

Advisory Opinion
[Samuel Adams]
Case No. 05010.A, Interest in City Business
April 13, 2005

You are Commissioner of the City's Department of [] . In a March 3, 2005 letter, you requested an advisory opinion addressing whether the Governmental Ethics Ordinance restricts or prohibits City employees from participating in the program established by authority of the City's Affordable Housing Commitment Ordinance (the "AHCO")¹. After carefully considering the facts presented, the Board has determined that the Governmental Ethics Ordinance: 1) prohibits City employees from purchasing any unit of affordable housing through this program if the difference between the unit's market price and affordable price, or the "City Subsidy Recapture Amount," is \$5,000 or more, and 2) does not prohibit City employees from renting units offered through this Program. Our analysis follows.

FACTS: The City's Affordable Housing Requirement Ordinance Program (the "Program") was created when the City Council passed the AHCO on April 9, 2003. Under the Program, persons who develop residential housing projects and receive City assistance, either in the form of grants, loans, tax credits (including Tax Increment Financing, or TIF, assistance), or who construct the units on real estate sold by the City at less than fair market value, are required to develop a percentage of the housing units at "affordable"² prices and make them available to qualifying buyers or renters. If the units are constructed on land conveyed by the City at less than market price, the developer must establish at least 10% of the units as affordable housing; if the developer receives City financial assistance, the affordable "set asides" must be at least 20% of the units. §2-44-090(b), -(c). A developer may establish affordable housing by developing the required number of units, or by paying a fee of \$100,000 for each affordable housing unit not developed, or through any combination thereof. Fees are deposited into the Affordable Housing Opportunity Fund, which is administered by [G] department; the Fund then invests and disburses its assets to construct affordable housing and provide rent assistance, as provided in §2-44-090(e) of the AHCO.

[G] staff explained that developers typically begin the process of constructing and marketing affordable housing by meeting with the Department of [L] . After receiving its approval, the developers meet with [G] staff to discuss and finalize Program requirements. The final development, complete with affordable housing component, is presented to City Council for final approval.

Buyers and renters of affordable housing units through this Program do not receive any subsidy directly from the City. Rather, developers (some of whom receive City financial assistance) make

1. This Ordinance is codified in the City's Municipal Code as §2-44-090 et seq., and attached to this opinion as Exhibit 1.

2. The AHCO defines "affordable housing" as rental housing affordable to households earning up to 60% of the Chicago Primary Metropolitan Statistical Area median income, or owner occupied housing affordable to households earning up to 100% of that median income figure.

the units available to eligible buyers or renters at below market prices. Prospective buyers of affordable units apply to [G] and submit income affidavits and tax returns. [G] then verifies their eligibility to participate in the Program and buy the units. If approved, buyers, at closing, and in addition to the other closing documents signed with the home's seller, enter into a "Mortgage, Security and Recapture Agreement" (the "Mortgage Agreement") with the City (see below; a copy of such an agreement, which [G] staff provided, is attached as Exhibit 2). Applicants wishing to rent housing through this Program apply directly to the developers or property owners, who then determine their eligibility to participate, and report to [G] annually regarding these leases. Approved renters do not enter into any agreements with the City. Members of [G] staff explained that this provision creates, in effect, a separate "market" for affordable housing.

The AHCO specifies that rentals and sales of affordable housing units developed under the Program shall be made only to households meeting the income eligibility criteria, unless the units' sellers or owners pay the "recapture fees" (described below). §2-44-090(g). It also provides that an "affordable housing unit required by this Ordinance shall continue to be affordable housing for a period of 30 years" after its initial sale or lease, unless either: 1) the property is foreclosed upon or condemned; or 2) its owner sells or leases it for more than the affordable price or to a household that does not meet the income-eligibility criteria. §2-44-090(i). To ensure that such housing remains affordable, the AHCO provides that if, during the 30-year period after the initial sale or lease, the owner of an affordable unit sells or rents it for more than the affordable price (or rental rate), or to a household that does not meet the income-eligibility criteria, a "recapture fee" must be paid. For sales of affordable units, the recapture fee equals the difference, at the time of the unit's initial sale, between the unit's appraised market price and its affordable price, plus 3% per annum in simple, non-compounded interest from the date of the initial sale, and is a sum certain in all cases (in some cases, the interest is 1% per annum). For rental units, the AHCO specifies that the property's owner (or landlord) must pay a fee of \$500 per unit per day that the owner or landlord is "in noncompliance," that is, as long as there is a lease at above the affordable rate.³

For sales of affordable units under this Program, at the closing of the home's sale to its first income eligible buyer, the City (as Mortgagor), enters into the Mortgage Agreement with the buyer (as Mortgagee). Through the Mortgage Agreement, the City "records" its lien for each affordable unit sold, in order to secure the "recapture fee" in the event it is triggered. This is one of the purposes of the Mortgage Agreement, which recites the following: "WHEREAS, the City has required Mortgagor to execute this Mortgage in order to both (a) impose the Affordability Requirements upon the Mortgaged Property and give notice of the Affordability Requirements to Mortgagor, to any subsequent purchaser of the Home, and to any lender having a mortgage secured by the Home, and (b) to secure the recapture payment described" later in the Mortgage Agreement. [G] staff confirmed that [G] will verify the income eligibility of all subsequent proposed buyers in the same manner as in the initial sale. In this way, the City's lien, which is represented by the Mortgage Agreement, becomes "attached" to the property, and, you said, acts as a "silent second" mortgage, entitling the City to recover the "City Subsidy Recapture Amount" if triggered during the 30-year

3. See § 2-44-090(i). According to [G] staff, the Program assumes that the price (or rental rates) of affordable units will remain constant, as the goal is to maintain property at affordable levels. However, it is consistent with the AHCO's purpose to allow buyers to take advantage of market value appreciation of their units by selling them for an amount above the affordable price, provided, of course, that the appreciation in value exceeds the amount they must pay to satisfy the City's lien or Mortgage Agreement—which is 1% to 3% per annum plus the difference between their unit's original affordable and market price.

“compliance period.” The Mortgage Agreement also recites that the Mortgagee—i.e. the buyer—acknowledges and agrees that the price of the home is less than fair market value by an amount equal to the City’s contribution (whether through TIF assistance, reduced sale price of land to the developer, etc.) and that the buyer is able to purchase the home for less than fair market value because of the City’s contribution (which has subsidized a portion of the construction cost of the home), and because of the affordability requirements of the AHCO and the Mortgage Agreement. (See Exhibit 2, Recitals, § 3.01.)

As provided for in the AHCO, and in the Mortgage Agreement, if, during this compliance period, the unit is sold to an eligible household, then that household, and all of its successors, assume this Mortgage Agreement. These parties thereby remain responsible for the “recapture fee,” which becomes due and payable if the property is sold (or leased) to a non-eligible household or at a price above the affordable housing price. (See Exhibit 2, Recitals, §§ 3.02, 3.03, 5.01, and Exhibit 2 thereof, which specifies the amount of the “City Subsidy Recapture.”) For rental units, the property owners/lessors enter into regulatory agreements with the City; renters of units are not parties to or liable under these regulatory agreements.

In most instances involving unit sales, [G] staff explained, the amount of the lien, or the “City Subsidy Recapture Amount,” is (and will be expected to be) more than \$5,000. Under this program, the City has, to date, recorded several hundred liens, but none have yet become due and payable. [G] staff’s current estimate is that approximately several hundred such units will be developed per year. [G] staff also said that there are no rental units under this Program to date, estimates that fewer than 100 per year will be developed. You ask whether City employees are restricted or prohibited from participating in this Program as eligible buyers or renters.

LAW AND ANALYSIS: The provision of the Governmental Ethics Ordinance relevant to your question is § 2-156-110, “Interest in City Business.” It states, in pertinent part:

No elected official or employee shall have a financial interest in his own name or in the name of any other person in any contract, work or business of the City, or in the sale of any article, whenever the expense, price or consideration of the contract, work, business or sale is paid with funds belonging to or administered by the City, or is authorized by ordinance.

“Financial interest,” defined in §2-156-010(I), means, in pertinent part, “(ii) any interest with a cost or present value of \$5,000.00 or more.” As the Board has interpreted this provision, City employees are prohibited from receiving loans from the City with a present value of \$5,000 or more (Case nos. 90075.A, 90076.A), or loans of \$5,000 or more if the program is administered by a City department but paid with non-City funds (Case nos. 90028.A, 90057.A). Under this Program, buyers and renters do not receive funds from the City. Rather, City financial assistance is directly extended to the developers. However, purchasers benefit—financially and quantifiably—from the City’s financial assistance to the developers, as this assistance (either tax credits, loans, etc., or below-market land sales) effectively lowers the purchase price of the units, usually for a sum certain greater than \$5,000, thereby enabling them to purchase otherwise unaffordable housing. In consideration for receiving this (albeit indirect) financial assistance, and for owning their home, buyers must contractually obligate themselves to repay the City for the amount of this City

assistance, plus interest, if they take advantage of market appreciation and sell (or lease) their unit at above the affordable price (renters also benefit from the City's financial assistance, but unlike purchasers, do not assume any legal or contractual obligations to the City, nor apply to [G] to be approved as renters). The City, through its Mortgage Agreement with the owner, which the property's subsequent owners remain responsible for satisfying, maintains a continuous (30 year) interest in ensuring that the buyer's ownership interest, i.e. the housing unit, remains at the affordable price. Clearly, this Mortgage Agreement, which the buyer applies to [G] to receive the right to enter into, and which the buyer signs, is a City "contract," or "work or business of the City." Further, the City Subsidy Recapture Amount, which the buyer contractually agrees to repay (plus interest) to the City upon sale of the unit under certain conditions, gives the buyer an interest in City business, and, if \$5,000 or more, gives the buyer a financial interest in City business. (We note that the Ordinance authorizing this Program, unlike Ordinances authorizing other [G] programs, does not contain an exemption to the Governmental Ethics Ordinance effectively allowing City employees to participate to the same extent as members of the general public.) Therefore, we conclude, were a City employee to purchase any unit of affordable housing through this Program, where the difference between the unit's market price and affordable price is \$5,000 or more, or the "City Subsidy Recapture Amount" (if the contract form of Exhibit 2 were used) is \$5,000 or more, that City employee would have a prohibited financial interest in City business.

In contrast, renters under this Program do not apply to [G] to be approved to rent units through the Program, do not obligate themselves to or sign any mortgages, pledges or other contracts with the City (for a sum certain or otherwise), and would not be obligated to pay any fees to the City in the event the unit were leased at rates above the affordable amount (the property owner would be so liable). [G], in fact, does not take an active role in monitoring the rental aspect of the Program, nor its participants. For these reasons, we conclude, renters do not have an interest in City business by virtue of their participation in the Program, and thus City employees are not prohibited from participating in it.

Our conclusion is supported by the Board's decision in Case No. 90075.A. There we also considered a housing assistance program (likewise administered by [G]) in which applicants received no funds directly from the City. We were asked whether City employees could participate in a program in which the City sold 40 City-owned lots to a developer for \$1 each, and waived fees (including outstanding sewer and water liens and miscellaneous construction fees) in connection with the development of housing units on the lots. Because (as with the rental aspect of this Program, but in contrast to its purchase aspect) the City had no further involvement in that program, and all decisions as to who would be allowed to participate in it were made by the developer, and because it was difficult to calculate the amount of financial benefit contributed to the participants by the City, we determined that City employees were not prohibited from participating in that program.

DETERMINATION: The Board determines that the Governmental Ethics Ordinance: 1) prohibits City employees from purchasing any unit of affordable housing through this Program if the difference between the unit's market price and affordable price, or the "City Subsidy Recapture Amount," is \$5,000 or more, and 2) does not prohibit City employees from renting units offered through this Program.

The Board's determination does not necessarily dispose of all the issues relevant to this situation, but is based solely on the application of the City Governmental Ethics Ordinance to the facts stated

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in this opinion. If the facts presented are incomplete or incorrect, please notify the Board immediately, as any change in the facts may alter the Board's opinion. Other laws or rules may also apply. The Board notes that any City department may adopt restrictions that are more stringent than those imposed by the Governmental Ethics Ordinance.

RELIANCE: This opinion may be relied upon by: 1) any person involved in the specific transaction or activity with respect to which this opinion is rendered; and 2) any person involved in any specific transaction or activity that is indistinguishable in all its material aspects from the transaction or activity with respect to which this opinion is rendered.

Michael F. Quirk
Acting Chair

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