

## **Conversion to Condo for Homeownership Opportunities**

On October 17, 2006, the Internal Revenue Service issued Private Letter Ruling 200703024 with respect to a request involving offering residents of a multifamily apartment development the right of first refusal to purchase the unit in which they reside at the end of the initial 15-year compliance period. IRS responded with two conclusions:

1. The right of first refusal granted by the Owner to each resident as part of a condominium homeownership plan to purchase their unit after the close of the compliance period applicable to that unit satisfies the requirements of § 42(i)(7)(A) of the Code.
2. Assuming the existing LURA on the tax credit project otherwise satisfies § 42(h)(6) of the Code, the LURA may be amended to grant each resident occupying their unit a right of first refusal to purchase that unit and, following the end of the compliance period of the buildings in the projects, be terminated and replaced with a new LURA that will provide for (a) continuing § 42 rental income restrictions for all units which continue as rental units, and (b) § 42 income restrictions for all buyers (other than the existing residents) of the units sold.

MHDC may entertain plans by owners of tax credit developments to request the release of the LURA and substitute it with a new LURA that follows the baseline of the PLR in order to offer the residents homeownership opportunities through a condominium structure. The following factors will be considered by MHDC in connection with future requests to MHDC for a PLR based conversion.

1. The following general procedure must be followed for submission of information to MHDC:
  - a. An Owner must provide a “Notice of Intent” to MHDC to convert from a rental project to the home ownership mode.
  - b. The Owner must immediately include language stating the potential of the right of first refusal in all new and renewal leases.
  - c. Any properties that received a tax credit allocation from 1990 to 1995, inclusive, may submit the Notice of Intent, now, along with the other required documents described herein. Any other property receiving an allocation after 1995 may submit a Notice of Intent, and other documentation required herein, in year 13 of its compliance period or thereafter.
  - d. MHDC anticipates a 6 – 9 month processing time, but that is not a pre-set, yet known timeline.

- e. A Notice of Intent, the submission to MHDC, and even MHDC's approval, will not require an Owner to make the election to commence the conversion. However, the Owner must give MHDC a Notice of Conversion when the Owner makes the irrevocable election to commence the conversion.
2. MHDC must approve any plan to convert any property from rental to home ownership.
3. MHDC will order (at the Owner's costs) a Physical Needs Assessment to establish the upgrade requirements to all interior and exterior elements, all on a case-by-case basis. MHDC will also perform an inspection of the property. Reserves are expected to be used for repairs. If the reserves are not sufficient, the owner will provide other sources of funds to make repairs. If there are remaining reserves, the reserves should be passed on as an initial deposit to the replacement reserve to be utilized by the condo association.
4. MHDC has the right to impose a processing and administrative fee, yet to be determined, for the conversion review.
5. MHDC has the right to impose an annual compliance fee in connection with the review of both the condominium manager's required report and the physical maintenance standards required to be maintained by the LURA.
6. The owner must provide documentation illustrating how the purchase price is being determined, what expenses the condo fees will include, and evidencing the tenants' monthly anticipated mortgage payment, condo fee, and tenant-paid utilities will not exceed the maximum HUD established tax credit rent limit.
7. Evidence of zoning and the condominium plat, as approved by the City, must be provided to MHDC.
8. The final drafts of the condominium documents must be submitted to MHDC for approval. A memorandum from a qualified Missouri law firm must be provided to MHDC demonstrating that condominium documents comply with the Missouri Uniform Condominium Act.
9. Owners are expected to provide a discount off the sales price at a minimum of 1% per year of residency for existing tenants.
10. Owners must make homeownership education and budget counseling available to tenants no later than one year prior to the anticipated conversion date through referrals to homebuyer counseling agencies or providing it as a part of a tenant services program.

11. In addition to all the documents required and specified above, the Owner shall provide MHDC with the following:
  - a. Proposed time line for the conversion process.
  - b. The Owner's plan for discounts or incentives to be offered to tenants, no less than the standards set forth above.
  - c. The proposed application of the mathematical formula for the mortgage payment and the condominium fee consistent with the baselines herein.
  - d. The lease language for the right of first refusal.
  - e. The notice to the tenants that a conversion has started (the Notice of Conversion is provided to MHDC).
  - f. The details of the home ownership counseling program.
  - g. The details of the sales plan, contract processing and brokerage arrangements with tenants and with prospective homebuyers.
  - h. The resume of the manager of the condominium association.
12. MHDC will require a new LURA, so that the period of affordability (including the compliance period) will be at least 30 years. MHDC will develop and provide to owners this LURA documentation. The Notice of Conversion cannot be given or effective until after the end of the Compliance Period. The old LURA will be released and replaced with the new LURA at this time.
13. The Owner will not be approved for a conversion if there are any outstanding Form 8823 notices or adverse findings incurred for the Property.
14. Tenants who purchase their units must keep them as owner-occupant.
15. After the Notice of Conversion is given, tenants who do not wish to or are unable to qualify for purchase their units, shall have the right to continue to rent the units for as long as the tenant is in good standing under the lease. Extended compliance rules must be followed.
16. If a renter vacates the unit, the unit may be sold to a Section 42 income qualified household.
17. The qualified contract process is not applicable to the units that are not purchased.

18. A copy of the original tenant income certification must be provided to MHDC to prove the tenant initially qualified at move-in as a qualifying tenant.
19. It was anticipated that any Section 8 voucher tenant would be offered within the guidelines established by the PHA, a chance to enroll in the HUD Homeownership Program. Tenant must be qualified by the PHA and Owner.
20. No annual recertification will be required on purchased units.
21. MHDC will require the condo manager to report specific compliance information annually to include sales, subsequent sales, and remaining rental units. The condo manager must confirm that subsequent purchasers of condo units are income-qualified at the time of purchase until the expiration of the LURA. Reviews and compliance checks of rental units must follow normal extended use period compliance policies.
22. The Condo Fee includes at a minimum: annual replacement reserves, insurance for all exterior and common areas, annual property tax, and appropriate D & O insurance.
23. The Condo manager must be experienced in Section 42. They will be required, at its expense, to post a fidelity bond of not less than \$250,000.
24. MHDC may require additional documentation or information consistent with the foregoing at any time.

### **Owner (Developer) Imposed Requirements**

In connection with the condominium conversion of the Property, the Partnership may impose on itself additional restrictions.