

Chapter 11-B

Commentary on the 2011 CLT Network Model Ground Lease

This chapter comments on the terms of the Model Lease. The commentary is designed to provide information about the considerations that have gone into drafting and revising the Model Lease over the years – and in some cases the considerations that have gone into common variations of the model adopted by some CLTs – so that each new CLT can decide what particular provisions are most appropriate for its own situation. The commentary also touches upon certain legal issues that may deserve research under the laws of the particular jurisdiction in which the CLT will operate.

Headings in this commentary refer to specific articles or sections of the Model Lease. The section headings in the current version of the Model have been expanded (beyond those appearing in earlier versions) in order to give readers a more immediate sense of the gist of the section. In the commentary, more concise headings are used. It should be noted that section 14.9 states explicitly that all headings are for convenience only and “do not in any way limit or amplify the terms or conditions of this Lease.”

Recitals

The recitals, or introductory “whereas clauses,” set out background information about the parties to the transaction and their motivations. The clauses in the Model Lease probably apply to the majority of CLTs, but can and should be modified or supplemented to better fit the goals and purposes of a particular CLT.

There are several important legal effects of these clauses to bear in mind. If there is ever a dispute over the legal validity of some other section of the Lease, the understanding of the parties at the time of the original transaction, including the Homeowner’s willingness to give up certain typical rights of real estate ownership in return for the benefits provided by the CLT, may play a significant role in a court’s analysis. This section tries to make explicit the trade-offs that the prospective Homeowner was willing to accept and thereby emphasize that she entered the transaction voluntarily.

It is therefore important to have the “whereas clauses” accurately describe the goals and purposes involved. Because this Model Lease is designed for residential use, affordable housing goals are emphasized, but, if non-residential uses of the property are provided for or permitted in a CLT Lease, there may be a need to include references to such purposes as provision of social services, economic development, or environmental protection, among other possibilities.

All statements of the CLT’s purposes, including those that make reference to specific income levels, should be consistent with the CLT’s corporate purposes as stated in the Articles of Incorporation and as represented to the IRS in applying for recognition of tax-exempt status (see Chapters 4 and 6). In the Model, the references to the purposes of the CLT are framed with reference to “low and moderate income households.” Some CLTs may need to modify this language.

The Model Lease is drafted on the assumption that the parties are the CLT and an individual or family homeowner of a single family house on the Leased Land. There are, of course, other variations that could occur. A CLT may lease land, for a variety of purposes, to other nonprofit corporations, housing co-ops, condominium associations, mobile home park

associations, or private businesses, among other possibilities. (See Chapter 15, “CLTs and Limited Equity Housing Coops,” and Chapter 16, “Other Ground Leases.”)

It should also be noted, in the case of single-family residential properties, that more than one homeowner on a single tract of land. Care must be taken to clearly modify the identification of the parties and the introductory language to conform to the actual parties involved.

Definitions

The terms defined here are key to a clear understanding of the most important relationships, rights and responsibilities established by the Lease. If you use these terms differently in your lease, the definitions should be adjusted accordingly. If you replace these terms with others you should of course define the others in this section. You may also want to add definitions of terms that are key to the particular resale formula that you decide to use (see commentary on Article 10).

It should be noted that in this 2011 version of the Model Lease several very basic terms are different from those used in earlier versions:

- The term *Homeowner* has replaced the term *Lessee*.
- The term *CLT* has replaced the term *Lessor*.
- The term *Home* has replaced the term *Improvements*.
- The term *Leased Land* has replace the term *Premises*, or *Leased Premises*.

ARTICLE 1: Letters of Agreement and Attorney’s Acknowledgment

The Homeowner’s Letter of Agreement and the Attorney’s Letter of Acknowledgment (in previous versions identified as “Letter of Stipulation and Letter of Acknowledgment”) are designed to provide further evidence that the Homeowner understands the transaction and enters into it willingly. Although a sample Letter of Agreement is attached, this letter could be written by the prospective Homeowner in her own words, describing her individual situation and motivations in purchasing a resale-restricted CLT home, both personally and in terms of the larger CLT goals. This letter should not just be another document in small print signed at the closing. Of course, it is not always practical to ask the Homeowner to produce such a letter. The CLT probably will need to prepare something like the sample, which could be modified to fit individual circumstances.

The Attorney’s Letter of Acknowledgment indicates that the Homeowner had the benefit of legal counsel and that counsel explained the documents being signed. Any real estate transaction is complicated, particularly one involving limitations on the potential profit from resale. Counsel is not being asked to give any opinion on the adequacy of the legal documents or the fairness of the transaction. Counsel is only being asked to acknowledge that the documents were so reviewed.

It should be noted that there are some states where attorneys are not normally involved in closing real estate transactions. The appropriateness of an Attorney’s Letter of Acknowledgment has sometimes been questioned in these states, but in most cases CLTs have proceeded on the assumption that it is still important that the documents be explained to the Homeowner by a qualified, impartial third party, and that it is appropriate for attorneys to play this role. The sample Attorney’s Letter of Acknowledgment attached to this Revised Model Lease can be adapted to suit the circumstances of the particular situation.

ARTICLE 2: Leasing of Rights to the Land

Section 2.1 CLT Leases Land to Homeowner

Exhibit LEASED LAND is a legal description of the property being leased. Care should be taken to include as appurtenant to the Leased Land the right to use any easements or other benefits serving the Leased Land. Rights to use utilities and other physical matters serving the buildings on the Leased Land should also be included, as well as rights of access to repair and maintain such utilities. If the situation is such that certain portions of the land or certain facilities are shared by multiple owners – for instance shared utility or septic systems, shared driveways or parking areas – the circumstances will need to be addressed both in the description of the Leased Land and in other provisions of the Lease.

This section also states that the Leased Land is leased “as is,” so that the CLT is making no representations as to the quality of title to the Leased Land. The risk of a title problem is of concern to both the CLT and the Homeowner, and the Homeowner’s lender is likely to require a title certification or title search running in favor of the lender in the event of a loss due to a title problem. This is a cost typically borne by the buyer of property, and similarly the risk (and therefore by implication the cost of investigation), has been allocated to the Homeowner here. The parties could, of course, change this allocation.

Section 2.2 Reservation of Mineral Rights

This reservation of mineral rights is probably relevant only to rural situations. Where mineral or other subsurface rights might be of particular value, this section could be altered or expanded. For example, rather than prohibiting the CLT from removing minerals from the leased Land without the Homeowner’s permission, the CLT might be allowed to proceed with removal without permission if its actions do not disrupt the Homeowners use of the property or if it takes certain steps to minimize the disruption and/or compensate the Homeowner.

In any case where the CLT does not in fact own the mineral rights, this section must of course be revised to accord with the facts.

In addition to mineral rights, there may be other types of property rights that need to be clarified in a particular area. For example, if some of the Leased Land is wooded, are the timber rights being leased to the Homeowner or are they being reserved to the CLT? If there is farmland, are there standards for farming practices that are important to the CLT? Any reservation of rights to the CLT or regulation of the Homeowner’s activities should be spelled out as clearly as possible to avoid conflicts and confusion in the future.

ARTICLE 3: Term of Lease; Change of Land Owner

Sections 3.1 and 3.2 Principal Term and Homeowner’s Option to Extend

The Model Lease uses a 99-year lease term because this is typically the longest lease term allowable before there is a question of whether the Homeowner’s property interest is really in the nature of fee simple ownership. As a general rule, the longer the leasehold term the more closely the Homeowner’s property rights resemble those of a full fee simple owner of the Land and Home. Also, as noted in Chapter 20, “Financing CLT Homes,” the longer leasehold term minimizes lenders’ concerns regarding the potential impact of the end of the lease term on their security.

The Homeowner’s option to renew the Lease extends the potential duration of the Homeowner’s security of tenure even further. The potential disadvantage of such provisions for the CLT is that the Land can be tied to a particular use for a very long time (though CLTs

will normally have the opportunity to exercise the purchase option and issue new leases, perhaps with modified provisions, when homes are resold). Community needs and goals may change during the term of a lease. A shorter lease term without a renewal option would give the CLT, as representative of community interest, a more certain opportunity to review whether the use permitted under the Lease still meets the needs of that community. In balancing these individual-versus-community interests, most CLTs have opted for a 99-year initial term, and most have followed the Model Lease in providing for renewal of such a term.

In most jurisdictions, a 99-year lease term is allowable. However, in some states, such as California, the option to renew at the end of a 99-year term is a remote interest in property which is invalid by statute or by common law application of the Rule Against Perpetuities (see discussion of Rule Against Perpetuities regarding Section 14.4 below; see also Chapter 9, “Enforceability of the CLT’s Preemptive Right”). In some cases the rule can be satisfied technically, for instance by making the renewal automatic. If in a particular state there is no way around this problem, then the choice is either to shorten the lease term to a legally acceptable length or not to provide a renewal option and leave the question of renewal to the decision of the parties at the end of the 99-year initial term.

A lease without a renewal option leaves the Homeowner in a weakened bargaining position at the end of the lease term. In that case, under current law, the CLT would be under no legal obligation to renew the Lease, except possibly an obligation to bargain in good faith. If the CLT or a successor were ever tempted to change course and use its land for other purposes, it could refuse to renew the Lease except on terms more favorable to it. On the other hand, after 99 years some of the terms of the Lease might no longer make much sense or might be unduly disadvantageous to the CLT, so there might be legitimate reasons to refuse a renewal on the same terms. In Section 3.2 a middle ground has been chosen, providing for a full 99-year term with an option to renew, but giving the CLT some flexibility to modify terms upon renewal so long as the modifications are not “materially adverse” to the Homeowner’s rights. The concept of “materially adverse” is admittedly open to interpretation, but is intended to distinguish changes which would cause some significant hardship to the Homeowner (e.g. a substantial increase in the Lease Fee) from generally benign changes (e.g. a new method of notice).

Note that the CLT is required to give written notice to Homeowner, 180 to 365 days prior to expiration, regarding the impending expiration of the Lease term. A Homeowner wishing to renew the Lease must then, within 60 days, give written notice to CLT, exercising the option to extend. The requirement that CLT give notice regarding impending expiration is intended to protect the Homeowner (by this time an heir of the original Homeowner) who may have no clear knowledge of when the Lease expires or of exactly what must be done to extend it.

Section 3.3 Change of Land Owner

By giving the Homeowner a right of first refusal in the event of a sale of the Land to other than a public agency or nonprofit organization carrying out the CLT’s goals, the Model Lease provides an extra measure of security to the Homeowner. Some CLTs might choose to go a step further and give the Homeowner a right to buy for a limited (designed to be affordable) price in such a situation.

Note that the attachment “Exhibit FIRST REFUSAL” establishes specific terms for both the right of first refusal described in this section and the separate right of first refusal granted

to the CLT in Section 14.5. The Exhibit gives the holder of the right 45 days in which to notify the seller of her intent to purchase. The holder then has 60 days in which to complete the purchase. For CLT's seeking to facilitate FHA mortgage insurance for their homebuyers, it should be noted that FHA regulations limit the period in which such a right can be exercised to 45 days. At least as the language is understood by FHA, the right is "exercised" when the holder gives notice of intent to purchase.

ARTICLE 4: Use of Leased Land

Section 4.1 Residential Use Only

As drafted, the Model Lease assumes that the CLT will want to limit use of the Leased Land primarily to residential uses. Also allowed are uses that the local zoning code would permit as "incidental" to residential use. Such incidental uses are typically home occupations, such as haircutting, professional offices with minimal or no staff, and the like. Finally, if the CLT wishes to impose any restrictions on use that are not currently compelled by law, it can add them in an Exhibit RESTRICTIONS. A CLT can modify the terms of such an Exhibit from one leasehold to another, depending on the circumstances of the different sites, without modifying the body of the Lease in each case.

Use restrictions raise a number of important choices for the CLT. A private agreement like a lease can prohibit some uses permitted by local zoning, but cannot permit uses which local zoning prohibits. Therefore, the effect of Section 4.1 is to "freeze" the allowable uses according to zoning at the time the Lease begins unless zoning itself later becomes more restrictive. The CLT must question carefully whether the existing zoning furthers its policies and priorities. It must also consider whether uses that come to be permitted by local zoning in the future should automatically be permitted under the Lease. For instance, if later zoning regulations allow commercial uses of the property, should the CLT allow such use? Most CLTs want to prevent commercial uses from replacing residential use, but many may not want to freeze in current zoning provisions regarding uses incidental to residential use, since the nature of appropriate incidental uses may change substantially in 99 years and it may be appropriate in the future to allow certain uses prohibited by zoning at the time the Lease commences.

In deciding these questions, the CLT must consider its own view on the balance between individual interests and community interests and should not simply adopt local zoning without carefully considering the possible consequences.

Finally, although the Model Lease assumes a residential use, CLTs sometimes lease to businesses, nonprofits and social service providers. Such cases are likely to call for a very different set of use provisions (see Chapter 16, "Other Ground Leases").

Section 4.2 Responsible Use and Compliance with Law

This section imposes a general obligation of responsible use of the property. It could be tailored to include specific obligations for particular leaseholds, such as an obligation to maintain the productive capacity of agricultural land (or such specific obligations may be included in an attached Exhibit, like the restrictions noted above). The section also establishes as a condition of the Lease the requirement that the Leased Land and Home be maintained in accordance with all applicable laws, so that a violation of any such law will constitute a default under the Lease. In addition, the Model explicitly provides that the property must be maintained "in such condition as is required to maintain the insurance

coverage required by Section 9.4 of this Lease.” This provision is implicit in Section 9.4 itself but is included here to emphasize it as one of several significant criteria for required maintenance.

Section 4.3 Responsible for Others

This section makes it clear that the obligations under the Lease remain the Homeowner’s even if the violation of the Lease is caused by someone else who is on the Leased Land with Homeowner’s consent.

Section 4.4 Occupancy

The owner-occupancy requirement established by this section is an important feature of CLT homeownership programs, and thus of the CLT residential Lease. The Model Lease leaves the exact definition of the requirement up to the individual CLT, but CLT leases typically require occupancy for at least eight months – and sometimes as much as ten or even eleven months – out of each year of the Lease. This restriction does limit the Homeowner’s flexibility, but it is usually assumed that a CLT will in fact grant permission for extended absence when there are legitimate reasons for such an absence in a particular year. In any case, new CLTs are encouraged to consider carefully the exact number of months their Lease will require Homeowners to occupy the home each year when they do not have specific permission to do otherwise.

In states that have adopted legislation defining the rights of “domestic partners” CLTs will want to revise the second sentence of the section to read “Occupancy by Homeowner’s spouse or *domestic partner*... shall be considered occupancy by Homeowner.” (In states that neither legally define “domestic partners” nor allow same-sex marriage, the best way to protect the rights of a person in such a role is of course to see that the person is named as co-owner and co-lessee.)

The last sentence in this section 4.4 makes it clear that neither compliance with the occupancy requirement nor CLT’s specific permission for an extended absence constitutes permission to sublease the Home. Permission to sublease must be sought separately in accordance with the following Section 4.5.

Section 4.5 Subleasing

The issue of subleasing, which was addressed in Article 11 in previous versions of the Model, is now addressed here in Article 4, since it is an issue that is often raised in connection with the separate issue of occupancy addressed in 4.4.

When a CLT does permit a Homeowner to sublease the Leased Land and Home for some period of time, the usual assumption is that the sublessee should pay a reasonable fee for use of the property but that the Homeowner should not profit unduly. In applying this principle, some CLTs may wish to modify the description of the amount that can be charged as presented in “condition b.”

Section 4.6 Inspection

This section involves sensitive policy questions that must be addressed by individual CLTs. Each CLT must decide for itself on the exact nature of the inspection rights it will retain. Each must decide how frequently inspections should be permitted and how much advance notice should be required. Each must also decide whether the right to inspect the Leased Land will include or exclude the right to inspect the interiors of buildings. In the Model Lease, the right to inspect the interiors of buildings is explicitly excluded. The CLT should carefully consider whether it will allow the additional degree of privacy provided by

this exclusion, or whether it feels the right to inspect interiors of buildings is necessary if the CLT is to carry out its stewardship responsibilities. This 2011 Model does give the CLT the right to inspect the interiors of buildings after a homeowner has given notice of intent to sell, so the CLT can determine whether there is a need for interior repairs that will need to be addressed before the Home can be sold (note also that Section 10.13 calls for inspection by a professional building inspector at this time). You may also decide that the CLT should be given the right to inspect interiors of buildings in the case of emergencies.

Not surprisingly, the drafting of this section of a new CLT Lease often involves considerable debate between those especially concerned with guaranteeing the rights of privacy usually associated with homeownership and those especially concerned with the CLT's ability to monitor and preserve the quality of housing in which the community has invested. Such debate is appropriate and should not be avoided. The differing perspectives should be thoroughly aired and a reasonable balance should be agreed upon. In this connection, it is important to emphasize that, by establishing a right to inspect the Leased Land, a CLT does not commit itself to a policy of regular inspections. For some CLTs it may be the case that the right will be exercised only if there is reason to think that serious damage is being done to the Home or that the Homeowner's use of the Leased Land is endangering others. It should also be noted that conventional mortgages give the mortgagee a comparable (and often less specifically limited) right of inspection.

Section 4.7 Homeowner's Right to Quiet Enjoyment

This section is intended to comfort the Homeowner by declaring that the CLT's role should be limited to avoid undue interference with the Homeowner's enjoyment of the Leased Land. The term "quiet enjoyment," has a technical legal connotation concerning the right to continued possession of real property without being "dispossessed" by any party.

ARTICLE 5: Lease Fee

A detailed discussion of the concept of the CLT Lease fee and the various approaches to its definition and calculation can be found in Chapter 13, "Establishing and Collecting Fees." The approach to the lease fee taken in the Model Lease has changed over the years. In early versions of the Model, the fee was defined as the sum of a set of specified components, including the taxes on the land, as well as an "administrative charge" and a "land use charge." In later versions, taxes on the land are not charged to the homeowner as a component of the lease fee (the homeowner is required to pay them directly), and the "land use charge" and "administrative charge" are no longer distinguished from each other. Thus, in the 2002 version of the Model, the lease fee is treated as a single amount paid to the CLT as compensation for use of the land – and usable by the CLT for whatever purposes it sees fit. In the this 2011 version of the Model, however, the fee is once again treated as the sum of two components – a "land use fee" and a "repair reserve fee," as explained below.

Section 5.1 Amount of Lease Fee

Although the fee consists of two components, the dollar amounts of both components can be established when the lease is executed (unlike the "pass-through" components of earlier models that included taxes, etc., and needed to be adjusted from year to year). The Land Use Fee can be used by the CLT for any purpose it sees fit, but the use of the "Repair Reserve Fee" (called a "stewardship fee" in some CLT leases) is restricted to "preserving the physical quality of the Home for the long term." It is normally assumed that this restricted purpose

will be served through the establishment of some form of “repair reserve fund.” How such a fund will be managed and allocated is to be described in Section 7.6, which is reserved for this purpose. See the commentary on Section 7.6 regarding potential approaches to this subject.

If you choose not to establish a repair reserve – or not to fund such a reserve through a monthly fee – you can modify this section 5.1 to establish the lease fee as a single amount rather than as the sum of two fees.

Section 5.2 Payment of Lease Fee

CLT lease fees are normally paid on a monthly basis, like other regular housing costs but unlike some other types of ground rent, such as rents for agricultural land, which are often paid annually.

Section 5.3 Calculation of Land Use Fee

(Note: If the lease fee is to consist of a single amount (with no repair reserve fee), the term “Land Use Fee” should be replaced in this section with the term “Lease Fee.”)

This section describes the calculation of the Land Use Fee (but not the Repair Reserve Fee) in terms of two basic necessary considerations – fair rental value on the one hand and affordability on the other hand – but it does not spell out a detailed method for applying these considerations. As noted in Chapter 13, “Designing and Collecting Fees,” there is no precise method of calculating the amount by which fair rental value is reduced by the special restrictions imposed by a CLT lease; nonetheless, it is normally assumed that the amount of a CLT lease fee should be *at least somewhat less than* what the fair rental value would be if there were no special restrictions. The method by which affordability is calculated is normally dictated by the requirements of particular funders and lenders – typically the requirement that total monthly housing costs, including mortgage payments, taxes, insurance, and Lease fee, not exceed a specified percentage (e.g. 30%) of gross monthly income.

Section 5.4 Reduction or Suspension of Lease Fee

This section recognizes the CLT’s right to waive all or part of the Lease Fee in a hardship situation. Section 14.6 insures that a waiver or reduction by the CLT in one instance will not obligate it to make the same arrangement in a later instance.

Section 5.5 Periodic Increase of Fees

(If the lease fee is to consist of a single amount (with no repair reserve fee), this section should be revised to refer to just to the Lease Fee, rather than to the separate Land Use Fee and Repair Reserve Fee.)

This section allows the CLT to increase either or both of the components of the Lease Fee from time to time, provided the total increase since the date of the execution of the Lease does not exceed the increase in the Consumer Price Index over that time. Several variations of this approach are possible. You may *require* that either or both of the fees be recalculated at specified intervals, rather than just preventing the CLT from increasing them more frequently than once in a specified number of years. You may also choose to call for periodic recalculation of the Land Use Fee (but not the Repair Reserve Fee) through the same process described in section 5.3, rather than through the CPI-based process. And you may choose to call for separate adjustments of the Repair Reserve Fee based on periodic projections of likely long-term costs of repairs.

It should be noted that some mortgage lenders and mortgage insurers (e.g., FHA) may

insist on tighter limitations of the CLT's right to increase the Lease Fee than the CLT would otherwise choose, or may insist on a right to approve any increase in the Fee. Such lender-imposed limitations, if necessary, should be established in a rider to the Lease, applicable only during the term of the mortgage in question, rather than in the body of the Lease.

Section 5.6 Increase in Land Use Fee if Restrictions are Removed

(If the lease fee is to consist of a single amount (with no repair reserve fee), the term "Land Use Fee" should be replaced in this section with the term "Lease Fee.")

This important section allows the CLT to increase the Land Use Fee in the event that resale and/or occupancy restrictions are removed from the lease as a result of a mortgage foreclosure or for any other reason. Since the amount of the Land Use Fee has been calculated as the fair rental value of the land, as restricted by the Lease and adjusted for affordability, it is reasonable to allow this increase to reflect the unrestricted value of the land in a situation where the Home is no longer reserved for lower income owner-occupants. The limitation on the initial amount of the increased fee to a specified dollar amount is intended to address the concerns of mortgagees or buyers who might acquire the home pursuant to foreclosure.

5.7 Late Payment Penalty

As the penalty is structured here, interest can be charged for late payment as soon as the "due date" is passed, but will be forgiven if payment is made within 30 days of the due date. This approach gives the CLT a bit of added leverage when it notifies the Homeowner, during the 30-day period, that the payment has not been received.

5.8 Collection of Unpaid Fees from Proceeds of Sale

This section explicitly provides for collection of any unpaid lease fees by the CLT out of the Homeowner's proceeds when the Home is sold. The last sentence of the section strengthens the CLT's hand in this matter by providing for a lien on the Home. Nonetheless, in a situation where a significant amount is owed, the CLT should consult with its attorney regarding actions that may need to be taken to ensure full enforceability of this provision.

ARTICLE 6: Taxes and Assessments

Sections 6.1 and 6.2 Taxes and Assessments

In this version of the Model these sections assign responsibility for taxes on the Leased Land as well as on the Home directly to the Homeowner. As noted above, it is also possible for the CLT to pay the taxes on the land but to pass this cost on to the Homeowner as a component of the Lease Fee. See Chapter 13, "Designing and Collecting Fees," for discussion of the advantages and disadvantages of the two approaches.

Section 6.3 Homeowner's Right to Contest

Jurisdictions may differ somewhat on whether a ground lessee can contest real estate taxes in her own name. For example, in Massachusetts, any tenant having an obligation to pay more than 50% of the taxes on a property can contest real estate taxes in her own right (although a tenant, unlike an owner, must pay the taxes first and then file for an abatement).¹ This section 6.3 clarifies that Homeowner can do so, even if the law does not grant such a right, by providing that the CLT shall join in such abatement proceeding in response to a "reasonable request from Homeowner for assistance in this matter."

Section 6.4 Payments in Event of Delinquency

This section specifically allows the CLT to add to the Lease Fee any delinquent taxes or

assessments on the Home and/or the Land.

ARTICLE 7: The Home

Section 7.1 Ownership of Improvements (the Home)

The Home is owned by the Homeowner. This separation of ownership of land and buildings is at the core of the CLT approach to ownership (see Chapter 10, “Legal Issues Re. CLR Ownership,” where this principle is discussed, along with some variations from it). Nevertheless, the ownership of the Home is intended to be subject and subordinate to the Lease; that is, the Lease imposes some limits on the usual rights of ownership of the Home. Especially important is the question of whether at the end of the lease term (or sooner) the Home – or any permanent part of the Home – can be “severed” from the Leased Land and moved elsewhere. Commercial Leases typically prohibit such severance and provide for a forfeiture of the title to any leasehold improvements to the lessor at the end of the lease term. Section 7.7 follows this practice but requires that the CLT compensate the Homeowner. However, in some states a ground lessee’s ownership of the Home may in part turn on having the right to sever. (See comments on Section 7.6 below.)

Section 7.2 Purchase of Home by Homeowner

A deed is used for conveyance rather than a bill of sale to signify that the Home is to be considered as real (rather than personal) property. However, some jurisdictions may consider the Home technically to be personal property, in which case a bill of sale will be the appropriate instrument.

Section 7.3 Construction and Alteration

The CLT has a fundamental interest in preserving the quality of the permanently affordable housing on its land and protecting future residents of the property against inferior work. Some CLTs have gone further than the Model Lease and have required prior approval of all construction – at least where the home in question is newly constructed and where there should be little need for further construction and where inappropriate changes by residents may interfere with a carefully developed design.

The second paragraph of this section, spelling out a process to be followed in situations where the CLT’s approval is required for major alterations, was added in this 2011 version of the Model Lease. You may wish to modify the details. It should be emphasized that CLTs using resale formulas that include a “capital improvement credit” will need to specify a different or additional process for handling situations in which a Homeowner requests not only that certain construction be permitted but that its value be added into the purchase option price. The latter process would be described in Article 10 in connection with the resale formula. It is possible to combine or coordinate the processes, but it is important that the two issues – consent for construction as such and approval of a capital improvement credit – not be confused.

Section 7.4 Prohibition of Liens

Liens are a potential threat to the CLT’s title to the Land and to the transferability of CLT Homes, so the provisions of this section are designed to prohibit all liens (other than permitted mortgage liens). In some situations involving the Home and/or the Homeowner, however, some party may need to protect itself against non-payment by filing such liens. The provisions for “bonding-off” liens put the burden on the Homeowner to make arrangements for a source (other than the property) of payment of any meritorious claim while the claim is

being resolved. Note that generally a “prohibition of liens” such as that contained in this section cannot defeat the rights of certain parties to obtain a lien under local law. Rather, the provision just bars the Homeowner from allowing such a lien to occur and remain in place.

Section 7.5 Maintenance and Services

Supplementing the provisions of Section 4.2 with specific reference to the lessee-owned Home, these provisions are intended to see that the Home will remain in good condition, both to protect residents and to minimize the possible CLT liability. The section also explicitly establishes that the Homeowner is responsible not only for routine maintenance but for any major repairs or replacements that become necessary.

Section 7.6 Repair Reserve Fund

Model provisions for a repair reserve fund are not included in the body of the Model Lease, but Section 7.6 is “reserved” for this subject, and it is recommended that CLTs establish some form of repair reserve. A number of factors should be considered before deciding on a particular approach to such a reserve fund. In one way or another, however, a CLT must deal with the question of how the necessary long-term reinvestment in the home is to be ensured.

Designing a reserve for repairs and replacements entails two sets of questions: (1) how to fund such a reserve, and (2) how to manage and allocate the reserve to pay for repairs.

Funding. The reserve may be funded by charging the homeowner a monthly fee and/or by collecting a single larger sum when the home changes hands (as a separately designated percentage of the purchase price when the initial homeowner buys or as a component of a “transfer fee” upon resale). The monthly fee is probably the more common approach among CLTs, though some rely, at least in part, on committing a larger sum to this purpose at the time of transfer. In this 2011 version of the Model Lease, Section 5.1 establishes a Repair Reserve Fee as a component of the Lease Fee but does not state how the funds are to be used.

Note that Section 10.12 or 10.13 (depending on which version of Article 10 is used) provides for a transfer fee “to compensate the CLT for carrying out its responsibilities with regard to the [resale] transaction,” but does not provide for use of the fee to assist with repairs for which the Homeowner is responsible. The section might be modified, however, to allow this use.

Management and allocation of funds. There are a number of issues that a CLT must address in deciding how to manage and allocate a reserve fund. The decision will depend in part on circumstances specific to the particular CLT (involving both the capacity of the organization and the type of housing with which it deals), so we are not proposing a specific model at this time, but it is important that each CLT consider the issues carefully and then develop clearly defined policies that will avoid confusion and the potential for disagreement between CLT and homeowners.

1. The first question is whether there will be a separate reserve fund for each home, to be used only for repairs on that particular home, or whether there will be a single fund for all of the CLT’s homes, to be used wherever it is needed. Both are possible, though at this time most CLTs that have established repair reserve funds have maintained separate reserves for each home. Maintenance of a single master fund does provide more flexibility for the CLT in dealing with major repairs, but it creates the potential for resentment by those homeowners who have paid into the fund and then find that they have contributed more to the repair of someone else’s home than to their own.

2. If house-by-house reserves are maintained, the next question is whether the funds can be withdrawn by the homeowner when she sells the home, or whether the funds will “stay with the home.” If the reserve is seen only as the equivalent of a rental damage deposit, then it is reasonable to allow the homeowner to withdraw whatever remains in the reserve when the home is sold. However, most CLTs that maintain such reserves see them not as a deposit against undue damage but as a way of accruing funds to pay for those replacements and repairs for which a need accrues inevitably in due course – for instance, to pay for a new roof when the original roof has eventually been “used up.” A homeowner who sells a home after having used up only half of the life expectancy of the original roof will not have occasion to draw on the reserve for roof repair, yet it is reasonable for that homeowner to contribute toward the cost of what she has used. It must be acknowledged, however, that what is reasonable with some other types of repairs is less clear. The homeowner who has faithfully performed the maintenance tasks necessary to avoid or forestall certain types of repairs may not have occasion to draw on the reserve for those repairs, and may therefore feel that she has been required to pay twice for the maintenance of her home.
3. The question then is what exactly should such reserves be used for. A range of approaches is possible.
 - One approach, particularly appropriate for new homes, is to state in the lease a specific list of items for which funds can be used. Usually the idea is to include major items that have rather well defined life expectancies, regardless of year-to-year home maintenance efforts. Items such as roofs and exterior paint clearly fall into this category, but with many other items it becomes more difficult to distinguish between *inevitable* life expectancies and life expectancies that vary greatly depending on intensity of use and consistency of maintenance. If an explicit list is included in the lease, it may be presented as a list of the *only* items for which the reserve funds can be used, or it can be presented as a non-exclusive list of items that can be expected to qualify for use of the funds, so that other kinds of replacements and repairs can also be funded if they meet certain criteria.
 - A somewhat different approach is to establish an explicit list as a matter of policy but not to include it in the lease, so that it can be modified without amending the lease. In such case the lease may simply state that the reserve fund shall be used for purposes consistent with duly approved CLT board policy. This approach may be more appropriate for older homes where the life-expectancy of specific components at the time the home is purchased will vary substantially from home to home – and of course from original purchase to resale. (You may also address such variables through customized exhibits attached to leases on a home-by-home basis.)
 - The CLT may also be given more flexibility by stating in the lease basic criteria for the allocation of funds, rather than specific uses. Policy statements that are not included in the lease may or may not then provide specifically for the application of the criteria to different kinds of repairs. Any statement of what the reserve *can* be used for (whether containing an explicit list of items or not) should normally be accompanied by a statement of the kinds of things that it *cannot* be used for. Such proscribed uses of the reserve typically include replacement of original components with expensive components or materials that are significantly more luxuries, but not

more functional or durable, than the originals; and replacements or repairs that are necessitated by the homeowner's misuse or neglect rather than normal wear and tear. The application of such provisions may of course involve conflicting views of what is or is not luxurious and what does or does not constitute misuse or neglect, but it is generally wise to establish the principles even if they are applied only in extreme cases.

- The lease and/or CLT policies may or may not provide explicitly for use of the reserve to pay for repairs that may be required (as under Section 10.13 or 10.14) at the time of resale.

Section 7.7 Disposition of Home upon Expiration of Lease Term

If the Lease were silent on the matter, in some jurisdictions the Homeowner might be able to "sever" the improvements from the Leased Land and move them elsewhere when the Lease expires or terminates. Some CLTs do permit severance but specify certain conditions (e.g., Homeowner must repair all damage to the Land). See Chapter 10, "Legal Issues Re. CLT Ownership," for further discussion of this matter.

Regarding the CLT's obligation to compensation the Homeowner upon the reversion of ownership, this 2011 version of the section, unlike past versions, provides explicitly for full payment to Permitted Mortgagees before any amount is paid to the Homeowner. The current version also explicitly holds the Homeowner responsible for clearing any liens on the improvement at the time of reversion, or for reimbursing the CLT for its costs in clearing such liens, including attorney's fees.

In the current Model Lease, the CLT is required to pay for the improvements regardless of whether the Lease has expired or has been terminated as a result of a default by Homeowner. However, some CLT leases (and early versions of the Model) impose this requirement *only* in the case of expiration of the full term of the Lease, leaving the CLT (or a successor lessor) without an obligation to pay for the Home if the Lease is "sooner terminated" as a result of a default by Homeowner. New CLTs should weigh the additional protection for the Homeowner that is provided by the current version against the additional protection for the CLT provided by the alternative version. In any event, however, it should be noted that the CLT cannot terminate the lease without paying whatever is owed to – or otherwise accommodating the interests of – any Permitted Mortgagees (see "Permitted Mortgage Exhibit," Section B).

ARTICLE 8: Financing

For a thorough discussion of leasehold mortgages and the issues that they raise for mortgage lenders and for CLTs, see Chapter 20, "Financing CLT Homes."

The CLT has important reasons for overseeing the Homeowner's access to mortgage financing. Regarding any proposed mortgage financing, the CLT wants to be sure (a) that the mortgage lender is fully aware of the terms of the Lease, (b) that the CLT's fee interest in the land is not mortgaged or otherwise endangered, (c) that the total amount of debt, the repayment schedule, and other terms of the loan are reasonable and manageable for the lower-income Homeowner, (d) that in the event of a mortgage default the CLT will have every possible opportunity to prevent foreclosure, not only for the Homeowner's sake but for the sake of preserving the public's investment in the Home, and (e) that, in the event a foreclosure

is unavoidable, the CLT will have the best possible chance to regain control of the home for future lower income owner-occupants.

For these reasons, the Lease allows only “Permitted Mortgages.” In past versions of the Model, a Permitted Mortgage was defined as any mortgage that was permitted in writing by the CLT *and* that included (in the mortgage document or related documents) certain provisions, protective of the CLT’s interest, that are not common to conventional mortgages. In practice, however, CLTs generally agreed to permit mortgages for which these provisions were not written into the documents. The 2002 edition of the CLT Legal Manual contains a model Permitted Mortgage Agreement, which, it was suggested, CLTs should ask mortgagees to sign. However, such written agreements with mortgagees have continued to be rare. Therefore, the current Model Lease takes a somewhat different approach, as described in the commentary that follows.

Section 8.1 Definition of Permitted Mortgage

In this 2011 version of the Model, the term “Permitted Mortgage” is defined simply as any mortgage that the CLT has permitted in writing.

Section 8.2 CLT Permits Original Mortgages by Signing Lease.

This version of the Model explicitly incorporates something that, in the past, has often been assumed but not explicitly stated. At the time when the Homeowner acquires the Home and the rights to the Leased Land, the CLT has usually been working closely with the Homeowner to see that appropriate financing is arranged. The CLT is necessarily in position to know what kind of financing has been arranged before the CLT proceeds to sign the Lease. For this reason it seems unnecessary to require the signing of a separate “permitted mortgage document” at that time. If the CLT finds the proposed mortgage financing unacceptable it will not sign the Lease and Deed.

Section 8.3 Permission for Refinancing or Other Subsequent Mortgages

At any time subsequent to the closing of the original transaction it is possible for the homeowner to seek refinancing or additional financing without the CLT necessarily being aware. In such situations it is important that the Homeowner be required to provide essential information about the financing to the CLT and get specific written permission from the CLT before proceeding. Refinancing and second mortgage financing are a particular concern because they may allow the Homeowner to assume additional debt on terms that she cannot realistically manage – and may possibly result in total debt that is greater than the purchase option price. Careful lenders should of course share these concerns. In reality, however, lenders have sometimes made (non-permitted) loans to CLT Homeowners without even realizing that a ground lease existed, much less that it contained resale price restrictions.

The Model Lease requires that the Homeowner inform the CLT of the proposed terms and conditions of any such mortgage loan at least 15 business days prior to the expected closing of the loan. Some CLTs may wish to stipulate a different minimum number of days. Some may also wish to modify or expand the list of information that must be provided to the CLT – or may wish to revise the section to state that the Homeowner must notify CLT of its intention and that the CLT will *then* inform Homeowner of the specific information its current policy requires be submitted before approval can be granted.

The final sentence of the section establishes basic criteria for the CLT’s approval of such loans. One such criterion is the maximum ratio of total mortgage debt to the Purchase Option Price. In the Model, the percentage is left blank. A CLT must either fill in a specified

percentage or, perhaps, eliminate the specific requirement from the Lease and deal with this issue in terms of policy that the organization may modify from time to time. Among those CLTs that have established specific maximum ratios, the common range is from a conservative 80% up to 100%. (It should be noted that no CLT would want to prohibit a homeowner from refinancing her original first mortgage debt on favorable terms that reduced her monthly payment, even if the total debt exceeded some prescribed percentage of the purchase option price.)

Section 8.4 Standard Permitted Mortgage

While the CLT is not required to permit most mortgages, it is required to permit mortgages that meet all of the relatively strict conditions laid out for a “Standard Permitted Mortgage,” including the condition that the mortgagee enter into a “Standard Permitted Mortgage Agreement” that conforms with the model document presented in the Permitted Mortgages Exhibit, Part C. The intent of this provision is to protect the Homeowner in a situation where an owner of the land might want to prevent a sale of the Home by refusing to permit *any* mortgage.

With regard to the blank that must be filled in to indicate the maximum allowable percentage of mortgage debt to purchase option price, the usual expectation is that the matter will be handled in the same way as in Section 8.3 above.

Section 8.5 Obligations of a Permitted Mortgagee

With the approach taken in this 2011 version of the Model, the basic protections for CLT and Homeowner that the CLT would like to ensure are treated as conditions of the lease itself, binding on any Permitted Mortgagee unless CLT and Homeowner have executed a lease rider that modifies or contravenes the stated obligations. On this matter, the current version of the Model departs from the earlier strategy of asking (in theory) that the mortgagee include these conditions in mortgage documents or sign a separate document agreeing to such protections. If such a Permitted Mortgage Agreement is signed by a mortgagee, it might be more strictly enforceable than the current provisions of this section 8.5 regarding mortgagee obligations, but the reality is that mortgagees have rarely agreed to sign such a document (and probably were not asked). In the past, what actually happened in most cases was that CLTs, after negotiating the most favorable terms possible, went ahead and permitted the mortgages anyway.

In such situations, whatever conditions were agreed upon in negotiations between Permitted Mortgagee and CLT were often incorporated in lease riders (like the Fannie Mae Uniform CLT Ground Lease Rider) which were signed by the Homeowner and the CLT but not by the mortgagee. The current approach accepts the reality that a mortgagee may insist on such a lease rider. But, in turn, it establishes the obligations of a Permitted Mortgagee as conditions of the Lease itself (defining an essential element of the collateral for the leasehold mortgage) except in so far as any of these obligations are removed or altered by a lease rider.

In the current approach we have also eliminated the requirement that the “cure period” (the time in which the CLT has a right to cure a Homeowner’s mortgage default) must last a specified number of days – a definition that in the past was usually either ignored or modified by a lease rider. The cure period is now defined simply as “that period of time in which the *Homeowner* [emphasis added] has a right to cure such default” (Exhibit: Permitted Mortgages, Section A-1).

It should be emphasized that any concessions made to specific mortgagees should always

be incorporated in a rider to the lease (binding only for the life of the mortgage), not in the lease itself.

Section 8.6 Rights of Permitted Mortgagees

Like the obligations of a Permitted Mortgagee, the rights of a Permitted Mortgagee stated in the Permitted Mortgagee Exhibit can be modified or supplemented by a lease rider.

The rights stated here are those that most careful lenders will insist on having guaranteed to them. The fact that the Lease does guarantee them only for *Permitted* Mortgagees provides some important protection for both the Homeowner and the CLT. If the CLT ever discovers that the Homeowner has in fact granted a mortgage on her property that does not meet the requirements of a Standard Permitted Mortgage and that has not otherwise been permitted by the CLT, the mortgagee can be advised that it does not have the rights specifically assigned to Permitted Mortgagees by the Lease (including the right to prevent the termination of the Lease in the event of a default under the Lease by the Homeowner), and it can be advised that the mortgaging of the Home and leasehold interest without the CLT's permission constitutes a default under the Lease which could lead to termination. Given these circumstances, it is likely that the mortgagee will choose to come to terms with the CLT.

In past versions of the Model, two specific rights of the Permitted Mortgagee – the right to have resale restrictions removed from the Lease pursuant to foreclosure, and the right to approve amendments of the Lease before they become effective – were stated in the body of Article 8 rather than in the Permitted Mortgage Exhibit. In the 2011 version, however, these rights are included in the Exhibit, so that all Permitted Mortgagee rights can be found together in one place.

Section 8.7 CLT's Right to Proceeds in Excess of Purchase Option Price

This provision addresses a situation that could arise if the home is sold, pursuant to foreclosure, for an amount that would allow the Homeowner, after the mortgagee is paid in full, to realize proceeds in excess of what is permitted by the resale restrictions in Article 10. The enforceability of this provision may vary depending on state laws relating to foreclosure, but it remains important that the Lease contain language whereby, as far as is legally possible, the Homeowner explicitly gives up any claim to such excess proceeds.

ARTICLE 9: Liability, Insurance, Damage and Destruction, Eminent Domain

Most of the provisions of this article are similar to standard provisions for liability and casualty matters found in most long-term leases. The Model is careful, however, to limit the value that can be taken away by the Homeowner and to protect the CLT's right to preserve the value invested in the Home as well as the land by the public.

For a discussion of liability issues affecting long-term ground lessors and ground lessees, see Chapter 10, "Legal Issues Re. CLT Ownership."

Section 9.5 Damage or Destruction.

This section limits the Homeowner's right to terminate the Lease in the event of a fire or other casualty if insurance proceeds will not fully pay for restoration. In the 2011 version of the Model, however, these limitations are not as rigidly defined as in previous versions.

Whereas past versions of Section 9.5 allow termination of the Lease by the Homeowner only if damage is such that insurance proceeds will cover less than 80% of the cost of restoration, the present version abandons the "80% criterion," on the grounds that it potentially leaves a

low-income homeowner responsible for paying higher restoration costs than are likely to be affordable for such a person. Instead, this version calls for the CLT to help find a way to cover any costs that are not covered by insurance and not affordable for the Homeowner. If a way to cover these costs cannot be found that is acceptable to both parties, then the Homeowner can terminate the Lease.

If the Lease is terminated, the Homeowner cannot receive more from the insurance proceeds than the Purchase Option Price allowed under Article 10, thus eliminating any possible incentive to use arson as a means of avoiding the equity limitations of the Lease. The 2011 version of section 9.5 also ensures that if the Lease is terminated, “the expenses of enclosing or razing the remains of the Home and clearing debris” must be paid out of the insurance proceeds before any proceeds are paid to the Homeowner.

Note that in this section the Purchase Option price is to be determined “as of immediately prior to the damage.” For CLTs with appraisal-based resale formulas, this situation may require an appraiser to calculate the value of what can no longer be observed. However, methods for such calculations have been developed and can be employed by a professional appraiser. The possible need for determining the value of something that has been lost or damaged is not unique to CLTs.

Section 9.6 Eminent Domain

In the 2011 version of the Model, provisions for allocating the amount of an award between CLT and Homeowner are somewhat simpler than in previous versions and are more closely parallel to provisions relating to allocation of insurance proceeds in the event of damage or destruction.

ARTICLE 10: Transfer, Sale, or Disposition of Home

For this 2011 version of the Model Lease, four possible versions of Article 10 are presented (in the Appendix at the end of Chapter 11-A). These versions differ with regard to three important variables: (1) whether the homeowner is given an absolute right to select an income-qualified buyer, (2) the type of resale formula that is used, and (3) whether the original Base Price is (or may be) greater than the original appraised value of the Home. No one of these versions is offered as THE model. Every CLT must make important decisions before adopting one of these versions (or its own variation of one of these versions).

In the commentary offered here we will first discuss all sections of “Version 1.” We will then discuss those features of “Version 2,” “Version 3” and “Version 4” that differ from comparable features of Version 1.

VERSION 1

In which:

- a) The Homeowner does *not* have an absolute right to identify a buyer.
- b) An “improvements-only appraisal-based formula” is used.
- c) The original Base Price is *not* greater than the original appraised value of the Home

Section 10.1 Intent

Article 10 is of course a very important part of the Lease, as it spells out the process by which affordability is to be preserved and the transfer of the Home is to be regulated. Section 10.1 is included to reinforce the acknowledgment by all parties involved that the limitations on resale, though not found in conventional housing transaction, are appropriate and willingly accepted in this context.

Section 10.2 Transfers to Income-Qualified Persons

This section states explicitly that the Home and the Homeowner's interest in the Leased Land can be transferred *only* in accordance with the sections that follow and that any other "purported transfer" shall be null and void.

It is important that the definition of Income-Qualified Person be precisely what is intended for each CLT leasehold. Some CLTs may apply the same definition to all of their leaseholds, but some define income qualifications differently depending on the level of affordability initially achieved and on the level required by a subsidy source. Thus some deeply subsidized homes may be reserved for buyers with household incomes below 60% of median income. Others may be available to buyers with household incomes below 80% of median income. Still others may be available to buyers with household incomes below 100% or 115% of median income. In any case, one should avoid the mistake made by some early CLTs that defined income qualifications simply as "low income household" or "low and moderate income household," since there is no universally applicable quantitative definition of these terms.

Section 10.3 Transfer to Homeowner's Heirs

The intent of this section is not to limit the Homeowner's right to bequeath the value of the Home, as an asset, to any person or persons of the Homeowner's choosing. The intent is to limit the categories of individuals that will have a right, upon inheritance, to assume the Lease and occupy the Leased Land on a continuing basis. Most CLT leases, like the Model, limit this right to spouses and children of the Homeowner and established members of the Homeowner's household, as well as those who are Income-Qualified Persons. Anyone outside of these categories may inherit the value of the (resale-restricted) asset but may not occupy the home as a permanent resident-owner. To realize the value of the asset in such cases, the property must be sold in accordance with the resale restrictions established in this Article 10.

Some CLTs have modified this Section so that it applies not only in the event of Homeowner's death but also in the event that Homeowner chooses to transfer title, while living, to a person or persons who would qualify as transferees if Homeowner had died after naming them as heirs. In such cases the initial sentence may be revised to read "Upon the receipt of a written request from Homeowner at any time or upon receipt of notice from the executor..."

In states where legislation has given legal definition to the role of "domestic partner," most CLTs will want to include "domestic partner" as well as "spouse" among those eligible to assume the Lease.

It should be noted that some subsidy sources will impose different eligibility requirements. A number of sources do not allow transfer to members of the household who are neither spouse nor children of the Homeowner (category "c") unless they are income-qualified. In these cases the usual practice is to attach a rider to the lease modifying this section for so long as a regulatory agreement with the funder is in effect.

Letters of Understanding and Attorney's Acknowledgment must be signed, submitted and attached to a lease as a condition of its assignment to an heir. This requirement is intended to prevent the problems that could arise if a person who had never specifically accepted the restrictions contained in the Lease were to become the Homeowner by inheritance.

Section 10.4 Homeowner's Notice of Intent to Sell

This section requires that the Intent-to-Sell Notice “include a statement as to whether the Homeowner wishes to recommend a prospective buyer as of the date of the Notice,” but does not require the CLT to accept the recommendation. Homeowner may also recommend a prospective buyer at a later time. See Section 10.6 regarding CLT's response to such recommendations.

Section 10.5 Appraisal

This section deals with the appraisal that will be required to determine the purchase option price if an “improvements-only appraisal-based formula” is used. If either a “simple appraisal-based formula” or a “compound appraisal-based formula” is used, then you can omit the sentence that states, “The Appraisal shall state the values contributed by the Leased Land and by the Home (consisting of improvements only) as separate amounts.” (See Chapter 12, “Resale Formula Design,” regarding the three types of appraisal-based formula.)

This version of the Model requires the *CLT* to commission and pay for the appraisal, whereas earlier versions of the Model (and a number of CLT Leases based on it) required the *Homeowner* to commission and pay for the appraisal when it is necessary to the application of an “appraisal-based” formula. The rationale for shifting responsibility to the CLT is that (a) appraisals are usually the responsibility of the buyer, not the seller, and (b) the CLT will normally be in a better position – with more experience and contacts – to see that the task is appropriately carried out. It is of course possible to require the CLT to commission the appraisal but to allow it then to charge all or part of the cost to the Homeowner.

It should be emphasized that the appraisal required here is one that is conducted “as though title to Leased Land and Home were held in fee simple absolute.” The appraised value of the property should not be discounted to reflect a reduction in value resulting from the restrictions imposed by the Lease. In applying an appraisal-based resale formula, the purpose of the appraisal is to determine how much the value of the Home *would have* increased in the absence of lease restrictions. The restrictions then allocate *a part* of this market appreciation to the Homeowner.

In many – perhaps most – cases the appraisal process that is carried out for the purpose of establishing the resale price can also serve the new mortgage lender's purpose of establishing the market value that the property would have pursuant to foreclosure. Since the resale price restrictions are removed following foreclosure (or the taking of a deed in lieu), the mortgage lender wants to know the value that the collateral would have *in the absence* of those restrictions. However, the collateral with which the lender is concerned consists of the Home *and the leasehold interest in the Land*, whereas the CLT, in calculating the price under an improvements-only appraisal-based resale formula, is concerned with the value of the Home alone (unless the original Base Price is greater than the original appraised value of the Home – the situation addressed in Versions 3 and 4). Thus, although the same basic appraisal *process* can serve the purposes of the CLT and the mortgage lender, the “*bottom line amounts*” that are finally calculated for the purposes of these two parties will differ. The bottom line for the CLT is the value that the Home alone would have without restrictions (or the value that the Home and Leased Land would have without restrictions if a “simple” or “compound” appraisal-based formula is used). The bottom line for the lender is the value that the *Home and leasehold interest* would have without restrictions (See “Chapter 20, “Financing CLT Homes,” regarding the valuation of a leasehold interest). The CLT should

clearly distinguish these amounts and should be careful not to use the wrong amount in calculating the formula price.

When appraisal-based resale formulas are used it is important that an appraisal be completed soon after an intent to sell notice has been given, as provided in this section, so that the Formula Price, and thereupon the Purchase Option Price, can be definitively established as early in the resale process as possible.

Section 10.6 CLT's Option to Purchase the Home

The content of this section is identical to that of the comparable section in Versions 3 and 4, but fundamentally different from the content of sections 10.6 and 10.7 in Version 2, which describe the exercise of the Purchase Option in relation to the process by which the Homeowner's right to select a buyer can be exercised.

One of the more important issues that a CLT must address in drafting a lease is the question of whether to retain an absolute right to exercise the Purchase Option (as in Version 1), and thus retain full control of the future use and occupancy of the Home, or whether to allow homeowners to sell their homes to income-qualified buyers of their choice (as in Version 2). CLTs that choose the approach embodied in Version 1 tend to be those that expect to have a waiting list and want to be sure that a home is sold to someone from this list, who has already been oriented and prequalified and has been waiting for an opportunity to buy a CLT home, rather than to a friend of the seller who has not been through the CLT's orientation process and may be less ready for homeownership. For the long-term, Version 1 also assures that the CLT will have an opportunity to change the use of a property at the time of resale – perhaps in a situation where residential use has become less appropriate for some reason and the property would better serve the community's interest if used differently. In such a situation Version 1 assures that the CLT can exercise its option and commit the property to the different use.

10.7 If Purchase Option Expires

Every new CLT should carefully consider how it wants its lease to provide for situations where the purchase option has expired (or purchase under the Option has not been completed) because neither the Homeowner nor the CLT has been able to identify a qualified buyer and the CLT is not able or willing to buy back the home and hold it until a buyer can be found. Such situations are rare for CLTs offering deeply subsidized homeownership opportunities in active housing markets where demand is strong, but are not necessarily rare for CLTs offering less deeply subsidized homeownership opportunities in weaker markets. The Model Lease keeps in place the resale restrictions, as to both the income qualifications of the buyer and the permitted resale price, for a period of six months after the expiration of the CLT's Purchase Option (or the expiration of the 60-day period allowed for completion of the purchase if the Option has been exercised). After the six-month period, if the Homeowner has made diligent efforts to sell the Home and it still has not been sold, restrictions regarding income qualifications are dropped, but the restriction regarding the price is retained (so the home will remain affordable for future low-income buyers even if market conditions change). Some CLTs may want to handle the matter differently – and a subsidy source may insist on a rider that will prevent the expiration of the income restriction during the life of a subsidy agreement.

10.8 CLT's Power of Attorney to Conduct Sale

This section addresses the potentially serious problem that could arise if a Homeowner

does not actively pursue the sale of a vacated property after the expiration of the CLT's Purchase Option. The section gives the CLT the right to step in after a long wait (here, one year, but it could be longer or shorter) and attempt to complete the resale of the home.

10.9 Calculation of Purchase Option Price

It should be noted that in early versions of the Model (and in CLT leases still based on those versions) the term "Purchase Option Price" was used to mean what is now identified as the "Formula Price." The term "Actual Purchase Option Price" was then used to designate what is now called the "Purchase Option Price." Not surprisingly the older practice resulted in some confusion and some drafting errors as individual CLTs worked to design their own resale formulas and adapt their leases to accommodate them.

The Section makes it clear that the Purchase Option Price is the maximum price that may be charged in any circumstances, regardless of whether the CLT has exercised its option or the Homeowner is selling the Home directly to another buyer.

In Version 1 and in Version 2, the purchase option price is the lesser of the Formula Price or the appraised value of the Home (improvements only). In versions 3 and 4 the purchase option price is the lesser of the Formula Price or a certain percentage of the appraised value of the whole property (Homeowner's Ownership Interest), as noted in the commentary on those versions.

10.10 Calculation of the Formula Price

See Chapter 12, "Resale Formula Design," for a full discussion, including examples, of the improvements-only appraisal-based formula presented in this version, as well as the other possible types of appraisal-based formula.

As with other types of appraisal-based formulas, the percentage of appreciated value allocated to the homeowner by improvements-only appraisal-based formulas need not be 25%. Though 25% is common, the percentage can be set at higher or lower levels – and the formula can also allow the percentage to increase incrementally with increased years of ownership.

10.11 Qualified Purchaser to Receive New Lease

Early versions of the Model allowed the existing lease to be assigned to purchasers of the home, rather than requiring the issuance of a new lease. However, as the remaining term of an existing lease diminishes over time, the right to a new full-term lease becomes an increasingly important protection for a purchaser (and thus for a seller in search of a purchaser). Therefore, in practice, most CLTs have chosen to give a new full-term lease to all purchasers. This 2011 version of the Model makes this practice an explicit requirement. It also departs from earlier versions of the model in describing the terms that the new lease must contain. Whereas previous versions gave the purchaser a right to a new lease "substantially the same as" the old lease "in the rights, benefits and obligations assigned to Lessee and Lessor," the current version states that, "The terms of such lease shall be the same as those of *new leases issued to homebuyers at that time* for land not previously leased by the CLT." This change was occasioned by the fact that a number of CLTs have found compelling reasons to add significant features to their ground leases, such as provisions for a repair reserve fee (now included as a component of the lease fee in section 5.1 of the Model) and maintenance of repair reserves (see Section 7.6 and related commentary). Such provisions substantially strengthen a CLT's ability to see that the quality of its homes is preserved over

the long term, and it has therefore seemed important that a CLT be able to add such provisions to new leases when existing CLT homes are resold.

10.12 Transfer Fee

It is clear that money collected by CLTs through a monthly lease fee is not sufficient to cover the costs entailed by their ongoing stewardship responsibilities – particularly the responsibilities involved in overseeing the resale of homes. Many CLTs now do charge a “transfer fee” to cover the costs related to oversight of resale. This section (new in the 2011 Model) introduces language permitting such a fee to be added to the purchase option price and paid to the CLT in all situations where the CLT does not directly exercise its purchase option and take title to the improvements. (If the CLT *does* exercise the purchase option it, does not need the lease to authorize a transfer fee: it can simply mark up the price to the next homebuyer or charge a fee for assigning the option to the next buyer.)

CLT leases that provide for transfer fees generally cap the amount of the fee at percentages of the purchase option price ranging up to 6% (i.e., up to the amount that might be charged by conventional real estate brokers). CLTs can of course waive or reduce the fee as necessary to preserve affordability.

10.13 Repair Requirement at Transfer

The requirement that the Homeowner make necessary repairs at transfer is another provision that is new with the 2011 version of the Model. The section clearly assigns to the Homeowner a responsibility that, in the absence of this provision, the CLT itself might have to assume. The process – with necessary repairs identified through a professional inspection – parallels what is typical with conventional real estate transactions, where the seller normally expects either to pay for such repairs prior to the transaction or to accept a reduced price.

The second paragraph under “d” should be included only if the lease does in fact include provisions for a repair reserve fund (see commentary on Section 7.6).

VERSION 2

In which:

- a) The Homeowner *does* have an absolute right to select a buyer.
- b) An “improvements-only appraisal-based formula” is used.
- c) The original Base Price is *not* greater than the original appraised value of the Home.

Section 10.6 Homeowner Has a Right to Designate a Qualified Buyer

Section 10.7 CLT May Exercise Purchase Option if Homeowner Does Not Sell To a Qualified Buyer

Version 2 differs from version 1 only in the content of these two sections (which replace the single section 10.6 in Versions 1, 3, and 4). The provisions of these two sections of Version 2 are necessarily more elaborate, since they entail two separate processes and the relationship between them: (a) the process by which the Homeowner is allowed to designate a buyer and (b) the process by which the CLT can exercise its purchase option if the Homeowner does not designate a qualified buyer or does not proceed to sell the Home to a designated buyer.

CLTs that choose this approach are likely to be less concerned with seeing that homes are sold to prequalified buyers from their waiting list (or may have no waiting list), and more concerned with giving their homeowners a significant right usually enjoyed by conventional

homeowners – the right to sell the home to whomever they wish. CLTs favoring this approach may in fact want to encourage homeowners to take responsibility for marketing the home themselves, so the CLT will need to spend less staff time on this process.

Section 10.6 requires a Homeowner who has identified a prospective buyer to submit documents that will allow the CLT to determine “that the prospective buyer is an income-qualified person who understands and accepts the terms of the Lease and that the price and other terms of sale are consistent with the terms of the Lease.” The documentation described here can be modified or supplemented by individual CLTs. The current version does not specify how income-eligibility must be documented but simply calls for “such documentation of household income as CLT’s policies then require for confirmation of a buyer’s income-eligibility.” Some CLTs have developed a form that the Homeowner can use (or is required to use) to report the required information. Some of these CLTs have attached such a form to the Lease as an exhibit. Some have not attached it to the Lease but have made such a form available to a Homeowner who designates a buyer. The advantage of the latter approach is that the form can be modified or updated from time to time without amending the Lease.

VERSION 3

In which:

- a) The Homeowner does *not* have an absolute right to identify a buyer.
- b) A “compound appraisal-based” formula is used.
- c) The original Base Price *is* (or *may be*) greater than the original appraised value of the Home.

Version 3 uses a “compound appraisal-based formula,” which gives the Homeowner a specified share of any appreciated value of the “Homeowner’s Ownership Interest rather than the appreciated value of the improvements alone. The Homeowner’s Ownership Interest is defined as that portion of the original appraised value of the entire property (land and improvements) that the Homeowner has paid for through the original Base Price.

Though they are a reasonable approach in any type of real estate market, compound appraisal-based formulas are most often used in expensive markets where the original Homebuyer’s Base Price is likely to be greater than the original appraised value of the Home (improvements only). In other words, the available subsidy will cover only a part of the market value of the land, leaving the Homebuyer paying a Base Price that must cover all of the value of the improvements plus part of the value of the land.

This type of expensive real estate market also calls for a way of defining the purchase option price that is different from the way it is defined in Versions 1 and 2. In Section 10.9 of Version 3, the Purchase Option Price is defined as the lesser of the Formula Price or the appraised value of “Homeowner’s Ownership Interest,” rather than the lesser of Formula Price or the appraised value of the Home (improvements only), as in Versions 1 and 2, since the latter approach could result in a Purchase Option Price that is less than the original Base Price even in an appreciating market (because the value of the improvements represents only part of the value that the Base Price covered).

Note that the approach taken in this version to defining the Purchase Option Price is *fair* even if the Base Price is *less than* the original appraised value. However, this approach becomes *necessary* (to avoid *unfairness*) in any situation where the Base Price is *greater* than the original appraised value. Therefore, if a CLT does not know whether its base prices will

be greater than original appraised values but has reason to believe that base prices *could* be greater than original appraised values in some circumstances, it should define the Purchase Option Price as the lesser of the Homeowner’s Ownership Interest or the formula price. However, in defining the formula price, it may still choose to use an indexed or fixed-rate approach (as in version 4 below) rather than the compound appraisal-based formula used here in version 3.

Section 10.5 Appraisal

Because all resale price calculations in this version (in both sections 10.9 and 10.10 start with the value of the entire property rather than the value of the improvements only, the appraisal called for here does not require separate valuation of land and improvements.

10.9 Purchase Option Price as Lesser of Appraised Value of Homeowner’s Ownership Interest or Formula Price

Because the concept of “Homeowner’s Ownership Interest” is essential to both sections 10.9 and 10.10 it is identified here in section 10.9 only through reference to section 10.10.

Section 10.10 Calculation of Formula Price

The logic of compound appraisal based formulas is simple: the Homeowner is allotted a portion of the appreciated value of that part of the total value that Homeowner has paid for. However, the calculations required to apply the formula can be confusing and can result in errors if care is not taken. Some CLTs have therefore included in the lease a form such as the following:

1	Homeowner’s Base Price, as stated above.	\$
2	Initial Appraised Value, as stated above.	\$
3	Ratio of Homeowner’s Base Price to Initial Appraised Value, as stated above (equal to line1 divided by line 2).	___.%
4	Appraised Value at Time of Resale: Determined in accordance with Section 10.5 above.	\$
5	Total Appreciated Value: Subtract line 2 from line 4.	\$
6	Portion of Appreciated Value to be shared: Multiply line 5 by line 3.	\$
7	Homeowner’s Share of Appreciated Value: Multiply line 6 by 25%	\$
8	Resale Formula Price: Add lines 1 and 7.	\$

Whether such a table is actually included in the lease, or not, it can be duplicated in the form of a live spreadsheet that can be used in doing actual calculations at the time of resale – and perhaps also in presenting sample calculations in the course of orienting CLT homebuyers.

VERSION 4

In which:

- a) The Homeowner does *not* have an absolute right to select a buyer.
- b) An “indexed” formula is used (with 3 different “indexes” described in three alternative versions of section 10.10).
- c) The original Base Price *is* greater than the original appraised value of the Home.

In Version 4, the section that appears as “10.5 Appraisal” in Versions 1, 2, and 3 is omitted, since the formulas used in this version are not appraisal-based. An appraisal is not needed to determine the purchase option price, except in certain circumstances as noted below. (The buyer’s mortgage lender will still want an appraisal, but for a different reason.)

10.8 Purchase Option Price as Lesser of Appraised Value of Homeowner's Ownership Interest or Formula Price

Version 4 is like Version 3 in that the Purchase Option Price is defined as the lesser of the Formula Price or the appraised value of "Homeowner's Ownership Interest," rather than the lesser of Formula Price or the appraised value of the Home (improvements alone). Unlike Version 3, however, Version 4 does not use a compound appraisal-based formula. So the value of "Homeowner's Ownership Interest," cannot be established through reference to section 10.10, and is calculated instead within section 10.9.

As noted in the commentary on Version 3 above, the definition of the Purchase Option Price in terms of the "Homeowner's Ownership Interest" is *necessary* (to avoid *unfairness*) whenever a CLT's base prices *could* be greater than original appraised values in some circumstances.

10.9 How the Value of Homeowner's Ownership Interest Is Determined

Version 4 does not provide for an appraisal *unless* the CLT believes that the value of the Homeowner's Ownership Interest is less than the Formula Price. If the CLT does believe that this may be the case, the first paragraph of section 10.9 gives the CLT the option of commissioning an appraisal of the combined value of the Land and improvements in order to calculate the value of the Homeowner's Ownership Interest.

It should be noted that, although an appraisal may not be required to establish the resale price when the Homeowner intends to sell, it *is* necessary to establish the Initial Value through an appraisal when the Homeowner purchases the Home, and to enter this amount (together with the Base Price and the ratio of the Base Price to Initial Value) in the second paragraph of this Section 10.9. The appraisal required by the Homeowner's mortgage lender may be used as the basis for establishing the Initial Value. An appraiser who is determining the value of the leasehold estate as collateral for a leasehold mortgage must first determine the value of the entire property (before then breaking out the separate values of the leased fee and leasehold interest), so the Initial Value can be drawn from such an appraiser's report, but it is again important to note that this amount is not the same as the value of the leasehold estate, which is the lender's ultimate concern.

Section 10.10 Calculation of Formula Price

Three different formulas are presented in the three variations of this 10.10 – a formula using a CPI index, a formula using area median income as an index, and a formula that increase the purchase option price by a fixed rate of "interest." Although the last of these does not involve an index, it is like the indexed formulas in that it applies a single factor to the original Base Price to determine the purchase option price, and it affects the other sections of this article in the same ways as the indexed formulas do.

See Chapter 12, "Resale Formula Design," regarding the considerations involved in choosing an indexed formula.

ARTICLE 11: Reserved

In previous versions of the Model, this article dealt with assignment of the lease and subleasing. In the current version, (a) assignment is no longer permitted under section 10.11, which now calls for a new lease whenever the Home is sold, and (b) the subject of subleasing is dealt with in Section 4.5, immediately following the occupancy provisions in Section 4.4. We have retained Article 11 as "Reserved" for whatever additional provisions a CLT may

wish to include, rather than allowing the numbering of articles in this version to differ from that in previous versions.

ARTICLE 12: Default

If an action or omission of the Homeowner rises to the level of a defined event of default, then the remedies available to the CLT will force the homeowner to give up the home. For this reason, this Model builds in fairly generous rights to cure violations by the Homeowner.

Section 12.1 Monetary Default by Homeowner

Earlier versions of the Model provided for notification to Permitted Mortgagees regarding a lease violation only after the expiration of an initial 30-day “grace period” during which the Homeowner had a right to cure the violation. There was then an additional 30-day period during which the Permitted Mortgagees could cure the default. However, a good deal of confusion resulted when a mortgage lender required that it receive copies of *all* “notices of default” under the Lease and have an immediate right to cure such defaults. More recent versions of the Model take the simpler approach of requiring that a notice of Homeowner’s violation of the Lease be sent to any Permitted Mortgagee at any time such notice is sent to the Homeowner (see PERMITTED MORTGAGES, section B(6)). This Section 12.1 then provides for a 30-day cure period during which *either* Homeowner or Mortgagee may cure the violation.

Section 12.2 Non-Monetary Default by Homeowner

Considerations involving protection for both Homeowner and CLT are approximately the same for non-monetary violations as for monetary violations. Note, however, that the Model provides for a longer cure period in the case of non-monetary violations, since violations of non-monetary provisions may be more complicated and time-consuming to correct.

As discussed in Chapter 20, “Financing CLT Homes,” mortgagees may have particular concerns with the possibility of non-monetary defaults, since it will normally be impossible for the mortgagee to cure such defaults (e.g. a violation of the owner-occupancy requirement). Some national financial institutions have therefore insisted that a lease rider eliminate such a possibility during the life of the mortgage in question. (However, the Fannie Mae “Uniform Rider” does allow defaults relating to the two non-monetary requirements of greatest concern to CLTs: resale restrictions and owner-occupancy requirements.)

In order to address mortgagees’ concerns with non-monetary defaults, Some CLTs have provided for substantial fines for non-monetary violations. A failure to pay such fines becomes a monetary default, which a mortgagee has the ability to cure. Any such fines for major violations, such as unauthorized subleasing, must be heavy enough so that it will not be in the homeowner’s interest to just pay the fine and continue the violation.

12.4 CLT’s Remedies: Termination or Exercise of Purchase Option

The provisions for termination of the lease and eviction of the homeowner (Section 12.4-a) have been a standard part of all versions of the Model Lease and the CLT leases based on the Model. Such provisions have rarely – if ever – been fully implemented and carried through to actual termination and eviction, but their presence in the Lease provides important leverage for any CLT that must deal with a serious violation. The language in this 2011 version has been modified to make it clear that, upon termination of the lease, the CLT’s right to enter and reposes the Home and evict the Homeowner is subject to whatever due process is established by applicable law. No CLT should attempt to follow through with termination

and eviction without the involvement of an attorney who is familiar with the law affecting that process.

The provision for exercise of the purchase option (Section 12.4-b) has been added to the 2011 version of the Model and is based on language used by some California CLTs. Its enforceability may vary from one jurisdiction to another. Some CLTs may choose not to include it in their lease. Those that do wish to include it should consult with their attorneys regarding its enforceability and potential consequences. When it can be exercised, however, it can be an easier, friendlier remedy than termination and eviction.

12.5 Default by CLT

The CLT does not want to be too quickly subject to being in default if the Homeowner is looking for a “technicality” to which to object. On the other hand, the CLT does have certain important responsibilities under the Lease, and the Homeowner should not be hurt by too long a failure of the CLT to perform its obligations. The time period in this section is again a suggested reasonable compromise.

ARTICLE 13: Mediation and Arbitration

Previous versions of the Model Lease have not provided for mediation but have called for a specific arbitration process, as follows.

13.1 ARBITRATION PROCESS: Should any grievance or dispute arise between Lessor and Lessee concerning the terms of this Lease which cannot be resolved by normal interaction, the following arbitration procedure shall be used.

Lessor or Lessee shall give written notice to the other of its selection of a disinterested arbitrator. Within fifteen (15) days of the receipt of this written notice, the other party may give written notice to the first party appointing a disinterested arbitrator of its own choice. These two arbitrators shall select a third arbitrator. If the other party fails to name an arbitrator within fifteen days of receiving the notice from the first party, the arbitrator selected by the first party shall be the sole arbitrator.

The arbitrator or arbitrators shall hold a hearing within thirty (30) days after the initial written notice by the initiator of the arbitration process. At the hearing Lessor and Lessee shall have an opportunity to present evidence and question witnesses in the presence of each other. As soon as reasonably possible, and in no event later than fifteen days after the hearing, the arbitration panel shall make a written report to the Lessor and Lessee of its findings and decisions, including a personal statement by each arbitrator of his/her decision and the reasons for it. The arbitrators shall decide the dispute or claim in accordance with the substantive law of the jurisdiction and what is just and equitable under the circumstances. The decisions and awards of the majority of the arbitration panel shall be binding and final.

Some CLTs have provided for mediation as a first step, but have then provided for arbitration if either party is not satisfied with the results of mediation – with the arbitration process described more or less as stated above.

It is important to note that the effect of an arbitration provision in a lease will vary from state to state. Some states (e.g., California) have very detailed statutes concerning arbitration clauses and the effect a court must give to an arbitration award. Other states do not have such

a statute, but typically judicial decisions will try to give an arbitration requirement the effect of making an attempt at arbitration a prerequisite to a lawsuit.

In the 2011 version of the Model Lease, the more specific arbitration *requirement* has been replaced with a broad statement of what is *permitted* (any form of mediation or arbitration that the parties agree to pursue). The reasons for the change are (1) the variations in the legal treatment of arbitration from state to state, and (2) the fact that an arbitration process can be as time-consuming and expensive as the court process it is intended to replace.

Before a CLT chooses either to adopt the new short version of Article 13 or to include a specific arbitration provision, it would be advised to ask its attorney to determine how the law of the state in question deals with the arbitration process and its effects.

ARTICLE 14: General Provisions

This article contains a number of provisions that do not fit elsewhere in the Lease. In addition to the provisions included in the Model, a CLT may wish to include other provisions, such as those that its attorney finds necessary or useful with regard to specific features of local or state law.

Section 14.1 Homeowner's Membership in CLT

It is the practice of most CLTs for Homeowners to be entitled to CLT membership without having to do anything more. This Section should, of course, be consistent with the bylaws and other organizational documents of the particular CLT (see Chapters 4 & 5 regarding bylaws issues).

Section 14.2 Notices

Notice provisions are often ignored as “boilerplate.” This is unfortunate, as in many states the notice provisions of a lease are strictly interpreted by courts when one party is attempting to terminate the significant property rights of the other party. Timing is important. In an area where mail service is slow, the effective date of a notice could be made two business days after deposit in the mails, or upon actual delivery by hand, whichever is earlier.

Section 14.4 Severability and Duration of

As discussed in Chapter 10, “Legal Issues Re. CLT Ownership,” some question may arise as to whether a particular provision of the Lease violates the Rule Against Perpetuities. Although, as is demonstrated in Chapter 9, “The Enforceability of the CLT’s Preemptive Right,” the Lease should withstand such a challenge, it is prudent to protect against an adverse outcome. Therefore, this “savings” clause is designed to accomplish two goals. First, it contains standard language stating that the invalidation of one provision of the Lease does not invalidate the Lease as a whole. Secondly, it provides “measuring lives” for the purpose of determining the applicable time period under the Rule Against Perpetuities. If a court were to find some “interest” in the Lease to be subject to the Rule, that interest should at a minimum survive for the duration of the measuring lives plus 20 years (or, stretching all the way, 21 years). Given a large group of measuring lives including infants, odds are high that the interest would last the full 99 years of the Lease even in such a worst case legal situation.

Note that some states have taken the approach of the Model Rule Against Perpetuities statutes and exempted all “nondonative” transactions from the common law rule (see, e.g., Mass. Gen. Laws, Ch. 184A, Sec. 1). In those states it would be prudent to specifically refer also to the statutory exemption.

Section 14.5 Right of First Refusal in Lieu of Option

In the event that foreclosure of a Permitted Mortgage eliminates the CLT's option to purchase for a restricted price [see Exhibit PERMITTED MORTGAGES, B(7)], the CLT will want an alternative means of "recapturing" the housing. This Section therefore says that if for any reason the purchase option is not available, the CLT still has a "right of first refusal." The price to the CLT in such a situation would of course be established by a third party in an open market situation. (In a foreclosure situation, the CLT may also have an opportunity to buy the home back directly from the mortgagee for the amount owed the mortgagee [see Exhibit PERMITTED MORTGAGES, A(3)] The right of first refusal thus represents a last-resort means of regaining control of the home.

Note that in early versions of the Model this provision of a right of first refusal appeared as the final section of Article 10, following the provisions relating to the purchase option. In later versions it has been moved out of Article 10 so that there will be no possibility of its being wiped out in a foreclosure situation along with the purchase option provisions it is intended to replace as a fall-back measure.

The specific terms of this right of first refusal (as well as the separate right of first refusal established in Section 3.3) are spelled out in Exhibit FIRST REFUSAL.

Sections 14.6 - 14.11

These are all standard lease clauses. Section 14.6 is intended to protect the CLT against arguments that its conduct implicitly waived rights that were otherwise explicit in the Lease. Section 14.7 deals with potential challenges to title affecting the Homeowner's occupancy, and obligates the Homeowner to give "all reasonable aid" in such actions. This is a corollary to Section 2.1, in which the Homeowner takes its leasehold without any representations from the CLT and without an obligation of the CLT as lessor to defend title actions. Section 14.8 makes it clear that, in the language of the Lease, no pronouns are intended to be restrictive as to gender or number. Sections 14.9 and 14.11 address different aspects of legal interpretation of the language of the Lease, stating what might be the rule anyway if the clauses were not included. And Section 14.10 in several ways points out that the Lease is a document that is intended to stand on its own and govern the CLT-Homeowner relationship notwithstanding discussions to the contrary and changes in the parties unless the parties go through the formality of a written amendment of the Lease. The effectiveness of such provisions will vary from jurisdiction to jurisdiction.

Section 14.12 Recording

In many states, the recording of a lease or some notice that the lease exists is essential for the rights of the Homeowner to be protected against the rights of the holder of a mortgage on the fee interest in the land. For example, Mass. Gen. Laws, Ch. 183., Sec. 4. provides that any lease for greater than 7 years must be recorded, or a notice thereof must be recorded, in the appropriate registry of deeds or the leasehold interest is subject to foreclosure by a mortgagee, even one with a mortgage recorded subsequent to the date of such unrecorded lease. In the CLT context, if the CLT were to obtain financing (including subsidies structured as deferred loans to the CLT) secured by a mortgage of its fee interest in the land, and that lender were to foreclose, the lease might be "wiped out" if there were not recorded notice of its existence. There are other doctrines of actual notice which might protect the Homeowner, but the safest method is for there to be a recorded notice of the Lease.

¹ Mass. Gen. Laws, Ch. 59, Sec. 59.