markets where housing prices are increasing faster than household incomes (see Figure 4.2). Recaptured funds must be regularly supplemented, therefore, by a fresh infusion of public capital at every resale of a subsidized home. Otherwise, fewer and fewer first-time homebuyers are going to be assisted as the subsidy pool is gradually drained and eventually depleted. The flaw in this arrangement has been succinctly described by Cohen (1994: 110):[145]

> Many cities are faced with the troubling reality that they cannot maximize the return on their investment without minimizing the affordability of the housing they subsidize. Conversely, they cannot ensure the affordability of the subsidized housing, as it changes hands at an unrestricted price, without assisting fewer and fewer buyers or adding more and more dollars to their original investment. This is the paradox at the heart of subsidy recapture: the preservation of the public subsidy is incompatible with the preservation of affordability, and vice versa.

Although this paradox is readily acknowledged by many public officials whose cities or states employ subsidy recapture, they continue the policy nonetheless. Their reasons are varied, and sometimes valid. Their real estate market may be depressed enough to allow recaptured funds to close most of the affordability gap for the next low-income homebuyer.[146] Their municipality may be rich enough to replenish the pool of homeowner subsidies whenever it dips below an acceptable level. They may have an abundance of cheap land within their boundaries in need of redevelopment or an indifference to sprawling development beyond their boundaries, either of which may provide plenty of newly constructed, low-cost starter homes to replenish the pool of assisted homes that are lost to the market on resale. Or they may simply be ideologically resistant to any form of tenure other than market-rate homeownership. Whatever the reason, recapture, not retention, remains the guiding policy.

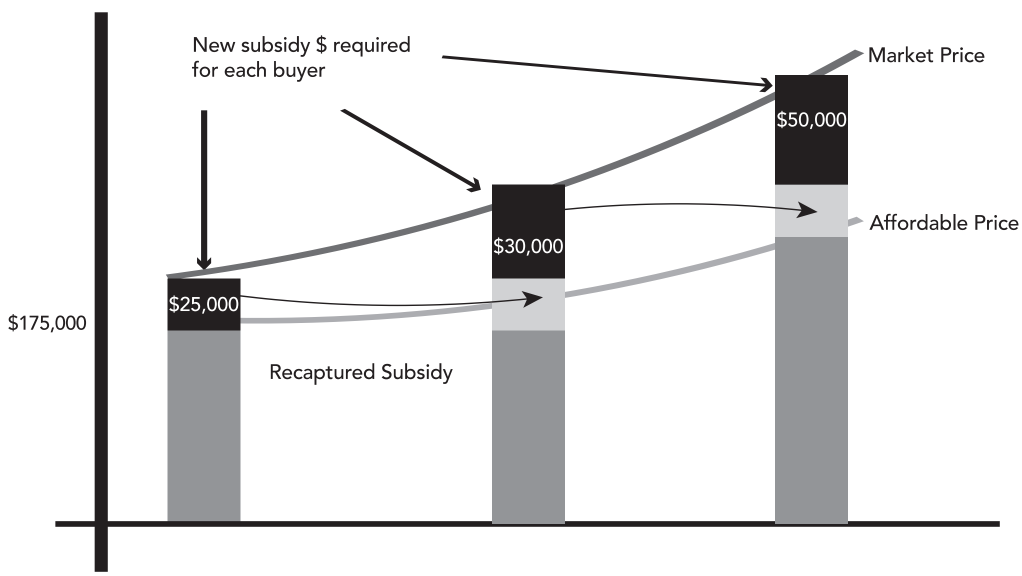
There are many other places where policies of recapture and retention coexist within the same jurisdiction, usually to the detriment of the latter. Either funding is provided on parallel tracks, with some subsidies subject to recapture and some subsidies retained in the housing, or funding is provided to resale-restricted housing under terms and conditions dictated by a policy not of subsidy retention, but of subsidy recapture. Neither is favorable to the expansion of shared equity homeownership.

Parallel programs create a marketing nightmare for shared equity housing. Offered to a limited pool of credit-worthy, income-eligible homebuyers are two competing opportunities for publicly assisted homeownership. Under the recapture program, prospective homebuyers are provided with a public subsidy to purchase homes with few restrictions on use and no restrictions on resale, except for a requirement to return a portion of the subsidy when the home is resold. Under the retention program, prospective homebuyers are provided with a public subsidy to purchase homes with multiple restrictions on both the use and resale of this shared equity housing.[148] If the size of the subsidy is similar and the price of the homes is similar, none of the resale-restricted homes will be sold until all of the unrestricted homes have been sold. Shared equity homeownership, under a parallel policy universe, is set up to fail.[149]

The uncomfortable coexistence of recapture and retention is also found among many jurisdictions that have firmly embraced resale-restricted models of tenure, but continue to structure their investments in affordable housing in a manner more appropriate to subsidy recapture or subsidy removal. The policy has changed; the procedures have not. Thus, instead of subsidies being granted or loaned to a project's sponsor, they are granted or loaned to individual homeowners. Instead of the subsidies being locked into the assisted property, staying with the housing across successive resales, they are recaptured by the public funder or removed by the homeowner at resale. Instead of relying on a grantee agreement or loan agreement between the funder and the sponsor of shared equity housing to convey the subsidies

Figure 4.2

Reinvestment of Recaptured Subsidies Still Leaves a Growing Affordability Gap[147]



Imagine a family whose monthly income allows them to qualify for a $170,000 mortgage. If they could put $5,000 down, they would be able to afford a $175,000 house. But if the only suitable houses available cost $200,000, they would need $25,000 in homebuyer assistance. Five years later, when they move, their house might sell for $250,000. With that money they would have to repay the remaining mortgage balance (say, $160,000) and repay a portion of their silent second mortgage (say, $20,000), which would leave them $70,000 in equity. The local government could then reinvest that $20,000 to help another family. The problem is that to help a family at the same income level buy the same kind of house now costs $50,000 instead of $25,000, because prices have risen so fast. The government would have to put in another $30,000 to make this same house affordable. And the next time it will cost even more. And the time after, even more. Even with subsidy recapture, over time, larger and larger amounts of subsidy are required to keep the same housing affordable to the same kinds of families.

– and instead of relying on deed covenants, ground leases, and corporate documents contained in the models themselves to enforce the funder's requirements for occupancy, eligibility, and affordability – the funder executes a regulatory agreement with each and every homeowner, ignoring the regulatory framework that is already in place. In short, models that retain subsidies are often forced into administrative boxes designed for subsidy recapture or subsidy removal. At best, this squanders the strengths of the shared equity models that a city or state has decided to support. At worst, it interferes with the sponsor's efforts to produce, mortgage, and market such housing.

A declared commitment to shared equity homeownership on the part of public officials becomes an empty gesture without a uniform policy (and consistent procedures) for retaining the public's investment. Absent a policy of subsidy retention, cities and states either steer their funding for affordable housing away from deed-restricted homes, community land trusts, and limited equity cooperatives, or structure their funding in ways that cripple both the production and performance of these alternative models of tenure.

Equitable Taxation

Rarely is the owner-occupied property developed through a community land trust, through a limited equity cooperative, or under a deed-restricted regime removed from local tax rolls.[150] The owners of shared equity homes, like the owners of market-rate homes, pay property taxes. That is true even for homeowners who lease land from a CLT. Since they have sole possession of their leasehold for 99 years, they bear sole responsibility for paying whatever local taxes are levied against both the house they own and the land they occupy.[151]

Although expected to pay and willing to pay their fair share of local property taxes, the owners of shared equity housing are too often required to pay much more. In assigning values and levying taxes, many local assessors take little or no account of the fact that shared equity housing is heavily encumbered with durable restrictions on subletting, resale, and use – restrictions that significantly constrain a property's marketability and profitability. The owners of shared equity homes are frequently forced to pay taxes not only on value that is theirs, but also on value they can never claim for themselves.

Consider, for example, a deed-restricted house produced through a municipality's inclusionary zoning program that is sold to a lower-income household for $85,000, despite appraising for $210,000 at the time of purchase. If the house appreciates at an annual rate of 7%, its appraised value after five years would be nearly $295,000. The maximum resale price that an affordability covenant would allow the homeowner to charge, however, should she decide to move after five years, could be as low as $94,000.[152] Note that the homeowner, in this hypothetical example, only buys 40% of the property's value when purchasing the house. Five years later, she may claim as her own only 32% of the property's value, were she to resell the house. If the municipal assessment of her property does not take into account either its below-market purchase price or its restricted resale price, the homeowner will be taxed as if 100% of this value belonged to her. By her fifth year of occupancy, in this particular case, she would be forced to pay property taxes on $201,000 of value she does not own.

This can be an enormous barrier to the expansion of shared equity housing, especially in places where the market value of residential real estate is rapidly rising and where property taxes are keeping pace. Shared equity homes continue to sell and resell for prices well below their market value, but they are taxed as if their owners are realizing the same gains as any other homeowner. At a certain point, no matter how affordable the cost of purchasing these resale-restricted homes may have been, taxes that are pegged to the property's market value will render the cost of holding these homes unaffordable for persons of modest means.

A more equitable approach to taxing resale-restricted property is necessary if the affordability of shared equity homes is to be respected and protected, rather than eroded. Jurisdictions that would tax such property more fairly must address two questions:

- What is the value of shared equity housing when it is entered on the tax rolls, considering that these properties are encumbered with durable restrictions on both the equity a homeowner may earn when these properties are resold and the income a homeowner may earn if the properties are sublet (if subletting is even allowed)?

- How is this value adjusted over time – i.e., what is the rate of increase in the assessed value of a shared equity home – considering that the property must be resold for a formula-driven price that may be far below its market value?

In jurisdictions where shared equity housing is being developed on land that is leased from a community land trust, a third question must be addressed:

- What is the value of land that is owned by a CLT when it is entered on the tax rolls, considering that this land is encumbered with a 99-year-lease, this land will generate only modest fees for the laowner during the term of the lease, and this land will be immediately leased again to another low-income homeowner whenever it reverts to the CLT?

There is neither uniformity nor consistency in the myriad ways in which cities and states have answered these questions when attempting to cope with forms of tenure that do not fit neatly into familiar boxes for the valuation and taxation of residential real estate. An observation made several years ago about the taxation of CLT homes is applicable to every form of shared equity homeownership:

> Local taxation of land and buildings within the price-restricted domain of the community land trust is a crazy-quilt pattern of rational innovation, political calculation, and irrational expediency. The variability from one state to another, even from one jurisdiction to another within the same state, is extraordinary. (Davis, 2001: 44)

Because of the sheer variety of the approaches that different jurisdictions have taken in setting the value of resale-restricted housing, in adjusting its value over time, and in setting the value of land that is owned by a CLT, it is difficult to propose a "best practice" that would be acceptable, defensible, and effective in every locale.[153] It is possible only to sketch out a few general guidelines, suggesting what the equitable taxation of resale-restricted property should look like.

SETTING THE VALUE OF RESALE-RESTRICTED HOUSING

Ideally, the assessed value of a shared equity home should reflect the durable controls that have been contractually imposed on the use and value of this property. Its value should reflect the property's value to the owner. Because these encumbrances reduce the value that an owner can derive from his or her property, its assessed value should be significantly lower than that of a similar property not so encumbered. The taxes a town can expect to collect, accordingly, should be lower as well. This was, in fact, the reasoning of the Appellate Division of the New Jersey Superior Court in the 1989 case of *Prowitz v. Ridgefield Park Village* (568 A.2d 114) in considering whether deed-restricted housing should be taxed at a reduced rate. Upholding the lower taxation of residential property encumbered with an affordability covenant, the Court stated:

> The deed restriction limiting resale price constitutes a patent burden on the value of the property, not on the character, quality or extent of title. It is, moreover, a restriction whose burden on the owner is clearly designed to secure a public benefit of overriding social and economic importance, namely, the maintenance of this State's woefully inadequate inventory of affordable housing.

Although the opinion of a New Jersey appellate court is not binding on the courts of other states, the reasoning behind the *Prowitz* decision has been echoed elsewhere. Outside of New Jersey, the question of whether resale restrictions impose a "patent burden on the value of the property," which must be recognized in taxing shared equity housing, has sometimes been settled by a state court,[154] sometimes by a state legislature,[155] and sometimes by a state board of equalization.[156] More often, however, it has been left to local assessors to decide for themselves whether to recognize the affordability restrictions contained in the covenants, ground leases, or bylaws of shared equity housing and what the encumbered value of these homes should be. Although the majority opinion, emerging among the nation's assessors, is that a shared equity home should be valued and taxed on the basis of the restricted price for which the property is actually sold (and resold), many local assessors still refuse to accept such a below-market valuation when entering resale-restricted housing onto their tax rolls.

ADJUSTING THE VALUE OF RESALE-RESTRICTED HOUSING

Prices rise not only for market-rate homes, but also for resale-restricted homes. It follows that tax assessments should increase as well. Resale prices seldom rise as fast for the latter, however – which is, of course, what resale-restricted housing is all about. The formula-determined price of a shared equity home, under most resale formulas and under most conditions, will tend to rise on a trajectory that is lower and flatter than the trajectory followed by market-priced homes without resale controls. The argument made to local assessors by the sponsors and owners of shared equity housing, therefore, is that post-purchase adjustments to the assessments (and taxes) of shared equity homes should take these long-lasting controls into account.

Assessors have only been amenable to this argument when the sponsors or owners of shared equity housing have been able to convince them that the restriction on the resale price of their homes (and, for that matter, the restriction on any rental income that owners could collect from subletting their homes) is a durable, enforceable encumbrance. Different assessors have established different tests in this regard, but most have insisted on the following requirements:

- Affordability restrictions are embedded in covenants, ground leases, or other contractual documents recorded in the land records.
- Affordability restrictions are not revocable during the term of a homeowner's occupancy.
- Affordability restrictions are not amendable during the term of a homeowner's occupancy.
- Affordability restrictions encumber individual properties.
- Affordability restrictions endure for many years.[157]

For properties that meet these requirements, the challenge confronting a local assessor is to determine the actual impact of these affordability restrictions on the rising value of shared equity homes. Many assessors adjust their valuation of shared equity homes already on their tax rolls by looking to the prices actually paid for comparable resale-restricted homes that have recently changed hands within the same neighborhood. Some assessors calculate the maximum price for which a shared equity home could have sold, based on the resale formula appearing in the home's deed covenant or ground lease, and adjust the home's value accordingly.[158] Some assessors simply determine that the assessed value of shared equity homes should rise at a rate that is 10% lower, 25% lower, 40% lower, or some other percentage below whatever the increase might be for market-rate homes. Although these percentages sometimes look suspiciously like a number that was grabbed out of thin air, they at least represent an acknowledgment that the formula-driven price of a shared equity home is rising at a rate that is lower than the market-driven price of homes without resale controls.[159]

SETTING THE VALUE OF LAND OWNED BY A CLT

Ideally – and logically – the assessed value of a CLT's land should never be more than the "leased fee value," i.e., the economic value that is retained by the landowner. This amount is essentially the net present value (NPV) of the income stream which the CLT can collect from a parcel of land in monthly fees over the term of the lease, plus the discounted value of any proceeds the CLT might realize when the land reverts to the CLT at the end of the lease. CLTs tend to charge lease fees that are below their land's fair rental value.[160] Many charge lease fees of merely a few dollars a month. Thus the NPV of these lease fees, for most CLTs and for most CLT land, is extremely low. So too is the land's reversionary value, since any leasehold that comes back into a CLT's possession is immediately re-leased on similar terms to another low-income homeowner. The CLT typically derives no economic value from this transaction, aside from the lease fees themselves. Acknowledging these realities, the city assessor in Albuquerque, NM, for one, has concluded that the land held by the Sawmill Community Land Trust has no value at all. Other assessors in other communities have made NPV calculations of a CLT's income stream and concluded that a CLT's land does have a taxable value, but one that is far below that of lands that are leased for a market-rate rent. On Orcas Island, for example, in Washington State, the local assessor has decided that the encumbered value of the lands owned and leased to individual homeowners by the OPAL Community Land Trust is 40% lower than their market value. CLTs in New Hampshire, by contrast, are paying property taxes on values that are based on the highest-and-best use of a CLT's land. Assessors there have taken account of neither the below-market lease fees being charged to CLT homeowners nor the distant and miniscule reversionary value of these lands, a policy that has slowed the development of CLT housing throughout the state.

Despite the burden and barrier that market-based taxation can pose for shared equity homeownership, many advocates for deed-restricted housing, community land trusts, and limited equity cooperatives in New Hampshire and elsewhere have been reluctant to push for a fairer approach to valuing and taxing their properties. Developing housing for low-income households, they worry, is already controversial enough without adding a volatile issue like equitable taxation to the mix. While it is hard to fault the political calculations of these local activists, who are often fighting the good fight for affordable housing in hostile environments against enormous odds, their refusal to confront this long-term threat to the continuing affordability of shared equity housing seems terribly shortsighted. It is akin to the refusal of many public officials to confront the loss of publicly provided subsidies and publicly produced affordability in their homeownership programs because they are worried what the political fallout might be if they insisted on locking both in place. The failure to press for the equitable taxation of resale-restricted housing has this in common with the failure to press for subsidy retention and durable affordability. All three seem like good politics, at least some of the time. All three are bad policy, nearly all of the time.