

COMMUNITY LAND TRUSTS: A Primer for Local Officials

A Product of Community Legal Resources
Community Land Trust Project
www.clronline.org/clt

I. BACKGROUND

A. What is a Community Land Trust?

A community land trust (CLT) is a private, nonprofit corporation created to provide secure affordable access to land and housing for the benefit of the community. The CLT provides access to ownership of housing for people who would otherwise be priced out of the housing market.

CLTs are unique in that they separate ownership of land and homes. CLTs permanently own the land on which homes and other structures or facilities are built, while individuals own the home (or other structure/facility) on the land pursuant to a long-term (usually 89-year) renewable ground lease.

The CLT model does not lend itself to a “hard sell”; informed consent is essential. CLTs work to ensure that prospective homebuyers know what they are getting and what they are giving up upon purchase of a CLT home. The ground lease entered into by every CLT homeowner requires that owners live in their homes as their primary residences. CLT homeowners and their descendents have a right to occupy and use the leased land for the term of the ground lease, provided that they abide by the terms of the ground lease. In exchange for an initial subsidy from the CLT that is built into the price of the home, the terms of the ground lease place some limitations on the resale of the home—preventing resale to a household that does not qualify as low-or moderate-income, and limiting the sales price to keep it affordable. The lease lays out a “resale formula” that determines the maximum allowable price that may be charged upon resale of the home. Each CLT designs its own resale formula to give homeowners a fair return for their investment, while keeping the price affordable for other lower income people. In addition, the CLT has the right to buy each home back for an amount limited by the CLT’s resale formula.

Typically, CLTs are used in neighborhoods that are experiencing or are expected to experience gentrification. In many communities today, population growth and economic investment are driving up real estate prices so that fewer low- and moderate-income workers can afford to buy homes or rent in the communities where they work, thus posing a problem to both the workers and the business base in that community. Limited public funds are available to subsidize housing costs for lower income households. However, the gap between the amount of subsidy needed and the amount of subsidy available for affordable housing continues to widen as housing costs soar.

According to the U.S. Census, from 1990 to 2000 the median value of owner-occupied homes increased by 97% in the State of Michigan. While housing prices have escalated, government funding for affordable housing has decreased, and private funders are unable to subsidize these projects at the level previously supported by the government. While CLTs do not build equity for low-income communities as fast as conventional homeownership would, CLTs are designed to serve a population that otherwise would not have homeownership opportunities in the current conventional market. In addition, the initial investment in the affordability of the housing is preserved for future owners, thereby maximizing the utility of that investment.

CLTs are being developed in a growing number of communities – in expanding metropolitan areas from Cleveland, Ohio to Portland, Oregon; in university communities from State College, Pennsylvania, to Boulder, Colorado; and in expensive resort communities from the Florida Keys to the San Juan Islands of Washington State. In Michigan, CLTs have been formed in Traverse City, Boyne City, and Oceana County, among others.

B. The “Basics” of the Community Land Trust Transaction

The deal that a CLT homeowner makes with the Community Land Trust is the ability to purchase an affordable house now in exchange for giving up a portion of the future appreciation of the home when the CLT homeowner sells the home later. Here is a brief outline of the typical terms of a CLT purchase:

- The Homeowner purchases the house but not the land (which lowers the purchase price).
- The Homeowner leases the land from the CLT.
- The term of the lease is usually 89 years; the lease can be renewed once for another 89 years.
- When the Homeowner sells his/her house, a portion of the appreciated value stays with the land under the ground lease, so the home price is more affordable for the next buyer.
- The CLT home can be inherited.

1. The Ground Lease

An outline of a standard community land trust ground lease is provided at www.clronline.org/clt. Although each local CLT may modify the standard CLT ground lease to meet its needs and to best serve the community and the CLT homebuyers, the basic components of the CLT ground lease remain the same. Note that in some cases the overall CLT development may be organized as a condominium, and both land and homes may be owned and leased as condominium units.

2. The “Resale Formula”

The basic element of a Community Land Trust’s mechanism for preserving the affordability of a CLT home is the Resale Formula. Typically, the Resale Formula limits the CLT homeowner to some percent of the gain in value of the CLT home. When the CLT homeowner wants to sell their home they are limited by the Resale Formula in their ground lease which determines the Purchase Option Price. The Resale Formula typically provides that the Purchase Option Price is equal to:

- (a) What the CLT homeowner paid for the CLT home when s/he first bought it;
plus:
- (b) Some portion (often between 20 – 35%) of the appreciation in value of the CLT home, as determined by subtracting the appraised value when the CLT homeowner originally purchased the CLT home from the current appraised value of the CLT home at the time the CLT homeowner seeks to resell.

EXAMPLE (Assuming CLT homeowner retains 25% of the appreciation in value of the CLT home):

- CLT homeowner paid CLT \$90,000 when it purchased the CLT home.
- At the time of purchase the CLT home was appraised at \$105,000.
- At the time CLT homeowner seeks to resell the CLT home, the appraised value is \$125,000 – an appreciation in value of \$20,000.
- Twenty-five percent (25%) of \$20,000 is \$5,000.
- The Purchase Option Price equals what the CLT homeowner originally paid (\$90,000) plus twenty-five percent of the appreciation in value (\$5,000).
- Therefore, the CLT homeowner can resell their CLT home (to either the CLT or another low-income purchase) for the Purchase Option Price of \$95,000.

C. Making Homeownership Affordable

CLTs have no magic method of creating the initial affordability in housing. The greatest advantage of a CLT is its ability to preserve affordability for future generations. Nonetheless, a CLT can use a variety of tools to make housing affordable. CLTs have arranged financing for people who cannot qualify for home mortgages from conventional sources. Other CLTs have worked to minimize the hurdle of large down payments for first-time homebuyers by creating a down payment loan pool. CLT homeowners generally must be able to handle monthly mortgage payments and other costs (including the ground lease fee for use of the land). However, the “standard permitted mortgage” for a CLT homeowner will also give the CLT the ability to step in and “cure” homeowner mortgage defaults or otherwise maintain control of the property for CLT purposes in face of a potential foreclosure.

D. Transferring Ownership Between CLT Homeowners

After giving the CLT adequate notice, a CLT homeowner can sell the CLT home to an eligible buyer (i.e., someone who meets the income qualifications), transfer the lease, and move away. Since CLTs commonly retain an option to buy the CLT home, a CLT homeowner who wishes to leave may sell his/her house to the CLT. The CLT will, in turn, sell the CLT home and lease the land to a new CLT homeowner.

Long Term Effectiveness of CLTs*

Between 1984 and 2002, the Burlington Community Land Trust (BCLT) in Burlington, Vermont developed 259 moderately-priced single-family houses and condominiums. All of these homes were sold to first-time homebuyers subject to durable controls over their occupancy and resale, controls designed to maintain their availability and affordability for low-income households far into the future. The first resale of a BCLT home occurred in 1988. By the end of 2002, the BCLT had overseen the resale of 97 houses and condominiums.

This pool of resales provided a rare opportunity to evaluate the performance of a housing model that promises to secure the benefits of homeownership for persons of limited means, while achieving larger social goals like the preservation of affordability, the stewardship of public subsidies, and the stabilization of residential neighborhoods. There had been no systematic evaluation of these claims heretofore, because most of the nation's CLTs are still too new and too small to have had a significant number of resales. The BCLT was an exception. Its sizable portfolio of resale-restricted housing offered enough cases to assess how effective the BCLT had been in actually delivering – and equitably balancing – the individual benefits and the community benefits promised by its innovative model of homeownership.

The study's principal findings were as follows:

- **Preserving affordability.** Affordability not only continued between successive generations of low-income homebuyers, but improved – even when the favorable effect of falling mortgage interest rates was eliminated. The average BCLT home was affordable to a household earning 62% of Area Median Income (AMI) on initial sale. On resale, it was affordable to a household earning 57% of AMI.
- **Retaining community wealth.** Public subsidies invested in these houses and condominiums remained in the homes at resale, underwriting their affordability not only for the first buyers but for subsequent buyers as well. Only in two cases of foreclosure were these subsidies lost. More typically, these subsidies not only remained in the property but increased in value. On the initial sale, the total value of the public subsidies put into the BCLT's homes was \$1,525,148. On resale, the total value of these retained subsidies was \$2,099,590.
- **Enhancing residential stability.** Land and housing brought under the stewardship of the BCLT were rarely removed from its portfolio. Affordability and owner occupancy protections remained in place for ninety-five percent (95%) of the 259 units of owner-occupied housing developed by the BCLT between 1984 and 2002. Even in cases where homeowners defaulted on their mortgages, their resale-restricted homes stayed under the BCLT's care – neither lost to the market nor lost to absentee ownership.
- **Expanding homeownership.** Access to homeownership for persons excluded from the market was expanded. All of the households served by the BCLT earned less than median income. A majority earned considerably less than 80% of AMI.
- **Creating individual wealth.** When reselling their BCLT homes, most homeowners walked away with more wealth than they had possessed when first buying a BCLT home. Their equity gains were modest when compared to what they might have realized from the resale of an unrestricted, market-rate home, had they been able to afford such a home, but BCLT homeowners still earned a respectable return on their initial investment. Their annualized rate of return, across all 97 resales, averaged 17%. The average BCLT homeowner, reselling after five years, recouped her original downpayment and then realized a net gain in equity of \$6,184.
- **Enabling residential mobility.** Mobility was assured, with households who left the BCLT doing so for similar reasons, with similar destinations, and with similar success as homeowners buying and selling on the open market. Probably the most surprising finding, in light of the relatively modest equity gains realized by these homeowners on resale, was that a majority of them bought market-rate homes after leaving the BCLT. Sixty (60) households made the leap into market-rate homeownership; four (4) bought another resale-restricted BCLT home; sixteen (16) became renters; and one died. (The subsequent housing situations of another sixteen (16) households could not be determined, primarily because they left the state.) Among the BCLT homeowners whose subsequent housing situations were known, 74% of them bought market-rate homes within six months of re-selling their limited-equity houses or condominiums; another 5% traded their first resale-restricted home for another, choosing to remain within the BCLT.

The Burlington Community Land Trust operates in a housing market with rising prices, a growing demand for moderately-priced housing, and a chronic shortage of houses and condominiums within the financial reach of persons earning below 80% of median income. Community land trusts operating in markets different from the BCLT's may achieve different results. Nevertheless, the performance of the BCLT's portfolio of resale-restricted, owner-occupied housing provides encouraging evidence of the model's effectiveness, while lending credibility to the limited-equity homeownership programs of many other organizations, CLT and non-CLT alike, that seek to promote the legitimate interests of first-time homebuyers, without sacrificing the legitimate interests of a larger community. For over nineteen years, the community land trust in Burlington, Vermont has been doing what it promised to do.

II. SPECIAL CONCERNS OF LOCAL OFFICIALS

A. Zoning

The development of CLT housing does not differ from the development of any other type of affordable or market-rate housing. Therefore, all applicable local zoning laws and regulations will apply.

B. Building Permits and Compliance with Municipal Codes

The acquisition, development and sale of CLT housing does not differ from the acquisition, development and sale of any other type of affordable or market-rate housing. Therefore, all applicable building permits and compliance with local building, safety and other codes and regulations will apply.

C. Land Division Act

The nature of a CLT housing development does not exempt a development from compliance with the Land Division Act. (MCL 560.101 – 560.293) In some cases, site condominiums may be used instead of platted subdivisions.

D. Affordable Housing

A community land trust, by its nature, provides for affordable housing. Where a local government makes funding or other forms of public support available to a CLT project in support of a CLT development based on assurances of continued affordability of a proposed development, a CLT structure provides assurances that the affordability of the home(s) will be maintained indefinitely. The local government should look to the terms of the CLT ground lease to determine the income restrictions imposed (e.g., low or moderate income) and the length of time for which the ground lease shall apply (usually 89 years).

Note that in certain situations the ground lease may provide for the lifting of the affordability restrictions – generally, in deference to the entity that has financed the CLT homeowner's mortgage. However, it should also be noted that the Community Land Trust's main mission is to preserve the affordability of its CLT homes and therefore it will generally do everything in its power to prevent the CLT home from being returned to market rate.

E. Transfer of Property/Recording of Deeds

The CLT will remain the owner of the land occupied by the CLT home. At the time of the initial sale to the CLT homeowner, the CLT will issue a warranty deed for the improvements (i.e., the home) and will execute a long-term (usually 89 years), renewable ground lease with the CLT homeowner for the land on which the CLT home sits. The recorded warranty deed for the improvements will reference the ground lease and a "Memorandum of Lease" will be recorded along with the warranty deed to place the interest of the homeowner in the land of record. Among other things, this helps make the homeowner's interest financeable and insurable.

F. Taxation

Community land trust properties are issued two tax bills. The first, to the CLT homeowner is for the value of the improvements (i.e., the home). The second, issued to

the CLT is for the value of the property. The CLT may, via the ground lease, provide that the CLT homeowner will pay the bill for the taxes on the property.

The tax levied on the improvements should reflect the restricted market value of the improvements given the restrictions on resale price imposed by the CLT via the CLT ground lease. Similarly, the tax levied on the land should reflect the limitations on use or resale of the land imposed by the ground lease and the substantially below-market ground lease rentals.

A sale of the improvements will be a “transfer” of that property for purposes of Proposal A. However, because of the restrictions on transfer that apply to the property, the increase in taxable value resulting from the transfer should be limited in accordance with the resale formula in the ground lease. The taxable value of the land will not be affected since the CLT continues as the owner.

G. Financing

CLT homeowners, although purchasing the CLT home at a reduced/affordable price, will almost always need to seek a loan from a commercial lender in order to buy the CLT home. CLTs make an effort to work with and educate local lenders regarding the nature of CLTs so financing will be available to potential CLT homebuyers.

Of course, because all CLT programs have the purpose of promoting, or at least preserving, the availability of affordable housing, federally regulated depository institutions can expect to receive Community Reinvestment Act (CRA) credit for participation in, and financial support of, these programs.

CLT-related mortgages are increasingly accepted in secondary markets. State housing agencies are often willing to purchase them, and FNMA offers a CLT program. The increasing acceptability of CLTs is demonstrated by the fact that FHA insurance is available for CLT purchase mortgages, and financing has also become available under the Rural Services 502 program. Of course, financial institutions may, instead of selling a CLT mortgage, hold it itself.

When first approached, lenders may be concerned that a CLT will inhibit their ability to foreclose in the event of a default and make it difficult to remarket the property in a timely manner. CLTs have been able to negotiate mortgage agreements that address the legitimate concerns of lenders and also protect the CLT’s long-term interest in the property by allowing the CLT to step in and cure a default, when necessary, to prevent the property from being sold on the open market (without price restrictions to retain the home’s affordability).

H. Title

The instruments used to perform the sale of the property are a ground lease of the land and a deed for the improvement on the land. What will be recorded is usually a memorandum of ground lease and a warranty deed both extending from the CLT to the CLT homeowner. The memorandum will typically set forth the restrictions on title including a reservation of mineral rights, the right to purchase retained by the CLT, the duration of the lease, and use and transfer restrictions.

As a consequence of the transaction, title to the land will continue to be held in the CLT, subject to the lessee-homeowner’s leasehold interest in that land. Title to the improvements will vest in the homeowner. The homeowner’s leasehold interest

in the land and ownership interest in the improvements may both be given as security for a loan so a mortgage will often be recorded.

A homeowner may sell his or her interest to another qualified purchaser. At that time, usually the original lease will be terminated and a new lease will be executed by the CLT and the new purchaser. The selling homeowner will also execute a deed for the improvements to the new purchaser.

The deed will recite the consideration paid for the improvements on the land and will be subject to transfer tax based on that consideration.

Generally, CLT transactions are insurable like other residential transactions. The primary difference is related to the nature of the ground lease. Therefore, an endorsement will be added to the both the owners and the loan policy to reflect the nature of the interest insured as being a leasehold owners interest or a mortgage secured by the leasehold interest in the land and the full ownership of the improvements.

I. Control and Accountability of the CLT Homeowner

Leaseholders – homeowners, farm owners, or business owners – retain most of the rights that go with ownership. CLT control is generally limited to areas where the CLT has a long-term interest. For example, it is vital to the CLT to preserve affordability of housing units. Most CLT ground leases also prohibit absentee ownership of housing. Also, CLTs want to protect the condition of the land and buildings which would be left at the end of the lease term.

J. Dissolution of the CLT

If a CLT is dissolved and ownership of the land is transferred, the new owner is obligated to honor the long-term lease agreements between the CLT and its leaseholders. Typically, if the CLT ever offers the land for sale to a non-charitable buyer, the CLT homeowner will have the right of first refusal to buy the land.

This document is a product of the Community Legal Resources Community Land Trust Project. Please check the CLR CLT Project website for updates to this document: www.clronline.org/clt.

This publication is intended to provide general information, and is not a substitute for legal advice. If you have additional questions about this issue, contact Community Legal Resources at 313/964-4130.

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