1989

Non-Profit Housing Organizations

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ARTICLES

NONPROFIT HOUSING ORGANIZATIONS†

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> Drawing a distinction between home and shelter is, I hope, more than an academic exercise. Shelter, if it's warm and safe, may keep a family from dying. Only a home allows a family to flourish and to breathe. When breath comes hard, when privacy is scarce, when chaos and crisis are on every side, it is difficult to live at peace, even with someone whom we love.[1]

INTRODUCTION

As the increasing visibility of homeless individuals and families leads to a greater public awareness of their plight, a general consensus is developing among persons who work with homeless persons that any solution to the phenomenon of homelessness must include a substantial component of permanent, affordable housing.[2] Emergency shelters serve an indis-

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 Portions of this paper were presented to the Notre Dame Community, March 21, 1989, as part of the Thomas J. White Center on Law & Government Lecture Series.

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The valuable research assistance of Brian Lipton, J.D. 1988, St. Louis University, Jeanne Stich, J.D. 1988, Saint Louis University, as well as Susan Kircher, David Lawrence and Charles Reed, 3 Ls at Notre Dame Law School, is acknowledged with thanks.

1. J. KOZOL, RACHEL AND HER CHILDREN 50 (1988).

2. *See, e.g.*, L.C. KEYES, HOUSING AND THE HOMELESS 22 (MIT Housing Policy Project, HP # 15, 1988); NATIONAL HOUSING TASK FORCE, A DECENT PLACE TO LIVE 11-12 (1988); Kaufman, *Homelessness: A Comprehensive Policy Approach*, in HOUSING THE HOMELESS 335, 341 (J. Erickson & C. Wilhelm eds.

pensable function in helping homeless persons stabilize their immediate situations, but are not a source of permanent housing. Shelters generally are viewed as the first step along a path toward transitional and then permanent housing.[3]

Since the 1930s, efforts to provide permanent, affordable housing for persons in the lower economic levels of American society, where most of the homeless tend to be congregated, have been led by the federal government through the public housing program[4] or through subsidies to private housing developers and managers.[5] These efforts have met with substantial success when examined from the perspective of the entire population, but with very limited success when the viewpoint is that of a family living on the streets of America.[6]

For a variety of reasons during the 1980s, most of which can be attributed to frustration over the seeming intractableness of the housing problems of low-income persons,[7] attention has shifted from the traditional approaches of publicly or privately owned rental housing to nonprofit forms of housing, both ownership and rental. Called "social housing"[8] or "com-

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1986); Wolch, Dear & Akita, *Explaining Homelessness*, 54 J. AM. PLAN. A. 443, 451 (1988).

3. Kaufman, *supra* note 2, at 339-41. *See also* McKinney Act 42 U.S.C.A. §§ 11,301, 11,381-11,394 (West Supp. 1989) (authorizing a limited amount of federal funds for demonstration programs to provide transitional housing and permanent housing for handicapped homeless persons).

4. 42 U.S.C.A §§ 1437-1437s (West 1978 & Supp. 1988).

5. *See, e.g.*, *id.* § 1437f (Section 8 Housing Assistance Payments Program) and 12 U.S.C.A. § 1715z-1 (West 1980 & Supp. 1989) (Section 236 Rental Housing Subsidy Program).

6. *See, e.g.*, NATIONAL HOUSING TASK FORCE, *supra* note 2, at 4-8 (substantial success in reducing number of substandard housing units but access to adequate units has declined for low-income persons because of "growing disparity between rents and incomes"); PRESIDENT'S COMM'N ON PRIVATIZATION, PRIVATIZATION: TOWARD MORE EFFECTIVE GOVERNMENT 7 (1988) (percentage of housing rated inadequate by U.S. Census statistics declined from 40 percent to 5 percent since World War II, but 47 percent of very low-income renters were estimated by Department of Housing and Urban Development (HUD) to have paid over 50 percent of their income for rent in 1983).

7. The high point or low point of frustration, depending on one's point of view, was the precipitous decline (80 percent) in federal spending for new subsidized housing commitments during the decade between 1978 and 1988. NATIONAL HOUSING TASK FORCE, *supra* note 2, at 10. *See also* M. STEGMAN & J. HOLLEN, NONFEDERAL HOUSING PROGRAMS 9 (1987) (new assisted starts per year fell from 300,000-400,000 in the early 1970s to fewer than 100,000 by 1985).

8. Kuttner, *Bad Housekeeping*, THE NEW REPUBLIC, Apr. 25, 1988, at 22, 25.

munity-based housing"[9] by its proponents, this type of housing is developed and managed under nonprofit principles by private organizations. Efforts to produce such housing are being considered with increasing frequency by persons associated with shelters for the homeless.[10]

This article surveys the variety of forms that community-based housing has taken, discusses some typical problems that nonprofit housing organizations have faced in obtaining and maintaining tax-exempt status, reviews the landlord-tenant relationship when the landlord is a nonprofit organization, compares home ownership, cooperatives and nonprofit rental housing as sources of permanent housing for low-income persons, and recommends a housing program that is limited in size per nonprofit sponsor, but comprehensive in the scope of housing services offered.

Two critical components of a successful housing policy, sufficient funding to satisfy housing supply (production) and housing demand (rental/mortgage assistance) needs and the presence of a market not artificially constrained by racial or social discrimination, are not discussed specifically in this paper. The recommendations in this paper are not intended to suggest that the need to address those components can be wished away.[11]

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9. J. GILDERBLOOM & R. APPELBAUM, RETHINKING RENTAL HOUSING 182 (1988).

10. For example, the Council of Providers of Services to the Homeless (COPOSH), a partnership of the United Religious Community, the University of Notre Dame and social service agencies in South Bend, Indiana which organized the South Bend Center for the Homeless (opened in December, 1988) has prepared plans for the development of over 100 units of low-income rental and purchase housing that would be managed by a not-for-profit corporation. Interview with David T. Link, Dean, Notre Dame Law School and President, COPOSH (Mar. 21, 1989).

11. Despite the constraints of the federal deficit, public pressure has been building for renewal of federal leadership in efforts to provide decent housing for persons of low and moderate income. A comprehensive housing bill has been introduced in both the Senate and the House with broad bipartisan support (S. 565, H.R. 1180). 17 Hous. & Dev. Rep. (BNA) 434 (1989); Toner, *Senate Gets Housing Measure Aimed at Keeping Costs Low*, N.Y. Times, Mar. 16, 1989, at B11, col. 3.

A book review in the *Journal of the American Planning Association* includes a discussion of the following books and reports: R. STRUYK & C. WALKER, AMERICA'S HOUSING NEEDS TO THE 21ST CENTURY (1988); NATIONAL ASSOCIATION OF HOME BUILDERS, A BLUEPRINT FOR NATIONAL HOUSING POLICY (1987); NATIONAL HOUSING TASK FORCE, A DECENT PLACE TO LIVE (1988); R. STRUYK, M. TURNER, & M. UENO, FUTURE U.S. HOUSING POLICY: MEETING THE DEMOGRAPHIC CHALLENGE; MIT CENTER FOR REAL ESTATE DEVELOPMENT, MIT HOUSING POLICY PROJECT, HP PUBLICATIONS (1988);

I. COMMUNITY-BASED HOUSING ORGANIZATIONS

The old saying, "Necessity is the mother of invention,"[12] had particular meaning for the low-income housing industry during the 1980s. When the federal government withdrew its support for housing subsidy programs, profit-motivated developers lost their incentive to provide housing for low-income persons and generally pulled out of the field.[13] At the same time, the inability of the public housing program to garner significant local or national support throughout its 50-year life[14] left it collapsing under the weight of unconscionably long waiting lists[15] and newly-enacted restrictions against construction of additional units.[16] The resulting public displeasure with

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JOINT COMMITTEE ON BANKING, FINANCE, HOUSING AND URBAN AFFAIRS, A NEW NATIONAL HOUSING POLICY (1987); NATIONAL LOW INCOME HOUSING PRESERVATION COMMISSION, PREVENTING THE DISAPPEARANCE OF LOW INCOME HOUSING (1988); PRESIDENT'S COMMISSION ON HOUSING, THE REPORT OF THE PRESIDENT'S COMMISSION ON HOUSING (1982); W. APGAR, JR. & H. BROWN, THE STATE OF THE NATION'S HOUSING (1988); S. NEWMAN & A. SCHNARE, SUBSIDIZING SHELTER: THE RELATIONSHIP BETWEEN WELFARE AND HOUSING ASSISTANCE (1988); NATIONAL ASSOCIATION OF HOME BUILDERS, NATIONAL ASSOCIATION OF REALTORS, & MORTGAGE BANKERS ASSOCIATION OF AMERICA, TOWARD A NATIONAL HOUSING POLICY (1987). Lowry, *Book Reviews, Housing Policy for the 1990s: A Planner's Guide*, 55 J. AM. PLAN. A. 93 (1989).

Extensive changes in the Federal Fair Housing Act, 42 U.S.C.A. §§ 3601-3631 designed to encourage more aggressive efforts to respond to racial discrimination in housing, went into effect March 12, 1989. Finder, *Housing Bias Still Pervades the New York Region*, N.Y. Times, Mar. 13, 1989, at B1, col. 2, B2, col. 3. One day after the legislation became effective, the Justice Department filed suits in Minnesota (United States v. Klinkner) and Florida (United States v. Rent America, Inc.) seeking compensatory monetary damages on behalf of persons allegedly victimized by "pattern(s) or practice(s)" of rental housing discrimination. 16 Hous. & Dev. Rep. (BNA) 925 (1989).

For a discussion of prospects of success for such legislation, see generally J. KUSHNER, FAIR HOUSING, §§ 10.04-.05 (1983 & Supp. 1988).

12. J. BARTLETT, FAMILIAR QUOTATIONS 134:9 (15th ed. 1980).

13. Federally-subsidized housing starts declined from a high of over 300,000 per year in the late 1970s to less than 25,000 per year by 1988. NATIONAL HOUSING TASK FORCE, *supra* note 2, at 6.

14. The public housing program has been extremely controversial from its inception. For reviews of the program which identify the elements of the continuing public controversy, see L. FREEDMAN, PUBLIC HOUSING: THE POLITICS OF POVERTY (1969), E. MEEHAN, PUBLIC HOUSING POLICY: CONVENTION VERSUS REALITY (1975) and M. MEYERSON & E. BANFIELD, POLITICS, PLANNING AND THE PUBLIC INTEREST (1955).

15. One million persons were estimated to be on public housing waiting lists in 1988, with an expected duration of several years not uncommon. Some lists were closed to new applicants. NATIONAL HOUSING TASK FORCE, *supra* note 2, at 7.

16. 42 U.S.C.A. § 1437c(j) (West Supp. 1988) (construction of new

both traditional forms of housing for low-income persons led community leaders in a number of areas to consider private, nonprofit sponsorship of housing as an alternative.

Nonprofit housing has a long and valued tradition in Western Europe but a somewhat checkered history in the United States.[17] Substantial defaults by nonprofit housing organizations, many of which were created in response to federal housing and community development programs, in the 1960s and 1970s fueled the belief that nonprofits had neither the experience nor the "staying power" to be successful in the housing field.[18] The vacuum created in the 1980s by the withdrawal of federal assistance for private-sector housing and the collapse of support for public housing revived interest in nonprofit housing efforts.

Nonprofit organizations are being recognized as having a potentially significant role in housing. In the words of the Director of the Office of Economic Development, Berkeley, California:

> Nonprofits deliberately seek to provide housing to concentrations of low-income people, to population subgroups, and to distressed neighborhoods—often in conjunction with critically needed supporting neighborhood revitalization activities—that are not the targets of action of other developers and providers. And they con-

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public housing units limited to responding to unmet demand for family housing, replacing units being disposed of or demolished by local public housing authorities, or complying with court orders and directions from HUD requiring housing in integrated settings).

17. For a discussion of the European experience, see J. CULLINGWORTH, ESSAYS IN HOUSING POLICY: THE BRITISH SCENE (1979); J. GILDERBLOOM & R. APPELBAUM, *supra* note 9, at 150-80; THE HOUSING CORP., HOMES THROUGH HOUSING ASSOCIATIONS (1987) (annual report of the National Housing Corp. in Great Britain, charged with channeling funds to and monitoring activities of nonprofit housing associations in Great Britain).

For reviews of recent American experience with nonprofit housing efforts, see W. GRIGSBY & L. ROSENBERG, URBAN HOUSING POLICY 236-39, 285 (1975); N. MAYER, THE ROLE OF NONPROFITS IN RENEWED FEDERAL HOUSING EFFORTS (MIT Housing Policy Project, HP # 16, 1988); Kirkpatrick, Dillon & Bloch, *Developments in Nonprofit Production of Low-Income Housing*, 20 CLEARINGHOUSE REV. 1227 (1987).

For more general discussions of the nonprofit sector, see REVISED MODEL NONPROFIT CORP. ACT (1988); T. MCADAM, DOING WELL BY DOING GOOD (1986); P. TREUSCH, TAX-EXEMPT CHARITABLE ORGANIZATIONS (3d ed. 1988); Hansmann, *The Role of Nonprofit Enterprise*, 89 YALE L.J. 835 (1980).

18. *See, e.g.*, Stegman, *The New Mythology of Housing*, TRANS-ACTION, Jan. 1970, at 55.

sciously aim for permanent housing affordability for these often-neglected groups.[19]

A "new generation" of nonprofit housing organizations have taken a variety of forms, but have one thing in common—community identification.[20] Two basic types have emerged: 1) comprehensive, umbrella-type organizations that operate city- or area-wide to provide technical assistance, coordination, planning and leverage for community-based nonprofit housing activities,[21] and 2) housing development and management organizations that have an identity with a particular community and/or a particular mission, such as producing rental housing for low-income families, managing housing developments for

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19. N. MAYER, *supra* note 17, at i.

20. NATIONAL HOUSING TASK FORCE, *supra* note 2, at 24 ("new generation" of community-based nonprofit development organizations contains over 4000 community development corporations, nonprofit developers, religious institutions and other neighborhood-based groups).

21. For a review of the work of nonprofit umbrella organizations, see Kirkpatrick, Dillon & Bloch, *supra* note 17. From a survey of several large umbrella organizations including the Boston Housing Partnership, the Chicago Housing Partnership, and the Low-Income Housing Fund of San Francisco, the authors characterize the typical umbrella organization as a

> city-wide nonprofit group with competent staff to assist local nonprofits with training, financing, and direct development through joint ventures on specific projects. The board of the city-wide nonprofit is composed of people who are chosen for their ability to raise funds and to affect local policy development. This organization is then in a position to advocate for new policies, such as housing trust funds, linkage programs, or state tax credits.

Id. at 1230. The rationale for umbrella organizations and some consequences of their establishment are described as follows:

> The theory behind creation of these intermediaries is that there is a shortage of skills in the community and that, by addressing the lack of skills, more funding sources will be willing to put money into low-income housing and the productivity of local groups will increase, with less time spent on packaging of projects. Overall resources will increase and be used more productively. This theory usually turns out to be true in the long run. On a decision-by-decision basis, however, the theory may appear questionable. A local group may not receive funding for something crucial to its program when the area-wide intermediary draws on local support for its activities. The area-wide intermediary will tend to focus all resources for housing in the area through its own process. Groups that do not get along with the staff of the intermediary may find it significantly harder to approach funding sources than if the intermediary were not there. Unfortunately, progress rarely comes without some cost.

Id. at 1234.

the elderly, or assisting low-income persons in becoming home owners.[22]

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22. The National Housing Task Force identified the following "success" stories:

> In Boston, Inquilinos Boricuas en Accion has built or rehabilitated over 800 units for low-income residents in a rapidly gentrifying neighborhood.
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> In Washington, D.C., Jubilee Housing has renovated 350 low-income apartments and established a comprehensive support system of health care, job placement and transitional housing to help the very poor help themselves towards self-sufficiency.
>
> The Greater Miami Neighborhoods (GMN) is providing development services to six constituent neighborhood and city-wide low-income housing groups. Since 1985, GMN has raised over $1.5 million from local government and the business community for loans, grants and operating expenses, producing initial commitments for 266 dwelling units.
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> Headquartered in Sacramento, California, the Rural Community Assistance Corporation (RCAC) has assisted 408 rural communities and almost 500,000 individuals in 10 Western states. Operating primarily with grants and contracts from government agencies, RCAC has helped local communities develop 20,000 units of housing, including 5,000 constructed using self-help techniques.
>
> In Baltimore, The Loading Dock, Inc., a nonprofit salvage operation, collects donated new and used building materials and sells them to low-income people and nonprofit developers at one-third of their retail price. Donors receive tax write-offs for the goods.
>
> In Vermont and New Hampshire, the Northern Community Investment Corporation has sponsored over 400 units of affordable housing for low-income families and elderly renters in a depressed six-county rural area. A number of the group's 11 apartment projects not only created housing, but preserved local historic landmarks.
>
> The Cleveland Housing Network has rehabilitated over 300 units using ingenious techniques that have reduced rehabilitation costs to less than $20,000 per unit. Reduced-rate financing for this effort has been provided by a consortium of corporate investors.
>
> The members of the Federation of Appalachian Housing Enterprises, Inc., a coalition of nonprofit builders serving communities in central Appalachia, have completed 623 new houses, 1,393 rehabs, 4,031 repairs and 7,880 weatherization projects. The groups have served 13,127 families with an average income of $4,800.
>
> In Mississippi, the Delta Housing Development Corporation has supervised the construction of 125 self-help housing units and has constructed 157 others. It has rehabilitated another 50 and weatherized 2,000 units.
>
> Neighborhood Housing Services (NHS) of Chicago serves nine neighborhoods housing over 220,000 people. It has directly managed $44 million in rehabilitating 8,181 units and originated loans totalling $9.5 million to more than 1,800 families, the majority of whom have low or very low incomes.

Community-based nonprofit housing organizations may be organized and controlled by residents of a particular neighborhood, in which case they usually have a broader mission such as neighborhood revitalization or community development.[23] They may be identified with a particular goal, such as the South Atlanta Land Trust's concern for cleaning up vacant lots and preserving housing being vacated as owners die or move away,[24] the Urban Homesteading Assistance Board of New York's (UHAB) emphasis on sweat equity rehabilitation,[25] or the Ecumenical Housing Production Corporation of St. Louis' (EHPC) focus on providing single-family rental housing for large families in suburban locations.[26] They may be local affiliates of a national or international organization, such as Habitat For Humanity,[27] or spin-offs of a religious community.[28]

Whatever their particular mission or method of organization, community-based nonprofit organizations are "gap-fillers" in the housing marketplace because they operate where other housing providers (except public housing authorities) do not. They seek to provide housing for the most neglected groups—very low-income persons, large families, single-parent

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> In the rural San Joaquin Valley of California, Self Help Enterprises, Inc., has assisted 3,130 families build their own homes; rehabilitated 2,700 units; weatherized over 10,000 homes; and provided technical assistance to over 90 small rural community projects to improve water and sewer systems.

NATIONAL HOUSING TASK FORCE, *supra* note 2, at 24-25.

23. *See generally* NATIONAL HOUSING AND ECONOMIC DEVELOPMENT LAW PROJECT, A LAWYER'S MANUAL ON COMMUNITY BASED ECONOMIC DEVELOPMENT (1974); Shadburn, Stokley, Wallace & Wang, *Problems and Possibilities: Community Development Corporations*, 15 N.Y.U. REV. L. & SOC. CHANGE 99, 99-112 (1987); Williams, *The Nonprofit Cooperation and Community Development in Bedford—Styvesant*, 42 WASH. & LEE L. REV. 1259 (1985).

24. LOW INCOME HOUSING INFORMATION SERVICE, LOW INCOME HOUSING ROUND-UP 1 (Dec. 1986).

25. URBAN HOMESTEADING ASSISTANCE BOARD, A RETROSPECTIVE REPORT AND REVIEW 9 (1985).

26. Baker, *Shelter*, ST. LOUIS BUS. J., Dec. 2-8, 1985, at 1B.

27. *See, e.g.*, M. FULLER & D. SCOTT, LOVE IN THE MORTAR JOINTS (1980); R. STEVENS & T. SWISHER, HABITAT FOR HUMANITY COMMUNITY SELF-HELP HOUSING MANUAL (1986).

28. For example, see *infra* notes 103-08 and accompanying text for a discussion of the Nehemiah Project started by a coalition of religious leaders in Brooklyn, New York. *See also* PONTIFICAL COMM'N "IUSTITIA ET PAX," WHAT HAVE YOU DONE TO YOUR HOMELESS BROTHER? 26-28 (1987) (participation in housing programs is one of three ways local churches address housing problems); UNITED STATES CATHOLIC CONFERENCE, THE RIGHT TO A DECENT HOME 17 (1975) (reviewing nonprofit housing activities sponsored by Catholic institutions and organizations).

households, physically or mentally disabled persons,[29] and they are willing to go where the poor and the homeless are found—in distressed neighborhoods.[30]

II. Tax Treatment of Community-Based Housing Organizations

Production and management of housing, whether it be for persons who can afford to pay market prices or for persons who cannot, is a business fraught with the usual business risks and requiring the usual business skills of planning, attention to detail, sensitivity to market forces and concern for the "bottom line." While nonprofit organizations who enter the housing business must recognize the business aspects of their endeavors, they bring a critically different perspective to their work—their goal is not to earn a profit for themselves or their members. Federal and state tax policies recognize the value of activities carried on for charitable purposes by allowing deductions for contributions to charitable organizations[31] and by exempting the income of charitable organizations from taxation.[32]

A. *Federal Law—The Charitable Deduction*

While there is no specific mention of nonprofit housing activities in the tax exemption statutes, the Internal Revenue Service has been willing to recognize the charitable nature of certain types of housing activities. In addition, provisions of the Tax Reform Act of 1986 that created the low-income housing tax credit[33] and restricted the use of tax-exempt municipal bond financing[34] contain specific acknowledgment of and special treatment for low-income housing activities by nonprofit organizations.[35]

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29. Housing analysts report that in 1987 over 7 million households with incomes less than $10,000 were living in non-subsidized housing, and that most were paying more than 50 percent of their income for rent. National Housing Task Force, *supra* note 2, at 6-7 (1988).

30. N. Mayer, *supra* note 17, at 3-5.

31. I.R.C. § 170 (West Supp. 1989). *See generally* 2A C. Antieau, Municipal Corporation Law § 21.14 (1988), for a discussion of state exemption of the properties of charitable organizations from taxation.

32. I.R.C. § 501(c)(3) (West Supp. 1989).

33. I.R.C. § 42 (West Supp. 1989).

34. I.R.C. §§ 141-149 (West Supp. 1989).

35. *See, e.g.*, I.R.C. § 42(h)(5)(C)(ii) (West Supp. 1989) (at least 10 percent of tax credit allocations to each state must be set aside for low-income housing projects in which § 501(c)(3) tax exempt nonprofit organizations whose "exempt" purposes include "the fostering of low-income housing" materially participate); I.R.C. §§ 145(a), 146(g) (West

Attainment of tax-exempt status is important to nonprofit housing organizations for two reasons: 1) access to donations from individuals and corporations, the life blood of nonprofit enterprises, is determined in large measure by tax-exempt status, and 2) exemption from the payment of taxes, particularly state and local property taxes, can be a significant factor in the feasibility of a particular housing development.

The provision of housing for low-income persons is not a designated tax-exempt activity as are religious, scientific, literary or educational activities, so nonprofit housing organizations must seek to qualify for tax-exempt status as "[c]orporations . . . organized and operated exclusively for . . . charitable . . . purposes."[36] While there is little or no case law directly deciding the questions whether nonprofit housing corporations qualify under the charitable purpose, Treasury Department Regulations and Revenue Rulings issued by the Internal Revenue Service establish a framework for analyzing individual cases.[37]

1. Charitable Purpose Test

The term "charitable," as defined in the Regulations, includes activities in relief of the poor and distressed or the underprivileged, and efforts to promote social welfare by organizations designed to lessen neighborhood tensions, to eliminate prejudice and discrimination, or to combat community deterioration.[38] Beginning in 1970, the Internal Revenue Service has issued a series of Revenue rulings concluding that certain types of housing activities may qualify for tax-exempt status under Section 501(c)(3).[39] In its most important ruling,[40] the Service concluded that in general:

Supp. 1989) ("qualified 501(c)(3) bonds" not subject to state volume caps on private activity bonds if the housing meets the tests for qualified residential rental projects).

36. I.R.C. § 501(c)(3) (West Supp. 1989).

37. The basic test is a factual one, to be determined by analysis of the specific facts in each case. *See generally* 26 C.F.R. § 1.501(c)(3)-1(a)-(e) (1988).

38. 26 C.F.R. § 1.501(c)(3)-1(d)(2) (1988).

39. Rev. Rul. 79-19, 1979-1 C.B. 195; Rev. Rul. 79-18, 1979-1 C.B. 194; Rev. Rul. 77-3, 1977-1 C.B. 140; Rev. Rul. 76-408, 1976-2 C.B. 145; Rev. Rul. 72-124, 1972-1 C.B. 145; Rev. Rul. 70-585, 1970-2 C.B. 115; Rev. Rul. 70-535, 1970-2 C.B. 117. Revenue Rulings are interpretations of law issued by the Internal Revenue Service based on specific factual situations presented to the service. They do not have the force of law of Treasury Department Regulations but often are used as precedent by the Service. 1987-2 C.B. iii.

40. Rev. Rul. 70-585, 1970-2 C.B. 115. The discussion of Revenue Rulings is drawn from material included in Chapter Three of C. DAYE, D.

> where an organization is formed for charitable purposes and accomplishes its charitable purposes through a program of providing housing for low- and, *in certain circumstances* moderate-income families, it is entitled to exemption . . . . The fact that an organization receives public funds under State or Federal programs for housing is not determinative; qualification is based on whether or not the organization is charitable within the meaning of section 501(c)(3).[41]

The Service applied its basic conclusion to four types of organizations.

1) A nonprofit organization that was formed to build or renovate houses for sale to low-income families on long-term, low-payment plans qualified for tax-exempt status because "[b]y providing homes for low-income families who otherwise could not afford them, the organization, . . . [was] relieving the poor and distressed." Low-income families were eligible to participate in the program if they qualified for loans under a federal housing program but could not obtain financing through conventional channels or did not have the necessary down payment. The cost of the homes was recovered, if possible, through very small periodic payments. Operating income came from federal loans and private contributions. Volunteer help was used for renovation work whenever possible.

2) Also exempt was an organization formed to provide housing for low- and moderate-income minority groups in integrated settings because its activities were "designed to eliminate prejudice and discrimination and to lessen neighborhood tensions."

3) A neighborhood organization formed to develop plans for redevelopment of a particular area as a residential community which, as part of the renewal project, purchased an apartment house to be rehabilitated and rented at cost to low- and moderate-income families was tax-exempt because its purposes and activities "combat community deterioration by assisting in the rehabilitation of an old and run-down residential area."

4) However, a corporation formed by community organizations concerned about a growing housing shortage for moderate-income persons to build new housing units and rent them at cost to moderate-income families was not entitled to tax-exempt status because its program was "not designed to pro-

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MANDELKER ET AL., HOUSING AND COMMUNITY DEVELOPMENT 182, 184-85 (2d ed. 1989).

41. Rev. Rul. 70-585, 170-2 C.B. 115 (emphasis added).

vide relief to the poor or to carry out any other charitable purpose within the meaning of the [applicable] regulations" (e.g., eliminating prejudice and discrimination, lessening neighborhood tensions, or combatting community deterioration).[42]

In a comparison ruling, the Service denied tax-exempt status under Section 501(c)(4)[43] to a nonprofit corporation organized to manage low- and moderate-income housing projects owned by exempt nonprofit corporations.[44] Fees were charged for the management services and were used to meet expenses. The organization operated similarly to the way profit-motivated real estate management firms operated. Under applicable regulations,[45] the Service concluded that the organization's primary activity was "carrying on a business . . . in a manner similar to organizations operated for profit" rather than "promoting . . . the common good and general welfare of the people of the community" and the fact that services were provided exclusively to tax-exempt organizations did not change the business nature of the activity.[46]

In an important ruling regarding homes for the elderly, the Service concluded that nonprofit organizations could qualify for tax-exempt status if their housing developments were "designed to satisfy the three primary needs of aged persons":

> (1) housing . . . designed to meet some combination of the physical, emotional, recreational, social, religious, and similar needs of aged persons. . . .
>
> (2) health care . . . [by providing services] designed to maintain the physical, and if necessary, mental well-being of its residents . . . [and]
>
> (3) financial security . . . [through a policy] of maintaining in residence any persons who become unable to pay their regular charges [with exceptions allowed for Federal or state assistance programs for persons of low or moderate income who are required to pay sufficient rent to enable the owner to recover operating costs] . . .

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42. *Id.* at 115-16.

43. Under section 501(c)(4) of the Internal Revenue Code, qualifying organizations are exempt from paying tax on their income if they operate "exclusively for the promotion of social welfare," but persons who make donations to such organizations may not take a charitable deduction. I.R.C. § 170(c)(2)(B) (West Supp. 1989).

44. Rev. Rul. 70-535, 1970-2 C.B. 117, 118.

45. 26 C.F.R. §§ 1.501(c)(4)-1(a)(2)(i)-(ii) (1988).

46. Rev. Rul. 70-535, 1970-2 C.B. 117.

> [and operating] so as to provide its services to the aged at the lowest feasible cost . . . .[47]

This ruling suggests that housing for non-elderly families stands a better chance of IRS approval if social services, such as day care and employment counseling are provided along with the housing services, and a good cause eviction standard is employed by the housing managers. These items are discussed in greater detail in Part III.

Later rulings gave specific approval to housing for the elderly,[48] for physically handicapped,[49] and provision of interest-free home repair loans to low-income homeowners in badly deteriorated areas,[50] but denied tax-exempt status to a nonprofit organization that leased housing to a city at cost for use as free temporary housing for families displaced because of fire. While the housing was free to occupants, the city rather than the nonprofit organization was providing the service and the city had to pay the nonprofit organization for use of the housing.[51]

Several important points should be noted about the Service's approach to the tax status of nonprofit housing corporations. Perhaps most significant is the Service's willingness to accept the argument that the provision of housing for low- and moderate-income persons can serve a charitable purpose. However, the mere fact that an organization sets out to provide such housing does not mean that it will automatically receive tax-exempt status. A formal application must be made to the Service and decisions regarding tax-exempt status are made on a case-by-case basis.[52]

The mission of the organization is the starting point for analysis of tax-exempt potential. The regulations and revenue rulings identify two main categories of charitable activities that have relevance for housing: 1) relief of the poor and 2) promotion of social welfare. Subcategories of promotion of social welfare are lessening of neighborhood tensions, elimination of prejudice and discrimination, and combatting community deterioration. While none of these categories and subcategories specifically mentions housing, the Service has accepted programs that provide housing "for low-income families who otherwise could not afford them" as qualifying for tax-exempt

47. Rev. Rul. 72-124, 1972-1 C.B. 145, 146-47.
48. Rev. Rul. 79-18, 1979-1 C.B. 194.
49. Rev. Rul. 79-19, 1979-1 C.B. 195.
50. Rev. Rul. 76-408, 1976-2 C.B. 145.
51. Rev. Rul. 77-3, 1977-1 C.B. 140.
52. 26 C.F.R. § 1.501(a)-1, (a)(2) (1988).

status.[53] Housing programs for moderate-income persons, on the other hand, are not likely to qualify for tax-exempt status, even though the moderate-income persons may not be able to afford market-priced housing, since such programs would not be providing "relief for the poor." They should be able to qualify as tax-exempt, though, if they are linked to some other recognized charitable purpose such as removing prejudice and discrimination (housing in integrated settings) or combatting community deterioration (renovating existing housing in deteriorated neighborhoods).[54]

The line between low income and moderate income is often difficult to draw. The Service provides little guidance in its published rulings except to say that the determination of what is low income is a "factual question based on all of the surrounding circumstances."[55] The targeting provisions included in the low-income housing tax credit program[56] and the private activity bond regulations[57] suggest that the line should be drawn at the 50-60 percent of median income range, while the Section 8 housing subsidy program draws the line for program eligibility at 80 percent of area median income. Persons whose incomes are below that level are said to be persons of "lower income."[58]

Nonprofit organizations who target their housing efforts to persons at the bottom of the economic ladder, such as homeless families coming out of shelters and transitional housing into permanent homes, should have little difficulty meeting the charitable purpose standard, but organizations that serve a wider market such as "first time home buyers" or persons whose incomes are at or near median income levels but who cannot afford decent housing because of high housing costs will most likely have to identify some additional social welfare purpose as the basis for achieving tax-exempt status for their housing activities.

2. Business Test

The business test may cause nonprofit housing corporations more problems. All housing developments, whether they be for low, middle, or upper income persons, must generate sufficient income to meet both capital and operating expenses.

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53. Rev. Rul. 70-585, 1970-2 C.B. 115.
54. *Id.*
55. *Id.*
56. I.R.C. § 42 (West Supp. 1989).
57. *Id.* § 142.
58. 42 U.S.C.A. §§ 1437a(b)(2), 1437f(a) (West 1978 & Supp. 1988).

The classic way to accomplish this is to operate efficiently—"in a sound, business-like manner." A recent analysis of nonprofit housing potential identified the following "business characteristics" as essential ingredients of increased capacity: "a sufficient[ly] skilled executive director, technical and project skill requirements for key staff members, financial and market analysis capability, a division of responsibilities and skills among a variety of actors, competent bookkeeping and other basic business skills."[59]

If the Service means what it said when it denied tax-exempt status to a nonprofit housing management company that was organized to manage housing developments owned by other exempt organizations because it "operates in a manner similar to organizations operated for profit,"[60] then nonprofit housing organizations who meet the business skills standards advocated for increasing capacity (and eligibility for federal support under new housing initiatives)[61] would do so at the risk of jeopardizing their tax-exempt status. Since it is hard to fathom the reasonableness of such a position, it is likely that the Service had something else in mind when it distinguished business activities from social welfare activities.

A possible alternative to a business/non-business dichotomy is an analysis that focuses on the type of housing services offered. Traditional rental housing services are offered in a "hands off" manner, with the profit-motivated owner offering little in the way of services to tenants other than possession of a housing unit and maintenance of the complex, including provision of utilities. If that is what the Service had in mind when it considered the management services of the nonprofit housing organization to which it denied tax-exempt status, the ruling does not appear to cause too many problems. Nonprofits presumably could avoid being characterized as a business by offering management services that the typical real estate management business did not offer. How many real estate management companies offer day care service to children of tenants while the parents work or attend school? How many

59. N. MAYER, *supra* note 17, at 25.

60. Rev. Rul. 70-535, 1970-2 C.B. 117.

61. Comprehensive housing legislation introduced in Congress in March, 1989 (H.R. 1180 and S. 565) would create community housing partnerships and require state and local governments receiving proposed new federal support for housing development activities to set aside at least 10% of the funds for nonprofit community organization developed, sponsored or owned housing. 16 Hous. & Dev. Rep. (BNA) 880-81, 920-22 (1989).

offer employment referral services or family counseling? How many permit tenants to contribute management services in lieu of rent, or offer to train tenants in housing management skills? Services of this nature clearly would be different from services provided by profit-motivated business, and would also be consistent with conclusions being drawn concerning the need for low-income housing to be placed in a comprehensive setting that includes educational opportunities, job development and family counseling.[62]

B. *State Law—Property Tax Exemption*

In addition to seeking tax-exempt status under the Internal Revenue Code, nonprofit housing organizations often seek exemptions from state and local property taxes. For nonprofits that develop and own rental housing units, the taxes on the value of the real property can be a significant factor in their overall ability to maintain units at affordable rentals for low-income persons.[63]

Nonprofit corporate sponsorship of housing for low- and moderate-income persons has generated litigation concerning the tax-exempt status of charitable activities. Homes for low-income, aged and disabled persons, as well as apartments for elderly persons of low and moderate income, operated by religious and other nonprofit organizations generally have been accorded tax-exempt status.[64] However, housing for low- and moderate-income families who are not disabled or elderly often have been denied tax-exempt status, particularly when the rents have been set at a level to amortize mortgage loans and pay operating expenses, operating funds do not come from public or private charity, and tenants are subject to eviction for non-payment of rent. In these cases, the receipt of federal housing subsidies by the nonprofit sponsor has not been sufficiently persuasive that the organization was engaged in purely charitable activities.[65]

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62. *See infra* notes 69-100 and accompanying text (Section III).

63. *See generally* 2A C.J. ANTIEAU, MUNICIPAL CORPORATION LAW § 21.14 (1988).

64. South Iowa Methodist Homes v. Board of Review, 173 N.W.2d 526 (Iowa 1970); Banahan v. Presbyterian Housing Corp., 553 S.W.2d 48 (Ky. 1977); Pentecostal Church of God v. Hughlett, 737 S.W.2d 728 (Mo. 1987); Appeal of Harrisburg, 18 Pa. Commw. 440, 337 A.2d 303 (1975) (Bowman, P.J. & Mencer, J., dissenting). *Contra* Clark v. Marian Park, Inc., 80 Ill. App. 3d. 1010, 400 N.E.2d 661 (1980).

65. Clark v. Marian Park, Inc., 80 Ill. App. 3d. 1010, 400 N.E.2d 661 (1980); Mountain View Homes, Inc. v. State Tax Comm'n, 77 N.M. 649, 427 P.2d 13 (1967); Metropolitan Pittsburgh Nonprofit Hous. Corp. v. Board of

The distinction often drawn between housing for disabled and elderly and housing for low- and moderate-income families does not appear persuasive, particularly in view of substantial increases in demand for affordable housing for families with children. The correct approach appears to be taken by the Minnesota Supreme Court, which held that housing developed by a nonprofit corporation for families of low- and moderate-income that received federal interest reduction and rent supplement subsidies qualified for tax-exempt status because the provision of housing for low- and moderate-income families by private organizations lessens the burdens of government and the rent paid by the tenants was only a small fraction of the total income of the project, the balance being received from government subsidies and private donations.[66]

The Minnesota Supreme Court responded to the tenant rental payment requirement as follows:

> The most troublesome issue is presented by the application of the third factor—whether recipients of the charity are required to pay for the assistance in whole or in part. . . .
>
> The situation at Rio Vista cannot be distinguished easily from [cases denying tax-exempt status]. The monthly basic rents presently charged at Rio Vista are $125 for a 1-bedroom unit and $165 for a 2-bedroom unit, plus electricity. The commercial nature of the operation is also reflected in the fact that a tenant may be evicted for failure to pay rent. Further, the exhibits indicate that rents cover approximately 77 percent of the total operating costs at Rio Vista.
>
> However, our reading of the record also indicates that much of this rent is actually paid by the Federal Government. Thus, rents actually paid by tenants are not the major source of revenue to the project. This is a distinguishing feature of the Rio Vista situation: Tenants

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Property Assessment, 28 Pa. Commw. 356, 368 A.2d 837 (1977), *aff'd*, 480 Pa. 622, 391 A.2d 1059 (1978).

66. Rio Vista Non-Profit Hous. Corp. v. County of Ramsey, 277 N.W.2d 187 (Minn. 1979) (housing for low- and moderate-income families granted tax-exempt status). For a criticism of the decision as "ill advised" because of its potential for forcing municipalities to subsidize low-income housing developments by providing services without receiving property tax revenues, thereby undercutting the "quid pro quo" rationale for the charitable exemption, see Note, *Real Estate Tax Exemption for Low-Income Housing Corporations: Rio Vista Non-Profit Housing Corp. v. County of Ramsey*, 64 MINN. L. REV. 1094, 1103, 1105 (1980).

> receive the housing at considerably less than market value or cost. . . .
>
> . . . The fact that a purely public charity receives some remuneration from those it benefits does not deprive the institution of its charitable exemption. The amount of remuneration in relation to benefits conferred always require [sic] an analysis of the facts of each case.[67]

The Missouri Supreme Court reached a similar conclusion in a case involving a federally-subsidized housing development for elderly and handicapped persons:

> In its conclusions of law in support of its decision to deny a charitable exemption, the Commission . . . expressed doubt that the tenants would consider themselves objects of charity and emphasized that they were not indigent. This is but further evidence of the inappropriate focus of such cases. In other areas, we have often reaffirmed the premise . . . that charity is not limited to relief of the destitute. . . . Furthermore, we cannot believe that it is the intent of the people under § 137.100 to withhold the financial assistance of a tax exemption until such time as our elderly are totally incapable of providing for themselves. The whole thrust of projects such as Chariton is to assist its tenants in avoiding such status by providing an atmosphere where they can remain self-sustaining as long as possible. The payment of monthly rent at Chariton and similar projects may for some be as important as the other valuable activities. Although federal or other assistance is obviously being provided, the sense of paying one's own way can be an important intangible which reaffirms continued vitality and dignity.
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> . . . .
>
> The fact that rentals charged were to be applied in part to retirement of principal and interest incurred in acquiring or building the property in question does not dictate a denial of a charitable exemption if the facts otherwise support such an exemption, as they do here.[68]

III. LANDLORD-TENANT RELATIONSHIPS

Nonprofit housing organizations that accept federal housing subsidies either through direct subsidy or by admitting ten-

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67. *Rio Vista*, 277 N.W.2d at 191-92.

68. Franciscan Tertiary Province v. State Tax Comm'n, 566 S.W.2d 213, 225-26 (Mo. 1978).

ants who are the recipients of federal housing assistance must consider the impact such federal programs have had on traditional landlord-tenant law.[69] While eligibility for participation in federally-assisted housing programs is not equivalent to entitlement, expectations created by those programs can support due process claims that persons who meet the eligibility criteria for housing assistance are entitled to be considered for admission to subsidized housing on the basis of objective and ascertainable standards, such as waiting lists, consideration only of eligible applicants, and personal review of individual applicants rather than blanket rejection of categories of applicants such as persons receiving public assistance, etc.[70] These requirements do not mean, however, that a nonprofit housing organization must accept any eligible applicant who applies. Business judgment may be used to reject eligible applicants who would not be "responsible" tenants.[71] While private landlords generally do not have to give rejected applicants formal or informal hearings, or even reasons for the rejection, landlords who accept housing subsidies that are tied to buildings and who participate in the Section 8 certificate or housing voucher programs must give rejected applicants such protections.[72]

A. *Good Cause Requirement for Eviction*

Courts have recognized a "constitutionally protected expectation" of tenants remaining in their housing which requires owners of governmentally-assisted housing to take certain procedural steps before evicting tenants.[73]

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69. The discussion of admission and eviction procedures, *infra* notes 70-83 and accompanying text, is drawn from P. SALSICH, MISSOURI LANDLORD-TENANT RELATIONSHIP 141-45 (1988).

70. *Id.* at 141 & n.1 (citing Holmes v. New York City Hous. Auth., 398 F.2d 262 (2d Cir. 1968); Colon v. Tompkins Square Neighbors, Inc., 294 F. Supp. 134, 139 (S.D.N.Y. 1968); Baker v. Cincinnati Metro. Hous. Auth., 490 F. Supp. 520 (S.D. Ohio 1980)).

71. *Id.* at 141 & n.2 (citing Hill v. Group Three Hous. Dev. Corp., 799 F.2d 385 (8th Cir. 1986)).

72. *Id.* at 141 & n.3 (citing Williams, *The Future of Tenants' Rights in Assisted Housing under a Reagan Voucher Plan: An Analysis of Section 8 Existing Housing Cases*, 23 URB. L. ANN. 3, 35-36 (1982)).

73. *Id.* at 142 & n.1 (citing, Thorpe v. Housing Auth. of Durham, 386 U.S. 670 (1967) (public housing); Escalera v. New York City Hous. Auth., 425 F.2d 853 (2d Cir.), *cert. denied*, 400 U.S. 853 (1970) (public housing); Swann v. Gastonia Hous. Auth., 675 F.2d 1342 (4th Cir. 1982) (Section 8 existing housing (citing Joy v. Daniels, 479 F.2d 1236 (4th Cir. 1973) (221(d)(3)—rent supplement housing))).

While public housing tenants are entitled to fairly formal due process hearings prior to eviction,[74] tenants in privately-owned, federally-assisted housing generally are not entitled to pre-eviction hearings so long as the state landlord-tenant law will provide the tenants with a due process-type hearing.[75]

Perhaps the most important change in landlord-tenant relationships that has developed as a result of the federal housing programs, and the one that is most likely to influence state landlord-tenant law, is the requirement that public housing landlords and governmentally-assisted private landlords must show "good cause" before terminating or declining to renew a tenancy.[76] The good cause requirement originated in the procedural due process cases discussed above,[77] but has now been legislatively imposed.[78]

Under applicable federal statutes, public housing landlords and private landlords of governmentally-assisted housing may not terminate tenancies except for "serious or repeated violation of the terms and conditions of the lease, for violation of applicable federal, state, or local law, or for other good cause."[79] Regulations[80] and at least one judicial decision[81] extend the good cause limitation to nonrenewals of assisted leases.

While "other good cause" is not defined in the federal housing statutes, HUD regulations list as examples of good cause disturbance of neighbors, destruction or damage of

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74. *Id.* at 143 & n.5 (citing 24 C.F.R. § 866.58 (1983); Housing Auth. v. Caulder, 433 F.2d 998 (4th Cir. 1970), *cert. denied*, 401 U.S. 1003 (1971); Escalera v. New York City Hous. Auth., 425 F.2d 853 (2d Cir.), *cert. denied*, 400 U.S. 853 (1970)).

75. *Id.* at 143 & n.6 (citing Joy v. Daniels, 479 F.2d 1236 (4th Cir. 1973) (preeviction hearing unnecessary so long as tenant receives a full judicial hearing at some point)). *See generally* Williams, *supra* note 72, at 46-47.

76. The "good cause" requirement is not limited to governmentally-assisted housing programs, but may also be a component of state regulations of the marketplace such as rent control or condominium conversion legislation. *See, e.g.*, N.J. STAT. ANN. § 2A:18-61.1 (West 1987) (upheld against constitutional impairment of contract and takings challenges in Troy Ltd. v. Renna, 727 F.2d 287 (3d Cir. 1984)). *See generally*, D. MANDELKER ET AL., *supra* note 40, at 241.

77. *See* cases cited *supra* note 73.

78. 42 U.S.C.A. § 1437d(1)(4) (West Supp. 1988) (public housing); *id.* § 1437f(d)(1)(B)(ii) (West Supp. 1988) (Section 8 housing).

79. *Id.*

80. P. SALSICH, *supra* note 69, at 145 & n.5 (citing, 24 C.F.R. § 882.215 (1983)). *See generally* Williams, *supra* note 72, at 51-52; Cooper, *Section 8 Existing Housing Evictions*, 27 WASH. U.J. URB. & CONTEMP. L. 417, 420-22 (1984).

81. Mitchell v. HUD, 569 F. Supp. 701 (N.D. Cal. 1983).

property, violent criminal activity, and withdrawal of a unit from the assisted housing program.[82] Not all violations of lease covenants will justify a good cause eviction, however. Violations of "minor" covenants, such as "no pet" clauses, have been held not to be good cause justifying termination of the lease.[83]

B. *Policy Considerations for Nonprofit Organizations*

The good cause requirement for termination of a tenant's right to possession that has been imposed on private landlords who have accepted federal and state housing subsidies underscores the special role that nonprofit housing organizations play when they assume the guise of landlord. There are two related aspects of a nonprofit organization's role as a housing developer and manager that create an important difference in that role from the role played by traditional private housing developers and managers: 1) the potential conflict between the need to run an efficient real estate business and the desire to provide social services along with the possessory right to a unit of physical space; 2) the potential conflict between a "hands-on" approach to low-income persons that seeks to use the provision of decent housing as a means of helping low-income tenants achieve "self-sufficiency" and a "hands-off" approach that offers housing in a "caretaker" fashion with no particular expectation that families who are selected as tenants will be able to rise to an economic level that will enable them to pay market prices for housing.

1. "Hard/Soft" Management Dichotomy

With respect to the potential business/services conflict, nonprofit landlords may find themselves pulled in two directions. Contractual and moral obligations to benefactors, lenders and government grantors require nonprofit landlords to operate their housing units as real estate businesses, collecting rents when due, keeping expenses under control, and enforcing rules and regulations regarding tenant conduct.

At the same time, the nonprofit mission that is "charitable" in nature—that impels nonprofits to become involved in housing as a contribution to social welfare—encourages nonprofits to play down the business aspects of the landlord-tenant relationship in favor of a more personalized approach in which the occupants of nonprofit housing are seen more as clients to

82. 24 C.F.R. § 882.215(c)(2) (1987).
83. Housing Auth. v. Rovig, 676 S.W.2d 314 (Mo. Ct. App. 1984).

be helped rather than as tenants. This inclination gives rise to the desire to provide various services along with housing such as counseling, day care, and employment referral, all of which can be quite costly, and the temptation to wink at non-payment of rent, particularly if the tenant has a good reason such as a job layoff or unexpected medical bills—an attitude which, if unchecked, can be fatal to the housing venture.

The inherent conflict between the "hard" management concern for rent collection and the "soft" management concern for tenant services may become even more troublesome if the nonprofit organization enters into a joint venture with a profit-motivated developer or into a limited partnership with private individuals as a means of raising equity capital.[84] The professionals who come into the joint venture and the investors who join the partnership will have their own agendas that are likely to emphasize "hard" rather than "soft" management concerns.

Managing the conflict between the "hard" and "soft" management forces is one of the most significant challenges facing nonprofit housing organizations. Rents must be collected on time from all tenants or the morale of the paying tenants will suffer and sooner or later the project will fail. At the same time, it is inevitable that a higher percentage of low-income tenants will have difficulty in paying rent, no matter how well intentioned they may be, because the marginal economic position they occupy leaves little breathing room for unexpectedly high utility bills, sudden medical expenses or an unanticipated lay-off.

2. Effect of Rental Subsidies

One of the significant improvements in the federal housing subsidy programs was the decision to tie tenant rent obligations to a percentage of income (originally 25 percent, later raised to 30 percent by 42 U.S.C.A. § 1437a(a)) when the Section 8 housing program, 42 U.S.C.A. § 1437f, was enacted in 1974. This provision gives tenants of Section 8 housing the security of knowing that they will not have to pay more than a fixed percentage of their income for rent, no matter how low their income may be. Since tenants pay their own utility costs under Section 8 and those payments are credited against their

84. *See* Stearns, *The Low-Income Housing Tax Credit: A Poor Solution to the Housing Crisis*, 6 YALE L. & POL'Y REV. 203, 218-223 (1988) for a discussion of the difficulties nonprofits can experience when attempting to use the syndication method of raising equity capital for housing development.

rental obligations, it is not uncommon for tenants with minimum-wage jobs or little or no income other than state or federal public assistance to pay nothing for rent. Their utility payments often exhaust the 30 percent of income limitation for rental payments.

Landlords derive a benefit from the 30 percent of income rental limitation also. Because tenants do not have to pay a fixed amount for rent that could amount to 50, 60 or even 70 percent of monthly income and thus necessitate cruel choices between shelter and food or shelter and clothing, landlords have a more realistic ability to insist that tenants pay whatever their 30 percent figure may be. A nonprofit landlord, then, can take a business-like approach to rent collection from Section 8 tenants without developing a guilty conscience on the basis that forcing a low-income person to pay rent will require that person to go hungry. In addition to being a vital element in the success of a housing development, a business-like rent collection policy can have a salutary effect on tenant morale. Tenants will feel better about themselves, knowing that they are paying what they can afford to pay without having to sacrifice food or other necessities to do so. The Ecumenical Housing Production Corporation (EHPC) of St. Louis has maintained near 100 percent rent collection for several years with such a rent collection policy, even though the average income of its tenant families is barely $7000 per year.[85]

Of course, landlords and tenants who are not able to obtain Section 8 subsidies or some other type of rental assistance may not be able to develop quite the same relationship regarding rental payments. Likewise, other limitations in the Section 8 program may undermine its effectiveness. But the policy of limiting the amount of rent charged tenants to some percentage of income that is perceived to be affordable offers a way for nonprofit housing organizations to reconcile their concerns about not being too hard on tenants who have little or no money with the necessity of insisting that the agreed rent be paid in exchange for the housing services being provided.[86]

85. ECUMENICAL HOUSING PRODUCTION CORP., ANNUAL REPORT (1987).

86. The housing voucher program that has been pushed by the Reagan/Bush administrations as a substitute for the Section 8 program contains a potential problem for nonprofit organizations in that rents that may be charged to recipients of vouchers and the percentage of income payable as rent by recipients are not regulated. 42 U.S.C.A. § 1437f(o)(1)-(2) (West Supp. 1988). If tenants agree to pay rents that consume a higher percentage of their incomes, will they be able to afford these rents and still eat? Will nonprofits be able to maintain a business-like rent collection policy

C. *Tenant Services*

In addition to rent collection issues, nonprofit housing providers face a second potential conflict between the business/service points of view on the question whether services other than shelter should be provided. Should a nonprofit housing organization offer day care services to tenants who work? Should employment referral services be available to tenants who are looking for work? What about family counseling, recreational programs for children or adult day care for elderly? If a nonprofit housing organization answers yes to these types of questions, which it may well do because it views inadequate housing as a symptom of other social and economic problems,[87] how will it pay for these services? Should "housing" as a concept be broadened to include the cost of such services as "expenses of operation" payable out of rents, which would really mean out of rental subsidies that may be available from public or private sources?

These questions cannot really be answered without inquiring about the reasons for nonprofit involvement in housing. The reasons for getting involved may be as numerous as the types of nonprofit organizations in existence,[88] but most nonprofits probably would include in an answer to such questions some reference to wanting to do things a little differently, or seeking to provide more than a roof and four walls, or desiring to help a particular class of people improve their lot in life.[89] The interpretations that courts and the Internal Revenue Ser-

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if such difficulties arise? *See generally* C. DAYE, D. MANDELKER ET AL., *supra* note 40, at 145-52.

87. A recent example of a nonprofit organization's way of thinking occurred in St. Louis when Catholic Charities, Inc., a not-for-profit corporation organized by the Archdiocese of St. Louis to carry out social welfare programs, announced it would no longer manage a public housing development in St. Louis for the St. Louis Housing Authority. In discussing the decision to end its management of a public housing complex of over 1,100 units after less than two years, officials were quoted as saying their intention in entering into the management contract was not to maintain the status quo but instead to provide quality renovations and social services to the tenants. *Charities Ends Management of Blumeyer*, St. Louis Review, Mar. 10, 1989, at 1, col. 1.

88. *See supra* notes 12-30 and accompanying text.

89. For example, Habitat for Humanity describes itself as "not a give-away program, but a joint venture where those who benefit from the housing ministry are involved at various levels in the work." R. STEVENS & T. SWISHER, *supra* note 27, at 7. The mission of the Ecumenical Housing Production Corporation in St. Louis includes encouragement and support for "tenants' efforts to become self sufficient." ECUMENICAL HOUSING PRODUCTION CORP., *supra* note 85. The Urban Homesteading Assistance

vice have given to charitable purposes exemption provisions of state and federal tax laws suggest that it may be necessary to answer at least some questions about social services in the affirmative to support a charitable purposes exemption for nonprofit housing activities.[90]

D. *Nonprofit Housing Goals*

Aside from the question of who pays for such services since low-income tenants are not going to be able to afford to pay through higher rents, answering the question whether social services should be included as part of the housing package offered by a nonprofit organization requires the nonprofit to face the issue of what it wants to accomplish through its housing efforts. Is it motivated by a desire to help low-income persons become "self-sufficient"? Instead of self-sufficiency, will it be satisfied with a program that offers low-income persons "self-determination" of the question of becoming self-sufficient? Or does it not wish to become involved in low-income persons' growth or lack of growth as individuals, and seeks merely to provide decent housing for persons who have little apparent ambition or drive to remove themselves from a life of dependency?

Nonprofit housing organizations who seek to accomplish social goals such as self-sufficiency for low-income families or integrated living environments through choice of residency by the development and management of housing for low-income persons are likely to face a potentially serious conflict in their relationships with their tenants. What should be done about a tenant who meets her rental obligations on time, observes the living arrangement regulations, and keeps to herself but does not make "adequate progress" toward self-sufficiency? She may have signed up for an education course at a nearby school, but fails to attend classes. Or she may have lost a job that the nonprofit's social services director arranged for her because of repeated absences. Should that person be evicted from her apartment or house so that the scarce housing resources of the nonprofit can be offered to someone who is more likely to progress towards, and eventually reach, self-sufficiency? What should be done if the persons who apply for rental units offered by a nonprofit are predominately of one race, creed or color? Would a goal of achieving an integrated housing envi-

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Board in New York City stresses "self help and sweat equity." URBAN HOMESTEADING ASSISTANCE BOARD, *supra* note 25, at 13.

90. *See supra* notes 36-68 and accompanying text.

ronment justify a nonprofit housing organization faced with such a situation making a decision to withhold some of its units from the market until acceptable tenants of other races, creeds or colors were located?[91]

A demonstration program supported by the Department of Housing and Urban Development (HUD), called Project Self-Sufficiency, has spurred interest in efforts to link housing with other types of social services. In May of 1984, HUD announced the availability of Community Development Block Grant funds and additional Section 8 existing housing certificates to help Project Self-Sufficiency, designed to encourage local governments to develop programs to enable unemployed and underemployed very low-income (50 percent of median income or less) single parents with young children to become economically self-sufficient through the cooperative efforts of the public and private sectors. A special feature of the demonstration was the use of Personal Needs Assessments and Individual Action Plans for participating individuals. These assessments and plans, designed to be developed with the active participation of the participants, detailed the resources and services to be made available to the participants (e.g., day care, adult education, job training, etc.) as well as the responsibilities of the participants (e.g., attend adult education classes, seek employment through job training and referral programs, participate in counseling and personal development training activities, etc.).[92]

One of the pilots for the demonstration program, operated by the nonprofit agency, Warren Village, in Denver has been offering transitional housing for up to 18 months to single parents over 18 with no more than four children, all of whom must be under 12 at the time of admission. Applicants must be "willing to set and work toward tangible, personal and career goals," a provision which is incorporated into leases for the housing units in Warren Village.[93] Early reports based on

91. For a discussion of the legal questions raised by affirmative action programs such as "integration maintenance" rental policies, see United States v. Starrett City Assoc., 840 F.2d 1096 (2d Cir.), *cert. denied*, 109 S. Ct. 376 (1988) (occupancy quotas designed to prevent "tipping" held violative of the Federal Fair Housing Act). *See also* South Suburban Hous. Center v. Greater South Suburban Bd. of Realtors, 713 F. Supp. 1068 (N.D. Ill. 1988) (affirmative marketing techniques seeking to attract home buyers based on race do not violate Fair Housing Act). *See generally* J. KUSHNER, FAIR HOUSING, § 7.18 (1983 & Supp. 1988).

92. Department of Housing and Urban Development, Notice of Fund Availability and Solicitation of Proposals for Project Self-Sufficiency, 49 Fed. Reg. 21,433 (1984).

93. WARREN VILLAGE, INTRODUCTION TO WARREN VILLAGE (Denver, CO

Warren Village's experience prior to HUD's decision to establish the demonstration program indicated significant success in reaching self-sufficiency, as measured by employment rates (increasing from 47 percent upon entry to 94 percent within two years after leaving) and reduction in welfare assistance (dropping from 65 percent to 6 percent within the same time period).[94]

During the first year of the demonstration program, HUD received over 220 proposals from communities and selected 78 communities for participation. Announcing a second year of funding, HUD stated that it was particularly interested in reaching the "hard to serve" single parents who were "motivated but have long-standing problems such as lack of adequate, basic education, long-term unemployment, and other special problems that severely limit their ability to become self-sufficient."[95]

The potential conflict between good cause eviction standards and failure of tenants to make satisfactory progress toward self-sufficiency was handled by stressing the need to screen carefully applicants for admission to Project Self-Sufficiency units to insure selection of persons "motivated to become self-sufficient,"[96] extension of individual demonstration programs to a maximum of 30 months to enable participants to complete adult basic education and training courses,[97] and a provision authorizing local task forces to drop a candidate "prior to the issuance of the Section 8 certificate" who "fails to actively participate" in activities specified in the mutually agreed upon Individual Action Plan. A policy for termination of participants must be established which must contain "reasonable and specific criteria for assessing . . . progress and participation."[98]

The Self-Sufficiency Demonstration Project is cited merely as an example of laudable efforts underway throughout the

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Mar. 1987); Lamm, *Village II Offers Crucial Support*, Denver Post, Apr. 9, 1985, at 1C.

94. Lamm, *supra* note 93.

95. Department of Housing and Urban Development, Fund Availability and Solicitation of Proposals for Project Self-Sufficiency, 50 Fed. Reg. 28,884, 28,885 (1985).

96. 49 Fed. Reg., *supra* note 92, at 21,433.

97. 50 Fed. Reg., *supra* note 95, at 28,886.

98. *Id.* The 1988 President's National Urban Policy Report cited Project Self Sufficiency as an example of efforts to provide low-income persons with "active roles in pursuit of self-sufficiency and shared responsibility for their environment." 16 Hous. & Dev. Rep. (BNA) 721-22 (1989).

United States by nonprofit organizations that have become involved in housing development and management efforts with broader goals than merely providing housing for persons who cannot afford market-rate housing. As previously noted, nonprofit housing organizations are using their housing skills to pursue goals of community revitalization, historic preservation, home ownership, integrated neighborhoods and family environments.[99]

These broader goals offer the strongest justification for public support of nonprofit housing activities, but also carry with them the seeds of potential landlord-tenant conflicts. Regardless of the motivation for involvement in housing, a nonprofit organization that chooses to develop and manage housing is undertaking a business that is subject to increasing regulation by federal and state governments. The non-discrimination in admissions and good-cause eviction provisions discussed above are examples of this reality. Nonprofits who fail to consider carefully the implications of their decision to enter the housing field and who fail to appreciate the potential conflicts that they may face do so at their peril.[100] As an old friend of the writer and veteran of religious organizations' efforts in housing once observed, "There are plenty of sharks in those waters."

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99. *See supra* notes 20-30 and accompanying text.

100. Conflicts in relationships are not necessarily confined to landlord-tenant matters involving tenant progress toward goals of self-sufficiency or self-determination promulgated by a nonprofit landlord. A particularly bitter conflict arose in St. Louis between a neighborhood development corporation legally separate from but organized by St. Louis University Medical Center along with several local medical facilities and residents of the area served by the corporation. The dispute was over the standards to be used in determining the extent of rehabilitation residents would be expected to complete. The corporation imposed strict standards of rehabilitation under a development plan designed to upgrade the neighborhood surrounding the medical center. Low- and moderate-income homeowners feared that they would lose their homes to the process of gentrification because they could not afford to comply with the corporation's standards. After more than three years of litigation and often-bitter negotiations, a settlement was reached in which the corporation agreed to drop its requirements for what residents believed were unnecessarily costly and "cosmetic" repairs and resident homeowners agreed to make basic repairs such as painting and tuckpointing. A threat of eminent domain which residents feared would cause their displacement from the neighborhood was removed by the settlement. Poor, *Homeowners in Tiffany Hail Settlement of Suit*, St. Louis Post-Dispatch, Nov. 10, 1987, at 4, col. B. For a discussion of the problem of displacement in conjunction with urban reinvestment, see Salsich, *Displacement and Urban Reinvestment: A Mount Laurel Perspective*, 53 U. CIN. L. REV. 333 (1984).

IV. Homeownership Alternatives

Homeownership has long been a cherished part of the American housing ideal. It is important not only because of the potential for accumulation of wealth or "equity" through monthly payments on a mortgage rather than monthly payments of rent, but also because of the deep psychological need for most Americans to "own" their home as a sign of control over their destinies.[101]

Nonprofit housing organizations have experimented with a number of models for offering homeownership to families of low and moderate income, with four approaches being the most prevalent: 1) sale of individual units with highly-leveraged financing; 2) sale through acceptance of sweat equity in lieu of cash, with or without additional subsidies; 3) organization of a housing cooperative; and 4) rental of detached single family homes with options to purchase.

A. *Sale of Individual Units with Highly-leveraged Financing*

In the nonprofit homeownership approach closest to the traditional model of single-family housing development, a nonprofit housing organization, either by itself or in joint venture with real estate developers,[102] constructs or rehabilitates single family homes, duplexes or townhouses for sale to qualified buyers.

An example of this approach that has gained national attention, the Nehemiah Project,[103] is being replicated in a

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101. Analysts have long believed that the ability of homeowners to take federal income tax deductions for real property taxes and interest on home mortgages, which survived the Tax Reform Act of 1986 and amendments in 1987 and 1988, I.R.C. §§ 163(a) & (h)(3), 164(a)(1), constitutes one of the most significant, if not the most significant, housing subsidy program in existence. A report by the Congressional Budget Office estimated that $38 billion will be foregone in fiscal 1989 because of these two provisions. When additional homeownership provisions in the tax code are included, the total estimate in foregone revenue increased to $53.6 billion. In contrast, direct spending programs to provide housing assistances to lower-income families amounted to approximately $16.3 billion in fiscal 1987. CONG. BUDGET OFFICE, CURRENT HOUSING PROBLEMS AND POSSIBLE FEDERAL RESPONSES 3-4 (1988).

See generally Hellmuth, *Homeowner Preferences*, in COMPREHENSIVE INCOME TAXATION 163 (J. Pechman ed. 1977); Note, *Federal Income Tax Discrimination Between Homeowners and Renters: A Proposed Solution*, 12 IND. L. REV. 583 (1979).

102. *See infra* notes 140-42 and accompanying text.

103. The Nehemiah Project is named after the Old Testament layman, Nehemiah, who rallied the Jews to rebuild the Temple of Jerusalem after its destruction during the Babylonian Captivity. *Neh.* 2:17-18; *see* Hull, *Building from the Bottom Up*, TIME, Feb. 9, 1987, at 22.

number of cities by nonprofit organizations formed by coalitions of churches and religious organizations. Extensive use is made of low or zero interest second mortgage loans from public funds funneled to cities through the Community Development Block Grant program[104] to reduce the monthly principal and interest payments homebuyers are required to make. A new federal housing program authorizes assistance to Nehemiah organizations of up to $15,000 per unit to enable nonprofit housing corporations to reduce the borrowing costs for purchasers of Nehemiah homes.[105] Assistance to homebuyers comes in the form of zero interest second mortgages up to the maximum $15,000 authorized.[106] Amortization payments are not required, but a Nehemiah second mortgage must be repaid if and when the purchaser resells the house, unless the Secretary of HUD approves a transfer without repayment of the second mortgage.[107]

An important limitation on the use of the Nehemiah concept to assist homeless persons is the fact that conceptual and financing arrangements are geared to families whose income is in the median income range, which in many areas approaches $30,000. By contrast, median incomes of renters, the group from which homeless persons are more likely to originate, were reported to be in the $15,000 range in 1986.[108]

B. *Sweat Equity Purchases*

Habitat for Humanity[109] is perhaps the best known practitioner of the "sweat equity" approach to homeownership. Prospective homeowners join volunteers organized by a local nonprofit Habitat[110] corporation to construct or rehabilitate housing units. Construction materials and supplies are donated where feasible, and work of the volunteers is supervised by experienced contractors and members of the building trades, who also may be volunteers. Local Habitat affiliates estimate that they can produce housing for approximately 50

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104. 42 U.S.C.A. § 5301 (West 1983 & Supp. 1989).

105. Nehemiah Housing Opportunity Grants, Pub. L. No. 100-242, Title VI, §§ 601-612, 101 Stat. 1951-56 (1988).

106. *Id.* § 604.

107. *Id.* § 606(e)(5).

108. NATIONAL HOUSING TASK FORCE, *supra* note 2, at 5.

109. *Supra* note 27 and accompanying text.

110. All local Habitat affiliates must be approved by Habitat for Humanity International, located in Americus, Ga. R. STEVENS & T. SWISHER, *supra* note 27, at 23-26, 73.

percent of the cost of comparable housing in their respective markets.[111]

A distinguishing feature of the Habitat sweat equity program is that the organization does not use traditional mortgage financing and does not participate in government supported housing subsidy programs. Houses are sold to selected families at cost through zero interest loans.[112] Other nonprofit sweat equity programs, such as the Urban Homestead Assistance Board in New York, have made extensive use of federal, state and local housing assistance programs.[113]

C. *Housing Cooperatives*

Housing cooperatives have been a feature of middle- and upper-income homeownership choices for years in selected parts of the country such as Chicago and New York.[114] Mortgage insurance for the financing of cooperative housing developments is available from the FHA programs.[115] The current push to offer homeownership opportunities for residents of public housing projects includes a program to permit the conversion of public housing apartment buildings into cooperatives.[116]

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111. For example, the St. Louis Habitat affiliate established a budget for its first five homes on the expectation that it could produce them for $35,000 per unit. To accomplish that goal, the organization was seeking "cash or materials or services equivalent to $140,000 to $175,000 in 1987." Annand, *Letter from the President*, ST. LOUIS HABITAT UPDATE, Apr. 1987, at 2.

112. Point Three of the Habitat Covenant, R. STEVENS & T. SWISHER, *supra* note 27, at 24.

113. URBAN HOMESTEADING ASSISTANCE BOARD, CURRENT PROGRAMS AND PROJECTS (1988); URBAN HOMESTEADING ASSISTANCE BOARD, TENTH YEAR REPORT AND RETROSPECTIVE (1985).

114. *See, e.g.*, NATIONAL CONFERENCE OF COMMISSIONERS ON UNIFORM STATE LAWS, UNIFORM COMMON INTEREST ACT prefatory note at 7-8 (1982); MODEL REAL ESTATE COOPERATIVE ACT Commissioners' prefatory note at 5-6 (1981); SUBCOMMITTEE ON HOUSING AND URBAN AFFAIRS, REAUTHORIZATION OF HOUSING AND COMMUNITY DEVELOPMENT PROGRAMS 362 (1987); Woodrow, *Co-operative Housing: A Proposal for Reform*, 41 U. TORONTO FAC. L. REV. 34 (1983).

115. 12 U.S.C.A. § 1715e (West 1980 & Supp. 1989).

116. *See, e.g.*, Shapiro, *A Conservative War On Poverty*, U.S. NEWS & WORLD REPORT, Feb. 27, 1989, at 20, 23.

The actual sale of public housing units to tenants is proving to be costly and difficult. A study by the Council of Large Public Housing Authorities (CLPHA) of a three year demonstration program begun in 1984 by HUD reported that less than 25% of the units originally proposed for sale had been sold, and many of these were scattered-site single family units which public housing agencies often find hard to maintain. Average income of purchases

Housing cooperatives can offer low-income persons an opportunity to gain some of the "control" benefits of home-ownership without requiring an assumption of the full financial risks of fee simple title. In a housing cooperative, the housing units actually are owned by a nonprofit housing cooperative which assumes the responsibilities for developing, financing and managing the housing. Low-income residents purchase a membership share in the cooperative corporation which entitles them to a vote in the management of the cooperative corporation and a long-term, proprietary lease in one of the housing units owned by the cooperative corporation. Recent amendments to the public housing statutes authorize HUD to assist local public housing authorities and tenant management corporations convert public housing units to tenant-controlled housing cooperatives.[117]

D. *Options to Purchase Single Family Rental Units*

A fourth approach to homeownership that may be considered by nonprofit housing organizations is the rental of housing units together with an option to purchase. A portion of the

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was reported to be slightly over $18,500 a year and prices usually were set at about 50 to 60% of appraised value to make the units affordable.

Under a separate program authorized in the Housing and Community Development Act of 1987, 42 U.S.C.A. §§ 1437r, 1437s, sales will be made to resident management corporations, who in turn will sell the units to tenants. According to Dr. Michael Stegman, professor and chairman of the Department of City and Regional Planning at the University of North Carolina, the possible prototype for future activity under the 1987 Act is the proposed sale of Carr Square, a 658-unit project in St. Louis, to the Carr Square residents management corporation for $1. The sale would be the second under the 1987 Act, with the first being the sale of the Kenilworth-Parkside project in Washington, D.C. The Carr Square resident management corporation will in turn syndicate the project to a limited partnership, which would make available low-income housing tax credits, I.R.C. § 42 (West Supp. 1989), to investors and use the tax credit investment proceeds (estimated at $11.5 million) along with $15 million from the Missouri Housing Development Corporation in the form of a 7.5% blended interest rate taxable bond/soft loan package and community development block grant funds to rehabilitate the units. Total rehabilitation costs are expected to be $32 million, which amounts to approximately $66,000 per unit for a scaled down development of 485 units. Under the proposal, the resident management corporation will manage the project as rental housing during the 15-year tax credit compliance period and then sell the units to interested tenants. While the current average income of Carr Square residents is $6,500, incomes in the $17,000 range will be needed to afford the purchase. Under the 1987 Act, if the sale goes through HUD will be required to replace all 658 units of public housing. *See* 42 U.S.C.A. § 1437s(a)(3)(A)(iv) (West Supp. 1988); 16 Hous. & Dev. Rep. 896-97 (BNA) (1989).

117. 42 U.S.C.A. § 1437s(a)(4)(B)(i) (West Supp. 1988).

rent is credited toward the required down payment. When a sufficient down payment has been accumulated, the tenant may exercise the option to purchase provided that adequate financing arrangements can be arranged for the balance of the purchase price.

The original Turnkey III model of public housing offered this option to public housing tenants, but was not successful primarily because potential ownership units for the most part were constructed as multi-family apartments and ownership possibilities did not contain effective mechanisms for creating cooperatives that could assume maintenance obligations for common areas. The condominium model was not suitable for public housing tenants in the 1970s.[118]

More recent attempts at homeownership in the public housing area attempt to blend a tenant services "self-sufficiency" model of rental housing with the development of tenant management corporations that can serve as vehicles for converting public housing units into tenant-controlled housing cooperatives.[119]

Nonprofit housing organizations that prefer to offer options to purchase housing units without a cooperative corporation intermediary may wish to consider renting single family houses or duplexes. In this way, the complexities of organizing maintenance responsibilities for common areas can be avoided. Options to purchase single family rental units would appear to be a natural end state for a "self-sufficiency" model of nonprofit housing.[120]

In considering homeownership alternatives, nonprofit housing organizations must be careful to avoid raising expectations to unrealistic levels, as well as restricting personal aspirations through paternalistic limitations on homeownership opportunities. To what extent, for example, is it feasible to expect a homeless family with only a minimum wage job to be

118. *See* 42 U.S.C.A. § 1437c(h) (West Supp. 1988); 24 C.F.R. Ch. IX, §§ 904.101-904.309 (1987). *See also* 42 U.S.C.A. §§ 1437r, 1437s (West Supp. 1988) (home-ownership possibilities for public housing through sale to tenant management corporations enacted in 1987).

Only 3000 units have been sold under the Turnkey III program since 1972, reportedly because of "bureaucracy and high costs," while 1.25 million units of publicly owned "council housing" have been sold in Great Britain since 1980 where admittedly a far greater percentage of all housing is publicly owned. Shapiro, *supra* note 116, at 23.

119. 42 U.S.C.A. §§ 1437r, 1437s.

120. One of the major findings of the CLPHA study of the HUD public housing sale demonstration was the high percentage of scattered site single family units that were sold to tenants. *See supra* note 116.

able to sustain the monthly mortgage and maintenance expense responsibilities of single family or condominium ownership, even with heavy subsidies? On the other hand, why cannot that same family be offered the opportunity to join a nonprofit housing cooperative or rent a single family house with an option to purchase exercisable if and when the family becomes "self-sufficient"?

V. SUGGESTIONS FOR NONPROFIT HOUSING ORGANIZATIONS

The charitable purpose of contributing to the social welfare of its community that drives a nonprofit organization is perhaps the most important reason for encouraging nonprofit involvement in low-income housing development and management. Nonprofit housing organizations can play an especially significant role in a renewed national effort to produce housing designed to enable persons who are homeless to leave the streets and shelters and to prevent other persons from being driven to those streets and shelters. For the promise of nonprofits to be fulfilled through housing developments that last for the useful life of the buildings constructed, however, nonprofits must learn to survive in a twice risky environment (i.e. the risks of the normal real estate market, as well as the risks of working with people who cannot afford to pay market prices for their housing). The following suggestions are offered as a means of confronting those risks.

A. *Small is "More Humane"*[121]

Because the homeless have become so visible and the need for decent, permanent housing for low-income persons is so great, nonprofits are understandably tempted to think big, to make an impact, and to measure their housing achievements by quantity of units added to their inventory.[122] This can prove to be a trap for nonprofit housing efforts as it has been for the

121. Interview with Dr. Peter Rossi, Professor of Sociology and Director of the Social and Demographic Research Institute of the University of Massachusetts, at Notre Dame Law School (Jan. 19, 1989). According to Dr. Rossi, nonprofit organizations tend to do a better job of providing shelter for homeless persons than do municipalities because nonprofits usually cannot afford to operate on a large scale, while municipalities tend to think in economies of scale terms and do everything "wholesale." The result, in Dr. Rossi's view, is that a shelter operated by a nonprofit organization tends to offer a cleaner, safer and more congenial environment.

122. For example, a nonprofit group, New Housing Ventures in Worcester, Massachusetts, completed 18 three-bedroom apartments for low-income families in nine two-story buildings on six scattered sites, then had difficulty finding suitable sites for larger, mixed-income projects which it

public housing program and the homeless shelter program in many cities.[123]

A sociologist who has studied the homeless population in urban areas advocates the use of small shelters operated by nonprofit organizations in lieu of massive, city-run shelters because "small is more humane."[124] The same can be said of permanent housing for low-income families. A small number of units on different sites scattered throughout a neighborhood is likely to create a more pleasant atmosphere for the occupants than is a large housing complex. The small development is also less likely to attract the shrill, almost mindless opposition to low-income housing so prevalent when developments of substantial size are proposed. Finally, small developments of "infill" housing on vacant lots or rehabilitation of individual multifamily buildings of 20 units or less often are not perceived to be economically feasible by profit-motivated developers.[125]

The dilemma faced by a nonprofit housing organization that creates the temptation to expand is that the costs of development of a small project are as great or greater than the large ones, and the small ones do not appear to make any impact on the overall need. Succumbing to the temptation to grow larger to "make a greater impact," however, can produce the "wholesale" or "warehouse" effect so severely criticized in municipal shelters[126] and a corresponding failure of the social welfare purpose for getting involved in low-income housing in the first place.[127]

B. *Define the Housing Mission Clearly*

As discussed previously,[128] there are many reasons why nonprofits become involved in housing activities. The value of the nonprofit housing effort lies in the fact that nonprofits are motivated by something other than producing housing units in order to make a profit. What that "something other" is,

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wished to build in order to "produce more units more quickly." Notebook, N.Y. Times, Sept. 11, 1988, at 30, col. 4.

123. *See supra* notes 14-16 and accompanying text.

124. Rossi, *supra* note 121.

125. Comment by William Whiteside, Executive Director, Neighborhood Reinvestment Corporation, 15 Hous. & Dev. Rep. 741 (BNA) (1988).

126. Controversy over the use of large barracks shelters has plagued the City of New York's efforts to respond to the homeless. Barbanel, *Reacting to Homelessness*, N.Y. Times, Dec. 17, 1988, at 32, col. 1.

127. *Supra* notes 29-30 and accompanying text.

128. *Supra* notes 12-30 and accompanying text.

though, must be fully discussed and clearly articulated at the outset of the venture.

There is true wisdom for nonprofit housing organizations in the Chinese proverb that "[a] journey of a thousand miles must begin with a single step."[129] The development of a successful nonprofit housing program is an evolutionary process that often begins with a discussion over breakfast or lunch among a few people sharing a common goal and is nurtured for weeks, months, and even years by that common goal as an organization is formed and plans are developed.

For example, are members of the nonprofit organization in agreement that the thrust of the nonprofit housing effort is to help low-income persons "control their own destiny"? That may mean, of course, that individuals who occupy the organization's housing may choose to live a different lifestyle from that chosen by the members of the organization's board of directors. Are members in agreement that achieving "self-sufficiency" is the goal of the housing effort? If so, will the necessary services be provided and steps be taken to create the supportive environment conducive to fostering self-help efforts? What will be done about persons who do not make "substantial progress" toward self-sufficiency, and what does "substantial progress" mean?

No general answers can be given to such questions, nor is a particular type of mission being advocated. The point is to confront the questions and answer them earlier rather than later.

C. *Long-term Commitment*

A serious problem has developed in the past few years with respect to federally-subsidized housing built in the 1960s and 1970s by private developers because obligations to retain those units at low-income rental levels are expiring. Most of the subsidy contracts developers received from the federal government under the Section 8 program were for 15 years,[130] and long-term, low interest rate mortgages obtained in conjunction with Section 8 and the old 221(d)(3) and 236 programs contain provisions allowing pre-payment of those mortgages after 20 years with a corresponding cancellation of regulatory agreements requiring the units to be rented to persons of low or

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129. Lao-tzu, in J. BARTLETT, BARTLETT'S FAMILIAR QUOTATIONS, 65:1 (1980).

130. 42 U.S.C.A. § 1437(e)(1) (1978), *repealed by* Pub. L. No. 98-181, Title II, § 209(a)(3) (1983).

moderate income.[131] Estimates of the number of low- and moderate-income apartments currently being subsidized that will be eligible for conversion to market rate units in the next decade range as high as 300,000, with the peak years likely to be 1991 to 1995.[132] If even a small portion of those units are withdrawn from the low-income housing market, a bad situation will become markedly worse.

When those apartments were built, 15 and 20 year commitments seemed like a long time. Today, in light of current low-income housing problems, it is clear that those commitments were far too short.

While from a housing policy standpoint, 15 and 20 year commitments to retain housing in a low-income rental status may be too short, it is difficult to argue with the private developers' point that they cannot be expected to retain housing at artificially low rentals after subsidies expire, and that 20 years is a reasonable time to expect profit-motivated individuals to restrict the profit-making potential of their property.

Recent history suggests that someone has to be ready to make a longer-term commitment to retaining affordable units for low-income persons. That someone, in an increasing number of instances, is likely to be a nonprofit organization. A commitment to low-income housing "in perpetuity"[133] may be

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131. 12 U.S.C.A. § 1713(c) (West 1980 & Supp. 1989); 24 C.F.R. Ch. II, § 221.524 (1988).

132. Gold, *States Working to Avert Evictions of Multitudes in Subsidized Housing*, N.Y. Times, Mar. 15, 1989, at 14, col. 3.

133. Whiteside, *supra* note 125. "In perpetuity" in the housing context should be defined as the expected useful life of the housing structures, which could be well over 50 years if the buildings were suitably constructed and properly maintained. The California low-income housing tax credit program requires recipients of state tax credits to operate projects as low-income housing for 30 years. To maintain the low-income feature for the full 30 years, an Oakland, California syndication, 1989 Oakland Housing Partnership, will invest as the limited partner in individual project partnerships in which managing general partners will be nonprofit corporations. Between the 12th and 15th years, the nonprofit sponsors will have the option to purchase properties for the lower of 1) the outstanding debt, plus $1 and the amount needed to pay investors' exit taxes, or 2) 90% of the prevailing fair market value of the property appraised as low-income housing. Hobby loss restrictions that deny deductions and credits for not-for-profit activities to individuals or S corporations, I.R.C. § 183, will not necessarily be violated by such "bargain sales" to nonprofit organizations, according to an Internal Revenue Service private letter ruling to the Local Initiatives Support Corporation (LISC), whose affiliate, National Equity Fund, is the nonprofit sponsor of more than $50 million in corporate investor commitments for over 30 projects across the country. 16 Hous. & Dev. Rep. 737-38 (BNA) (1989); 16 Hous. & Dev. Rep. 641-42 (BNA) (1988).

one of the most important roles for nonprofit housing organizations. Such a commitment is not to be taken lightly. It requires an organization that has enough stability to survive as long as the useful life of its housing units, as well as careful financial planning in advance of entering the market to establish an endowment fund that can enable housing units to be retained permanently in a low-income rental status. The experience of private educational institutions that engage in extensive fund raising efforts so that tuition payments are not required to meet all the institutional costs of delivering educational services offers a guide to what nonprofit housing organizations should be doing.

D. *Housing Focus*

The housing needs of low-income persons are as varied as the types of people who fall into that category. For example, at least four separate types of housing can be identified as necessary to serve the permanent housing needs of identifiable classes of homeless persons. Homeless families with children will most likely be best served by single family houses, townhouses and small apartment complexes. Traditional apartment developments can serve the housing needs of married couples or other small family groups with no children. Homeless single persons with no family contacts and no serious physical or mental disabilities will perhaps be best served by single-room housing (SROs), much of the existing stock of which has been lost to urban revitalization efforts.[134] Homeless persons with mental or physical disabilities can best be served by group homes and other forms of shared living arrangements in which individual privacy is preserved but food, counseling, treatment and other social services are provided on a regular basis.[135]

Nonprofit organizations entering the housing business are likely to have persons from all four groups on their doorsteps as soon as the existence of their housing activity becomes known. Organizational problems can be reduced considerably if conscious choices regarding the type of person to be served and the form of housing to be emphasized have been made.

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134. Note, *A Right to Shelter for the Homeless in New York State*, 61 N.Y.U. L. Rev. 272, 275 n.18 (1986) (reporting a loss of over 110,000 SROs in New York City since 1976).

135. *See* Rossi, *The Family, Welfare and Homelessness*, 4 Notre Dame J.L. Ethics & Pub. Pol'y 281 (1989).

See generally Salsich, *Group Homes, Shelters and Congregate Housing: Deinstitutionalization Policies and the NIMBY Syndrome*, 21 Real Prop., Prob. and Trust J. 413 (1986).

E. *Housing services*

It has become almost axiomatic that permanent housing for people in the homeless or near-homeless states will not succeed without a coordinated relationship with other services such as day care, education, employment, health care and social opportunities.[136] Findings that a state of chronic homelessness can result from experiences in homeless shelters that are not sufficiently well organized to provide necessary support services lend credence to the notion that permanent housing alone will not solve the problem of homelessness.[137]

Nonprofit housing organizations can ill afford to ignore the necessity of support systems, social opportunities and services. The need for social services may trigger the potential landlord-tenant conflicts discussed earlier.[138] The "hard" management side of the landlord personality may conclude that the organization cannot afford to provide social services; that it must concentrate on collecting rent, maintaining the property, and paying off the debt. The "soft" management side of the nonprofit personality may believe that management resources should be concentrated in the services area. If those two personalities clash in the daily decisions an individual property manager must make, the stress and tension can become intolerable. "Burnout," staff turnover, board resignations and project failures can occur if that conflict is not recognized and reconciled.

Two approaches to resolving the "hard/soft" management conflict suggest themselves: 1) contractual arrangements with social services providers to bring necessary services to the housing development on a regular basis;[139] 2) providing a support staff and corresponding budget as part of the housing program. The support staff would not be the property manager "landlord," but instead would be someone whose role would be to provide counseling and assistance to tenants.

Again, one particular approach is not necessarily better than another. What is essential is to recognize the need for tenant support services and to plan and budget for such services from the beginning of the venture.

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136. *See, e.g.*, Wolch, Dear, and Akita, *supra* note 2, at 451 (discussing the "service hub" concept, a collection of housing, service and social opportunities to serve the poor and homeless in a coordinated way).

137. *Id.*

138. *Supra* notes 87-100 and accompanying text.

139. The "service hub" concept is an example of this approach. Wolch, Dear, and Akita, *supra* note 126, at 451.

F. *Cooperation With Private Developers*

Housing development and management is a complicated process that requires sophisticated skills in construction, finance, and marketing, as well as budgeting and accounting, planning, governmental operations, land use regulation, property law and taxation. Services from professionals such as accountants, architects and attorneys often can be obtained by in-kind donations. Technical assistance may be available from local or national umbrella organizations established to provide such assistance.[140]

Rather than "go it alone," nonprofit housing organizations may find it to their advantage to negotiate an agreement for a joint venture with one or more experienced, profit-motivated developers. If members of a nonprofit organization can work through the fears and suspicions about private developers' motives that often plague low-income neighborhoods, they may be able to speed the process of providing housing to their constituency by a joint venture approach.

A model for such an approach that has been used with considerable recent success has been developed in St. Louis, Mo. A nonprofit organization formed by a number of neighborhood associations, the St. Louis Association of Community Organizations, has entered into a series of agreements with an experienced private developer, Charles F. Vatterott and Co., to develop both rental and purchase housing for persons of low or moderate income. Under the agreements, a separate corporation is formed by the two organizations with an equal number of directors from each organization. This separate corporation holds legal title to the property and is the vehicle through which the housing is developed. Responsibilities and tasks are divided between the nonprofit and the developer according to their respective skills and interests. For example, the nonprofit is primarily responsible for marketing surveys, negotiations with governmental officials and lending institutions, and tenant/purchaser screening and selection. The developer is responsible for site acquisition, and housing design and construction. Actual decisions on development matters such as site selection, housing design and borrowing of money are made through the joint venture corporation and at least one director from each organization must favor a decision before it can be made. Both the nonprofit and the developer are paid fees for their respective services.[141] While the tax conse-

140. Kirkpatrick, Dillon & Bloch, *supra* note 17, at 1229.

141. St. Louis Ass'n of Community Organizations and Charles F.

quences of such arrangements must be considered carefully by participating nonprofit organizations,[142] the advantage to such an approach is that the skills of both organizations can be maximized in the housing effort.

G. *Involvement in the Community*

One of the most substantial barriers to low-income housing is the fear and resulting opposition that inevitably surfaces when such housing is considered for any area but the most distressed neighborhood. Some of the most celebrated examples of housing litigation stemmed from community opposition and took years to resolve, during which time little or no housing was being produced.[143]

Nonprofit organizations that have a strong community base and which are sensitive to the concerns of resident property owners can play a critical role in gaining neighborhood acceptance of low-income housing. Acceptance is unlikely to be gained, however, unless the twin concerns of potential decline in property values (resident property owners) and possible displacement through gentrification (low-income persons) are met. A nonprofit organization that has a stable and visible presence in the community is in a good position to allay both fears, particularly if it has a clearly defined housing mission that demonstrates sensitivity to both concerns. Experience demonstrates that the task of gaining community acceptance is one of the most difficult aspects of low-income housing, but is also one that community-based nonprofit organizations are best equipped to handle.

CONCLUSION

Nonprofit organizations have much to contribute to efforts to resolve the housing crises of homeless persons. Perhaps the

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Vatterott and Co., Joint Venture Agreement Form (1985) (on file with the author).

142. *Supra* notes 31-62 and accompanying text.

143. *See, e.g.*, Hills v. Gautreaux, 425 U.S. 284 (1976); Huntington Branch, NAACP v. Town of Huntington, 844 F.2d 926 (2d Cir.), *aff'd*, 109 S. Ct. 276, (1988), *reh'g denied* 109 S. Ct. 824 (1989); Park View Heights Corp. v. City of Black Jack, 605 F.2d 1033 (8th Cir. 1979), *cert. denied*, 445 U.S. 905 (1980) (settled after 10 years of litigation); Metropolitan Hous. Dev. Corp. v. Village of Arlington Heights, 558 F.2d 1283 (7th Cir. 1977), *cert. denied*, 434 U.S. 1025 (1978); Metropolitan Hous. Dev. Corp. v. Village of Arlington Heights (Arlington Heights II), 469 F. Supp. 836 (N.D. Ill. 1979), *aff'd*, 616 F.2d 1006 (7th Cir. 1980) (settled by consent decree after eight years of litigation). *See also* C. DAYE, D. MANDELKER ET AL., *supra* note 40, at 415.

most significant aspect of their potential lies in the fact that nonprofits are by nature disposed to accept the fact that homeless persons do not have the resources to obtain market rate housing. If they did, they would not be residents of the shelters and streets of American cities. As a result, nonprofits are more attuned to "non-market" ways of doing business, such as tenant "self-sufficiency" programs, housing cooperatives, group homes and sweat equity ventures.

Nonprofits should be encouraged to increase their housing activities, not as competitors for the market-rate housing dollar, but as providers of housing for persons who have no realistic alternatives in the marketplace. A possible model for future study is the role that religious and other nonprofit organizations have played in education. Well-organized programs with clearly articulated goals have been successful in delivering a valuable service at a reasonable price and have been able to raise millions of dollars from generous benefactors in the process. Can nonprofit housing organizations be no less successful?