

**PLAIN LANGUAGE POLICY GUIDELINES
FOR
SECTION 61 (FORMERLY 34.18)
CO-OPERATIVE HOUSING PROGRAM, AND
CO-OPERATIVES COMMITTED UNDER
SECTION 27 (FORMERLY 15.1)
OF THE NATIONAL HOUSING ACT**

These reader-friendly modules have been prepared in simplified non-technical language for the convenience of a general readership. They have been made available on the Agency's website for use by housing co-operatives who are interested in gaining an understanding of how the federally funded co-op programs work.

It is important to note that these modules do not replace CMHC's guidelines and policies. In the event of any conflict or lack of clarity, CMHC's guidelines and policies will prevail. Further, any and all references to the Agency should be interpreted to mean "the Agency on CMHC's behalf."

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1. OPERATING AGREEMENTS

The co-op is required to sign an operating agreement with CMHC and it has to execute a first mortgage on the housing project.

The operating agreement outlines the conditions under which a co-op must operate in order to continue benefiting from assistance provided under the *National Housing Act (NHA)*.

The operating agreement is in effect until the mortgage loan and interest are paid in full.

The co-op must comply with the operating agreement in order to earn the federal contribution, RRAP loan forgiveness, and interest reduction grants.

2. BREACH OF OPERATING AGREEMENT

If the co-op breaches the operating agreement, CMHC with the recommendation of the Agency may:

- obtain a court order to force the co-op to comply with the operating agreement (specific performance); or
- appoint a receiver to manage the project.

If the co-op breaches the operating agreement, CMHC can require immediate repayment of the mortgage loan. It can also increase the interest rate on the loan amount outstanding, including the unearned portion of capital grant and RRAP loan forgiveness.

2.1 *Federal Capital Contribution*

Under the National Housing Act, CMHC is permitted to make a 10% capital contribution based on agreed-to project costs to eligible co-operative housing organizations.

The contribution is earned in equal monthly instalments over the mortgage amortization period and is affected by a reduction in the mortgage payments.

If a co-op's mortgage is paid out early with the approval of CMHC, the co-op may be required to repay the unearned portion of the capital contribution.

3. INTEREST REDUCTION GRANT

Under the National Housing Act, CMHC may make an interest reduction grant to co-operative housing organizations which received a loan under Section 27 & 61 after December 31, 1975.

The amount of the interest adjustment grant is the difference between the maximum interest rate (under NHA Section 26 at the time of commitment) and the minimum interest rate as was prescribed by the then Governor-in-council, based upon the repayable loan after deduction of the 10% capital contribution.

4. RENT SUPPLEMENT

In some cases, Section 82(1)(b) Rent Supplement Program provides rent subsidies to eligible co-ops designated by the Province.

4.1 *Rent Supplement cost sharing*

The federal and provincial governments cost share the rent supplement program paying 50% each, based on a federal-provincial agreement where applicable.

Rent Supplement is administered by CMHC in some provinces and by the Province in others.

The exception is in Ontario, where 100% of the rent supplement program is paid by CMHC under the terms of the Federal/Provincial Social Housing Agreement.

Note: The actual ratio may vary when CMHC subsidies such as the preferred interest rate and the 10% capital contribution, are compared with provincial assistance, if any, granted to the co-op.

4.2 *Signed agreement with CMHC and the province*

Under the Rent Supplement Program, each co-op must sign an agreement with the province and/or CMHC. The co-op must agree to operate the project according to certain terms and conditions to qualify for monthly rental subsidies.

4.3 *Calculation of rent supplement*

Rent supplement is the difference between the housing charge as determined by the rent-geared-to-income scale and the economic rent as approved from time to time by the Active Party.

5. OCCUPANCY AGREEMENTS

Occupancy agreements may also be referred to as “leases”, although the more common and appropriate term for housing co-ops is occupancy agreements.

5.1 *Occupancy Agreement in accordance with the Operating Agreement*

The co-op has to rent units in accordance with the operating agreement, and enforce the term of the lease or occupancy agreement.

Occupancy agreements and leases must be in a form acceptable to the Agency.

5.2 *Parties to the occupancy agreement (does not apply to Section 27 Housing Co-ops)*

The occupancy agreement or lease must be signed by at least one adult in the household. If there are adult occupants who are not married or in a common-law relationship, each of those adults must sign the occupancy agreement.

5.3 *No agreement in excess of 12 months*

All occupancy agreements between the co-op and the household must give the co-op the right to change the housing charge annually.

5.4 *Income verification*

Income verification must be provided by all applicants prior to occupancy.

5.5 *Co-op to follow provincial laws and regulations*

The co-op must follow the provincial laws and regulations that govern how co-ops lease housing units. This applies to both members and non-members.

5.6 *Only persons named in the occupancy agreement to occupy a unit*

Only the people named in the agreement or lease will occupy the unit.

Subleasing is to be considered an exceptional tenancy arrangement. Co-ops may include language in the project occupancy agreement that prohibits subleasing.

6. SECURITY DEPOSITS OR PRE-PAID RENT

The co-op will adhere to the provincial laws that apply to co-op occupants in all occupancy matters, such as security deposits and pre-paid rent.

7. INCOME DECLARATION

Income verification must be provided prior to signing an occupancy agreement. To become or remain eligible for reduced housing charges, occupants must provide evidence of income satisfactory to the co-op each year. The co-op is responsible for collecting adequate proof of income.

8. INCOME LIMITS

8.1 *Maximum ingoing income limits*

In order to provide access to housing to low-and moderate-income families as prescribed by the *National Housing Act*, the maximum ingoing income for family and senior citizens in a self contained unit will be;

- The maximum of Statistics Canada’s “second quintile” of family income in that province as supplied annually by the Agency.

8.2 *Enforcing the ingoing income limit*

The co-op is responsible for enforcing ingoing income limits. If the co-op is unable to find eligible occupants because of the ingoing income limit, the Agency may approve an increase to the income limit in order to reduce vacancy loss and ensure project viability.

8.3 *Household income exceeds income limit*

A household occupying a unit will not be forced to move from the co-op if its income exceeds the income limit.

8.4 *Verification of ingoing income limits*

Annually, co-ops will verify that ingoing income limits are being enforced.

8.5 *Ingoing income limits come to an end*

Five years prior to repayment of the mortgage, ingoing income limits will no longer apply.

9. HOUSING CHARGES

The co-op will lease the housing units at or below a rental level acceptable to the Agency.

9.1 *Approval when adjusting occupancy charges*

The co-op shall seek Agency approval for any rental adjustment.

When the Agency reviews housing charges, it will recognize the need to fully recover all acceptable project operating costs from project revenue. The Agency does have the right to request changes to the occupancy charges.

9.2 *Changing housing charges more often than annually*

The co-op will not change the housing charge more often than once every 12 months unless;

- the operating agreement allows for changes more often, and
- the Agency approves an increase.

9.3 *Increasing housing charges*

The co-op may increase occupancy charges in order to recover a deficit. However, retroactive housing charges will not be approved.

9.4 *Notification of a housing charge change*

When housing charges change, the co-operative will notify the occupants in accordance with applicable provincial law.

9.5 *Maximum housing charges*

The maximum housing charge, including surcharges are set out in the operating agreement and cannot be changed without the written approval of the Agency.

10. NON-SHELTER COMPONENT

10.1 *Commercial space at full market rent*

Any commercial space should be rented at the greater of market or economic rent. Profit from commercial space is to be applied to the reduction of housing charges for the shelter component.

10.2 *Commercial space at break even*

Commercial space must at least break even. No deficits are to accrue to the shelter component.

A co-op may have operating costs for non-shelter components. The co-op cannot recover these costs from housing revenue.

11. RENTAL SURCHARGE

11.1 *Voluntary program*

Rental surcharging is considered a voluntary program feature.

11.2 *Definition of rental surcharging*

Rental surcharging is used to transfer funds within the co-op from higher income earners to lower income earners. This reduces the need for external subsidy, and helps to achieve an income mix.

11.3 *Decrease in surcharge*

Where housing charges, including the surcharge, exceed market rents, the amount of surcharge may be adjusted downwards temporarily, subject to the Agency's approval. The Agency may direct the co-op to make appropriate changes in the surcharge amounts.

12. PHYSICAL INSPECTIONS

12.1 *Review period for inspections*

The Agency will inspect a project every two years. The visual inspection will be limited to the exterior, common areas of the property, and vacant units unless the results of the

inspection indicate that an inspection including inspection of occupied units is also required.

12.2 *Property inspections*

The inspection will look at the property's marketability and overall upkeep, including standards of maintenance and repair.

12.3 *Full inspections*

The agency will carry out a full physical inspection if it determines that one is needed based on the results of the annual compliance analysis or after a property inspection. The Agency may also decide to carry out an inspection if the co-op breaches its operating agreement.

The Agency may require the co-op to have a building condition assessment carried out at the co-op's expense.

Based on the results of the building condition assessment, the co-op may be required to complete certain repairs or carry out general maintenance.

13. ON-SITE REVIEWS

13.1 *Triggers for on-site reviews*

If the Agency's risk assessment of the co-op or other indicators has raised compliance concerns, the Agency will initiate an on-site review.

13.2 *On-site review*

The Agency may

- review the books and records
- meet with the co-op's board, staff or committees
- inspect the property or the units
- carry out other examination and analysis as necessary

13.3 *On-site review report*

Following the on-site review the Agency will complete an on-site review report. A copy will be sent to the co-op's board of directors with the Agency's recommendations for improvements. The Agency will follow up, if necessary, to make sure the co-op is

complying with the operating agreement and addressing any problems identified in the on-site review.

14. MANAGEMENT

14.1 *Management in keeping with operating agreement*

The co-op is to keep to the terms and conditions of the operating agreement as it operates the project.

14.2 *Management*

The co-op is to manage the project effectively. It will maintain and repair the project based on professional management standards that, in the Agency's opinion, will reduce operating risk to acceptable levels.

The co-op can hire suitably qualified staff to manage the co-op. Except for the employment of its own staff the co-op will not enter into an agreement for management or maintenance services without the prior written approval of the Agency.

14.3 *Poor Management*

If the Agency believes that the co-op is not meeting the standards in **14.2**, it can require the co-op to make changes to the management of the project, even if the co-op is not behind with its mortgage payments.

If the Agency believes the co-op is in financial trouble, it can require the co-op to hire a professional manager. A professional manager means a firm or individual with the skills to assess project difficulties, and put in place ways to solve the problems and keep the problems from returning.

If the co-op breaches the mortgage agreement and will not agree to a management change that the agency thinks is necessary, the Agency will advise CMHC that professional management must be hired.

14.4 *Giving control of management back to the co-op*

When the Agency requires the co-op to hire professional management, it will give back the right to choose management to the co-op as soon as the Agency and co-op agree that the co-op is ready.

If there are outside directors on the board, the Agency will agree with the board on a plan to replace them with resident directors over time.

14.5 Governance

The co-op will ensure good governance of the association and its affairs by having a trained, committed board of directors.

Any board member or manager with a conflict of interest must tell the board that there is a conflict. That person may not take part in discussions or in making decisions about the matter that causes the conflict.

A conflict of interest can happen when a director, officer, employee or committee member is involved in co-op decisions that could give that person, or a relative or business associate of that person, some benefit the rest of the co-op wouldn't have.

14.6 Weak Governance

If the Agency believes that the co-op is not meeting the governance standards as set out in 14.4, the co-op may be asked to

- get training for board members
- require directors to resign if they are in breach of their duty
- hold elections for new directors to fill vacancies on the board
- appoint temporary directors from outside of the co-op

14.7 Administration Cost

When the Agency reviews the amount of expenses, it considers industry standards and best practices.

CMHC has historically used a 6% guideline to assess the reasonableness of administration costs. In effect, CMHC's guideline states that a co-op's administration costs should generally not exceed 6% of the total operating expenses including principal and interest payments. However, CMHC has recognized that many factors can affect the cost of administration for any given co-op and has considered these factors in applying the guideline. Until the Agency accumulates its own data regarding operating expenses for annual comparison, it will look to CMHC's administration cost guideline for comparative purposes.

15. ANNUAL INFORMATION RETURN - AIR

The Annual Information Return (AIR) is a new reporting document.

After the Agency has gathered and reviewed the data from the AIR, it will report to the co-op on its findings and analysis.

The annual key-indicators report will show how well the project has been performing. The report looks at income from housing charges and other sources, vacancy losses, turnover, households in arrears, bad debts, spending on upkeep and so on.

The report will also provide comparative information indicating project performance against the average performance of a similar project, and the whole portfolio.

16. FINANCIAL STATEMENTS

16.1 *Audited financial statements*

Within four months of the end of the co-op's fiscal year, the co-op has to send in its audited financial statements to the Agency, along with an Annual Information Return.

Audited financial statements include the:

- auditor's report,
- statement of financial position or balance sheet,
- statement of revenue and expenses for shelter and non-shelter components as applicable,
- statement of funded reserves,
- statement of cash flow,
- statement of changes in fund balance(s),
- notes to the financial statements, and
- Auditor's Confirmation.

16.2 *Duties of the auditor*

The auditor will complete and send in the Annual Information Return electronically.

The auditor will verify:

- the statement of financial position or balance sheet;
- the statement of revenue and expenses
- the statement of cash flow;
- the statement of changes in the fund balance,
- the statement of funded reserves, and
- the application of the rent-geared-to-income scale or rent determination process.

The auditor will provide a report saying whether:

- the audit has been conducted according to generally accepted auditing standards
- the financial statements fairly present the co-op's financial position
- the statements have been prepared according to Canadian generally accepted account principles, (GAAP) except for exceptions to GAAP required by CMHC

The auditor should also verify the Notes to the financial statements, as the Notes are an integral part of the statements.

16.3 *Auditors notes*

The notes must say whether or not the co-op has properly funded the replacement reserve fund. The notes must also say that the co-op has added investment earnings to the fund as required.

17. CONSOLIDATED FINANCIAL STATEMENTS

A co-op can provide consolidated financial statements for multiple projects, in which case the audit must have separate statements of revenue and expenditures for each project phase. In cases where consolidated statements are provided, disclosure should be provided for the funded reserves for each project.

18. OPERATING RESERVE

A project can accumulate up to \$500 per unit as an operating reserve, if the reserve is funded. This operating reserve will help absorb deficits from future vacancy losses and/or major maintenance and repair costs.

19. REPLACEMENT RESERVE

19.1 *Investing the replacement reserve*

The co-op can only invest replacement reserve money in investments insured by the Canada Deposit Insurance Corporation, by a credit union deposit insurance corporation or as otherwise approved by CMHC.

The replacement reserve fund and investment earnings of the fund must be shown separately in the co-op's books of account and on its financial statements.

19.2 *Replacement reserve – purpose of fund*

The co-op must maintain a replacement reserve fund. It uses this fund to replace or make all repairs to capital items. The capital items that can be replaced from the reserve fund are:

- a) **Major building components**
 - Roofs, including coating, flashing, eavestroughs and downspouts
 - Exterior wall finishes with a lower life expectancy than the rest of the project, including exterior painting and stucco

- Exterior doors and windows
 - Exterior caulking that is hard to reach and hard to replace,
 - Aboveground waterproofing, including vapour barriers
- b) **Major building services**
- Heating systems, including boilers (hot water or steam), forced air furnaces, radiant heat components, solid fuel burning systems, chimneys and related components
 - Domestic hot water tanks, booster pumps, circulating pumps and sump pumps found in multiple-unit buildings
 - Septic tanks and tile beds
 - Required air handling systems
- c) **Basic facilities**
- Kitchen facilities, such as stoves and refrigerators, sink and faucet installations, counter tops and cabinets
 - Bathroom facilities, such as toilets, sinks, vanities, tubs and fixtures
- d) **Safety features**
- Fire alarm systems, such as hardwired smoke alarms, and smoke and heat detectors linked to a central alarm
 - Required fire fighting or prevention equipment
 - Emergency lighting
 - Intercom systems in multiple-unit buildings
 - Other safety items
- e) **Other major facilities, equipment and features**
- Parking lots, enclosed garages and driveway and walkway surfaces, including multiple-unit garage surfaces and concrete slabs
 - Garbage disposal systems in multiple-unit buildings, such as compactors and disposers
 - Interior floor coverings, including those in common areas and suites
 - Exterior fences
 - Laundry equipment
 - Water softeners, where required by the hardness of well water
- f) **Regulated changes**
- Changes required by the law within a set period

Extensions to the standard list

Extensions to the standard list are items which were designed, manufactured and installed to function and perform for the life of the project, but have failed due to deficiency or environmental factors. Here are some examples:

- Foundations or significant sections of foundations

- Other structural components, such as walls, floors and roof framings
- Brickwork and pre-cast concrete panels
- Emergency generators
- Retaining walls
- Plumbing systems
- Electrical installations, including project transformers and emergency generators
- Balconies

The co-op can spend money from its replacement reserve under these conditions:

1. The co-op has an approved capital replacement plan

If a co-op has a comprehensive plan, it does not need Agency approval to spend from the replacement reserve if

- The plan has a complete schedule for replacing capital items, along with estimates of how much each item will cost
- The plan has been approved by CMHC or the Agency
- The co-op updates the plan every three years and;
- The co-op is setting aside the annual amount required by the capital replacement plan.

At the end of three years when the co-op updates its capital replacement plan, it does not necessarily need to do new technical studies. It may instead update the schedule of replacements and the cash flow forecast. When a capital replacement plan is updated, it must be approved by the Agency as it may affect the replacement reserve annual contribution. The annual contribution will have a direct impact on the budget and occupancy charges.

2. The co-op does not have an approved capital replacement plan

If the co-op does not have a long-term capital replacement plan, that the Agency has approved, the co-op needs the Agency's approval before it spends from its replacement reserve except as permitted in the operating agreement.

19.3 *Changes to Replacement Reserve*

When a co-op sends its audited financial statements to the Agency, it has to report any charges to the replacement reserve in the last year. Include the detailed report with the audited financial statement, showing the work done during the year and how much it cost. Present it separately or include it in the notes.

19.4 *Emergency Expenditures*

Emergency replacements are repairs to capital items that, if delayed, would create a health or safety hazard. Examples include the replacement of a heating system in the winter, or a structural failure that endangers the physical safety of members.

The co-op is expected to complete these repairs immediately and inform the Agency right away.

19.5 *End of the Operating Agreement*

Once the loan or mortgage is paid off and the operating agreement ends, the replacement reserve fund remains with the co-op. However, if CMHC approves an early payout, CMHC decides what happens to the reserve fund based on CMHC policy.

20. OTHER FINANCING COSTS

Financing costs or encumbrances other than the CMHC first mortgage may be included in the operating budget as legitimate operating expenses, as long as CMHC has already approved the loan and financing arrangements.

21. PROVINCIAL RENT REVIEW BOARD

21.1 *Provincial rent review board and housing charge increases*

Should a provincial regulator with jurisdiction approve a rent increase that is less than an Agency-authorized housing charge increase, the provincial increase is the maximum amount the co-op may charge the members. However, if a provincial rent review board approves a rent increase that is higher than an Agency authorized rent increase, then the maximum amount the co-op may charge members is the amount the Agency approved.

21.2 *Request to appear before the review board*

The Agency will consider requests to appear before a rent review board or similarly mandated body on its merits.

21.3 *Informal discussions between the Agency and rent review board officers*

Informal discussions may take place with provincial rent review officers about how rent adjustments are calculated. The Agency will decide whether such discussions are appropriate before holding them.

22. RENT REDUCTIONS

Co-ops may not reduce housing charges such that they will not be able to provide for the cost of operating the project. The co-op cannot reduce housing charges unless the market requires it or, the co-op gets prior approval from the Agency.

23. LENDING FUNDS AND ENCUMBERING PROJECTS

23.1 *Projects encumbered without CMHC permission*

A co-op can't charge, mortgage or otherwise encumber any part of a project unless it has prior written approval from its lender and CMHC, as recommended by the Agency.

23.2 *Lending or giving away project funds*

With the exception of reasonable nominal gifts and donations, a co-op can't lend or give away any project funds or guarantee or underwrite the repayment of any obligation by a third party without the prior written approval of CMHC, as recommended by the Agency.

24. ADDITIONS OR EXTENSIONS TO A PROJECT

A co-op will not add to or change the project, without the prior consent of CMHC.

25. MAJOR REPAIRS AND CAPITAL IMPROVEMENTS

25.1 *Pre-approval for financing*

The Agency will consider a co-op's proposal for a major repair and improvement program. The co-op must have the lender's pre-approval for financing.

25.2 *Approval for additional borrowing*

The Agency in consultation with CMHC may approve additional borrowing to cover the costs of repairs or improvements, but only if there is not enough replacement and/or operating reserve funds.

25.3 *Housing charge increases to reflect capital improvements*

The co-op can raise housing charges to reflect capital improvements and increases in operating costs.

26. SALE OF PROJECT

No co-op can sell all or part of its assets without the permission of CMHC, as long as the operating agreement is in force. CMHC will only consider the sale of a project in exceptional circumstances.

Here are some examples of exceptional circumstances:

- the merger or combining of a co-op with another non-profit project
- transferring some units to another non-profit project
- transferring a co-op to another non-profit housing provider, where the co-op says it is not able to carry out the governance duties needed in a housing co-op

The sale would only take place if it was in the best interests of the co-op and is in keeping with program purposes. The co-op would be sold for \$1 and the buyer would take on the outstanding mortgage balance. The buyer would assume the obligations of the project, operate it within the program, and follow the operating agreement with CMHC.

Under certain circumstances, it may be necessary for a co-op to sell a portion of the co-op to make it more viable overall. Any such sale must be at market value, and the specifics associated with it would require the prior approval of the Agency in consultation with CMHC.

27. PREMATURE PAY-OUT OF CMHC MORTGAGE

The Agency in consultation with CMHC will consider a co-op's proposal for early payout of the CMHC direct loan. Any repayment would be based on the payout provisions of the mortgage loan agreements, which would result in termination of the operating agreement.

Early payout may occur as a result of the sale of a co-op or the sale of individual units within a co-op.

The Agency will review the co-op's proposal or request for early payout and provide its recommendation to CMHC. In the event of an early payout, the co-op may also be required to refund to CMHC the unearned portion of the Federal Capital Contribution.