Foreword

Residents of Rust Belt cities harbor dark memories of past economic downturns. In cities like Lawrence, Massachusetts, and Cleveland, Ohio, economic shifts led to significant job losses and disinvestment, along with the related problems that frequently accompany such changes. In 1992, for example, Lawrence lost 120 buildings to arson. Crime and other illicit activity proliferated. But thanks to the hard work of community activists and successful public/private partnerships, the late 1990s and early 2000s saw redevelopment in Lawrence and dozens of cities like it. This urban renaissance also took hold in larger cities like Cleveland, which leveraged a robust community development corporation network to rehabilitate existing residences, construct new homes, and revitalize the city's commercial district.

The recent housing crisis threatens to undo the progress made in communities over the past 20 years. The viability of investments made in neighborhoods by banks, investors, nonprofits, foundations, business owners, and residents is in question as the foreclosure problem persists, compounded most recently by high unemployment levels. The issue of vacant and abandoned property threatens the very sustainability of many communities. But the effects of the housing crisis are not limited to urban areas; suburban and rural areas have been hit hard as well. Communities across the country have lost revenue because of dwindling property-tax bases; they face severe cuts in critical services such as police, social services, libraries, and schools despite sharp increases in demand. As older communities face familiar fears, neighborhoods in newer or rapidly expanding communities face different challenges, such as how to fund the provision of municipal services to the remaining residents of half-empty neighborhoods.

With this publication, we aim to shed light on how community development practitioners and policymakers can help stabilize the neighborhoods most at risk, that is, those beset by concentrations of foreclosures. The animating idea here is that community development practitioners should be guided by the best available research, by anecdotal reports of what efforts are working, and by the best new ideas about what other approaches might work. We culled the country for individuals and institutions that are deeply engaged in this issue, both academically and at street level. Our authors, figuratively speaking, have rolled up their sleeves and gotten their hands dirty in the data or in the field, whatever their institution or perspective. This publication is presented in two parts; one focuses on research and analysis and another focuses on policy solutions.

Market Dynamics

Several articles look at selected cities, counties, or metropolitan areas to identify patterns and draw broader inferences about the REO market. These articles highlight the distinctions between so-called weak and strong markets, and among inner-city, inner-ring, and "exurb" communities. Claudia Coulton, Michael Schramm, and April Hirsh look at foreclosures in the Cleveland area, which experienced the rise in foreclosures earlier than other parts of the country. They find compelling evidence of disproportionate numbers of foreclosures in minority communities, changes in how REO properties are sold and to whom, and that many REO properties are being left to deteriorate. Kai-yan Lee takes us to some of the cities and towns of Massachusetts, many of them former mill towns that successfully pursued revitalization plans, only to be at risk of having their efforts reversed. Both articles examine prices for REOs and find steep drops in value.

Foreclosures are not limited to the older, industrial areas of the country. Carolina Reid describes the outlying "boomburbs" of California's cities, which have dense concentrations of REO property. Dan Immergluck focuses on Fulton County, Georgia, where he finds that a few sellers account for most REO sales to a wide variety of buyers. Immergluck also finds increasing volume and sales of low-value REOs (the most distressed properties), many of which were sold to investors. This suggests that neighborhood stabilization policies need to incorporate thinking about what to do with investor-owned properties after their purchase, not just thinking aimed at lender-owners. Alan Mallach illustrates some broader findings with a close look at Phoenix, Arizona. Intriguingly, he unpacks the dynamic behind the so-called "shadow inventory" by looking at how short sales, loan modification, and sales to investors at foreclosure auction are likely to affect the inventory of REO properties.

The Slow Starts and Hard Slogs of REO Redevelopment

Designers and implementers of national efforts to address barriers in the acquisition of REO properties have faced a steep learning curve. Several authors address the federal Neighborhood Stabilization Program (NSP) and the difficulty of obligating money within that program's 18-month time limit. Drawing on case studies of more than 90 NSP sites around the country, Harriet Newburger highlights some of the program requirements that slowed NSP's start. Others point to similar challenges in using NSP funds in a competitive environment where many properties are sold singly and in as-is condition. In some areas, NSP administrators can only watch as properties are bought in bulk by investors who can afford to do so and who are not constrained by strategic neighborhood stabilization plans. By contrast, NSP's program stipulations (environmental and others) hinder communities' ability to bid on properties and limit bid amounts to maintain the affordability of rehabbed properties. With rare exceptions, municipalities cannot be nimble or flexible buyers.

Craig Nickerson describes the National Community Stabilization Trust as an effort to broker REO properties for communities and nonprofits with major servicers. The Trust provides a first look at REO properties for nonprofits, and although a possible complement to the NSP, it struggled initially to secure a good number of viable properties from participating servicers. Fannie Mae has also developed its own First Look program to sell REO properties to communities at a discount.

Acquiring and redeveloping REOs is a demanding process fraught with considerable uncertainty. At the local level, some authors highlight the challenges practitioners face, including "toxic title" problems, rehabilitation needs, and difficulty in contacting property owners, all of which impede efforts to prevent blight and to acquire and redevelop properties. Determining proper exit strategies in advance is difficult under current market conditions. Several articles address questions facing communities, such as what to do with properties where values continue to decline, credit standards are tight, and potential buyers have impaired credit. Demonstrating their resolve and initiative, the New Jersey–based Community Asset Preservation Corporation successfully completed the first bulk purchase by a nonprofit of foreclosed properties—47 in all, as described by Harold Simon—an accomplishment even more impressive considering that these were not REO sales but note sales, which are even more challenging.

The Importance of Targeting

Scarce funds make hard choices. Even a third round of NSP funding, included in the 2010 financial reform bill, cannot adequately address the REO inventory in targeted NSP areas, much less the massive number of REO properties throughout the country. Only a small fraction will be rehabbed or demolished with NSP funds. Ira Goldstein describes an analytical data tool that can be used to conduct a market analysis to target scarce funds and apply fresh strategies. Dan Fleishman details the varied development strategies that apply in different neighborhood typologies.

Innovative Approaches to Preserve Value

Despite the challenges, communities are responding in some innovative ways. Thomas Fitzpatrick describes a Cuyahoga County land bank, modeled on a similar effort in Flint, Michigan, that holds properties until they can be returned to productive use. The Cuyahoga County land bank is financed by fees and fines on property taxes. In some cases, properties are demolished and converted to green space or altered to fill another community need. In all cases, the land bank creates value from damaged goods. The Cuyahoga County Land Reutilization Corp., better known as the County Land Bank, is the lead agency for a consortium of municipal and nonprofit partners in implementing NSP2. The Land Bank has successfully negotiated REO acquisition agreements with Fannie Mae and HUD that align with the overall vision for neighborhood stabilization in the region.

Another way to stabilize neighborhoods is to keep foreclosed properties occupied. Anecdotal reports suggest that more REO servicers are realizing that keeping paying tenants in houses may be the best avenue to maintaining the property's value and the quality of the neighborhood—particularly if the only alternative is to try to sell in a market with high REO volumes. Elyse Cherry and Patricia Hanratty describe a model developed by Boston Community Capital to purchase foreclosed properties and sell them back, either to tenants or to the property's former owners, using a licensed mortgage affiliate. In a similar vein, Danilo Pelletiere describes the need to create rental housing from the inventory of foreclosed homes, not only to provide affordable housing, but also as a method to stave off blight and disinvestment.

Bringing the Government and Community to Bear

Neighborhood stabilization is about more than acquiring properties. Municipalities have tools, such as code enforcement, fines, and other legal options, to address problems. For example, in order to resolve issues of neglect, courts can appoint a receiver to take control—but not ownership—of a property. In some cases, threat of receivership or demolition is enough to spur recalcitrant actors to address blight and safety issues. Frank Ford's article highlights the phenomenon of bank "walk aways," where financial institutions fail to pursue or claim title to vacant and abandoned properties. He shows how property-based data and community partnerships can help organizations intervene to help homeowners stay in their homes and to target resources for REO acquisition.

For many communities, neighborhood stabilization may involve rethinking housing policy and retooling plans to adapt to the reality of shrinking populations and to offer more green space and affordable rental housing to attract and retain residents. Preserving neighborhoods involves complementary interventions—such as investments in police and fire safety, lighting, and maintaining streets—that preserve the perception of the community as a good place to live. These types of investments may, in fact, be some of the most cost-effective strategies of all. Many cities, which have memories of past crises, have intervened comprehensively. The entire region of Northeast Ohio, for example, is engaged in thinking through land-use challenges, led by the Youngstown and Cleveland examples of "shrinking," or "right-sizing." Cleveland's community development industry is engaged in "reimagining" the metropolitan area to find strategies for putting properties into productive reuse, including the possibility of urban agriculture.

Understanding Private-Sector Methods and Incentives

Negotiating for the disposition of REO property does not typically involve the lender, since the majority of mortgage loans have been sold into the secondary market. Rather, communities or their agents must negotiate with the loan's servicer, who has a fiduciary duty to the mortgage holders and may be guided by other incentives as well. This does not necessarily conflict with community interests. In fact, several articles report the positive results of collaborating with servicers, although many others describe the steep learning curve involved in negotiating successful transactions. Terry Theologides outlines the servicer guidelines in the REO process, with an eye toward improving the community's ability to understand and work within the process. He also highlights an unintended consequence of foreclosure moratoriums by pointing out that the extension of foreclosure timelines increases the chance that value is destroyed as the property deteriorates. Once a property has been abandoned, there is no economic reason to delay its return to productive use. Jay Ryan of Fannie Mae outlines the practices being developed by this holder of a huge REO inventory and highlights steps the agency has taken to avoid vacancies and convey properties to municipalities and nonprofits as efficiently as possible.

The Community Reinvestment Act (CRA) has been shown to influence private capital and activity by CRA-regulated financial institutions. Mike Griffin shows why the proposed CRA rules on neighborhood stabilization efforts in areas designated for NSP dollars may give banks sufficient incentive to make further investment in these areas.

Conclusion

Taken together, these articles provide hard-headed facts and advice for those trying to preserve the character and vitality of neighborhoods endangered by foreclosures. We also think they provide some measure of hope that committed practitioners and policymakers can address the issue of neighborhood stabilization effectively and creatively. Community groups were quick to identify the problem and articulate the fears. Several of the initiatives highlighted here are the product of many people's determination, innovative thinking, and willingness to work together. We dedicate our publication to their efforts.

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