

**An Analysis of the Strengths and Deficiencies of Washington, D.C.'s
Tenant Opportunity to Purchase Act**

Prepared by the Harrison Institute for Public Law
Georgetown University Law Center

INTRODUCTION

This report is the product of a study commissioned by the Fannie Mae Foundation (the “Foundation”) and conducted by the Georgetown University Law Center’s Harrison Institute for Public Law (“Harrison” or the “Institute”). It describes the process of tenant ownership in the District of Columbia pursuant to the Tenant Opportunity to Purchase Act (“TOPA” or the “Act”).

TOPA offers residents of rental housing the opportunity to purchase that housing when the owner puts it up for sale. While the Act applies to all types of rental housing (e.g., single-family rental units, one- to four-unit rental buildings, and buildings with more than four rental units), this report will focus on buildings with more than four units and the lower-income segment of the tenant population. We have chosen this focus because the larger buildings offer the greatest possibility to preserve affordable housing, and lower income residents have both the greatest risk of displacement and the fewest resources to protect their interests. TOPA was specifically designed to preserve affordable housing for the District’s most vulnerable citizens.

This report will analyze the process of tenant ownership under TOPA, identify obstacles to tenant purchase, and make recommendation to improve the Act. Our goal is to help more *potential* homeowners become *actual* homeowners. In preparing the report, we developed and analyzed a questionnaire that we distributed to participants in the tenant ownership process, including residents, developers, lawyers, lenders, government agency personnel, and trainers. The Harrison Institute also held focus group discussions, interviewed individual participants, searched governmental records, collected and reviewed other studies of the tenant ownership process, and culled its own files of tenant ownership cases.

Before beginning the substantive aspects of the report, we wish to point out our belief, based on data analysis and our experience in the field, that TOPA is critical to the preservation of affordable housing and the expansion of homeownership among the District’s low-income residents. TOPA has been the catalyst for preserving thousands of affordable homes in Washington, D.C., often in neighborhoods that have been undergoing gentrification. The Act has preserved hundreds of units that would have been converted to luxury rentals or to market-rate condominiums. And it has enabled residents to remain in their homes and neighborhoods despite pressures to relocate them to other neighborhoods or out of the District altogether. The Act has also made it possible for low-income residents to purchase homes, a development that most did not even see as a remote possibility. It has allowed some to obtain wealth that was inconceivable to them before their TOPA transaction.

Despite these positive outcomes, obstacles to TOPA’s full implementation remain. Some of the obstacles are financial, others technical. Some have to do with the organization and education of those who participate in the process, from residents to technical assistance providers to lenders. This study aims to identify the obstacles precisely, place them in context, and propose actions to overcome these obstacles.

Our report tracks the process of tenant ownership from its inception through acquisition, renovation, and operation of a building. At each point in the process, we will describe briefly the legal requirements of the statute,¹ discuss the data we collected, state our findings, and offer recommendations to improve the process. A series of appendices follow the body of the report.

THE LEGAL BACKGROUND

In the early 1980s, the Washington, D.C., Council passed the Rental Housing Conversion and Sale Act (The Act). Its goals included the preservation of rental housing for lower-income residents, the preservation of homes for the elderly poor, and the creation of homeownership opportunities for lower-income tenants. The Act included provisions that gave tenants the opportunity to purchase their buildings. These provisions, known collectively as the Tenant Opportunity to Purchase Act (TOPA), restrict owner rights. TOPA stipulates that owners of residential properties must “give the tenant an opportunity to purchase the accommodation at a price and terms which represent a bona fide offer of sale” before they may transfer the property to a third party.

TOPA’s benefits can be fully realized only if residents fully understand the Act. For example, the most obvious benefit to residents is the option to purchase. But there are other, more subtle benefits that few residents understand. These include the right to assign their right-to-purchase to a third party and to co-develop the property or obtain cash payments or other considerations if they choose not to co-develop the property. Few residents understand these benefits.

In the following section, we offer a concise statement of the statutory regime. We then discuss the areas in which the study participants have identified problems. We present the data, state our findings, and make recommendations to remedy the problems.

THE TENANT OPPORTUNITY TO PURCHASE ACT

In this section, we provide a brief description of the Act and the TOPA process. We will then point to some of the deficiencies in the process.

Triggering the Act

TOPA is triggered when an owner either takes steps to sell the property or issues a “notice of intent to recover possession, or notice to vacate, for purposes of demolition or discontinuance of housing use.” The original Act defined “sale” rather broadly,⁷ but a provision was later added that gives owners a way to avoid triggering TOPA. When the property is the sole asset owned

¹A copy of the statute as well as a more detailed description of the process is an appendix to this report.

D.C. Code Ann. §§ 42-3401.01 – 42-3405.13 (2001).

D.C. Code Ann. § 42-3401.02 (2001).

D.C. Code Ann. §§ 42-3404.02 – 42-3404.13 (2001).

D.C. Code Ann. § 42-3404.02 (2001).

Id.

D.C. Code Ann. § 42-3404.02(b) (2001).

by a partnership or corporation, a sale occurs only when 100 percent of all interest is transferred to a single transferee in less than one year. This means that if a partnership, corporation or, presumably, limited liability corporation owns a property as its sole asset, no “sale” occurs (and TOPA is not triggered) if less than 100 percent of the interest in the property is transferred or if the transfer occurs over several years.⁸ This technicality has come to be known as the “95/5 loophole” and has led to the transfer of many buildings without notice to residents. Efforts to remove this loophole have been introduced at District Council meetings but have not proved successful.

The Department of Consumer and Regulatory Affairs (DCRA), the District of Columbia agency that monitors the TOPA process, has taken a very broad view of the 95/5 exception. As a result, many buildings have been transferred pursuant to this exception, and a significant number of affordable units have been lost.

There are other, less common exceptions to TOPA. For example, TOPA is not triggered by the transfer of a decedent’s estate to members of the decedent’s family if there is no consideration for the transfer. Another exception is a transfer by foreclosure, tax, or bankruptcy sale.

Initiating TOPA Rights

The Act requires an owner to provide each tenant and the District of Columbia mayor with a written offer of sale. This offer must also be posted in a conspicuous place in common areas of the property. The offer must include:

- the asking price and terms of the sale
- a statement that the tenant has the right to purchase the accommodation [pursuant to the Act] and a summary of tenant rights and sources of technical assistance
- a statement as to whether a third party-contract exists
- a statement that the owner will make available certain information about the finances and physical layout of the property

As a practical matter, most notices to tenants occur *after* an owner reaches agreement with a third-party purchaser. Under these circumstances, the terms of the offer are set. In the absence of a third-party contract, residents need to test the proposed purchase price against the market to determine its fairness and appropriateness.

Tenant Registration

If the tenants wish to respond to the notice, they must incorporate a tenants association (unless

D.C. Code Ann. § 42-3404.02(c) (2001).

Id.

D.C. Code Ann. § 42-3404.03 (2001). The posting requirement is only for accommodations containing more than one unit.

Id.

one already exists)¹² and express their interest in purchasing the building with the owner and DCRA through an application for registration. If no tenant association exists, these actions must be taken within 45 days of the receipt of the owner's notice, and within 30 days if there is a pre-existing association. The application must include the names, addresses, and phone numbers of the organization's officers and legal counsel (if any); a copy of the association's articles of incorporation and bylaws; and documentation that the organization represents at least a majority of the occupied rental units.

The Negotiation Period

General Requirements

Once the tenant organization has registered its application, the owner must give the organization a reasonable amount of time (not less than 120 days) to negotiate a contract of sale. This period may be extended for up to an additional 120 days (for a total of 240 days) if a lending institution provides a written notice that the association has applied for financing and the institution needs additional time to make a decision.

In addition to the minimum periods required under the Act, the owner may also give the organization "reasonable" extensions without incurring liability to any third party with which it has a contract.

D.C. Code Ann. § 42-3404.11(1) (2001). Tenants in single-family accommodations and accommodations of two to four units are not required to incorporate before negotiating with the owner. D.C. Code Ann. §§ 42-3404.09, 42-3404.10 (2001). In the case of two- to four-unit accommodations, the tenants may respond first jointly and then severally to the offer.

The Act specifies the "Mayor," but the authority to register corporations and partnerships in the District of Columbia has been delegated from the Mayor to the Department of Consumer and Regulatory Affairs, Corporations Division of the Business and Professional Licensing Administration.

Id.

Id.

D.C. Code Ann. § 42-3404.11(2) (2001). For a single-family accommodation, the minimum negotiation period is 60 days, D.C. Code Ann. § 42-3404.09(2) (2001), and for accommodations of two to four units, 90 days, D.C. Code Ann. § 42-3404.10(2) (2001).

D.C. Code Ann. § 42-3404.11(3)(A) (2001). For single-family accommodations, the tenant has a minimum of 60 days to secure financing from the date of contracting, which may be extended to 90 days with a written estimate from a lending institution or agency. D.C. Code Ann. § 42-3404.09(3) (2001). Tenants in two- to four-unit accommodations have 90 days, which may be extended to 120 days with a written estimate. D.C. Code Ann. § 42-3404.10(3) (2001).

D.C. Code Ann. § 42-3404.04 (2001). Extensions may be set by agreement between the parties, although in at least one case the owners were found to have effectively extended the negotiation period by failing to respond to the organization's offer until after the end of the statutory deadline. *Lealand Tenants Association v. Johnson*, 572 A.2d 431, 433 (D.C. 1990).

Tenant Protections during the Negotiation Process

Good Faith Bargaining Requirement

The Act requires owners and tenants to bargain with each other in good faith. While the statute provides no definition of good faith, it does set forth several circumstances which, if present, shall constitute prima facie evidence of an absence of good faith. Such circumstances include:

- the owner's failure to offer the tenants "a price or term at least as favorable as that offered to a third party . . . without a reasonable justification for so doing"
- the owner's failure "to make a contract with the tenant [that] substantially conforms with the price and terms of a third-party contract . . ."
- the intentional failure of either party to comply with the Act
- the owner's failure to bargain in good faith (for example, offering the property to a third party for a price that is 10 percent or more lower than the price offered tenants)

Financial Capacity

The Act prevents owners from requiring tenants to demonstrate financial ability to purchase as a prerequisite for entering into a contract (unless the owner is providing financing).

Limit on Deposit

The maximum deposit an owner may require of tenants is 5 percent of the contract price, regardless of the amount of a third party's deposit. If the third party agrees to a deposit that is less than 5 percent, the tenant association may not be asked to pay more as a deposit.

Assignment of Tenant Rights

The Act specifically permits tenants to exercise their purchase rights in conjunction with third parties by either assigning or selling their rights to such parties. For example, the tenant organization may partner with a developer to form an acquisition entity and transfer its purchase rights to this entity, or it may sell its purchase rights to a third party.

Waiver

The Act prohibits tenants from waiving their rights to receive an offer from owners and prohibits owners from requesting such waiver. Other TOPA rights, however, can be waived "in exchange for consideration which the tenant, in the tenant's sole discretion, finds acceptable."

D.C. Code Ann. § 42-3404.05(a) (2001).
D.C. Code Ann. § 42-3404.05(a)(1) (2001).
D.C. Code Ann. § 42-3404.05(a)(3) (2001).
D.C. Code Ann. § 42-3404.05(a-1) (2001).
D.C. Code Ann. § 42-3404.05(b) (2001).
D.C. Code Ann. § 42-3404.06 (2001).
D.C. Code Ann. § 42-3404.07 (2001).

Right of First Refusal

The tenant organization has the right of first refusal for a 15-day period following receipt of a copy of a third-party contract. If the tenants receive the contract during the negotiation period, the 15-day period starts at the end of the negotiation period.

DISCUSSION OF THE DATA

Our data come from various sources: government records, questionnaires to participants in the process, focus groups, interviews, prior studies, and our own files and experience. After reviewing the material collected, we have identified several areas of concern:

- data management
- resident familiarity with the process and its goals
- the availability and efficacy of technical assistance
- funding the various stages of the process
- training
- management

In what follows, we differentiate between data gathered from respondents and those culled from our own experience. Where appropriate, we identify the status of the respondent (i.e., community lender, banker, resident, attorney).

Data Management

Limited records (at District agencies and elsewhere) make a comprehensive analysis of the TOPA process difficult. We could not, for example, determine how many buildings entered the process or how many tenant associations registered. At one point the Department of Consumer and Regulatory Affairs told us that the city had only four registered tenant associations. Because the Harrison Institute alone currently represents between 15 and 20 such associations, this statement alerted us to the incompleteness and inaccuracy of DCRA records.

There is currently no official way of knowing what happens to a building in which a tenant association registers pursuant to TOPA. While conversion records are available, they are not cross-referenced with registration records. Better record-keeping would enhance our understanding of the TOPA process and put advisors and technical assistance providers in a better position to help tenant groups.

Another difficulty with the TOPA process is that, as now implemented, it is somewhat closed

D.C. Code Ann. § 42-3404.08 (2001).

and reactive. If tenants in a building who have received a TOPA notice do not pursue their rights, there is very limited opportunity for outside professionals to intervene. This lack of intervention may have resulted in a number of missed TOPA opportunities. A more carefully documented TOPA process, from the first notice onwards, would allow for a proactive response by housing advocates and an opportunity to educate tenants about their rights.

Findings

- Records of TOPA transactions are both incomplete and inaccurate.
- Obtaining and using the existing records is very difficult.
- Existing data compiled by DCRA is not amenable to the analysis we wished to perform and is not helpful for tenant groups and the professionals who assist them.
- Determining the success of TOPA and improving its success by early intervention and provision of technical assistance requires vastly improved data.
- Proactive intervention to preserve tenant rights, create opportunities to purchase, and preserve affordable housing is essential.

Recommendations

- Encourage DCRA to implement and maintain a comprehensive record-keeping system, preferably electronically, that allows tracking of notices, registrations, transfers of ownership, and conversions.
- Provide appropriate organizations — University Legal Services and the District’s Department of Housing and Community Development (DHCD), for example — with notice of buildings that have received notices of owner’s intent to sell.
- Use this information to facilitate intervention by technical assistance providers. This intervention should educate tenants about their rights.
- Implement a research project that tracks TOPA transactions.
- Develop a network of technical assistance providers who will intervene early in TOPA situations.
- Develop a system to follow up with tenant associations after the TOPA process is complete.

Resident Familiarity with Goals and Process

Several respondents to our questionnaire commented on the degree to which the TOPA process

is misunderstood by residents. There was a general, but not unanimous, agreement among attorneys, housing advocates, and development consultants that the Act is beneficial to residents and to the District. These respondents were wary, however, of various features of the process. Several noted that residents lacked the understanding necessary to make TOPA work effectively. They cited incidents in which residents sold their rights to contract buyers for a tiny fraction of what residents in other buildings had received for the transfer of similar rights. Some respondents maintained that tenant purchase reduced the availability of affordable rental housing and pushed some residents into purchasing who were neither interested in nor prepared for ownership. Residents claimed that the process was confusing and that they needed experienced attorneys and other technical assistance providers. Residents used such terms as “frustrating” in describing the process, but they found the goal “worthwhile.”

General Lack of Knowledge or Misunderstanding of the TOPA Process

Residents felt that while they generally understood that they had an opportunity to buy, they did not know or understand the intricacies of the purchase and development process. They also did not know or understand the options of creating partnerships with third parties or selling their rights. Moreover, they were often intimidated by the magnitude of the financial transactions and the complexity of the overall process. The lack of a clear understanding of the process had several negative consequences. For example, often only one or a small group of leaders in a building organized the association and initiated and maintained the TOPA process. While it is not unusual for a community group to have one leader or a small cadre of leaders, the continuous and intense activity needed to obtain a building often wears on the leadership group. This fatigue often led to disaffection and, in some cases, to the withdrawal from the TOPA process.

Another problem arises, although on a much smaller level, when building-level leaders seek self-aggrandizement. Respondents talked of dominating but poor leadership. Either of these problems can seriously damage a group’s prospects for success. One resident noted that even when organizers help groups come together and operate democratically and effectively (an all too rare occurrence), it is sometimes difficult to sustain the group after the organizer leaves. This resident felt the organizer’s presence had produced no net positive effect.

Importance of Residents Being Familiar with the Process

As we have mentioned, various data suggest that tenant ownership among lower-income residents of the District has been a successful method of preserving affordable housing.²⁷ Particularly in gentrifying neighborhoods, tenant ownership has provided a bulwark against displacement. We did not test for, and our data do not reveal, whether neighborhoods in which there is disinvestment also benefit from tenant ownership beyond the provision of decent, affordable housing. It is worth studying whether tenant-owned buildings become an impetus for more generalized neighborhood improvement, such as improved municipal services, reduced crime, and greater neighborhood pride.

²⁷ A Study of Limited-equity Cooperatives in the District of Columbia, Coalition of Nonprofit Housing & Economic Development, spring, 2004.

Findings

- Residents have an insufficient grasp of the TOPA process and do not understand the scope and nature of the tasks that a residents association (or its leadership) must complete. This is due in part to a lack of familiarity with the process. In addition, the notice residents receive does not include a clear, accessible explanation of the process.
- Given the relatively short period in which tenant associations must be formed and registered, many tenant groups begin but do not complete the registration process.
- The insufficient cadre of technical assistance providers means that most are unable to remain with an ownership project long enough to allow the residents to become self-sufficient.

Recommendations

- Produce a video that describes the TOPA process, its benefits to residents, and various TOPA success stories. The video should be cited in the required notice that residents receive at the beginning of the process.
- Create a more comprehensive primer on TOPA and seek to have it included in the required notice.
- Design and implement, in conjunction with DCRA, a system by which an organization could track the delivery of notices to tenants and provide outreach and information services to such tenants.

Availability of Technical Assistance

One of the obstacles to successfully completing the TOPA process is the lack of competent technical assistance to resident groups. This shortage may soon be exacerbated by an increase (due to tenant education and early outreach) of the number of tenant associations taking advantage of TOPA.

There are several types of assistance providers that are required to navigate TOPA. These include organizers, lawyers, and development consultants. The insufficient supply of assistance providers means that at any time, a single provider may play more than one role. In addition to the standard providers mentioned above, we believe trainers and, eventually, management companies are also critical to success.

In the next sections, we describe the role and availability of each type of provider.

The Organizer

An organizer is a critical but often missing element in the TOPA process. An organizer's

function is to help bring residents together, determine whether they wish to undertake the TOPA process, and build internal capacity and leadership. Unfortunately, there are few trained organizers in the typical TOPA transaction.

The TOPA process normally begins when one or more residents react to the owner's notice of intent to sell. The forms on which this notice is transmitted indicate that technical assistance can be obtained from University Legal Services (ULS). Mike Dinkin, of ULS, is the starting point for most TOPA transactions. Mike normally goes to the building, meets with residents, informs them of their rights, and helps them obtain the support of other residents and comply with TOPA guidelines. He may make several visits to the building and several presentations to residents. He also gives the residents contact information for several lawyers with TOPA experience. Unfortunately, Mike is largely on his own in providing these valuable services. He is spread thin, and his involvement is generally limited to the registration stage of the project.

After ULS involvement ends, the severe lack of trained organizers becomes obvious. On occasion that role is played, with varying degrees of success, by a lawyer or development consultant. More frequently, the role is played by one or more residents who educate residents, solicit their participation, get them out to meetings, help to raise funds, and connect with the nonresident community. There are a great many benefits, and a few negatives, associated with this behavior. It permits the education and participation of residents, a sharing of the workload, the creation of leadership skills, and capacity building. On the other hand, it is often inefficient and frustrating for untrained residents to undertake the organizing effort. And this frustration often breeds distrust of the process.

Lawyers

Lawyers play a critical role in the successful negotiation of the TOPA process. This process is rife with legal issues surrounding real estate, taxation, landlord/tenant law, and contracts. Lawyers may also become heavily involved in other aspects of the process, such as organizing and tenant education. Others draft and/or review documents but do not become otherwise involved.

Lawyers are often the first technical assistance provider brought into a case. As a result, the shortage of lawyers with experience in tenant purchases is a serious problem. While a few lawyers regularly do this work, there is no professional pipeline to this work and little chance that new lawyers will gravitate toward the tenant-purchase process. Of the lawyers who undertake an occasional TOPA case, few expect to make these cases a regular part of their practice. Many are doing *pro bono* work.

Few lawyers who take on a *pro bono* TOPA case do so again. It is not clear whether the firms that permit their attorneys to take on TOPA cases take on additional cases. If not, the capital built up in assisting lawyers in their first TOPA case is lost. This repetitive search for competent legal assistance is costly. And it results in lost opportunities: A lawyer just learning about TOPA is unlikely to partner with a developer or take the lead in finding appropriate financing and

restructuring a deal.

While TOPA training programs have been offered by the D.C. Bar, the Coalition for Nonprofit Housing and Economic Development (CNHED), and others, these tend to be one-shot sessions that provide no more than an overview of the process. A regular training program, with a set of practical materials and a formalized curriculum, does not exist. If the goal is to increase the cadre of lawyers who might represent tenants groups in the TOPA process, the development of such a program is imperative.

Development Consultants

Development consultants are people (or companies) who develop real property for another — in the TOPA situation, for the tenants association. The development consultant works for a fee, often a percentage of the development costs of a project. The developer on the other hand, takes the profit from a job and bears the risk of loss. In some cases, a developer will enter a partnership with the tenant association and thereby obtain an ownership interest in the building. The fee in such cases will typically be tied to the sales of units not purchased by members of the association. Both for-profit and nonprofit developers exist in each category.

Experienced development consultants are rare. In smaller operations, there are no more than six consultants who historically work with resident organizations. Of this group, only two or three are consistent performers; the others often leave the field unexpectedly and for extended periods. Even among the more reliable consultants, many appear to be overextended. Since their fees normally come from financing that may occur only every few months, these consultants often have to work on several projects at a time in order to maintain a constant stream of income. Their availability for any particular project may be dependent on what is happening in another of their projects.

There are also a number of consultants from larger operations that have expertise in several areas of development. Six large Washington metro area organizations have worked with tenant associations on a TOPA project. Many of the projects involve larger buildings with more complicated development issues and more complex financing (including LIHTC financing). These developers charge a percentage of the total development costs (TDC). In some financing transactions, the fee is 10 to 15 percent of the TDC (often the maximum permitted by the financing program). This percentage is higher than the fees charged by the smaller developers and limits the size of a project in which a larger developer may be engaged. A development must have a substantial number of units to limit the cost per unit of the developer's fee.

While larger developers typically are committed to preserving affordable housing, they often have done so as owners and operators of affordable rental housing. Therefore, they tend to be less familiar with tenant groups as partners as opposed to tenants in a landlord/tenant relationship. This unfamiliarity becomes a factor in situations where the expert's opinion may conflict with the desires of residents. The resolution of such conflicts is critical to making these deals work. This is particularly true in LIHTC transactions when the interests of the investors

must be protected by the same developer who has made financial guarantees to investors.

Some of the larger, well-respected nonprofit developers have chosen not to work with tenant associations, further limiting the pool of competent providers. This refusal may result from a misunderstanding of TOPA, a bad experience with a tenant organization, a feeling that the process is too time-consuming, or a disinclination to develop cooperatives. It is important to interact with these developers to establish, or reestablish, their involvement with the TOPA process.

In some cases, the tenant association decides not to develop the property itself but to create a partnership with a third-party developer. For the most part, this partnership takes three forms: an LIHTC transaction in which the residents, a developer, and investors share ownership and the developer assumes operational primacy; rental housing with the developer as the owner, in which the tenants rights might be established and protected by contract; or a condominium in which the developer purchases the building and permits interested tenants to buy at a favorable cost and pays those tenants who do not wish to purchase a negotiated amount for relocating. The amount of the relocation benefit may be significant. It will depend, as will the insider buy-in price, on such factors as building location, profit potential, size and number of vacant units, and the investment needs of the developer.

If a partnership is formed for the purpose of developing homeownership opportunities for the residents, condominiums are the typical vehicle. Cooperatives are not normally an option in a partnership between a tenant association and a developer, because the developer expects to make his or her profit from the sale of rehabilitated units. In the District of Columbia, condominiums are the recognized and more marketable multifamily ownership vehicle among market-rate buyers. Several market-rate developers will make a deal with a tenant association to develop condominiums and will give residents the option of buying in relatively cheaply. Some of these developers are legitimate and trustworthy. Others are not, and some engage in practices that border on the predatory. In many cases, hearkening back to residents' understanding of the process, residents are at a loss in determining the value of the rights they have under TOPA and are exploited in setting up these partnerships.

Neighborhoods east of the Anacostia River are notable for their lack of development support. These neighborhoods are among the District's poorest and most in need of technical housing assistance. The community development corporations (CDCs) in the area do not assist tenants directly in the purchase of their buildings. Only one, the Marshall Heights CDC, provides services tied to the TOPA process. It helps residents form tenant associations (although this assistance is not specifically TOPA-oriented but rather for tenant organization generally) and provides some training and counseling.

The absence of a TOPA infrastructure has hindered residents in east-of-the river neighborhoods from gaining the full benefit of the District's tenant ownership opportunities.

Trainers

Several organizations offer training in the TOPA process as part of a broader body of services. This training is, in our view, critical. And the need for training is ongoing, not only throughout the TOPA process but after, as long as the residents own their building.

The need for more training is as constant theme among residents, lenders, managers, and technical assistance providers. ULS provides some basic help, but not enough to meet the needs of a typically unsophisticated resident group. One resident called the process “overwhelming” and recognized the need for ongoing training.

Specific training in operating a building is essential both during and after the TOPA process. This includes training on budgets and financial matters, record keeping, managing contracts and vendors (including the management company), and community relations. Moreover, because original leaders will give way to new leaders, there is a need for ongoing training of the general membership on the nature of cooperatives, running a meeting, financial management, changes in the law, and vendor management.

This kind of training now occurs only haphazardly. It may be provided if residents ask for it or if a development team member proposes it. Even then, training will be available only if resident groups can afford it. Little of the available training is free. Once a tenant association purchases its building, even less of this training is free, and much of it is not geared toward limited-equity cooperatives.

Management Companies

While not really technical assistance providers, management companies play a critical role in helping tenant-owners get off to a good start. A close and ongoing cooperative relationship serves to train residents in building operations and business relations on a practical, day-to-day level.

Findings

- Training in the TOPA process and community organizing is essential.
- Outside organizers are rarely used in TOPA buildings. Organization is usually undertaken, if at all, by residents or by other technical assistance providers.
- Ongoing training is critical to successful TOPA purchase and the successful operation of a building.
- Training is not readily available to resident groups, and what is available is often not affordable.
- Lawyers are an important element in the TOPA process, but too few are available,

and too few are trained in the tenant-purchase process.

- Pro bono counsel plays a role in the TOPA process, but these attorneys often have limited experience and limited time.
- Neither an ongoing training program for inexperienced lawyers nor organized backup support from more experienced lawyers currently exists.
- The number of experienced, TOPA-friendly development consultants is inadequate to the need.
- Experienced development consultants typically fall into one of two dominant groups: They are part of larger organizations with diversified staff but with significant overhead, or they are part of smaller organizations (often one-person) with limited overhead but also limited skills and limited time.
- Larger, more complex projects often need the help of the larger development consultants. Smaller projects do not provide the margins to accommodate fee requirements of the larger consultant organizations. These projects are taken on by smaller organizations.
- Smaller organizations often take on many projects to ensure a stream of income. This leads to overextension and an inability to give adequate time to each project.

Many of the regular technical assistance providers are overextended or lack sufficient skill or experience to handle TOPA projects.

Recommendations

- Persuade the nonprofit sector to take the lead in implementing — or funding others to implement — the recommendations in this section.
- Develop a list of community organizers who can organize residents in TOPA situations.
- Develop a list of organizations that can provide training to tenant groups.
- Identify or develop written, video, and electronic training materials for tenant groups that would provide information about such topics as:
 - tenant group options
 - the importance of organizing
 - how to run a meeting
 - responsibilities of boards and officers
 - community building and leadership

- conflict resolution
 - the development process
 - finances
 - building operations
 - managing contracts and vendors
- Ensure that the training of residents begins immediately after they receive notice of the owner’s intent to sell. This should be tied to the outreach recommendation in section B, above.
 - Establish ongoing resident training.
 - Develop and fund a “train the trainers” program.
 - Coordinate with the D.C. Bar’s *pro bono* program to develop and provide ongoing training and support for lawyers taking on TOPA cases.
 - Convene and facilitate periodic conferences in which ideas, practices, and policies are shared and discussed.
 - Develop “best practices” materials to distribute among TOPA technical assistance providers.
 - Consider options for providing more regular draws for the smaller development consultant organizations (This will be more fully discussed in the next section on Funding).
 - Educate outreach to the nonprofit development community and TOPA and working with tenant associations.

Funding

Funding of tenant ownership is one of the major obstacles to effective completion of the TOPA process. Lenders often said that the nature of tenant purchases adds a new and different dimension to their decision making. Many commented on the residents needing to be “together” and to have a shared vision of the project. They were concerned about lack of leadership and about the potential for the group to split into factions. They also pointed out that they were less concerned about the security for a loan (although this still was an important consideration) than they were about the group’s ability to repay it. Several stated that they were not interested in foreclosing on a property, either for social or practical reasons. Nevertheless, several mentioned the poor loan-to-value ratio in many of the TOPA deals they saw. They also regularly talked about the desirability of devices to enhance the creditworthiness of tenant association borrowers.

There are two problems with financing: availability and the use of funding to preserve

affordability.

Availability of Funding

Funding is necessary at several different points. A good faith deposit is needed when the tenant association goes to contract. Predevelopment funding is needed until renovation of the building is complete. Acquisition funding is needed when the association closes on the purchase and may be in the form of a permanent, long-term loan or a bridge loan. Construction funding is needed until renovation is complete. Each type of financing has its own problems, which we discuss in the next sections.

Good Faith Deposit Loans

Good faith deposits are amounts that are given, along with a proposed contract of sale, by a buyer to a seller. They demonstrate the buyer's seriousness in purchasing the property and, in a standard market transaction, give the seller an amount from which to recover damages in the event the buyer breaches the contract. In TOPA transactions, however, the amount of the good faith deposit is limited by statute to no more than 5 percent of the sales price. Moreover, the deposit is fully refundable to the purchaser if, after a good faith effort, the purchaser is unable to close the transaction. Thus, the good faith deposit is a relatively safe loan for a lender to make to a TOPA purchaser.

Loans for good faith deposits are usually outstanding for approximately eight months and, while they are not secured by the property, they have a relatively high degree of safety due to the statutory protections for TOPA buyers. As a result, these loans are generally available from a wide range of lenders. These include local government (DHCD), community lenders, larger national non-profits and, to a limited extent, commercial lenders.

The major problems associated with good faith deposit loans are the amount borrowed and timing of the closing. When a project is large (in excess of \$100,000, for example) obtaining a deposit in a timely manner may be difficult. Few lenders can provide a loan of this size on their own. Participation by two or more lenders may be necessary, and the coordination of these loans takes time.

While there are some lenders who can make larger loans, timing remains a concern. The lender must exercise due diligence: assessing the condition of the building, profiling tenants, and assessing a preliminary development plan. The contract must be completed within about 120 days of the time tenants register (longer if a third party is involved or the seller does not promptly provide necessary information).

Predevelopment Loans

Predevelopment loans make the exercise of due diligence possible. The funds pay for such things as professional fees, environmental studies, structural evaluations, and ongoing expenses. Because these loans are needed before the association takes title to its building, the loans are unsecured. Moreover, they do not have the statutory protection given to good faith deposit loans.

These factors make predevelopment loans extremely difficult to obtain.

The few lenders who will make these loans consist almost entirely of local government (DHCD) and community and non-profit lenders. On some occasions, larger developers advance funds, or guarantee their repayment, to supply predevelopment funding.

The predevelopment process has three parts. At the earliest stage, the residents must secure an attorney and, perhaps, a development consultant. These individuals require front-end payment. The amount of the payment varies from a small deposit to show the tenants' seriousness to a large payment to compensate assistance providers for their work during the time the prospects for the project are assessed.

This first predevelopment period, which often begins at the time of registration, continues until a contract is placed with the seller. During this period, the association needs to know about building conditions and the composition of the building's residents. There are few outside costs beyond payments due to the attorney and development consultant. The involvement of an organizer will increase costs.

The second predevelopment period begins in earnest after the contract has been signed. This period involves more due diligence and the creation of a development plan. It calls for various studies, such as a phase-one environmental study, perhaps a lead assessment, an appraisal, a detailed physical needs assessment, and the preparation of development and operating proformas.

The third predevelopment period focuses on property renovation. Loans are more easily obtained during this period. Preconstruction costs may include payments for interim repairs and maintenance of the property and for relocation of tenants in preparation for construction. Much of the funding for this period can be obtained from the acquisition lender as part of the acquisition loan. Since this is a secured loan and will normally be amortized over a long period, it is usually easier to obtain and more affordable than other predevelopment funding.

Acquisition Loans

Acquisition loans present their own problems. They cover not only acquisition costs but also working capital for the association. Because these loans are secured by the property, the primary issues for lenders are the residents' ability to repay, the total amount of the loan, the loan-to-value ratio (LTV), and the priority of the loan.

Acceptable LTV ratios differ widely from lender to lender. Many commercial lenders require that the loan be no more than 75 percent of the appraised value of the "as-is" property. Community lenders have more flexibility and are often willing to base the LTV ratio on the post-renovation value of the property. DHCD is perhaps the most flexible lender.

Priority is another area where there is wide variation among lenders. Private lenders typically

require a first position in any package of loans. Community lenders are more willing to take junior positions. Once again, DHCD is the most flexible lender. While many commercial lenders say that they only make loans they know will be repaid and do not want to foreclose, they require LTVs that necessitate significant capital contributions from residents (an unlikely prospect when dealing with low-income tenants) or loans from other lenders who are willing to take a junior position. Commercial lenders in TOPA projects tend to be overly cautious, an issue that might be addressed by further education of the commercial lending community.

The total amount of a loan presents a different kind of problem. Even where LTV and priority concerns are eliminated, the amount of a loan presents a problem for many lenders. Most of the community lenders and DHCD have limited capital, and large projects challenge their lending capacity. Even larger lenders are reluctant to put too much money into any one project. In one project in which we were involved, a midsized lender was concerned about holding an \$8 million loan in its portfolio. It explored the sale of the loan to Fannie Mae or its syndication among several other lenders before finally agreeing to make the loan on its own. For a considerable period of time, the uncertainty of the loan jeopardized the project.

The timing of loan closings is a major problem in all acquisition loans, especially given that TOPA rights expire if acquisition deadlines are missed. Timing is especially problematic in larger projects, where many layers of debt must be arranged. Part of the problem is directly related to the size of a loan and the complexity of a project. Part of the difficulty involves making sure the financing permits the project to be affordable when it is complete. This involves, in turn, issues of the cost of the financing and the possibility of bringing subsidies into a project.

Construction Loans

Construction loans are short-term loans for the construction or renovation of a building. Unlike other loans, they are not provided all at once when the loan is closed. Instead, they are held by the lender and drawn down periodically as needed to pay for completed parts of the construction. Before a construction loan can be obtained, all architectural and engineering drawings and specifications must be complete.

Obtaining a construction loan is relatively easier than obtaining other loans, in large part because residents already have purchased the building, eliminating the TOPA time requirements. In some cases, however, residents attempt to obtain the acquisition loan and construction loan simultaneously. This is a pressure-filled and time-consuming process, but substantial cost savings (the result of closing both loans simultaneously) are likely. Securing both loans simultaneously is likely to require the early assistance of a competent development consultant.

The major problem faced by tenants who have bought their buildings is to obtain a satisfactory level of renovation while keeping the project affordable. Certain items must be renovated to meet code or lender requirements. Beyond these mandatory reservations, there is a trade-off between what residents want and what they can afford. To make appropriate choices, the

residents will need carefully developed scopes of work and proformas containing accurate pricing information. Because all pricing is, to some extent, conjecture, contingencies are always built into the proformas. However, since there are also always change orders during construction, the final cost of construction often eats into the contingencies. This may necessitate finding additional funding to fill gaps in the budget.

Finally, because construction loans are short-term, lasting only during the expected construction period, tenants need a way to pay off these loans with additional long-term financing. While it is possible for a construction loan to be converted to permanent financing at the end of the construction period, this is not typical (although both DHCD and the Housing Finance Agency often do so). Therefore, tenants associations will have to arrange for a “take out commitment” from a permanent lender who will replace at least the construction loan and, perhaps, both the construction loan and the acquisition loan.

Affordability

Financing has a major impact on affordability. The major variables are interest rate and term. Other factors include up-front costs and the need (in some cases) for a bridge loan.

Finding subsidies is often a large part of the financing package. Typical of the subsidies are low-interest government loans or government loans that are repaid only out of the cash remaining after all operating expenses and senior mortgages are paid. A second form of subsidy comes from the sale of units or shares in the project itself. To the extent the market permits, vacant units in a building or occupied units not purchased by members of the tenants association may be sold at higher prices than those sold to members. The capital generated by such sales may reduce the amount needed from loans. New residents often pay market prices, while existing residents retain affordable housing. Finally, subsidies can come in the form of grants, rent subsidies such as Section 8 payments, or other subsidized loans.

Findings

- Financing presents one of the most difficult obstacles to creating affordable, tenant-owned housing.
- Availability of funds is limited, and availability of funds at affordable rates is more limited.
- Obtaining predevelopment and acquisition loans for larger buildings is particularly difficult.
- Of the various types of funding needed by tenant associations, predevelopment funding is the hardest to come by.
- Lenders are concerned about LTV ratios as well as with tenant associations’ capacity to repay debt.

- Equity capital or subordinated loans would improve loan-to-value ratios.
- Timing of loans is a problem, creating a need for bridge financing obvious.

Recommendations

- Create a loan fund to make short-term bridge loans to relieve acquisition time pressures. Buildings can then be “land-banked” quickly while development plans are in process
- Create a loan guaranty fund to enhance the credit of tenant association borrowers. This fund should have a set-aside for predevelopment loans.
- Convene a group of affordable housing advocates to structure these funds and to develop underwriting and allocation policies.
- Convene community and nonprofit lenders to discuss developing standard underwriting criteria and creating a collaborative loan fund for larger projects.
- Convene a meeting of commercial lenders to discuss the possibility of broadening the scope of lending to tenant associations pursuing TOPA projects.

Training

Although we addressed training in the section on technical assistance, we raise the subject again because of our belief that training is critical to the success of the tenant purchase process. Training is needed on an ongoing basis because of inevitable changes in the composition of boards of directors and of residents. This also will make it possible for interested parties to keep up with new developments in the field.

Because it is so important to success, we believe that nonprofit organizations should require ongoing training for tenant associations as a condition of receiving assistance. In addition, we think the nonprofit community should encourage lenders to require such training as a condition of loans. The most significant obstacle to the training would be cost. This problem could be ameliorated by creating training materials that would make possible more limited use of trainers. In addition, we think tenant-owned affordable housing projects should include training costs as a regular part of their budgets and that, to the extent possible, such costs should be subsidized by nonprofit housing organizations. Such training would benefit both residents and lenders.

Recommendations

- Require technical assistance providers, lenders, developers, and others receiving nonprofit assistance for tenant ownership activities to include tenant association training in their projects.

- Create a fund to subsidize ongoing training.

Management Companies

Management companies are not directly a part of the TOPA process, but they play a major part in the success (or lack of success) of TOPA projects.

In responding to our questionnaire, managers regularly pointed out that taking on buildings of fewer than 30 units is economically undesirable. Because so many TOPA projects involve fewer than 30 units, this issue needs to be addressed. Few companies operating in the District of Columbia take on such buildings. Of those that do, several have histories of poor management of such buildings with, in some cases, disastrous consequences. Of the competent managers, many become overextended by taking on too many buildings that provide marginal fees. These companies have limited staff, who are typically poorly paid, to cover multiple buildings. As a result, both staff and residents suffer. The heavy workload and relatively low pay result in high staff turnover and a lack of continuity among site managers. Better site managers tend to move on to higher-paying jobs, and there are few competent replacements.

Some management companies that might accept smaller rental buildings do not accept smaller cooperatives. They cite the additional (uncompensated) time it takes to attend evening meetings and deal with a less sophisticated ownership group. Part of the problem is that managers are not always familiar with the various forms of tenant ownership. For example, some companies that manage cooperatives are confused about the differences between a cooperative and a condominium. Another problem is that management fees are based on carrying charge levels. In a rental or market cooperative, these levels go up periodically; in affordable housing, they are designed to be kept at the lowest level consistent with decent operations. Therefore, management fees are less likely to rise significantly from year to year.

Another strain on management companies arises from the fact that the projects they manage are geographically dispersed. Staff members often spend excessive amounts of time in city traffic and must often travel to several evening meetings on the same night. Language poses an additional problem: In many of the District's residential buildings, English is not the predominant language. Few management companies have the bilingual or multilingual staff necessary to meet this challenge.

Findings

- Too few management companies are willing to take on buildings with fewer than 30 units.
- Management companies that do take on such buildings often lack the skilled staff necessary to manage them adequately.
- Many management companies do not have site personnel who speak the predominant language of tenants.

- The dispersed location of managed buildings, the lack of buying power, and fragmentation of services introduce inefficiencies into management systems.

Recommendations

- Convene a group of affordable housing professionals and managers to discuss making small building management more efficient.
- Create an incubator for new nonprofit management companies that might manage smaller rental buildings and small cooperatives.
- Develop support mechanisms for pooling services.
- Develop cooperative models for purchasing common items such as materials, supplies, and insurance.
- Consider developing subsidies to make management of smaller buildings more acceptable.
- Develop training materials for managers of small, tenant-owned buildings.

CONCLUSION

This report was designed to identify the practical difficulties in completing the TOPA process and to suggest potential solutions or, at least, a mechanism through which solutions might be developed. Each of these suggestions provides an opportunity for nonprofit organizations to become more involved in the TOPA process. We are happy to assist interested nonprofits in further discussion of our Findings and Recommendations. We believe that such discussions have the potential to streamline the TOPA process, assist tenant organizations, and help preserve the District's supply of safe, decent, affordable housing, especially for our city's most vulnerable residents.

APPENDIX A

Development Consultants (Partial Listing)

Consultants capable of taking on larger buildings (usually more than 50 units)

National Housing Trust/Enterprise Preservation Corporation

1101 30th Street NW

Suite 400

Washington, DC 20007

- Scott Kline

skline@nhtinc.org

(202) 333-8931 x 12

Community Preservation and Development Company

5513 Connecticut Avenue, NW

Suite 250

Washington, DC 20015

(202) 895-8900

- Gerry Joseph

The Jair Lynch Companies

1508 U Street NW

Washington, DC 20009

202-462-1092

- Jair Lynch

Telesis Corporation

1101 30th Street, NW

Fourth Floor

Washington, DC 20007

(202) 333-8447

- Marilyn Melkonian

Somerset Development Company

4115 Wisconsin Avenue, NW

Suite 210

Washington, DC 20016

(202) 363-2090

Jubilee Enterprise

1400 16th Street, NW

Suite 715

Washington, DC 20036
(202) 328-1472
-Christie Cunningham

New Columbia Community Land Trust
1419 V Street NW
Washington, DC 20009
(202) 986-9225
- Pamela Jones

Consultants who usually take on smaller buildings (usually up to 50 units)

Mi Casa
6230 3rd Street, NW
Suite 2
Washington, DC 20011
(202) 722-7423
- Fernando Lemos

Rinker and Associates
524 N. Jackson Street
Arlington, VA 22201
(703) 243-5775
- Charles Rinker
cwrinker@juno.com

APPENDIX B

Proposed Priorities

The following is a listing of proposed priority areas for the District's nonprofit community to address in the near term.

1. Develop training materials covering the various stages of tenant ownership process. This should include materials on the TOPA process, on managing a tenant association, and on operating a cooperative. The materials should be in a user-friendly form that can be easily reused by successive groups in a building and should be available in visual, audio, and written form. These might include DVDs, bound written materials, and reproducible workbooks.
2. The District's nonprofit community should encourage DCRA to develop a more comprehensive and user friendly record-keeping system. It should seek to have DCRA send notices of intent to sell to the Tenant Advocate or to other appropriate person(s) or organization(s) with the goal of have those persons take a proactive role in helping tenant groups form and take advantage of TOPA rights.
3. The nonprofit community should research the status of buildings that have received notices of intent to sell. Some of these have been tracked by the Coalition for Nonprofit Housing and Economic Development, others by the American University's Washington College of Law and the Georgetown University Law Center's Harrison Institute for Public Law. These studies are not comprehensive. In addition, they use different sources that are not entirely compatible. A comprehensive study is needed to know the results of TOPA notices.
4. The nonprofit community should generate an ongoing discussion among tenant ownership advocates, members of the affordable housing community, and management companies to address the difficulties in the management of smaller affordable housing developments.