



Rethinking Member Contributions in Housing Co-operatives

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One of the basic ideas in a limited-equity housing co-operative is for the tenants to pay a “true cost” rent. But that rent is typically determined by the cashflow requirements of the co-operative — particularly by the need to pay off the acquisition or construction loan. But then when the loan is paid off, the rent is suddenly reduced essentially to the cost of occupancy (without the cost of the loan payments). This means that the first cohort of tenants, in effect, pays off the acquisition debt and then is forced by the financial organisation of the co-operative to gift it to the later tenants and “go out naked.” But borrowing the concept of Internal Capital Accounts (ICAs) from worker co-operatives (e.g., the Mondragon co-operatives), there is a way to organise the housing co-operative so that, overall, each tenant pays for the true cost of their occupancy. This paper explains how such a “housing co-operative with ICAs” works. The result is that, over the whole time of tenancy, the tenants pay only for what they actually use, no more or less.

Introduction to Basic Ideas

This paper rethinks limited-equity housing co-operatives starting from basic principles — rather than having design driven by phrases like “limited equity,” “cost rent,” and so forth. The basic principle will be that tenants only pay over all for what they actually use, no more (e.g., no profit) and no less.

But this is not as simple as it sounds because of the differences between cashflows and expenses. In terms of accounting, the proportionate expenses should represent what tenants actually use up in terms of housing services (the true costs of their tenancy) but the extra cashflow needed to pay off the initial investment (construction or purchase debt) can be quite different and usually falls on the first generation of tenants in a housing co-operative.

These concerns do not arise to the extent that the buildings are gifted or granted by the municipal or state government so that there would be less construction or purchase debt. For instance, in Austria, financial assistance includes:

- Long term and low interest rate public grants or mortgages that cover between 20% and 60% of the construction costs.

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- Annuity grants/loans granted either instead of the loan for the construction costs or in addition to such loan to reduce the repayments of mortgages (Moreau & Pittini, 2012).

The concerns addressed here apply to financing by loans, not grants.

The idea of “cost rent” is often incorrectly identified with the needed cash outflows that can be much greater than the actual cost for the people who have tenancy in the period when the initial loans are being paid off. Such cost rents have the early tenants paying for more than they actually use (in terms of using services of a housing facility). When that is not taken into account properly, then the early tenants are forced to make a gift to the later tenants whose cost rents are calculated after the construction or purchase loan is paid off and these costs are thus much lower.

To put it differently, we can separate “true cost rent”, which is tied to actual expenses, from a “fake cost rent” (our expression), which is tied to the cash-flow. Expenses in a housing co-operative consist of asset depreciation, maintenance, interest, and governance costs and are consistent through time, while cash-flow implies paying of the initial investment through loan repayment in a relatively short amount of time. Cash-flow, therefore, is much higher than actual expenses for the years of loan repayment, and lower than actual expenses once the credit is repaid (e.g., ignoring the interest costs on using an asset of such value). Consequently, fake cost rent is a very volatile concept of a cost and dependent on when a tenant arrives at the housing co-operative, while the concept of true cost rent smooths out the financial obligations of members throughout all generations of tenants. To summarise:

Fake cost rent = true cost of occupancy + cash needed to pay off acquisition/construction loan

With proper design of a housing co-operative, tenants would only be paying the true cost rent, meaning that they would be covering only their actual expenses. The needed new mechanism is an idea brought over from worker co-operatives such as the Mondragon co-operatives in the Basque region of Spain (see also Ellerman, 1983a, 1983b; Hammer & Ward, 2025). The idea is a set of Internal Capital Accounts (ICAs) for each tenant-member (as opposed to non-member commercial renters) that keeps track of the amount each tenant pays in as cash rent (perhaps with an initial down payment) but that is not used up in the actual cost of their tenancy. In other words, the ICA balance for each tenant is the amount that each tenant should eventually get back so that overall they only pay for the real cost of their tenancy.

These ICAs are subordinate debts of the housing co-operative to the tenants or ex-tenants so they are not equity in the usual sense — although the members’ ICA may still be called “equity accounts” as in the following quote which makes the same point about recording a member’s payment of a share of the debt principal in their ICA.

Credit for amortisation without appreciation — Members’ equity accounts are credited with their initial down payment, plus a proportionate share of the principle [sic] on the blanket debt that has been paid down by the members’ monthly payments. (Northcountry Cooperative Foundation, 2004, p. 7)

The member ICAs are not equity in any conventional sense because the size of the account does not affect voting rights (always one-tenant/one-vote) or the size of their monthly contributions (usually based on area of a dwelling and number of occupants).

The rent covering the initial investment can be seen in part as members’ monthly credit instalments to the co-operative, which uses these instalments to repay the outstanding loan or other financing sources used to finance the enterprise. A tenant lends part of the rent to the co-operative, which uses this credit to repay the loan. Basically, it means extending some loan repayments (i.e., to the financing source or later to the ICAs) throughout the whole life expectancy of a building. The tenants have no property right to their particular apartment to sell on the housing market (as in a condominium or some full-equity co-operatives) and no share in the overall speculative value of the land-and-building-owning co-operative, as in some full-equity co-operatives. But as a creditor of the co-operative for the unpaid amount in a tenant’s individual

ICA, that is a property right just like being a creditor of a bank where one has an interest-bearing bank account, except the tenant's ICA cannot be drawn out at will but is paid out over a period of time.

One often hears the idea that low-income people tend to stay low-income since they usually pay high rents in private housing whereas in a no-equity housing co-operative, they can have lower cost rents. But there is another aspect to that narrative. Low-income people pay high rent in private housing and have nothing to show for it when they leave. Middle-class people are able to gather together enough down payment from family and friends to obtain a bank loan to buy property. They also have high monthly cash payments, but they acquire a property right (net of depreciation, maintenance, and other operating costs) which is usually more than counter-balanced by the market appreciation). Hence when they leave and sell the property, they get back the amount they paid in that was not used up in depreciation, maintenance, and operating costs plus the overall increase in market value. The here-suggested model partially mimics this ownership arrangement without the actual ownership in the property itself; in the housing co-operative with ICAs, the tenants will get back what they paid in but did not actually use up (as $\text{expense} = \text{depreciation} + \text{maintenance} + \text{other operating costs}$), but not the increase in market value.

If an existing rental property is being converted to a housing co-operative, then the two ways to finance the purchase are either by a loan from a bank or other financial agency, or if the seller is willing to be paid out over a number of years, then the seller is providing the credit. In the case of new construction, then there is no seller so the construction would have to be financed by a loan.

But it will be asked, if low-income people are getting a deal comparable in many respects to middle-class ownership, then how does the low-income tenant get the loan? The answer is that it is the housing co-operative that gets the bank loan, not the individual tenants, and then the tenant-members collectively pay off the loan in cash payments that are in excess of their actual expenses, with the excess recorded in the ICAs of the tenant-members. Those debts of the co-operative will be eventually returned to them by future members who do not have such a reduction in cash-rent after the loan is paid off. And it continues with each generation of tenants paying in an extra amount over their actual expenses (recorded in their ICAs) in order to pay back the earlier generation's ICAs, and then they in turn will have their ICAs paid off by the next generation of tenants. Thus, the ICA system is called a "rollover" system since the pattern rolls forward of each generation paying off the earlier one and in turn being paid off by the next generation.

Since the early tenants in an ordinary housing co-operative tend to pay a higher cost rent when the construction or acquisition debt is being paid off, the ICA housing co-operative does not differ in offering a lower rent but in eventually getting back the part of their cash rental payments that did not represent the actual expenses of their tenancy. Thus, the ICA housing co-operative provides low-income people with a housing strategy comparable to middle-class people (except without the speculative increases in land value) and except that the cash return to the tenants or ex-tenants is over a period of years, not all at once as when an individual property is sold. In a city or country with more co-operative infrastructure, then the ICA housing co-operative might take out a loan from a co-operative bank equal to the amount owed to an ex-tenant who could then be paid out in a lump-sum.

In comparison with a full-equity housing co-operative, the tenant-members in a housing co-operative with the ICA rollover system get a (non-speculative) return out in the end but the tenants do not have to buy in with an individual up-front payment. They only have to pay a sufficient cash rent (which they do anyway when the bank loans are outstanding) to pay off the loans or in later generations, to pay out the ICAs of the earlier generation who paid off the bank loans, and so forth. One way to look at it is that the original bank loan is replaced by the loan of money from the higher-than-actual-expense cash rents of the earlier generation of tenants that needs to be paid back, and so forth.

Concluding Remarks

This system for a housing co-operative is designed to implement the principle that each tenant pays for what they use up, no more and no less, the true cost rent, and it also ignores changes in the market value of the land and buildings. In comparison with ordinary housing, it does not require a tenant to have a large lump-sum to gain tenancy and it ignores changes in market value. Unlike many housing co-operatives, the tenants eventually get back what value they do not use up. The initial tenants are not forced to pay off the acquisition loan and then give up the unused portion of those costs when they leave. Tenants, who come in after the acquisition loan is paid off, would not get a lower rent for that reason (there may be other reasons) since the acquisition debt is shifted to the ICAs of the current tenants that need to be paid off, and so forth for future generations of tenants.

One reaction to the ICA housing co-operative, is to object to the attention to accounting. But this is due to the decision to have an institution that is partly insulated from the market. There is no accounting for value in an ordinary property; the market will make that decision for you. If a housing co-operative does not have an ICA system (based on the principle that tenants pay for what they use up, no more and no less), then it will, perhaps inadvertently, end up charging the early tenants much more than they used up (e.g., the principal payments on the loan) and then in effect forcing them to gift it to later generations of tenants in the form of lower rents. However, we do not see a reason why a systematic and automated way, which clearly defines the rules of the game, would not be preferred to ad hoc decisions that ultimately depend on the current governing body of a co-operative. The system of hidden unfair treatment of early tenants is not the only alternative to a full-equity co-operative or condominium. The alternative is a housing co-operative with ICAs and rollover — where more attention is paid to the internal accounting to make it fair.

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