Safe Harbor Residents Association, Inc

Business Plan

September 20, 2012

Andrew H. Danforth, CPA CSSBB
Housing Program Manager
The Cooperative Development Institute

Introduction:

Safe Harbor (“the community”) is a community of 100 homes that was built in Bayou La Batre, Alabama to house families whose homes had been left uninhabitable by Hurricane Katrina. The development was built with $15.7 million from the Federal Emergency Management Agency (FEMA) with a much smaller contribution for infrastructure coming from the Department of Housing and Urban Development (HUD). The community is managed by a municipal instrumentality, the Bayou La Batre Housing Authority, which was established by the FEMA grant to manage Safe Harbor and holds no other assets.

Current Financial Status:

In short, Housing Authority is losing money at an unsustainable rate and cannot continue as is without immediate action, which, under current management may include increasing rents or decreasing services-or both.

The community, in the 11 months ending June, 2012, lost about $ 105,000 (equal to an annualized rate of $ 112,000) on rental income of $ 303,000, meaning it is spending about 33% more than its revenue. This loss is due to two major budget variances: (1) a shortfall $ 71,000 in rental income, due to a collections rate of only 81%; and (2) Repair overages of $ 32K, which are 50+% over budget.

It should be noted that the budget included a 5% rent loss, so in reality rent collections are approximately 75% of those available and 25% is going uncollected. In comparable private rental real estate, current rent losses are around 7% and might be lower in a situation of lower rent, newer homes. The Housing authority’s rent loss is 3-5 times that which would generally be expected in the private sector.

The costs of running the community are also very high by private standards. The community has salaries of about $ 130,000, equal to about 40% of collections, 4 times what one would expect privately. Its legal costs, at the current clip of $ 34,000 are 8-10 those that might be expected. Its insurance is approximately 40% more than a recent quote. Repairs, at about $90,000, seem high for a community of its size and age. Other costs, such as office rent, utilities and supplies, would be much less or non-existent in an appropriate private setting.

About Housing Cooperatives

America has a rich history of cooperatives, its first cooperative being organized by Benjamin Franklin in 1760. Our nation is full of hundreds of diverse cooperatives in agriculture, fisheries, finance (credit unions and insurance companies), mercantile and housing. Many cooperatives are household names- a few examples being Ace Hardware, Ocean Spray, Nationwide Insurance, and the Associated Press. Much of rural America was electrified, and still is, by electric coops.

The first housing cooperatives in the United States was founded in the early 1800s and there are currently over 1.3 million American families in some form of cooperative housing. Specific to Manufactured Housing, there are about 600 cooperatives nationwide. A national non-profit, ROC USA, uses a 28 year old system which integrates technical assistance and oversight to resident cooperatives, and none of their communities have ever failed, or even defaulted upon a mortgage loan. The Cooperative Development Institute utilizes this system for all the communities it converts or consults with.

Cooperative is cost and life style effective and because it is owner occupied, owner maintained housing. The community exists for the members. The members decide upon all major issues, such as community rules, the level (and cost) of services provided to them, and the basis for new members joining. By utilizing professional contractors to handle specific services, such as financial management, legal affairs, repairs that the cooperative cannot handle, and taking on other tasks with volunteers, the members can manage as well and often better than those communities run privately. Since the profit margin is removed, rents in cooperatives will show marked savings over those in market-rate communities, and over time this becomes staggering.

Cooperative members own a share in a corporation that owns or controls the building(s) and/or property in which they live. Each shareholder is entitled to occupy a specific unit and has a vote in the corporation. Every month, shareholders pay an amount that covers their proportionate share of the expense of operating the entire cooperative, which typically includes underlying mortgage payments, property taxes, management, maintenance, insurance, utilities, and contributions to reserve funds. There are many benefits to cooperative ownership. Some of these include personal income tax deductions, lower turnover rates, lower real estate tax assessments, reduced maintenance costs, resident participation and control, and being able to prevent absentee and investor ownership.

Housing cooperatives come in many shapes and sizes: cooperatives include townhouses, garden apartments, mid-and high-rise apartments, single-family homes, student housing, senior housing, and mobile home parks. The purchase price of cooperative membership can be left to the market or the price can be maintained at below market in order to preserve affordability. All cooperatives share a common set of principles adopted by the International Cooperative Alliance.

The key aspect in any cooperative is democratic control by the members in order to achieve an agreed upon common objective. Democratic control is typically accomplished through governance by volunteer boards of directors elected from the entire membership. In addition to the board, co-ops often have many committees, such as a membership committee, maintenance committee, activities committee, and newsletter committee. Most co-ops hire a manager or management company to perform management functions and maintained.

Cooperatives are not charities and receive, overall, very little governmental subsidization. In fact, many of them lessen the burdens of government by providing quality affordable housing, and this in particular would be true of a resident's cooperative at Safe Harbor.

A Cooperative for Safe Harbor

Given the current financial issues with the community, as well as the issues of its founding and the current level of politics surrounding the community, it makes sense that the City move towards the privatization of the Safe Harbor community, and it makes perfect sense for residents to assume control of the their homes through collective democratic ownership and to relieve local state and federal governments of its financial issues going forward.

Toward this end, the Residents are working to incorporate a non-profit to own and operate the community. Safe Harbor Residents Association, Inc will be a non-profit corporation, with members, formed under Section 10A-1-3.05 and 10A-3-3.02 of the 1975 Code of Alabama. (It should be noted that Alabama does not have a housing cooperative form of corporation, hence the use of a member controlled non-profit.) In recognition of the public sources of funding that brought about the community, in its Articles of Incorporation will be the stipulation that no gain can be made on the dissolution of the corporation or the sale of the community. Any such proceeds would have to be given to a third party public charity or to a governmental entity.

By forming the corporation the residents protect themselves. The officers and directors, as well as the members, are legally shielded from any legal or financial issue of the cooperative.

It is envisioned that the community would be a low-equity cooperative, which is one that has a minimum buy-in or membership fee (Such as a single payment of $100 to $ 1,000), but which the residents accrue little or no further value for ownership. This removes all market based purchase price gyrations and results in a community focused upon long term tenancy with perpetual affordability, a quality of life shared by all. The focus of the community will be to serve the lower income segments of the population and those that still feel the effects of Katrina.

The Cooperative Development Institute, a non-profit cooperative developer, as well as the Federation of Southern Cooperatives, have pledged their long term support and stand to help the community to purchase and run the community for many years to come. Long Term Technical assistance has proven a steadying force to resident cooperatives, providing structure, leadership and training to an ever evolving population. In addition to that support, these entities can provide initial capital financing and working capital and serve to assist with grant funding where needed.

Pro-forma Financial Plan

The financial plan, attached, looks at the current levels of expenses and proposed levels of expenses under two different scenarios- one where the community owns the homes and one where the community owns only the land and provides only the land and infrastructure to resident homeowners. This pro-forma is a reasonable starting point but actual costs can only be established when we know the community can be assumed by a resident's cooperative.

The costs were compiled using current cost data in other communities of the size, bids or estimates and the knowledge of the writer. Significant assumptions are:

1. Replacement of current management with a third-party property management company that manages multiple communities or properties will be most cost effective.= due to the staring of services, personnel and systems. The cost for this can vary, in other areas of the country we see this as low as $ 20 per unit per month. We have budgeted this at $ 40 per unit month to be conservative.

2. We have budgeted $ 10,000 in legal fees, which is 2-3 times what we would in other communities. Again, to be conservative.

3. We have budgeted insurance based upon the estimation of a commercial insurance broker.

4. We have kept the current level of maintainance expenses, utilities and pest control since we have not reviewed the actual expenditures, but feel these are probably high.

5. We have corrected amounts for accounting, office expenses.

6. We have added a line for replacement reserve. This should be calculated after an engineer's assessment, but common estimates are shown.

Overall, the costs of resident ownership of the community come to $ 187-$254 per unit depending upon method of ownership. These are initial estimates and must be finalized through actual contracts; in addition a provision for resent loss must be established. However, in any event the final figure will be significantly less than the current cost of operating the community. Many older communities operate at a quarter or less of equivalent market rents.

Next Steps

The next steps for the community are forming the non-profit corporation, gaining membership and continued formalization of costs, while a settlement that results in the resident ownership is negotiated. A critical mass of membership shows to all the support of the residents for this plan.

Conclusion

The current financial with Safe Harbor is unstable, untenable and must change. It will change in one way shape or form, forced by its dire financial condition. No entity can continue to so badly under collect its income, overspend on expenses, and continue to draw down its reserves. Something has to give. If the current situation continues, the Housing Authority would be forced to again increase rents, which increase the writer believes would initially be in the range of $ 125-150 per month.

The collected taxpayers of the United States paid for the community to be established, and they as well as the residents deserve a community that is successful in meeting its goal of quality, affordable housing. We very much believe that government is not the most appropriate manager of these communities, that the private sector and the very people that live in the community are better suited, with appropriate vendors, to determine their own costs and own definition of quality housing.

About CDI

Cooperative Development Institute (CDI) is a 501c3 non-profit based in Shelburne Falls, Ma. It was formed in 1994 by a group of cooperative leaders in the northeast. CDI's mission is to build a cooperative economy through the creation and development of successful cooperative enterprises and networks in diverse communities. While our general operating area is New England and New York, we participate nationally and are pleased to assist this effort upon request from Federation of Southern Cooperatives.

Our organization provides education, training, financing and technical assistance to existing and start-up cooperatively-structured enterprises in all business sectors: food, housing, energy, agriculture, arts, health, forestry, fisheries, retail, service and more.

Andrew Danforth, CPA CSSBB serves as Manager of Housing programs at CDI, and founder of their New England Resident Owned Communities (NEROC) program which is working with 30+ communities in 7 states. He has in excess of a quarter century of diverse experience in housing finance, non-profit governance, and social outreach. During his career, he has worked for 9 of *the 20 largest US banks and Wall Street brokerages, has served as a liquidating Officer of the FDIC, and has assisted local lenders, government agencies, Indian tribes and regional non-profits. Internationally, he has worked on projects in Canada, Australia, the UK, and in several South Asian countries.*