Fair Market Valuation
of Resale-Restricted Affordable Housing Properties

Prepared by the Northwest Community Land Trust Coalition
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Summary

Community Land Trusts (CLTs) are non-profit organizations that provide affordable homeownership opportunities for low- and moderate-income households. Typically, the CLT does this by holding title to the underlying land and executing a long-term lease with the homeowner which restricts the resale price of the property in order to maintain affordability for future buyers. Currently, there is no uniform method for valuing these properties. In some counties, the properties are being valued without regard to the restrictions, resulting in a valuation that is substantially higher than the true and fair value of the property. In other counties, the properties are being valued with regard to the restrictions, but in a non-uniform manner.

County Assessors, CLTs, and homeowners of resale-restricted properties would all benefit from a Department of Revenue property tax advisory that provides guidance on the proper valuation of resale-restricted affordable housing properties and that takes into account the legally enforceable resale restrictions and affordability covenants encumbering such properties. The Northwest Community Land Trust Coalition is prepared to provide assistance to the Department of Revenue in its preparation of this advisory.

What is a Community Land Trust?

Even in difficult economic times, the increase in home prices in many parts of Washington continue to outpace any rise in incomes. Finding ways to keep homeownership within reach for low- and moderate-income families remains a top priority for our state. One solution to the affordability crisis has been to offer developers incentives to build homes that will be sold at below market rates. Another approach has been to provide buyers with down payment assistance and special loan programs. In both instances, the assistance programs focus only on the first generation of buyers. This means that the house may not remain affordable and buyers may reap a "windfall" when they sell their home for its full market value. Community Land Trusts (CLTs) are non-profit organizations whose mission is to increase the supply of *permanently* affordable housing. They do this by helping income-qualified families purchase affordable homes, while placing resale restrictions on those homes to preserve affordability for future buyers.

Under the typical CLT strategy, the CLT holds title to the underlying land, which it leases to the homeowner for a low rate under a long-term (99 year) renewable, inheritable lease. Under the terms of the lease, the home buyer agrees to restrict the resale of the home by an agreed-upon formula, which may involve a fixed annual appreciation cap, an increase in value tied to another index like CPI, or a percentage of annual appreciation. The homeowner is able to build equity in the home, though not as much as in the private market. By capping the home's appreciation, the CLT strategy is unique in its ability to guarantee a permanent supply of affordable homes.

The Valuation Problem
Calculating True and Fair Value for Resale-Restricted Properties

Resale-restricted properties are generally sold for considerably less than comparable, non-restricted properties, but County Assessors are given insufficient guidance to address resale-restricted properties. As a result, property tax assessments on these properties are currently being calculated differently from county to county. In a number of counties, Assessors are requiring owners of resale-restricted properties to pay taxes on values substantially higher than the value the taxpayer will ever be able to realize through the sale of the property. Excessive tax assessments on resale-restricted properties results in an unfair burden for the owners of these homes and is contrary to the CLT program's charitable purpose.

One suggestion is that CLTs apply for an exemption on CLT resale-restricted properties. CLTs believe the better approach is to have homeowners leasing CLT resale-restricted properties continue to pay the property taxes on the land and improvements, but find a way to assess these properties fairly and uniformly and in a manner that takes into account the resale restrictions.

RCW 84.40.030, the statute defining the basis for valuation, requires that "[all] property shall be valued at one hundred percent of its true and fair value in money and assessed on the same basis unless specifically provided by law." WAC 458-07-030(1) interprets the phrase "true and fair value in money" to mean "market value," which is "the amount of money a buyer of property willing but not obligated to buy would pay a seller of property willing but not obligated to sell, taking into consideration all uses to which the property is adapted and might in reason be applied." Thus, when determining market value, County Assessor must consider all factors that can, within reason, affect the price in negotiations between a willing buyer and a willing seller. These factors would include restrictions on use or sale of the property resulting from a resale restriction that encumbers the land through a lease or covenant for up to a 198-year period.

The statute then goes on to provide the criteria on which to base the true and fair value of real property for taxation purposes. These criteria include the sale of the same or similar property within the past five years. However, "[I]n the case of property of a complex nature, or… not having a significant number of sales of similar property in the general area, the provisions of [subsection (2) of the statute, the cost and income approaches] are relied upon for establishing values…" Because of their resale restrictions and long-term lease requirements, CLT properties exemplify properties of a complex nature in which there are not a significant number of sales of similar property to justify use of the comparable sales method over some other method.

In addition, RCW 84.40.030(3) and WAC 458-070-030(5) state with regard to real estate assessments that "*the valuation shall not exceed the true and fair value of the total property as it exists.*" The true and fair value of CLT properties is directly controlled by the legally enforceable resale restrictions encumbering the land through a lease or covenant for up to 198 years.

Finally, RCW 84.40.039 provides that the "person responsible for payment of taxes on any real property may petition the assessor for a reduction in the assessed value … within three years of adoption of a restriction by a government entity." The term "restriction" is defined in this section as "a limitation, requirement, regulation, or restriction that limits the use of the property, including those imposed by the application of ordinances, resolutions, rules, regulations, policies, statutes, and conditions of land use approval." The legally enforceable resale restrictions encumbering CLT properties would qualify as "restrictions" within the meaning of RCW 84.40.039 in situations where they are imposed by a government entity, such as where they are made a condition of an affordable housing agreement between a CLT and the Washington State Housing Finance Commission.

Recommended Valuation Approach

The approach described below provides a uniform methodology for determining the true and fair value of resale-restricted properties. If the long-term lease and resale restrictions to which a particular property is subject were ever removed, the valuation would convert back to a standard comparable sales approach.

CLT Resale-Restricted Property Approach	
Eligibility To be assessed as a resale-restricted property, the real property must be:	Encumbered by a durable restriction on the property's resale price or other component of economic value for the purpose of providing affordable housing. The resale restriction shall be set forth in a ground lease or covenant, conveying certain rights for the use of land on which housing is to be built or already exists, or shall be set forth in a separate and distinct document, entitled "housing affordability covenant," and shall run with the land. The ground lease or housing affordability covenant generally has a term of not less than 99 years.
Valuation The property valuation would be calculated in a two-fold manner:	1. The *land value* would be based on an income approach, capitalizing the income stream from the land rent stipulated in the applicable ground lease or other covenant; and 2. The *house value* would be valued at the maximum resale price determined by the recorded lease agreements or covenants.
Duration	Once a property has been classified as eligible "resale restricted affordable housing property" for purposes of valuation, it shall remain so classified until the removal of the restriction.

Conclusion

The Northwest Community Land Trust Coalition is grateful to the Department of Revenue for its work to address this issue of critical importance to CLTs, our donors, and the families we serve. There are currently over 250 households in Washington State living in resale-restricted properties, and the number will continue to grow as CLTs produce more perpetually affordable homeownership opportunities. Under existing Washington law, the true and fair valuation of the land must take into account all factors on the land that would affect the sale price. As some County Assessors recognize, this should include accounting for legally enforceable resale restrictions encumbering the land through a lease or covenant for up to 198 years. The approach proposed above provides County Assessors with a uniform approach to valuing these properties and a clear understanding of which properties should qualify as "resale-restricted" affordable homes.