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Community Development INVESTMENT REVIEW

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FEDERAL RESERVE BANK OF SAN FRANCISCO

Innovations in Neighborhood Stabilization: Responses to the Foreclosure Crisis

Lessons Learned from the Innovations Initiative

Commentary

CENTER FOR COMMUNITY DEVELOPMENT INVESTMENTS

Community Development INVESTMENT REVIEW

The Community Development Department of the Federal Reserve Bank of San Francisco created the Center for Community Development Investments to research and disseminate best practices in providing capital to low- and moderate-income communities. Part of this mission is accomplished by publishing the *Community Development Investment Review*. The *Review* brings together experts to write about various community development investment topics including:

Finance—new tools, techniques, or approaches that increase the volume, lower the cost, lower the risk, or in any way make investments in low-income communities more attractive;

Collaborations—ways in which different groups can pool resources and expertise to address the capital needs of low-income communities;

Public Policy—analysis of how government and public policy influence community development finance options;

Best Practices—showcase innovative projects, people, or institutions that are improving the investment opportunities in low-income areas.

The goal of the *Review* is to bridge the gap between theory and practice and to enlist as many viewpoints as possible—government, nonprofits, financial institutions, and beneficiaries. As a leading economist in the community development field describes it, the *Review* provides "ideas for people who get things done." For submission guidelines and themes of upcoming issues contact David Erickson, Federal Reserve Bank of San Francisco, 101 Market Street, Mailstop 215, San Francisco, California, 94105-1530, David.Erickson@sf.frb.org. The material herein may not represent the views of the Federal Reserve Bank of San Francisco or the Federal Reserve System.

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Foreword

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December, 2013

Five years ago, in July 2008, the Federal Reserve Bank of San Francisco convened a symposium in Los Angeles on the topic of stabilizing communities in the wake of foreclosures. The goal of the conference was to identify strategies that could help to mitigate the negative spillover effects of foreclosures on families and neighborhoods. At the time, there were few models to turn to for neighborhood stabilization–and many unanswered questions. How could we leverage federal funding to bring additional financing partners to the table? What strategies could be deployed in cities with weak markets, where rehab costs exceeded market values? Was it possible to managed scattered site rentals?

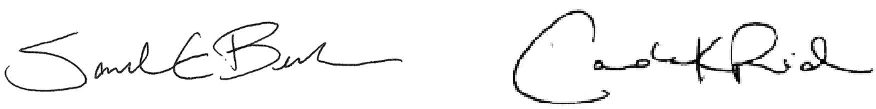
Since then, nonprofit organizations across the country have been responding to these questions in innovative ways, drawing on their expertise to meet the challenge of foreclosed and abandoned homes head on. It hasn't been easy–funding for neighborhood stabilization remains small in comparison to need, and the volatile housing market has required quick thinking and the ability to design new solutions on the fly. And although the housing market has finally begun to rebound, nonprofits are working to sustain their work in response to continued historically-high levels of foreclosures and bank-owned inventory. They are also looking ahead to develop strategies for community development work in the post-crisis environment.

In this issue of the *Community Development Investment Review*, we have brought together a series of articles that highlights some of the stabilization strategies emerging from the efforts of committed nonprofits across the country. The articles in the first section of this issue reflect the lessons learned from the Housing Partnership Network's (HPN) 2011-2013 Innovations in Neighborhood Stabilization and Foreclosure Prevention Initiative, funded by the Citi Foundation. The goal of the Innovations Initiative was not only to support emerging strategies for neighborhood stabilization, but also to share experiences across nonprofits and create a body of knowledge of successful strategies for the community development field. On behalf of HPN, we would like to thank the organizations who participated in the Innovations Initiative, as well as those who served on the advisory committee, including Eric Belsky, Pat Gamble-Moore, Patricia Garrett, Bill Gilmartin, Catherine Godschalk, Bob Kantor, Alan Mallach, Mike Mullin, Craig Nickerson, Rebecca Regan, and Laura Sparks.

* The authors would like to thank Laura Choi, Federal Reserve Bank of San Francisco, Matt Perrenod, Housing Partnership Network, and Peter Richardson, Housing Strategies, Inc. for their editing and support for this issue.

In the second section of this issue, we bring you a series of essays written by influential nonprofit and public sector leaders that enriches the conversation about neighborhood stabilization, providing new and provocative perspectives on this work. Together, the articles and essays reveal the passion and expertise that the field has brought to the crisis, and point us toward strategies that will continue to be relevant, post-crisis, for investing public and private resources to make a real impact in low- and moderate-income communities.

We hope you enjoy this issue of the *Review*.



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Innovative Strategies for Mitigating the Foreclosure Crisis and Stabilizing Communities

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The foreclosure crisis has been devastating to neighborhoods. Homes have been abandoned and fallen into disrepair, families have been displaced, and community anchors have been uprooted. The numbers are staggering. Since the crisis began in September 2008, approximately 4.5 million homes have been foreclosed, with roughly 2.1 million homes still in serious delinquency as of August 2013.[1] Throughout, high-capacity, entrepreneurial nonprofit organizations have developed innovative solutions to stem the tide of foreclosures and stabilize affected communities.

Working closely with public- and private-sector partners, nonprofit organizations have helped families and communities address the profound challenges and disruptions precipitated by the subprime mortgage crisis and subsequent Great Recession. An example of this collaborative model is the Innovations in Neighborhood Stabilization and Foreclosure Prevention Initiative launched by the Citi Foundation and the Housing Partnership Network (HPN), a business collaborative of the nation's leading housing and community development nonprofits.

In 2011, the Citi Foundation awarded HPN a $2.75 million grant to fund a two-year initiative that HPN had created to identify the most innovative and promising solutions to the foreclosure crisis among HPN members. Through a competitive proposal process, an advisory committee composed of HPN staff and external housing experts selected 12 member organizations, representing 10 separate projects, to participate in the initiative.[2] The goal: to seed emerging models for helping low- to moderate-income families successfully navigate the foreclosure crisis. The Innovations Initiative advisory committee selected participants on the basis of their potential to leverage external resources, effect lasting and transformative change, achieve scale and replication, and inform housing policy recommendations through their programs.

During the next two years, the 12 organizations used the funding to expand existing initiatives or launch entirely new enterprises to address the foreclosure crisis. Throughout,

1 CoreLogic, "National Foreclosure Report" (Irvine, California, August 2013).

2 Atlanta Neighborhood Development Partnership, Boston Community Capital, Cleveland Housing Network, HAPHousing, Housing Development Fund, Mercy Housing Lakefront, Neighborhood Housing Services of Chicago, Neighborhood Housing Services of New York in partnership with the Long Island Housing Partnership and the New York Mortgage Coalition, NHT/Enterprise Preservation Corporation, and Project for Pride in Living.

HPN worked as a partner with the organizations as they developed and refined interventions and strategies that could have a broader impact in practice and policy.

The following five articles, which comprise the first section of this issue of the *Community Development Investment Review*, were authored by representatives from the 12 organizations as well as HPN. They highlight lessons learned from the two-year initiative and provide a prospective look at strategies for replicating and expanding neighborhood stabilization programs.

- "Policy Lessons from the Neighborhood Stabilization Innovations Initiative" highlights the practitioner experience of the 12 participating organizations and the implications for policymakers.
- "Targeted Neighborhood Stabilization: Lessons in Resilience in Weak Market Cities" spotlights the added stress of the foreclosure crisis in weak-market cities, and explores the role of housing nonprofits in implementing targeted stabilization strategies to help buttress neighborhoods against future economic stressors.
- "Scaling Social Enterprises: Flexible Responses for Neighborhood Stabilization" discusses the rationale and effectiveness of utilizing social enterprise models to advance neighborhood stabilization activities, and how expanding their scale offers a flexible, low-subsidy response to the shifting marketplace borne out of reduced government resources and the ongoing foreclosure crisis.
- "Rethinking Tenure: Building a Diverse Landscape of Affordable Housing Options" explores the potential of rental, lease-purchase, and ownership tenure strategies to preserve the existing stock of one- to four-unit housing that serves low- and moderate-income families and makes up the fabric of many neighborhoods.
- "Strengthening Neighborhood Stabilization: Refining Business Models for Housing Counseling" advocates for developing new business models that embed homeownership advising and education within the home mortgage process, both pre-purchase and post-purchase, to increase the stability of individual homeowners.

In April 2013, at the conclusion of the funding period, HPN and the Citi Foundation convened a meeting in Washington, DC, where the 12 organizations presented their findings to an audience that included government officials, funders, foundations, other practitioners, and policymakers.

Although the Innovations Initiative brought to light several blueprints for expanding interventions, the work continues to develop and replicate strategies that stabilize neighborhoods, and to shape new policy responses to the issue.

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Policy Lessons from the Neighborhood Stabilization Innovations Initiative

John O'Callaghan
Atlanta Neighborhood Development Partnership

Paul Weech
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At an April 2013 gathering focused on innovations in neighborhood stabilization, Craig Nickerson, president of the National Community Stabilization Trust, accurately observed that "it's only half-time" in our collective efforts to help those neighborhoods and families hurt by the national foreclosure crisis. During the first half of the crisis, nonprofit developers, counselors, and mission-oriented capital providers used the Neighborhood Stabilization Program (NSP) and other resources to prevent foreclosures, slow neighborhood decline, and restore housing values. Their efforts helped millions of families stay in their homes and regain their financial footing. Clearly, some strategies worked well. However, others did not. In both instances, nonprofits have learned many lessons about how to respond to the challenge of foreclosed properties, and they have built the organizational capacity to increase the scale and effectiveness of their work.

The challenge going forward is to take advantage of the lessons learned from the foreclosure crisis to craft better tools and policies that can creatively leverage and build on existing programs and funding sources to take neighborhood stabilization and recovery efforts to scale. Many communities–especially low- and moderate-income neighborhoods–are still struggling with the aftermath of the foreclosure crisis, and in others it may be a false dawn. Mortgage delinquencies remain high in some markets, and many neighborhoods are blighted with vacant and abandoned homes. Other markets are booming as prices are driven up by the influx of private equity raised to acquire real estate owned (REO) properties. However, this influx is crowding out first-time homebuyers and raising concerns over the long-term community impact of investor owned homes.

But it's not only about responding to the crisis. The challenges facing low-income neighborhoods–their vulnerability to market changes, the effects of vacancies and/or inadequate and unsafe affordable housing on neighborhood health, the higher costs of acquisition and rehabilitation in relation to lower market prices–these all existed prior to the crisis and will continue even after most housing markets stabilize. As a result, the strategies that nonprofits have developed in response to the foreclosure crisis will have continued applicability after the crisis has subsided, and should be supported by federal housing policies and strategically targeted public subsidies.

This article attempts to capture some of the major lessons learned from the Neighborhood Stabilization Innovations Initiative, a series of demonstration programs funded with a $2.75 million grant from the Citi Foundation to the Housing Partnership Network (HPN), as well as drawing from the individual experiences of the Atlanta Neighborhood Development Partnership.[1] We hope that these lessons can inform public policies in housing and neighborhood stabilization, thereby ensuring that public resources are spent effectively to meet housing and community development goals.

Lessons Learned

At the core of HPN's business model is a commitment to peer exchange among the 100 nonprofit organizations that make up its membership. From the beginning of the foreclosure crisis, HPN members have come together regularly to solve problems and share best practices related to neighborhood stabilization. The Citi Foundation grant was designed to elevate some of the more innovative approaches and collect insights that would help shape ongoing and future neighborhood stabilization interventions.

The following are among the key lessons learned from these numerous neighborhood stabilization efforts.

Intervene Early

Perhaps the biggest lesson learned for neighborhood stabilization is the need to intervene quickly with families struggling financially. Both the public and private sectors failed to move quickly enough to respond to the scale of the foreclosure crisis. The unfathomable number of distressed borrowers overwhelmed the system, and the underprepared servicers learned the hard way that their relationships with borrowers were insufficient to initiate effective resolutions.

Similarly, limited capacity and contrary economic incentives meant that financial institutions held REO properties off the market too long. In many communities, by the time nonprofits could intervene to implement neighborhood stabilization strategies, properties had deteriorated to the point where the costs of rehab and repair were excessive and the negative effects on the community difficult to reverse.

Engage Skilled Housing Counselors

The financial crisis has demonstrated the importance of nonprofit housing counselors in creating the foundation for sustainable homeownership and in supporting homeowners

1 HPN is a business collaborative of 100 nonprofit organizations focused on housing. In addition to the Citi Foundation Neighborhood Stabilization Innovations Initiative, HPN and its members have played a broader role in the recovery effort. To learn more, visit http://www.housingpartnership.net. The Atlanta Neighborhood Development Partnership, Inc., (ANDP) is a 21-year-old affordable housing nonprofit developer, lender, and policy convener that is now focused on addressing metro Atlanta's foreclosure crisis. Benefiting from peer exchange with HPN members, ANDP has expanded its foreclosure redevelopment program from an initial six-home pilot in 2008 to more than 340 homes today. To learn more, visit http://www.andpi.org.

during times of crisis. Since 2007, housing counselors have served as trusted advisors for millions of troubled borrowers. Through targeted outreach programs, counselors have helped public entities and private mortgage lenders reach new populations and achieve program outcomes more effectively, helping families navigate difficult rules and options. In its evaluation for Congress, the Urban Institute found that borrowers who received counseling under the National Foreclosure Mitigation Counseling program were twice as likely to obtain a loan modification and 67 percent more likely to remain current on their mortgage nine months later compared with counterparts who received modifications without the assistance of a counselor.[2]

Ensure That Asset Disposition Strategies Are Community Driven

In early 2009, when the NSP first rolled out, one of the biggest challenges facing nonprofits and local governments was finding and successfully acquiring REO properties. It quickly became clear that traditional means of asset disposition–in which banks just put their properties on the market–did not work if the goal was to promote neighborhood stabilization. One of the key lessons to emerge from the crisis is the need for financial institutions and the public sector to structure asset disposition strategies that are sensitive to community needs and conditions.

Several positive models have emerged. "First Look" programs for bank, government-sponsored enterprise, and Federal Housing Administration (FHA) REO sales were extremely important in allowing local governments and nonprofits with access to NSP dollars to acquire foreclosed properties and redevelop the stock consistent with a broader plan for the neighborhood. Likewise, HUD's approach to FHA note sales introduced in 2012 was a breakthrough. As part of the Distressed Asset Sales Program (DASP), HUD worked with servicers and state and local governments to identify REO properties in at-risk and hard hit communities to create pools of loans for sale at auction. To promote neighborhood stabilization objectives, DASP incorporated rules into the disposition process for properties in the pools, such as preventing foreclosures for six months, requiring lenders to work with the borrowers to try to modify loans, limiting loan resales, and promoting rental strategies for REO properties. More recently, several bank servicers have increased donations of low-value REO properties to strong nonprofits serving distressed neighborhoods and at-risk populations to help ensure that the homes will be well managed as community assets. These community-sensitive distribution strategies grow even more critical as NSP funding diminishes and short-term investor competition for acquiring REO properties increases.

Ensure That Single-Family Rental Stock Remains Viable

The foreclosure crisis has underscored for policymakers the importance of the nation's single-family rental housing inventory as an affordable housing asset. Fifty-five percent of the

2 NeighborWorks America, "National Foreclosure Mitigation Counseling Program, Congressional Update." Washington, DC: NeighborWorks, June 2012, available at www.nw.org/network/nfmcp/documents/2012CongressionalReport.pdf.

rental units in the United States are in single-family homes or small buildings containing less than four units. Much of this rental housing stock is affordable to lower-income and working households without public subsidies. It is critical that policymakers consider strategies for ensuring that these rental units are well managed and well maintained. Large private-equity investors are purchasing thousands of homes in targeted areas. These new owners could engender the rise of a more professionally managed and maintained single-family rental stock as a new asset class. However, there are also significant concerns that these investors will sell off their single-family properties in three to five years with negative impacts on the community. There is a significant opportunity to build the capacity of nonprofits to manage single-family rental portfolios professionally and in ways that are more sensitive to the needs of the neighborhood.

Build the Capacity of Strong Nonprofits

The role of strong nonprofit organizations was critical to the success of NSP. In round two of NSP funding, nonprofit consortiums could apply for funding, which spurred innovation and collaboration among the organizations. The high-capacity nonprofits leading these consortia were, for example, able to create new early intervention approaches. They provided high-quality foreclosure prevention counseling and other services that linked borrowers to servicers in productive ways. They were sensitive to the needs of troubled homeowners and renters living in foreclosed properties, as well as to the concerns of the local communities. They also brought strong capabilities to the process of acquiring and managing assets, including rehab and property management skills. As a result of NSP and these experiences, these nonprofits have substantially expanded their capacity in the neighborhood stabilization arena. The next phase should build on this capacity by creating new pathways to continued growth and greater scale.

Policy Implications

There is a clear case for continued NSP and foreclosure mitigation and prevention funding. The Obama administration has proposed $15 billion in funding for Project Rebuild[3] and another round of NSP funding in its 2014 budget. These proposals should be supported. However, given stark budget constraints, the nonprofit housing sector also must identify policy strategies with little or no direct cost to the federal budget. These strategies should be able to scale up the response and better position families and neighborhoods to navigate the second half of the recovery. It will also be imperative to build the policy and practice infrastructure by applying the lessons learned to revitalizing still distressed communities even after the worst of the foreclosure crisis passes. Finally, the tools and institutions must be in place to prevent a repeat of this crisis.

3 The Obama Administration first proposed Project Rebuild as part of the American Jobs Act, announced on September 8, 2011. Project Rebuild was designed as the next phase of the NSP, providing more funding ($15 billion) to acquire and rehabilitate more homes, but also adding eligibility for the redevelopment of vacant commercial structures.

The steps policymakers should take include the following:

Invest in Pre- and Post-Purchase Counseling

The crisis has demonstrated the importance of early, high-quality education to ensure that home buyers are well prepared for homeownership. Policy should embed access to housing counseling in the home buying/mortgage acquisition processes and embrace efforts to increase the quality of the counseling provided. FHA is best positioned to lead on this issue and should work to quickly finalize recommendations on ways to either provide incentives to its lenders to encourage counseling or even require housing counseling for all new FHA homebuyers. Strong counseling organizations are doubly critical in the post-purchase homeownership experience and can help borrowers navigate the complicated loan modification process. This is not the time to cut back funding for housing counseling; rather, policymakers should prioritize a level of resources that can sustain a strong housing counseling industry and support research and innovation in the field to advance those approaches that work best.

For example, policies could build on new insights on how to deliver quality adult learning, including online approaches. Online curricula are already delivering effective pre-purchase counseling to consumers who want to learn at their own pace, and are doing so at a much lower cost than traditional counseling approaches. At the same time, the presence of strong counseling organizations is also important for those consumers who learn better in face-to-face settings or for those who may require more intensive services.

Expand Community-Sensitive Asset Disposition Strategies

DASP is a model for addressing the challenge of distressed assets in a way that is more sensitive to community needs and concerns while balancing institutional needs for financial recovery. DASP also illustrates that there are now nonprofit purchasers in the market with the mission and capability to develop positive outcomes for distressed borrowers and their neighborhoods. DASP should continue and expand to more markets.

Policy should also encourage similarly community-sensitive asset disposition strategies for REO properties by financial institutions following a foreclosure. A housing reform agenda could enact policies to support nonprofit enterprises in professionally managing single-family housing at scale. For example, policy could encourage high-capacity nonprofits to acquire single-family housing through the transfer of existing portfolios or bulk REO dispositions with joint venture or seller financing features.

New Financing Tools

As the nonprofit development community has moved to address the foreclosure crisis, a variety of capital and financing gaps have emerged. To participate in neighborhood stabilization activities at a greater and more beneficial scale, nonprofit development organizations need two new financing tools: hybrid-tenure products to bridge residents from renting to owning, and a portfolio-level product that would allow a strong nonprofit to acquire and finance multiple housing units in a single financing product.

A hybrid-tenure product can help to create new pathways to homeownership for young families and low-income households, especially in a tighter credit environment. Currently, mortgages are structured only for owning. Hybrid-tenure products include lease-to-own options, shared appreciation or shared equity models, and community land trusts. They are particularly helpful to borrowers who have damaged credit due to a foreclosure or short-sale. These types of products also allow low-wealth borrowers to build up savings to meet the higher down payments now require in the market and likely to remain even after we have reached full recovery. And, in many places, a hybrid-tenure product makes sense where the only demand for single-family housing is as a rental. It provides an approach for those people who are not yet ready to get into the home purchase market until they are sure the neighborhood has stabilized. Policy makers should focus on fostering products and services in this space that are replicable and scalable, beginning with FHA risk-sharing products to increase the availability of financing for hybrid-tenure approaches.

In this vein, policy makers should work to revitalize the existing FHA authorities under sections 203(k) or 203(b) of the National Housing Act that allow nonprofits to purchase single-family homes and rent them to their customers. A critical element of the FHA programs is the ability of the renter household to assume the mortgage from the nonprofit. The 203(k) program is potentially a tool for acquiring and rehabbing single-family properties and allowing nonprofits to create a larger portfolio of scattered-site rental assets, but its use overall has been limited. To be more effective, HUD must work to increase the number of lenders who offer this product. It must also allow a borrower to acquire more than seven properties, the current limit. Identifying and working with stronger, high-capacity nonprofit organizations will help ensure the product's success.

Even more transformational would be the creation of an FHA product–perhaps using existing risk-sharing authorities–that would allow strong, high-capacity nonprofits to finance the acquisition, rehab, and holding of single-family properties at an even larger scale. Ideally, the product would provide financing for nonprofits to buy a pool of properties. The nonprofit could then sell individual properties to home buyers and bring new properties into the pool as rental housing. The loans would be paid back by rents on the properties in the pool and proceeds from sales in some cases. With the enhanced ability to finance and manage single-family rental properties across a portfolio, nonprofit owners could lower the transaction costs and have greater flexibility to create operational efficiencies in managing these rental portfolios.

Enhance the Role of Strong Nonprofits

The ability of strong nonprofits to help stabilize neighborhoods, leverage private capital, work at the regional level to create economies of scale in property and asset management activities, and to do so in a manner that is sensitive to local community needs is an important role that policy should seek to support and expand.

There is an increasing role for nonprofits in promoting low-income homeownership and serving as a homeownership steward. Nonprofit organizations working in this area can help to ensure long-term homeownership success by providing their customers with access to a spectrum of services from homebuyer resources, hybrid-tenure financial products, first or second lien mortgage financing, down payment assistance, and an ongoing trusted advisor/counseling role.[4] To support these nonprofits, and to ensure that low-income homeowners have access to needed advisory services, policymakers could impose a new fee on mortgage servicing, which could become a revenue stream for these organizations.

Policy can also help strong and capable nonprofits grow and build even stronger balance sheets. The Capital Magnet Fund (CMF) is a promising approach to meet this objective. The CMF was enacted as part of the Housing and Economic Recovery Act of 2008. The program is designed to provide impact investments in high-performing, affordable housing lenders and developers. By law, CMF investments must leverage more than 10 times the CMF grant amount in private investments and strengthen the financial capacity of mission-driven affordable housing providers. For the first and only round of the program so far, the CDFI Fund received applications from 230 organizations requesting more than $1 billion in grants under the CMF. On October 1, 2010, the CDFI Fund made 23 awards totaling $80 million to organizations serving 38 states. Awardees have used their grants to leverage an estimated $15 for every $1 from CMF. The Reinvestment Fund, for example, used its $5 million grant to support eight housing projects, including a neighborhood stabilization project called Preston Place, a complex of 150 new and rehabbed energy-efficient townhomes for rent and for sale in Baltimore, Maryland.

Conclusion

The foreclosure crisis is not over and its detrimental effects on many communities will likely continue for years to come. However, it is not too soon to apply the lessons we have learned. The 10 projects funded under the Neighborhood Stabilization Innovations Initiative point to a wide range of workable approaches, spanning many local markets and housing challenges. In each case, the success of the demonstration began with a strong, highly capable nonprofit institution. Organizational capacity allowed these entities to tailor solutions on the basis of available resources, market conditions, and the proximity of public and private partners. Policy would go a long way toward more stable neighborhoods for people and communities if it increased its reliance on strong nonprofit institutions doing this work to deliver public resources.

4 For more on the homeownership steward model see "Toward a Housing Policy Reform Agenda," March 2013, by the Housing Partnership Network. http://www.housingpartnership.net/documents/policy_paper_web.pdf.

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Targeted Neighborhood Stabilization: Lessons In Resilience In Weak Market Cities

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Cities with little growth or shrinking populations are faced with tough choices when investing scarce public and private resources in neighborhood revitalization and stabilization. There is often a political tension between spreading resources equally across neighborhoods in a city and taking more strategic, targeted approaches designed to make the best use of limited funds and leverage additional investment. Responding to the foreclosure crisis has made the choices tougher and more pressing.

This article represents the on-the-ground perspective of nonprofit practitioners putting these policies into action, in coordination with partners in other sectors. The Cleveland Housing Network (CHN) in Ohio and HAPHousing (HAP) in Massachusetts have both played important roles in investing Neighborhood Stabilization Program (NSP) funds in response to the foreclosure crisis. Limited public resources have left local governments with difficult decisions about how to target resources to specific neighborhoods where stabilization efforts will jump-start private market activity. One of the key lessons learned is that public subsidy, land-banking, and private financing have all been essential to nonprofit housing practitioners in selectively demolishing, rehabbing or building new homes and selling them to lower- and moderate-income families.

Another lesson is that this targeted investment succeeds when it builds neighborhood resilience even after the limited public subsidies have been spent. Both CHN and HAP see signs that their work is having positive effects in restarting private market activity and improving the quality of life for residents in their targeted neighborhoods. Both organizations are now developing new strategies to maintain this positive momentum in an era of more constrained public resources.

In this article, we share our perspectives on these lessons. First, we define what we mean by "weak markets," and describe the challenges that weak markets pose to affordable housing development and neighborhood stabilization. We then provide an overview of our respective efforts in Cleveland, Ohio and Springfield, Massachusetts, and describe the initiatives that we have launched to target resources strategically as part of our neighborhood stabilization efforts. These cities have been hit hard by multiple cycles of disinvestment and, in

* The authors would like to thank Dennis Keating of Cleveland State University for his contribution to this article.

Springfield's case, a recent destructive tornado. As such, they face layers of challenges, but they have also been able to build on the foundation of previous efforts. When public dollars and commitment, such as the NSP funds and Cuyahoga County's land bank, are available, previous targeting decisions make nonprofit partnerships more effective at investing resources wisely in neighborhoods where they will leverage additional investment. In the final section of the paper, we examine two important financing tools for neighborhood stabilization in weak markets–public subsidies (in the form of the federal Neighborhood Stabilization Program) and land banking–and describe how these tools were used in the two different city contexts.

The Challenge of Neighborhood Stabilization in Weak Markets

Property values in older industrial cities like Cleveland and Springfield were already depressed when the crisis began and predatory lending practices leading up to the housing crisis infiltrated many communities. The subsequent recession only made matters worse, and the number of abandoned homes began to mount. As a result, affordable housing and community development nonprofits face significant challenges, both old and new, in revitalizing weak market neighborhoods. As scholar Alan Mallach described the situation, even before the crisis, "America's cities have not shared equally… in the economic gains of the past decade. While many cities have thrived, gaining new residents, companies, and visitors, others have not. Those 'weak market' cities continue to lose population, jobs, and businesses into the new century. Their threats are not land and housing shortages, but population loss and stagnant economies."[1]

All regional housing markets contain more and less desirable neighborhoods, and property values generally correspond with people's perceptions of the quality of life in each market. Cleveland and Springfield are weak market cities, where the costs of renovation or new construction exceed the market value of the homes. When rents do not cover the cost of operating an apartment building properly, an owner cannot justify further investment. When owners are unable to justify investment in their properties, homes and apartment buildings deteriorate. Similarly, when sales prices are lower than total development costs, building a new home or substantially renovating an existing structure even if the site is donated is unfeasible.[2] The financial imbalance in weak markets can lead to a downward spiral of neigh-

1 Alan Mallach, "Building a Better Urban Future, New Directions in Housing Policy for Weak Market Cities." Community Development Partnerships' Network, The Enterprise Foundation, Local Initiatives Support Corporation, and National Housing Institute, June 2005. Available at http://www.nhi.org/pdf/BetterUrbanFutureLong.pdf.

2 Peter Gagliardi, "Housing Programs in Weak Market Neighborhoods: Developing the Right Tools for Urban Revitalization." Working Paper 36. (Boston, MA: Pioneer Institute for Public Policy Research, December 2006).

borhood disinvestment and undermine community development efforts.[3] In these conditions, landlords often accept tenants willing to live in poorly maintained properties, without screening for rental histories or criminal backgrounds. This contributes to social and public safety problems. Ultimately, disinvestment leads to buildings that are so deteriorated and costly to repair and maintain that they are abandoned.

On the regional level, metropolitan areas experiencing minimal population growth or even population loss are particularly vulnerable to weak market dynamics that lead to vacant properties. In zero growth regions such as Greater Cleveland, for each new housing unit developed (typically in an outer ring suburb), one housing unit will inevitably go vacant, and this unit typically will be located in a troubled neighborhood (as all households strive to "move up" to the best living situation they can afford). The challenge for community development and affordable housing practitioners is to identify which neighborhoods have sufficient assets to build on, so that public subsidies can be used to leverage and spur private market reinvestment.

Opportunity Homes: Operating at Ground Zero

Foreclosures hit Cleveland early and hard. In 2012, more than 16,000 homes within the city stood vacant, drastically lowering neighborhood property values. The downward spiral, spurred by predatory lending during the early 2000s, undermined the positive investments that were occurring in many of Cleveland's inner-city neighborhoods. For example, the Slavic Village neighborhood became known nationally as "Ground Zero" in the nation's housing foreclosure crisis, undoing decades of community development investments. The number of foreclosure sales in the five-square-mile neighborhood swelled from 114 in 2001 to 840 in 2008, and average house prices dropped by 65 percent. In the aftermath of what has been termed "Hurricane Wall Street," the Slavic Village neighborhood hit bottom with countless vacant and vandalized properties offered as donations, and many more with sales prices significantly below $10,000.

It was against this discouraging backdrop that a group of community stakeholders and funders came together in 2008. A trio of nonprofits–Cleveland Housing Network (CHN), Cleveland Neighborhood Progress (formerly Neighborhood Progress, Inc.), and Enterprise Community Partners (Enterprise)–recognized the need for an immediate response to foreclosures and engaged key government agencies at the City of Cleveland and the Ohio

3 These weak market dynamics pose a different challenge from strong market dynamics, in which high property values cause total development costs to exceed affordability constraints (for either sale or rental). The significant difference is that in weak markets, the gap subsidy enables a house to be built that may cost double its market value, whereas in strong markets, the development cost does not exceed market value but requires a subsidy if the house is to be affordable to a family of modest means. In both scenarios, a significant grant or gap subsidy is required. However, the downward spiral of disinvestment in a neighborhood is unique to the weak market context.

Housing Finance Agency.[4] Together, they developed the strategic framework for what would become "Opportunity Homes." The aim was to stabilize neighborhoods and spur market recovery through a targeted, coordinated effort of housing redevelopment, demolition, reuse of vacant land, and foreclosure prevention.

At its core, Opportunity Homes, which was created as a single-purpose entity under the name Opportunity Housing Cleveland LLC, is a partnership of long-standing collaborators, public and private. Cleveland Neighborhood Progress (CNP) and CHN are the key planning and production partners for the initiative. CNP focuses on analyzing and mapping data in the target areas and evaluating the effort, while CHN is responsible for locating and acquiring properties, redeveloping according to Enterprise's Green Communities standard, and marketing and selling the homes, as well as taking on the overall coordination role.[5] Numerous sources provided funding for Opportunity Homes. The City of Cleveland provided demolition funds (additional demolition funds were later committed through the newly formed Cuyahoga Land Bank). The City also committed NSP funds for working capital and development gap funding. Additional development gap funding was secured from the Ohio Housing Finance Agency, Federal Home Loan Bank of Cincinnati, and the City of Cleveland's Community Development Block Grant program. Each source for buyer write-down had income qualifications, allowing for a range of buyers. The lease-purchase side was financed through Low Income Housing Tax Credits (LIHTC).[6]

Recognizing that the available subsidies were insufficient compared to the need, Opportunity Homes chose to target its resources to Cleveland's Strategic Investment Initiative (SII) areas. SII is a city-approved community development plan dating back to 2004 that focused on six neighborhoods–Buckeye-Shaker, Detroit Shoreway, Glenville, Fairfax, Slavic Village, and Tremont.

Opportunity Homes developed a strategy within a strategy, targeting select streets within the SII areas believed to hold the most promise for improving property values and restoring private developer engagement. This strategy also coordinated well with the city's long-range vision, the Connecting Cleveland 2020 Citywide Plan. Within these target areas, CHN and

4 Cleveland Housing Network has 30 years of experience as an affordable housing developer and service provider, and is known nationally for its large-scale, lease-purchase model using the Low Income Housing Tax Credit program. Cleveland Neighborhood Progress, is a local intermediary created in 1988 to provide technical and financial support to Cleveland's community development corporations (CDCs) as part of citywide revitalization efforts.

5 In addition to CHN and CNP, other implementation partners essential to the effort included City of Cleveland, Cuyahoga County Land Reutilization Corp., Case Western Reserve University's Center on Urban Poverty and Community Development, Cleveland State University, ESOP (Empowering & Strengthening Ohio's People), and six CDCs—Slavic Village Development, Tremont West Development Corp., Buckeye Shaker Square Development Corp., Detroit Shoreway Community Development Organization, Fairfax Renaissance Development Corp., and Famicos Foundation.

6 Additional funding partners included, Cuyahoga County Land Reutilization Corp., Dollar Bank, Enterprise Community Partners, First Merit Bank, Greater University Circle Living, Huntington Bank, Key Bank, Living Cities Catalyst Fund, Third Federal Savings and Loan, and CNP's Village Capital Corporation (VCC). All subordinate loan dollars to the LLC were also directed through VCC, a wholly owned subsidiary of CNP. Sources of subordinate loan funds included Enterprise Community Loan Fund, Living Cities, the Cleveland Foundation, and the George Gund Foundation. Most grant dollars flowed into the LLC through CHN.

CNP began to strategically redevelop vacant homes, target demolition of blighted homes, and prevent foreclosures in the target areas.

One of Opportunity Homes' greatest successes is arguably the Buckeye-Shaker neighborhood. Opportunity Homes redeveloped 97 homes, demolished 58, and prevented foreclosure in eight of 84 at-risk homes on the target streets. This work took place in a very small area that included the neighborhood's designated "Model Blocks" and a handful of blocks surrounding them, all close to anchor projects and the heart of the neighborhood. Although the foreclosure intervention effort proved difficult,[7] the development and demolition activities helped to stabilize neighborhood property values.

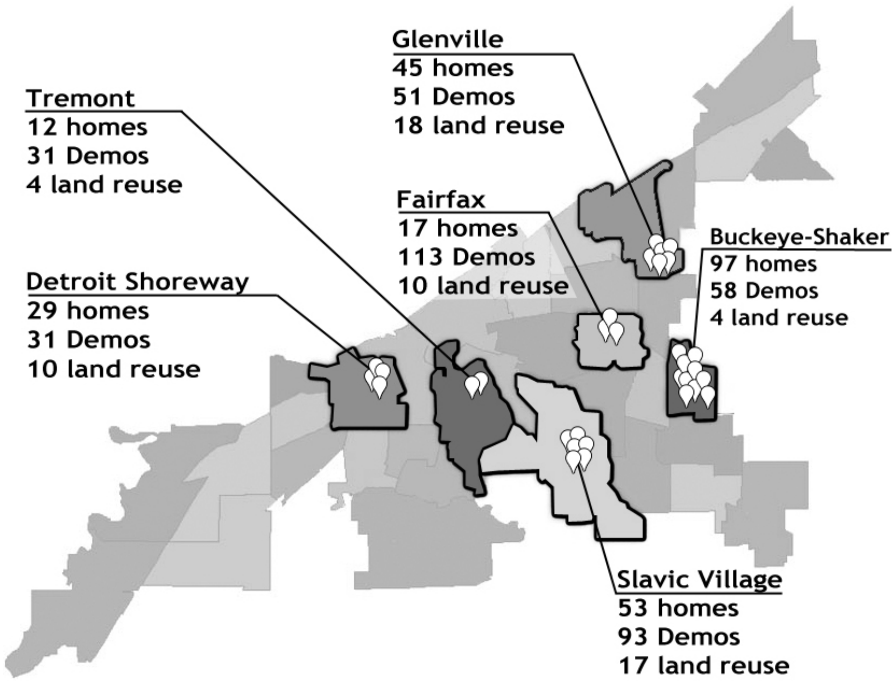
Perhaps more important, the efforts reinforced other significant investments in the neighborhood. Opportunity Homes' partner, CNP, together with the local CDC, worked together to revive a defunct hospital in the target area. Today, Saint Luke's is the centerpiece of more than $113 million in investments in the target area that include two new schools, a library, a reconstructed transit station, and a single family housing development. The impact is also evident in rising property values. From 2008 to 2012, the median property values in the target area increased by 24 percent (compared with a 14 percent decline for the entire neighborhood). The average Opportunity Homes sales price of $86,400 contributed to the increase, while the quality and chosen location of the rehabs contributed to quick sales.

The targeting strategy has been successful in other areas as well. Within all six SII neighborhoods, Opportunity Homes rehabbed 693 properties, created 253 infill homes, tore down 377 blighted homes, and sought land reuse in 63 cases (see Figure 1). Four of the six target areas saw property values grow more quickly than citywide rates. One area improved at the same rate as the city, and only one saw a market decline.[8] The success of each neighborhood depended on multiple factors including cost viability (i.e., home size and condition), neighborhood marketability, and the power of the anchor project to act as a catalyst for stabilization, suggesting the value of targeting investments in neighborhoods that have assets on which to build.

7 Opportunity Homes tried to go door-to-door to increase its foreclosure prevention outcomes, but families were skeptical, making the intervention less successful than was hoped.

8 Opportunity Homes had less impact on two areas (Tremont and Fairfax), but for vastly different reasons. Tremont remained relatively stable throughout the housing crisis. It had one of the highest housing values in the city because of its high desirability for urban living and market demand. The area simply had very few vacant homes. Fairfax began the crisis with extremely low values and an abundance of homes in extreme disrepair. The large size and extremely poor condition of homes made it infeasible to tackle a high number of rehabs.

Figure 1: Targeting Opportunity Homes Interventions in Cleveland's SII Neighborhoods, 2009–2012



However, choosing where to target limited resources even within the SII neighborhoods was a challenge. Among the thousands of vacant and abandoned properties, how does one decide which 50 to work on? In Cleveland, this targeting was data driven. To make informed decisions, CNP relied heavily on NEO CANDO, a database developed by Case Western Reserve University's Center on Urban Poverty. The system integrates multiple data sets to allow practitioners to make informed decisions and effect social change. Specifically, the data helped Opportunity Homes identify and map sites for potential acquisition and renovation targets. The data also helped them decide which blighted properties should be demolished and to pinpoint occupied homes whose owners were at risk of foreclosure. This system allowed CNP to prioritize and categorize destabilizing properties and use neighborhood market data to make decisions about returning properties to productive use. The data have also allowed Opportunity Homes to conduct more holistic assessments of neighborhood change, capturing emerging trends in neighborhood conditions (e.g., sales activity demonstrating signs of stabilization or further crisis) and measuring the impact of Opportunity Homes' investments. Finally, using data to make decisions about targeting scarce resources also helped to build political consensus around the location and nature of those investments and increased the transparency of why certain decisions were made.

Collaboration in Springfield: Old Hill and Six Corners

As in Cleveland, when the foreclosure crisis hit Springfield, Massachusetts, it was clear that any neighborhood stabilization efforts would need to build on existing community revitalization efforts. In the middle of the last century, Springfield boasted a strong manufacturing base with a robust downtown and healthy economic diversity. But as with many mid-sized Northeast cities, major losses in the manufacturing sector resulted in a slow and steady decline beginning in the 1970s.[9] Economic conditions were exacerbated by an early wave of foreclosures in the 1980s, and continued disinvestment and depressed property values throughout the 1990s. The recent foreclosure crisis only increased the number of vacant and abandoned properties in the lower-income neighborhoods of Springfield, along with speculation by investors who did not properly maintain or manage the properties.

Recognizing early on that there was a need to target its housing and community-building interventions, HAP had been working in the centrally located Old Hill neighborhood since the early 2000s. HAP had responded to neighborhood and stakeholder requests to assist in launching a revitalization initiative for three key reasons.

First, a significant share of the real estate was vacant and in distress; the neighborhood was known for its property abandonment, illegal dumping, and drug activity. Although some community development practitioners believe that revitalization initiatives should begin in areas where the neighborhood is relatively stable, HAP and its partners sought to have the greatest possible psychological impact by removing the most distressed buildings and interrupting crime habitats associated with abandoned properties.

Second, although Old Hill included several streets that were very distressed, the neighborhood as a whole had many assets. A driving factor in HAP's decision to target Old Hill was Springfield College, which anchors one end of the neighborhood. Springfield College was undergoing an expansion, and had launched its own master planning initiative, providing an opportunity for "town-gown" collaboration. Anchoring the other end of Old Hill is State Street, a central corridor of the city that leads from downtown Springfield to MassMutual, a Fortune 100 company that is an essential employer, tax-payer, and civic leader in the city. MassMutual launched the State Street Alliance that includes 40 other institutions committed to rejuvenating State Street as a vibrant urban boulevard. Along State Street are American International College, Springfield Technical Community College, and the Springfield Technology Park. Old Hill is also home to many churches including St. John's Church, which is a vibrant and growing African American church with a rich history.

Third, HAP believed that starting in Old Hill was also important from a social equity perspective. This traditionally African American neighborhood had properties languishing

9 The poverty rate in Springfield is nearly three times higher than the statewide rate in Massachusetts. Overall, 27 percent of Springfield residents live below the poverty line. In the abutting neighborhoods of Old Hill and Six Corners, the poverty rate is 35 percent and 45 percent, respectively. While the Springfield metropolitan area ranks among the 100 largest metropolitan areas in the country, Springfield is commonly acknowledged as a weak market city.

in land court and tax taking for more than a decade. It also suffered from illegal dumping, and a level of criminal activity that would not have been tolerated in other neighborhoods.

HAP's first commitment to Old Hill–and its own area of expertise–was an aggressive housing agenda. It became clear, however, that to transform the neighborhood, more than a housing plan would be needed. A comprehensive neighborhood revitalization approach was essential, and it required multiple investments in infrastructure, schools, public safety, and housing, all linked synergistically. After working closely with Springfield College, the Old Hill Neighborhood Council, and many community partners on a neighborhood master plan, HAP built the Partnership for the Renewal of Old Hill into a group of more than 45 partners and supporters. The group worked on a variety of improvements to public safety,[10] educational opportunities, and infrastructure such as parks and streets. Concurrently, HAP worked with collaborating developers Springfield Neighborhood Housing Services and Greater Springfield Habitat for Humanity to form the Old Hill Revitalization Collaborative and an associated limited liability company that served a land banking function. Initially, this group focused its efforts on acquiring, rehabbing, or demolishing and redeveloping distressed one- and two-family homes. To maximize impact, the group acquired additional properties to add to the land bank as part of a cluster development strategy. This land banking effort was financed through a line of credit from TD Bank, supported by two philanthropic grants and a loan guarantee from Springfield College.

Prior to the crisis, housing development targeted for first-time homebuyers was financed with construction loans paid off when buyers purchased their homes. Grants provided by federal HOME funds filled the development funding gap. When the foreclosure crisis hit and property values began dropping, however, taking on additional debt was risky and NSP funds became the main source of funding for real estate strategies. Just as in Cleveland, HAP's preexisting neighborhood targeting strategy provided a framework for foreclosure response strategies, and the Old Hill and adjacent Six Corners neighborhoods became targeted areas for federal NSP investment.[11]

In June 2011, another disaster struck in the form of a deadly tornado. The tornado cut a wide swath of destruction and the neighborhoods that had been targeted by HAP for neighborhood revitalization were two of the hardest hit. In the wake of the tornado, HAP has continued to focus on these neighborhoods, and continues to couple real estate owned (REO) disposition strategies with broader revitalization efforts. On the basis of its experience, HAP is not only addressing tangible housing redevelopment projects and distressed

10 The Partnership for the Renewal of Old Hill addressed public safety issues with a federally funded Weed and Seed Initiative. This program reduced gun violence related to the drug market and local gang activity through data-driven police intervention, a faith-based anti-gang initiative, and investment in area youth programs.

11 After making a significant commitment to revitalize the Old Hill neighborhood, HAP initially responded to the City's request to address deteriorated housing in a small pocket of the Six Corners neighborhood. With NSP funding, HAP later targeted another street in Six Corners. However, it wasn't until the tornado destroyed a swath of the neighborhood surrounding the HAP-developed homes that HAP made a more significant, multi-dimensional commitment to Six Corners.

REOs, but also looking at the neighborhood assets holistically. Working closely with neighborhood leaders, HAP is advocating for a commercial redevelopment plan in Six Corners and seeking to turn a newly built school into a full-service community school to meet parent and community needs.

Key to HAP's success is collaboration with other groups, as well as community engagement. HAP has hired a community-building manager to engage local residents, neighborhood councils, businesses, and other stakeholders in planning and advocating for transformative redevelopment of their neighborhoods. In addition, the City responded to the aftermath of the tornado by placing liens on properties to ensure that owners repaired or demolished property rather than walking away from the property with the insurance proceeds. The City received $21 million in Disaster Relief Community Development Block Grant (CDBG-DR) funds, a portion of which will be allocated to support housing interventions. Although CDBG-DR funding will not be enough to rebuild on all of the vacant land, there is the opportunity to leverage this funding with other sources to build new homes where problem properties once stood.

The investments of key stakeholders in Old Hill have spurred additional investment from both the public and private sectors. After HAP and the Old Hill Revitalization Collaborative (the Collaborative) began their targeted efforts in 2003, the City began to take a proactive role in investing in Old Hill and Six Corners. In addition, as a result of the attention HAP and its partners brought to Old Hill, the State of Massachusetts, interested in promoting the city's economic revitalization, directed a portion of its funds to neighborhood infrastructure improvements in the area. The result was the reconstruction of a key north/south corridor shared by these neighborhoods, punctuated with period lighting and other amenities. Public funding was also directed toward improving neighborhood roads and sidewalks, planting trees, and creating new playgrounds. Public funds also supported the private-sector initiative to transform the schoolyard of a neighborhood magnet school into outdoor classrooms and new athletic fields.

The success of the Collaborative's strategies is now starting to be visible in the upgrading of properties throughout the neighborhood, but especially on its target streets. After conducting extensive surveying using the Success Measures outcome evaluation tool in 2009 and again in 2012, HAP has found that residents' willingness to invest in their properties was correlated with increased confidence in their neighborhood's resurgence.[12] Compared with 2009, 20 percent more homeowners in 2012 reported that they were likely to make home repairs. The survey also documented a significant increase in the number of respondents who reported feeling safer in the neighborhood, and who linked these feelings to the removal of abandoned buildings.

12 Success Measures is an outcome evaluation resource used by community-based organizations to objectively assess programmatic impact. NeighborWorks America supports this program.

Financing Redevelopment in Weak Markets

The fundamental financial challenge in weak market cities is that development costs exceed market values. Debt financing, grant funding, and institutional resources for a land banking strategy in Springfield and a quasi-public land bank in Cleveland have all helped to bridge this challenge for CHN and HAP as they carry out housing development interventions in their communities.

The Importance of Public Subsidy: The Neighborhood Stabilization Program

In both Cleveland and Springfield, the importance of NSP funding as a resource during the depths of the foreclosure crisis is hard to overstate, notwithstanding the challenges associated with the program.[13] Both CHN and HAP typically finance their development costs with construction loans primarily through private debt. However, in this case, not only did public NSP funding fill the gap between development costs and market values, but it substituted for private debt when private investment was unwilling to put capital at risk and developers were unwilling to assume debt owing to market volatility.

In Springfield, because home prices had collapsed and were unstable, HAP's leadership felt it was too risky to borrow funds against a projected sales price and timeframe. Although the homes HAP built sold within a few months of completion at an appraised value close to its projections, that outcome was far from certain when construction began. NSP funds functioned effectively as a revitalization tool both because they filled development financing gaps, and because they allowed those with moderate incomes (up to 120 percent of area median income) to buy a home, and required resale restrictions of as few as five years. Other housing investment programs in Massachusetts usually impose long-term deed restrictions on income eligibility and resale, and have typically been designed to address housing cost inflation in booming markets or promote economic diversity in higher-income communities. In strong markets, long-term deed restrictions are appropriate for offering a fair return at resale while preventing a windfall profit. However, in weak markets these requirements can be counterproductive and add to economic segregation. In weak market neighborhoods where home value appreciation is already very limited, resale restrictions can result in returns that do not fairly reward a homeowner who made an investment in a revitalizing neighborhood. In Springfield, NSP funding enabled homes to be marketed to buyers with a larger range of incomes and offered enough financial incentive (because of minimal resale restrictions) to attract homebuyers who might not otherwise have invested in Old Hill or Six Corners.

As in Springfield, Cleveland used NSP funds to attract a relatively diverse income spectrum to Opportunity Homes, and to keep prices reasonable–at the 90–100th percentile of

13 NSP, deployed quickly and in the midst of the foreclosure crisis, was launched without implementation regulations in place, and it was administered with a level of detail and scrutiny that added to housing development administrative costs.

current market activity.[14] Thanks to the Cuyahoga Land Bank, acquiring the land was not the most difficult part of redevelopment, but NSP played a vital role in filling the gap between appraised values and total development costs. Its involvement also allowed Opportunity Homes to pursue multiple strategies, ranging from demolition to high-quality lease-purchase renovations to high-quality for-sale renovations. For example, NSP funds were used to finance second mortgages for first-time homebuyers who were unable to come up with a 20 percent down payment.[15]

CHN also used NSP funds to leverage LIHTC in a successful lease purchase model. The model offers homes with affordable rents to residents for 15 years and then, because there is little initial debt on the properties, sells the homes at an affordable, sustainable price to low-income owners.[16]

With NSP funds dwindling, both CHN and HAP anticipate that they will have fewer resources to operate their neighborhood stabilization efforts. While values have stabilized in many of their targeted neighborhoods, the basic problem of high-cost development and low property values remains in both communities. CHN and HAP are developing new strategies to ensure the positive momentum of the early success in jump-starting private market activity and improving the quality of life for neighborhood residents continues in an era with more constrained public resources. Some ongoing federal programs are important sources of funds that leverage additional capital to support their continued work.

In Cleveland, CHN has successfully used LIHTC investments since 1987 to finance the rehabilitation and new construction of scattered-site, single-family homes in weak housing markets. LIHTC allocations are becoming ever more competitive, and CHN's lease-purchase model competes with other types of affordable housing investment opportunities in Ohio, thus this funding source can no longer finance development at a consistent scale. In addition, without NSP, there is no subsidy to support second mortgages, which fill appraisal gaps and improve affordability for first-time homeowners.

In Springfield, it is anticipated that CDBG-DR funds could serve as a close substitute for NSP, filling development gaps and promoting new homeowners' investment in targeted neighborhoods. The disaster response has also spurred valuable public and private philanthropic investment in comprehensive planning, which is providing a new vision to guide ongoing neighborhood efforts. The Massachusetts Department of Housing and Community Development will reinstate its homeownership development program, which was suspended

14 However, this percentile varied widely from neighborhood to neighborhood, so homes were sold on the basis of "micro" market values. One target area might have a 100th percentile price point of $65,000 while another nearby area might be as high as $150,000. In the end, the median sales price across all target areas was $85,000. Even so, this price did not cover the costs of the extensive rehab needed on most homes.

15 In the context of the current banking environment, with loans capped at 80 percent of loan-to-value, second mortgages for first-time buyers are particularly important.

16 As the largest developer of LIHTC-funded single-family homes, CHN has three decades of experience in scattered-site rental housing. CHN has built significant organizational capacity (nearly 70 staff) to manage all aspects of its scattered site lease-to-purchase program, including lease-up, compliance, resident needs, property maintenance, sales, and asset management. CHN is quite successful with this model, having developed nearly 2,700 homes with an 85 percent transition rate to homeownership. CHN will continue this flagship program for as long as LIHTC funding is available.

during the foreclosure crisis. However, as with CHN, HAP anticipates that post–NSP resources will be fewer and support a lower level of real estate activity.

Land Banking

The experiences of Cleveland and Springfield—and the scale of the neighborhood stabilization efforts CHN and HAP have implemented—are distinguished by the degree of local institutional capacity in each city, and the greatest difference is the existence of the Cuyahoga County Land Bank. The Springfield area does not have a large, quasi-public land bank. Although HAP was instrumental in creating an LLC to undertake a land banking function in the early stages of its Old Hill efforts, it was a small, targeted, private effort based on private debt financing with credit enhancement, and a business model that assumed a stable housing market. The Old Hill Collaborative, described earlier, assembled $1.5 million in financing to acquire properties that HAP and its collaborators were interested in later developing. HAP served as the manager of the limited liability company. The intention was to hold properties acquired for a short period, while pursuing funding to assemble clusters of parcels for redevelopment. When the foreclosure crisis hit, the land banking model suffered greatly. Homeownership development funding programs administered by the Massachusetts Department of Housing and Community Development were suspended when the inventory of homes on the market began to grow, and NSP funds were targeted for foreclosed property. Most of the land banked property had been held too long to qualify as "foreclosed" and did not meet the other priority categories that local administrators used to guide NSP investments, leaving HAP unable to move forward with developing property in its land bank. HAP is still holding some of the property (and incurring ongoing costs) while the overall homeownership market recovers and the City of Springfield devotes its limited resources to rebuilding from the tornado.[17]

In contrast, the Cuyahoga County Land Reutilization Corporation (CCLRC, also known as the Cuyahoga Land Bank) is a quasi-governmental corporation that, while still insufficient to address the scale of the problem in Cleveland, has proved immensely valuable to redevelopment efforts (see Box 1). In Cleveland, CHN has partnered with the CCLRC since 2008. Projects that typically would have taken the organization 12 months to put together can be done in fewer than six months with the land bank's support. The land bank has helped to keep critical, affordable housing projects alive for CHN, stepping in to purchase and hold properties while other financing could be assembled—flexibility that simply does not happen in private-market deals. The partnership has allowed CHN to significantly reduce the intensive labor, time, and costs associated with locating and acquiring vacant homes. Previously, CHN might have spent months to research, assess, and negotiate the sale of a handful of vacant properties before rehab could even begin, paying as much as $15,000 per property—that is, if the owner could be located. Today, the CCLRC conducts the due diligence, holds the property as necessary (or demolishes), and sells for a nominal amount.

17 With DHCD reinstatement of its homeownership financing program, HAP may be able to develop some of the remaining parcels, and it is also looking for other potential buyers and strategic uses for the properties in the land bank.

Box 1:

The Cuyahoga County Land Reutilization Corporation

The Cuyahoga County Land Reutilization Corporation (CCLRC) was formed through advocacy efforts by local leaders. The leaders pushed for new legislation to gain more authority to deal with abandoned, vacant properties. The legislation that created the county land bank, Ohio SB 353, allows a local entity to accept, demolish, and transfer vacant properties to responsible redevelopers. (This is different from the City of Cleveland's own land bank, which can accept vacant land only; the county bank can accept vacant houses as well as land, execute a demolition system for unviable homes, and keep vacant homes out of the hands of ill-intentioned speculators.)

CCLRC has the ability to acquire vacant and abandoned foreclosed properties from a variety of sources and demolish or rehab the homes and get them quickly back into the market. These sources include banks, government-sponsored enterprises such as Fannie Mae or federal and state agencies such as HUD, as well as real estate lost to tax foreclosure and donated properties. Each city in Cuyahoga County is a major partner in decisions about CCLRC-owned properties within its borders. For example, CCLRC's partnership with the City of Cleveland and its land bank includes handing over title to all vacant land after completing demolition. The goal of the partnerships with local municipalities is to promote collaboration, spread risk, and to make joint code enforcement and nuisance abatement operations possible.

CCLRC has been instrumental in assuming responsibility for more than 1,000 vacant properties. It has established unprecedented agreements with several major lenders (Wells Fargo and Bank of America), who have agreed to donate vacant properties to the land bank and pay for demolition costs. The land bank also is the only bulk repository of vacant and abandoned properties with Fannie Mae and HUD. This has resulted in a significant slowdown of "flipping" and speculative trafficking in low value, abandoned properties in Cuyahoga County. The Cuyahoga Land Bank is also the first enterprise capable of receiving privately foreclosed, abandoned properties directly without sheriff's auctions. This allows properties to be more responsibly mothballed and repositioned for rehabilitation or demolition. These abandoned properties have gone through cycles of tax foreclosure and abandonment and speculative trafficking, which have proved devastating to large sections of the region.

CCLRC is based on the Genesee County, Michigan land bank, which was created to deal with similar problems in Flint and the surrounding county. While funded in part by Cuyahoga County, it is a nonprofit organization and as such is not subject to the normal political and bureaucratic constraints of government. Primary funding is from the accumulation of penalties and interest on collected delinquent real estate taxes and assessments. This primary revenue stream is supplemented by grants from the land bank's partners, CCLRC's sale of acquired properties to qualified rehabbers and housing developers, and from the donations and recoupment of funds from various banks. CCLRC has also received funding through the federal NSP and more recently through the Ohio Attorney General's allocation of $75 million (from a federal national settlement with five major banks).

Conclusion

The Springfield and Cleveland stories differ in many respects, particularly in the scale of the revitalization efforts and the resources, institutions, and partners available in each community. However, both HAP and CHN have started to see positive results from targeted housing investment as part of a comprehensive, multi-partner strategy in their targeted neighborhoods. Mission-driven housing organizations such as HAP and CHN bring both housing expertise and connections to private and public entities to effectively implement strategic investment approaches.

Both HAP and CHN's experiences underscore the value of long-term targets and plans. This approach offers a strategic path and institutional infrastructure when crisis hits, and helps to build resilience in neighborhoods, a critical factor in weak market cities and regions. HAP and CHN, along with their partners, are well positioned to build on the groundwork laid previously in targeted neighborhoods.

Both cities struggle under multiple cycles of disinvestment and, in Springfield's case, a natural disaster. Despite these layers of challenges, both cities have been able to build on the foundation of previous efforts. When public dollars, like NSP funds, are available, previous targeting decisions allow nonprofit partnerships to be more effective in investing resources wisely, in neighborhoods where they will leverage additional investment.

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Sarah Page is Senior Vice President of Community Building at HAPHousing and has been with the organization since 2004. HAPHousing is a large regional housing organization serving 43 cities and towns in Western Massachusetts with 40 years of experience offering a broad range of housing programs and is actively involved in developing and managing affordable housing across the region including in its urban core. She leads collaborative neighborhood revitalization including initiatives to rebuild sections of Springfield target neighborhoods destroyed by the June 2011 tornado in Springfield, MA. She has over 25 years of experience in the housing and community development field.

Scaling Social Enterprises: Flexible Responses for Neighborhood Stabilization

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The economic crisis has affected low-income and minority communities more severely than others, with falling home values, mortgage foreclosures, growing numbers of vacant properties, and high unemployment rates. This crisis has been distinguished by the micro-level, human impact of foreclosures and neighborhood distress, combined with business and macroeconomic impact and market failure. New social enterprises, led by community development nonprofits, have stepped into the breach. These groups have long histories of working with low-income and minority communities as well as an ability to address market failures with creative solutions. The best of these enterprises are building a track record of keeping families in their homes, putting people back to work, and stabilizing vacant properties.

Social enterprise models have been critical in the recent crisis because resources are few, the need is great, and the challenges are new. Since 2007, the market has changed rapidly and frequently. Significant federal policy response did not arrive until 2009; and in 2013, public stimulus has largely been exhausted even as foreclosures continue to affect millions. In this changing market context, social enterprises have the advantage of an inherently responsive and flexible approach to creating social impact through a self-sustaining, or at least highly efficient, business platform.

However, like all businesses, social enterprises face challenges in starting up, sustaining themselves, and growing to scale. Three enterprises demonstrate how entrepreneurial approaches have met some of the challenges of the recent crisis and have had a real impact at the human level. Boston Community Capital's SUN Initiative, Mercy Housing Lakefront's 180º Properties, and National Housing Trust-Enterprise Preservation Corporation (NHT-Enterprise) also demonstrate lessons learned about capitalizing, operating, and expanding a new enterprise.[1] Together, these examples show that a careful, analytical approach, appropriate capital, and the right partners are keys to meeting the demand to expand into new geographies and to grow the scale of their social impact.

1 All three organizations are engaged in a peer exchange community through the Housing Partnership Network's Innovations in Neighborhood Stabilization and Foreclosure Prevention Initiative, funded by the Citi Foundation.

The Importance of Capitalization and Operations Capacity

The right organizational capacity–both human and financial–is a key element in successful social enterprises. Working capital is critical to building an effective social enterprise, and many nonprofit social entrepreneurs still have a hard time accessing it. People and operating systems with the right expertise are also critical to nonprofits entering new industries.

Start-up, Working, and Expansion Capital

Mercy Housing Lakefront and The Cara Program

When Mercy Housing Lakefront (MHL) and The Cara Program (TCP) launched a new social enterprise, 180° Properties, in 2009, they began operations with a $400,000 start-up grant from the JPMorgan Chase Foundation. 180° Properties provides comprehensive property services, a positive community presence, and permanent jobs for low-income and disadvantaged workers. It trains workers, such as Darnella, to protect and maintain vacant homes. Darnella believes the company is turning around communities. "I know lots of people who appreciate what we do when we go into these properties and board them up, and clean them out. The neighbors, especially the more established ones, are so grateful." The program is also a turning point for the individual workers. "I made a 180 degree turnaround," Darnella explains. "I am not going back, no matter what. I came from the streets, rough areas, crime, and I grew up in it," she said. "I have four daughters and don't want them to grow up the way I did. I want them to prosper and do much, much, much greater things than I could possibly imagine."

The program relies on TCP's expertise in providing motivational coaching, case management, and life- and career-skills development to create a pipeline of entry-level applicants and the expertise of MHL in the housing market. As of January 2013, 50 employees were working to secure and maintain approximately 5,000 homes per year. Workers receive safety, equipment, and on-the-job training to clean, secure, rehabilitate, and maintain foreclosed homes. Crews change locks, install lock boxes, board up windows, remove debris, care for lawns, and perform various demolition and building chores. Individuals earn $12 to $13 per hour starting pay and full benefits, including long-term disability insurance.

When launching the program, both MHL and TCP insulated their core programs and mission from the risk of the new enterprise by not putting the organizations' existing assets at risk. Instead they began operations with the JPMorgan Chase Foundation start-up funds. They later raised additional funds for capital expansion costs from a succession of other philanthropic funders. In 2011 and 2012, nine funders from the philanthropic, financial institution, and nonprofit sectors combined to invest almost $1 million in expansion grants.

The plan was for 180° Properties to generate income for its parent organizations, a common driving force behind nonprofits' social enterprise endeavors. However, it soon became apparent that, although 180° Properties could break even on its operations by charging for its property maintenance activities, to meet growing demand, it would require ongoing reinvestment of the profit. To recruit, train, equip, and employ each three-person crew cost approximately $200,000 before the crew became economically self-sufficient. Current projections indicate that 180° Properties might reach a point of true self-sustainability in several years if it expands from the two cities in which it now operates to serve several major markets and if it continues to find a niche for its professional services in a constantly changing environment for property preservation and rehabilitation jobs.

MHL and TCP could have expanded the business faster and supported its expansion more efficiently if they had kept a modest operating reserve of approximately $250,000 to protect against seasonal and payment variations, while also maintaining cash on hand for budgeted operations. However, at the time, they could not afford to do so. They recently secured a low-interest working capital loan from the Housing Partnership Fund to assist in managing cash flow. It is rare, however, for nonprofits to have cash reserves available to support the development of a new enterprise. Even when nonprofits have adequate cash on hand, it is typically restricted for use in their core missions and programs.

Even though it is not yet self-sustaining, MHL sees a financial value in 180° Properties. The program does "more with less," making efficient use of limited subsidy dollars while allowing MHL to have a greater impact in distressed neighborhoods. MHL is seeking to raise an additional $1.5 million to employ 10 new crews. The crews will enable 180° Properties to secure, rehabilitate, and maintain more than 9,600 foreclosed homes per year. In all, the program will be able to secure and maintain more than 31,000 unique foreclosures and leverage $26 million in earned income over a five-year period–at a cost of just $47 per house in philanthropic support.

180° Properties projects that further expansion will enable it to generate profits that will not need to be reinvested in the business. As a result, 180° Properties is also exploring the potential for an equity investment of approximately $500,000 to $600,000 from a private or social investor to further accelerate and sustain growth.

Boston Community Capital's Stabilizing Urban Neighborhoods Program

Another way to capitalize a new social enterprise is the approach taken by the Boston Community Capital (BCC) Stabilizing Urban Neighborhoods (SUN) Initiative. This initiative purchases foreclosed homes or homes for which the loans are in default in order to keep families in their homes, like Delia.

"When I came to America in 1995, my goal was to live the American Dream," says Delia, a resident of Boston's Dorchester neighborhood, speaking through her daughter. "Owning my home is a big part of that." Delia operated a home day care business, which helped pay her mortgage. But the economic crisis hit her business hard, as the majority of her clients lost their jobs. She dipped into her savings to pay for her mortgage, but her savings were soon gone and she fell behind on her mortgage payments.

BCC met with Delia, reviewed her finances, and helped her understand what she could afford to pay monthly. BCC also got in touch with her lender, offering to purchase the property for its current market value. The bank agreed, and in July 2012, BCC's SUN Initiative helped Delia repurchase her home, reducing her monthly mortgage payment by 37 percent and her mortgage principal balance by 39 percent. "Working with SUN saved me," says Delia, "Today I have four grandchildren, who I am raising in this house. And that's my dream come true."

The SUN Initiative buys foreclosed or distressed homes from lenders at the price lenders can expect to receive at foreclosure–often as much as 50 percent less than the unpaid balance of the loan. After SUN acquires a home, it sells it back to the original owner with a new, affordable 30-year, fixed-rate mortgage. SUN loans help reduce homeowners' monthly housing expenses and mortgage principal balances, on average, by approximately 40 percent. As of June 2013, SUN had provided more than $60 million in new mortgages to more than 280 Massachusetts homeowners, stabilizing more than 400 households. SUN's parent organization, BCC, was founded in 1984 as a nonprofit community development financial institution (CDFI) and has made more than $900 million in community development investments.

Because BCC is a CDFI with a substantial track record, net worth, and a core mission of providing financing for community development, the organization was able to self-fund much of its new venture when it started SUN. Between 2009 and 2013, BCC contributed more than $5 million in seed capital and $10 million in debt from its loan fund to the initiative, which has leveraged more than $75 million in investment from individuals and institutions. BCC has raised additional philanthropic dollars as a supplement to support research and development, loan loss reserves, and closing costs for low-income individuals and families who would not otherwise be able to participate in the SUN program. The additional funds also support documentation and planning for replication.

However, BCC also faces capitalization challenges as it seeks to expand. BCC needs a secondary market source to recapitalize the initiative if it were to serve more customers and demonstrate a source of liquidity for investors. BCC has made significant progress toward addressing this challenge. In May 2013, it secured a $25 million investment from East Boston Savings Bank to support its expansion efforts, followed by an additional $10 million in August 2013. These investments, the first such transactions of their kind, are backed by revenue from a pool of performing mortgages SUN has made to homeowners who were previously facing foreclosure. These transactions, arranged by Zions Bank's Non-Profit Investment Banking Group, demonstrate that new, fair market loans to distressed homeowners can work for lenders and investors while keeping homeowners in their homes and providing them with a new affordable mortgage–the value proposition BCC set out to prove when it started SUN.

In addition to using the capital to support new mortgage loans as it expands SUN's model in Massachusetts, BCC is using these transactions as a model to raise additional funds for SUN on similar terms to support its expansion to other communities around the country hit hard by foreclosure. Community organizations and civic leaders interested in SUN's model have stated that the ability to raise long-term affordable loan capital has been a significant barrier to entry; BCC will use funds from its secondary market transactions as loan capital to support the launch of SUN in other states. This fall, for example, the organization entered Maryland, working with on-the-ground partners who identify foreclosed homeowners who may qualify for SUN. BCC underwrites the homeowners and provides mortgages using loan capital raised for SUN.

NHT-Enterprise: Energy Retrofits for Affordable Multifamily Developments

While not a stand-alone social enterprise, the National Housing Trust-Enterprise Preservation Corporation (NHT-Enterprise) provides another example of entrepreneurship and innovation. The organization changed the way it does business in order to tap into national utilities as a source of capital to retrofit affordable, multifamily housing to achieve energy efficiency, and thus reduce operating expenses for building owners. Although the programs have helped single-family homeowners to reduce energy costs, multifamily rental properties have been traditionally underserved.

NHT-Enterprise views energy efficiency as an important strategy for preserving affordable housing and community revitalization. High energy costs in existing multifamily housing make it difficult to sustain affordable rents. In subsidized properties, utilities are the largest operating expense in master-metered buildings, and the second largest in individually metered buildings. Controlling and reducing these operating expenses is needed to free up capital for maintenance, repairs, and other necessary improvements.

Mountain View Tower in Cumberland, Maryland, which provides affordable housing for low-income seniors, is an example of the program's impact. Built in 1977, it was not constructed to conform to modern energy codes. NHT-Enterprise redeveloped the property with significant energy efficiency upgrades. The Maryland Department of Housing and Community Development's Multifamily Energy Efficiency and Housing Affordability program (MEEHA) provided funding for the upgrades. MEEHA is funded by Maryland's investor-owned utilities. The energy efficiency improvements will maintain affordability for low-income seniors by lowering operating expenses.

NHT-Enterprise's engagement with the energy sector has led to the dedication of more than $40 million in private utility funding for retrofits of existing, affordable housing. NHT-Enterprise is currently pursuing its utility engagement work in eight states (Colorado, Minnesota, Illinois, Michigan, Ohio, Pennsylvania, Maryland, and Rhode Island) and the District of Columbia. NHT-Enterprise's approach has parallels to BCC's and MHL's experiences, particularly in that the organization operates in a new business sector and has strategically expanded its work, state by state.

Operational Capacity

SUN, 180° Properties, and NHT-Enterprise's energy work all differ in important ways from the core businesses of their parent nonprofits, and that distinction required the groups to adapt in various ways. An early adaptation was to hire or partner with people with industry-specific experience.

As did MHL and TCP in the property preservation business and BCC in the consumer mortgage niche, NHT-Enterprise faced a learning curve in entering an established industry of utilities and energy advocates. Initially, it had assumed that it would be easy to convince utilities that retrofitting an underserved sector was in their self-interest. NHT-Enterprise's first meeting with a number of nonprofits and utilities in California, however, proved otherwise, largely because they had not first engaged with energy efficiency organizations prior to meeting with the utilities. After almost four months of little progress, NHT-Enterprise began to understand that gaining the trust of utilities meant that it first had to meet with energy policy stakeholders–not the housing developers with which it was accustomed to dealing. That shift was transformational. Although utilities were not necessarily always in agreement with energy organizations focused on lower-income households, the utilities knew and trusted these organizations. After gaining the respect of the parties involved, NHT-Enterprise was able to bring in local housing developers to demonstrate the effect of energy retrofits to existing affordable housing.

Throughout its efforts, a series of partners has added to NHT-Enterprise's own organizational capacity, expertise, and relationships. This has allowed it to pave the way into a new industry. NHT-Enterprise now conducts its work with key national partners including the American Council for an Energy-Efficient Economy (ACEEE), the National Consumer Law Center, and the National Resources Defense Council.

MHL and TCP similarly recognized the need to broaden their expertise to be successful in developing a new venture. Both added management capacity, realizing that the capacity of organizations designed for another purpose cannot necessarily be efficiently deployed to support a social enterprise start-up with a different business model. In 2011, 180° Properties hired a new CEO with significant home building experience as well as dedicated administrative support staff. One of the CEO's first challenges was to implement new operational systems that could support high-quality services delivered efficiently and at scale. 180° Properties has now developed scalable job costing, billing, project management, and quality control systems to manage the work of scattered crews. Crews use cell phones and laptops with wireless connections to access work orders, upload status reports and property photos, and receive instructions while working remotely throughout the region. 180° Properties is still working to build an ideal team to manage its evolving business. For example, it needs to implement separate sales and collections teams so that staff recruiting new clients to the firm are not also responsible for managing cash flow and receivables from those clients.

For BCC, one key to its success was its mortgage brokerage affiliate, Aura Mortgage Advisors. In the mid-2000s, BCC recognized the opportunity to apply its lending expertise and community development mission to provide affordable, fixed-rate mortgages to low-income residents, and founded Aura. Aura eventually became licensed as a mortgage lender and became a key element in the SUN Initiative. Without that lending arm, it would have been much more difficult to get SUN off the ground. But BCC also recognized the need to reorganize its operations with the right staffing and processes. Specifically, BCC hires management and staff who combine a deep understanding of the mortgage finance business with an entrepreneurial spirit and dedication to the population they serve. BCC has also bolstered its staff by hiring consultants with expertise in compliance, underwriting, and strategic communications. In order to assure consistency in values and alignment of SUN's work and business strategies with BCC's long-term vision and direction, BCC's CEO functions as president of SUN, playing an integral role in management, strategy, capitalization and business development. These staffing changes led to a 300 percent increase in lending from 2011 to 2012.

The SUN Initiative is also complex. Because of its individualized approach to preventing displacement for families in foreclosure, it requires a high degree of customization and manual underwriting. In addition, it operates in a regulated, and quickly changing, environment. To manage this complexity, SUN has developed a set of flow charts, check lists, reporting and analysis systems, and staff training and certification procedures. However, it also recognizes that the operational demands of foreclosure relief and mortgage lending will continue to be resource-intensive. For example, it puts all potential applicants through two underwriting processes. The first stage ensures that the current property value and borrowers' ability to pay can support a successful transaction that will also support SUN's operating costs. The second underwriting process begins at the conclusion of a successful negotiation with the seller of the property, which can take months to accomplish.

Adapting to a Changing Environment

Another challenge for all of these enterprises has been adapting to changes in the housing market and the evolution of the foreclosure crisis. 180° Properties, for example, has altered its program focus as the foreclosure crisis in its home market of Chicago has progressed. At first, as banks began to accumulate vacant REO properties, 180° Properties deployed temporary workers participating in a training program as a way to get immediate work experience doing lock changes, clean-up, and basic maintenance. Eventually, as the inventory of REO grew and neighborhoods became more distressed, properties remained vacant longer and needed more substantial repairs, light rehab, and eventually full rehab. 180° Properties realized that the employment opportunities it could offer were no longer temporary, low-skilled jobs, but instead more substantial, permanent jobs that required training and offered real professional development and skill-building opportunities. Now, as the real estate market slowly recovers, private equity firms have begun to purchase, renovate, and rent foreclosed homes. These large-scale investors, with properties widely scattered throughout entire regions, have helped create a new market for 180° Properties, which has the potential to drive further growth. With each change in the market, 180° Properties has responded by changing its operations, marketing, and partners.

BCC, too, has created a highly flexible business model that can adapt to market opportunities. For instance, when acquiring the properties it intends to sell back to the original, underwater homeowner, the organization will purchase mortgages or properties, pre- or post-foreclosure. While BCC notes that banks can avoid the costs of foreclosure and eviction by selling distressed loans or properties to BCC prior to foreclosure, nearly all of SUN's initial transactions were negotiated after foreclosure with the REO departments of banks. Today, roughly half of its transactions are closed as short sales, while the rest are completed post-foreclosure, but before the original homeowner is evicted. To accommodate sellers' requirements, BCC has also been flexible in its approach to resale of properties to homeowners. Some lenders require that BCC hold a property on its books for up to six months before reselling it to the original homeowner. BCC addresses this challenge by signing a purchase and sale agreement with the homeowner, charging monthly fees equal to the monthly mortgage payment, plus $100 per month to cover water and sewer costs, for the "hold" period.

BCC also built flexibility into its business model to ensure that SUN could be self-sustaining at different levels of business activity. If the organization were to stop lending at its current size, the income from existing mortgages would be able to support the ongoing operating costs associated with maintaining them. (BCC would no longer need an origination, processing, underwriting, and closing function and could reduce staff accordingly.) On the other hand, if BCC expands the SUN Initiative, the businesses would reach operational break-even at approximately $150 million in mortgages, and the ongoing operations of the business would be self-supporting for continued growth. The flexibility of this model is important because of the changing nature of the markets in which BCC operates. In developing a program focused on mitigating the impacts of the housing foreclosure crisis, the organization needed a model that addressed the risk of not knowing how long that crisis would last.

In addition to adapting to circumstances in these ways, BCC has taken a proactive approach through policy change. After finding that several bank sellers required signing an "Arm's Length Affidavit," stating that the purchaser will never sell or rent the property to the original homeowner, BCC worked with the Massachusetts legislature to provide an exception for 501(c)(3) entities.

NHT-Enterprise adapted its engagement with utilities by collaborating with unusual partners in the eight states in which NHT-Enterprise is working with utilities. Rather than working directly with nonprofit housing organizations, NHT-Enterprise chose to work with local energy efficiency partners who were trusted by the utilities. Those local energy partners facilitated the initial and follow up meeting with utilities and helped explain how the utilities could increase funding for energy efficiency retrofits to satisfy the utility energy goals. This led to significantly increased funding for energy retrofits of multifamily housing in six of the eight states.

Managing the Pull of Expansion

SUN, 180° Properties, and NHT-Enterprise are being asked to expand their efforts into new markets to create more social impact. However, they all recognize that expansion requires a strong business model, partners with the right capacity, and political/community support.

BCC has chosen a communications-focused strategy, sharing its model and shaping the environment for potential replication of its model. BCC, from the start, has seen SUN as an effort that could be applicable in markets nationwide. BCC has received inquiries from nonprofit organizations, advocates, and public officials across the country who are interested in the approach SUN has taken. SUN has responded by expanding its reach in Massachusetts. It has also engaged in initial conversations with a wide range of potential partners who would like to franchise or replicate its model and moved forward with an expansion in Maryland in the fall of 2013. BCC's message to its partners in Maryland and in other locations reflects the organizational, regulatory, and financial challenges of launching SUN, alongside the fundamental mission and value proposition of the concept.

BCC has implemented two additional strategies for expanding SUN's reach, indirectly, beyond the borders of Massachusetts. First, it has published a detailed blueprint, "From Our Community to Yours: A Blueprint for Delivering Foreclosure Relief to Your Community," that walks readers through the details of every step of the SUN business model, including its marketing strategy, operational backbone, procedures, and legal structures. In addition, BCC has compiled a toolkit of even more detailed resources–marketing items, intake forms, applications, underwriting guidelines, financial templates–that are available on a limited basis to those who are serious about replicating the program.

It is also working to change the conversation about foreclosure, distressed homeowners, and neighborhood stabilization nationwide in order to change the environment in which SUN and related efforts operate. In a series of national media appearances and op-eds, BCC staff members have argued that the real and fully substantiated need to stabilize households and neighborhoods should not be subordinated to the unsubstantiated concerns of financial institutions about moral hazard (which discourages or prohibits investors from forgiving the principal balances on underwater mortgages, or from re-selling a home to the original owners at a lower rate). BCC has also advocated for policies that balance protection for low-income homeowners and communities with ensuring the ability of financial institutions to make good loans and provide low-income consumers with access to credit.

180° Properties has pursued expansion more directly but is cautious about entering new markets. Since their initial positive experiences in the Chicago market, MHL and TCP have been interested in expanding to fulfill the mission of 180° Properties to create jobs while protecting homes and communities. In addition, 180° Properties recognizes potential benefits to its business model from increased economies of scale. The enterprise has now expanded into one new market, Milwaukee; this experience has reinforced 180° Properties' understanding of the importance of three key precursors to expansion: philanthropic support, community partnerships, and business commitments.

Although 180° Properties could support the expansion of services to northern Illinois and Indiana, it could not efficiently and effectively deliver services to Milwaukee from Chicago. Expanding to Milwaukee would require greater infrastructure and planning than was involved in the previous growth phases in Chicago. The team determined that services would only be offered in Milwaukee if they were desired and requested by local community groups. Further, 180° Properties would not begin to hire staff, buy equipment, or establish an office in Milwaukee until philanthropic support was secured to cover the start-up costs. Finally, it was determined that the expansion would only be undertaken after one or more business clients had been secured.

All three key factors–philanthropic, partnership, and business–were aligned through the efforts of Common Ground, a coalition of Milwaukee churches and community organizations. Common Ground invited 180° Properties to Milwaukee to address the foreclosure crisis, helped identify neighborhoods and properties that needed remediation, provided bank contacts as potential clients for the business, helped recruit and refer candidates for employment, and helped secure philanthropic support. In addition, 180° Properties established a partnership with Goodwill to identify candidates and provide career skills training. 180° Properties was able to secure a significant contract with a major bank to protect and maintain vacant properties owned by the bank, and made the decision to move forward. Eleven Milwaukee-based staff were identified, hired, and trained by July, 2012. In the first six months of operation, 439 homes were secured and maintained. Since then, to mitigate the risk of relying on one major customer, 180° Properties has been working to expand and diversify its customer base in the region.

NHT-Enterprise's campaign for utility investments in affordable housing adds an additional perspective to strategic expansion. NHT-Enterprise opted for an explicit state-by-state approach to replication and expansion as it considers targeting four additional states and promoting its model at industry conferences and events. NHT-Enterprise's initial success in unlocking more than $40 million in new private-sector resources in six states–with more on the way–has attracted attention. More than 20 state housing finance agencies, and many more affordable housing nonprofits and energy groups, have met with NHT-Enterprise and hope to bring its efforts to their states.

Having learned from its initial foray into the energy efficiency policy field, NHT-Enterprise is strategic in choosing markets for expansion. Two elements are crucial for success. First, a local, fair-minded and trusted energy efficiency stakeholder or friend of the utilities must be in place to facilitate additional meetings. Second, securing the engagement of a state housing finance agency with a pipeline of properties makes it easy for the utilities to participate and increases the chance of program adoption. NHT-Enterprise has raised $570,000 in grants to pursue its campaign in eight states to date. As it identifies opportunities with the critical elements in place, it sees potential to continue leveraging this relatively small philanthropic commitment into a significant new resource for affordable housing.

NHT-Enterprise has learned that understanding who has the right relationships, both formally and informally, is a critical first step in advancing successful enterprises in a new location. NHT-Enterprise has been flexible in its approach to building relationships, guided by individual state contexts. In Michigan, NHT-Enterprise retained Martin Kushler from ACEEE, a Michigan resident with strong existing relationships, to speak with utilities on its behalf. In Maryland, it worked with the State Department of Housing and Community Development, which has a successful track record of providing weatherization services for low-income residents. In Minnesota, NHT-Enterprise retained Minnesota Green Communities; in Pennsylvania, the Pennsylvania Utility Law Project. Trusted local contacts were then able to introduce nonprofit housing-sector leaders in Michigan. Together, this strategy made it easier for the utilities to participate; they did not have to learn complex housing finance issues and instead could work with trusted intermediaries.

In Maryland, part of the success was attributable to the state housing department's experience administering housing programs. This experience facilitated targeted outreach and streamlined project execution. Property owners could submit one application for all their financing requests. Existing owners of rental projects who were seeking funding only for energy efficiency grants were also eligible to participate. To generate sufficient capital to expand the program, NHT-Enterprise joined Maryland's Department of Housing and Community Development in urging the Maryland Public Service Commission to direct utilities to provide funding. The Commission agreed, which produced an investment of $21 million in private utility capital.

Conclusion

BCC, MHL, and NHT-Enterprise have each created a successful entrepreneurial response to the foreclosure crisis. As a result of their work, communities have received new resources to improve the lives of underwater homeowners, underemployed job seekers, neighbors in areas with vacant properties, and tenants seeking affordable housing. Now established, their innovations have the potential and the staying power to sustain housing stability and improve people's lives even beyond the crisis.

As new social enterprises, SUN and 180° Properties, as well as NHT-Enterprise, have wrestled with challenges of start-up and early growth, including:

Start-up and operating capital. The SUN Initiative benefited from the substantial resources of an established CDFI. A strong organizational net worth has allowed BCC to invest more than $15 million in debt and equity to build the operating capacity needed to enter a particularly complex corner of the home mortgage business. 180° Properties' experience is perhaps more typical. Even though its two founding organizations have strong capacity to meet their core missions, 180° Properties had to raise ongoing philanthropic capital, now totaling more than $2 million, to build its operational capacity for this new business. Capital resources for start-up remain a challenge for most nonprofit organizations that start social enterprise affiliates, and grant funding is one of the very few sources available.

Expansion capital. 180° Properties continues to raise capital from philanthropic supporters to expand its capacity. BCC is just beginning to reach the tipping point for financially sustainable growth, with its recent secondary market transactions for SUN. In both cases, true financial sustainability can take years to achieve, particularly as an organization seeks to expand its programming and geographic reach, which requires ongoing reinvestment of income. The idea of generating income that is channeled back to the parent organization may be unrealistic, at least during the growth phase of a business. At the same time, as described above, BCC has shown that is possible to build a model that can be self-sustaining at multiple levels of business activity, and the social enterprises profiled here have made efficient use of the resources available to them, relative to other nonprofit models.

Leveraged capital. As a social entrepreneurial organization in the community development finance sector, NHT-Enterprise sees even greater potential for leveraging energy-efficiency grant dollars with debt. Utilities are generally prohibited from or reluctant to take on lending risk themselves; however, they are very interested in leveraging the impact of their dollars. Because CDFIs who focus on energy lending require significant loan loss reserves to manage their risk, NHT-Enterprise hopes to convince utilities to provide grants for loan loss reserves in a few key states. Based on its experience with its initial campaigns, it is seeking philanthropic support to add to its capacity to pursue this new strategy.

Operational capacity. Both SUN and 180° Properties have recognized the need to hire staff with industry-specific expertise to smooth their entry into new businesses. Given this, existing leadership must play an active role in ensuring consistency in values and alignment with the overall organization's long-term direction. Creating scalable systems to support growth and manage complexity has been a focus for both enterprises.

Adaptation to change. Because they were founded in response to a crisis, both 180° Properties and SUN are embedded in a changing market and policy environment. 180° Properties has adapted its strategy to meet the needs of a changing customer base and market conditions, and now is adapting to the market trend of investor-owned rental portfolios. SUN built a model that can support itself at multiple levels of lending activity in order to accommodate changes in the housing market. In addition to shifts in foreclosure activity, SUN has faced an ever-changing set of mortgage regulations as consumer and housing finance reforms proceed. It has taken a proactive role in advocating for state-level policy change to support its core innovation of re-selling a home to the original foreclosed or distressed homeowner and reducing principal.

A major question facing these entrepreneurs is how to find the right partners and develop the right relationships to continue growing and adapting to a changing environment. In the sphere of social innovation, social capital is almost as important for expansion as financial capital. Trusted relationships with funders, with community organizations and local officials, with individual households, and institutional clients are not easily replicated in new locales. Partners who provide important capacity and complementary skills are not always available elsewhere, and cannot always grow in scale at the potential pace of a social enterprise strategy.

All three organizations have adopted the following strategies for managing the challenge of expansion to new markets.

The right partners. Successful social enterprises rarely happen in a vacuum. BCC, 180° Properties, and NHT-Enterprise have all discovered that having the right partners–in the philanthropic, business, and community sectors–is critical to launching new ventures, particularly in new markets. All three ventures have invested resources in building and maintaining these relationships in order to expand their businesses.

180° Properties enters a new market only if it is invited by a community with partners who could provide political support, philanthropic connections, the on-the-ground job training and employment referrals it depends on, and a strong customer base. NHT-Enterprise chooses states to target on the basis of available, trusted partners to work with utility companies and an engaged housing finance authority to connect funds with projects.

Communications and public relations. BCC paves the way for expansion by documenting and communicating its approach in its blueprint document. It has also engaged in national-level communications work to address the underlying barriers to the SUN model, such as investors' concerns about moral hazard in making principal reductions. NHT-Enterprise, similarly, has documented its energy-efficiency funding strategy in a series of reports and publications intended to raise interest in and build support for the concept.

As they enter a new phase of response to the foreclosure crisis and community development challenges, SUN, 180° Properties, and NHT-Enterprise are making promising inroads in capacity-building and raising the right kind of capital to sustain and expand their impact. Their careful, analytical approach to expanding their reach–directly and indirectly–demonstrates both the challenge and the potential of social enterprises in responding to crisis.

Michael Bodaken serves as President of the National Housing Trust. He has served the Trust in that capacity for over 20 years. The Trust engages in preservation policy, affordable housing development and lending. He has been largely responsible for growing the organization to its current status as a nationwide leader in the field of affordable housing preservation. The Trust is a multi-faceted organization, performing a path-finding role in the housing preservation field through a unique mix of public policy development, lending, and real estate transactional activities. More recently, Mr. Bodaken has been responsible for the development of Trust's "Green Preservation" housing initiative.

Elyse D. Cherry is CEO of Boston Community Capital (BCC) and President of its affiliates Boston Community Venture Fund, Aura Mortgage Advisors and NSP Residential. Cherry helped found BCC in 1984, and has been integrally involved in its growth from a start-up to what is, today, a national model for community investment. Under her leadership, BCC has invested more than $900 million in underserved communities across the U.S., financing affordable housing, jobs and opportunities for low-income people. Cherry is an attorney whose legal practice focused on commercial real estate finance and development. She began her career as a VISTA volunteer in rural Tennessee.

Cindy Holler is President of Mercy Housing Lakefront. In this role, Ms. Holler oversees real estate development and operations for one of the largest and most innovative community development organizations in the Chicago and Milwaukee regions. Holler has held previous executive positions with Fannie Mae, South Shore Bank, and Catholic Charities.

Rethinking Tenure: Building a Diverse Landscape of Affordable Housing Options

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Multi-family properties have long been the focus of affordable housing research and policy. However, approximately 55 percent of the rental housing in the United States is in single-family properties or small buildings containing less than four units. These units deserve attention as an important part of the affordable housing stock. The recent foreclosure crisis has made the issue of single-family rentals even more salient. Many of these smaller rental properties are threatened by disinvestment, foreclosure, and abandonment. Like the proverbial canary in the coal mine, single-family and small-scale rentals signal important information about the overall conditions of the neighborhood; when these properties are poorly maintained, they indicate disinvestment and decline, which can lead to negative spillover effects on surrounding homes.

In this article, we describe the experiences of three regional nonprofit housing organizations—the Housing Development Fund (HDF) in Connecticut, Project for Pride in Living (PPL) in Minnesota, and the Atlanta Neighborhood Development Partnership (ANDP) in Georgia—that have amassed a broad base of experience in redeveloping single-family housing. Each of these nonprofits operates in distressed neighborhoods that have been affected by the foreclosure crisis. They have also been working to devise strategies that respond to the unique market conditions within their regions, which has required pursuing a range of tenure options for lower-income families. These options include long-term scattered site rental and asset management, hybrid-tenure arrangements (including lease-purchase, contract-for-deed, and other strategies that combine renting with a path to ownership), and ownership of properties by resident landlords in two- to four-unit buildings. These models demonstrate a range of promising solutions for meeting different market needs and for managing small properties in ways that support neighborhood stabilization goals.

We present case studies of each of the three nonprofits and their approaches to dealing with single-family and small-scale properties, and discuss the lessons learned and challenges associated with these strategies. We then look across the case studies to provide policy recommendations that could best support a wide variety of tenure options for low-income families.

Owner-Occupied Rentals in Connecticut

Connecticut's housing market includes both strong and weak market cities. In some cities, such as Stamford, lower-income families struggle to find affordable housing as home values are among the most expensive in the country. In contrast, Bridgeport, a mere thirty minutes away, is characterized by older buildings, units in need of rehab, and depressed prices. The housing mix is also quite different across areas. While higher-income neighborhoods tend to be dominated by single-family homes, two- to four-family buildings represent up to 40 percent of the housing stock in lower-income communities. Many of these buildings were originally built to house mill-workers at the turn of the century, so properties tend to require more rehab and maintenance than newer homes.

In Connecticut, Bridgeport was one of the cities hardest hit by the foreclosure crisis. HDF, which had a long history of working in Bridgeport, was selected as a sub-grantee for the city's Neighborhood Stabilization Program (NSP). As such, HDF helped to acquire and rehabilitate real estate owned (REO) units. Per NSP guidelines, HDF worked to identify single-family homes on a single block, with the idea that strategically targeted investment of scarce resources could help stabilize an area. However, this strategy proved to be insufficient for Bridgeport's neighborhoods. HDF found that on many blocks, stabilization was elusive due to the presence of two- or three-unit buildings that were poorly maintained, owned by external investors, or also in the foreclosure process. HDF quickly realized that any real neighborhood stabilization efforts would need to address the problem of small multi-family properties. There was also an opportunity to use these properties to anchor the block and place ownership back into the hands of community members.

HDF created the Landlord Entrepreneurship Affordability Program (LEAP) to support the purchase and rehabilitation of two- to four-unit properties by low- and moderate-income households, who would then live in the property and serve as the property's landlord. HDF's earlier work had shown that there was a demand for specialized financing and training to support new landlords interested in buying small-scale rental properties. Since the late 1990s, HDF has offered a combination of homebuyer preparedness and down payment assistance for new homebuyers, and over the years, a significant share of these homebuyers have purchased two- and three-unit properties to live in and provide rental income. In addition, a new wave of young professionals, immigrants, and do-it-yourself entrepreneurs are seeking the chance to own rental properties in which they reside. HDF thus seized the opportunity to support these new landlords and connect them to the organization's neighborhood stabilization goals.

LEAP provides both financing and training for low- and moderate-income households interested in purchasing small-scale rental properties. While the combination of lower house values and rising rents has made the economics of becoming a landlord more viable, interested buyers–especially if they are lower-income–often face challenges finding financing. Banks are wary of lending on properties that rely on rental income, especially when the borrower is taking on new landlord responsibilities. In addition, older housing is often in need of rehabilitation, which creates up-front costs that first-time owners may not be able to afford. New owners also need to develop specialized knowledge in housing maintenance and rehab.

On the financing side, LEAP offers low down payment mortgages to borrowers with good credit and steady income, but little savings. Connecticut's state housing financing agency provides an 85 percent first mortgage, which covers the majority of the acquisition costs, as well as a 10 percent second mortgage through its down payment assistance program. A $1.45 million grant from the CDFI Fund serves as a loss reserve to leverage $15-20 million in acquisition loans from the state housing finance authority. Borrowers are only required to put down between one and three percent for a down payment. The balance comes from HDF, supported in part by a million dollar grant from the State of Connecticut's Department of Housing. HDF is pursuing other grants from local and state community development agencies to scale up the program and improve the affordability for future owner-occupant homebuyers. HDF needs "patient" subordinate debt to make this model work and to ensure that it is supporting low-income families (at less than 80 percent of AMI) to become landlords, as well as to ensure that the units are rented to low-income households (HDF is targeting households at 60 percent of AMI). LEAP also incorporates financing for rehabilitation and funding for energy retrofits to help maintain affordability and improve the economics of owning older properties. HDF has secured a grant of $360,000 from the Clean Energy Finance and Investment Authority to leverage capital for energy retrofits.

The program mitigates financing risks through training and support. HDF combines one-on-one homebuyer counseling with training in landlord/tenant relations. The curriculum, which was approved by the Connecticut Housing Finance Authority, includes in-depth information about finding and managing tenants, complying with state and local ordinances, record-keeping, and working with contractors. LEAP also provides training in basic home repair and maintenance skills. In this way, LEAP provides important supports to the new landlords, ensuring that they are able to take on the debt as well as the long-term management of the property.

HDF is now exploring how it can expand LEAP and raise additional financing for the program. The early work on LEAP has shown that it is a viable model, and that it aligns several important goals. Not only does it preserve the affordable housing stock for renters, but it also simultaneously increases ownership and asset-building opportunities for low- and moderate-income homebuyers. By encouraging sustainable rehab work, the program also increases the energy efficiency of older units, which reduces environmental impacts and decreases landlord operating costs. And, by putting vacant and distressed small scale buildings back into the hands of people who want to live in the community, LEAP helps to stabilize neighborhoods hard-hit by foreclosures.

Single Family Sales, Rental and Lease-Purchase in Atlanta

In 2012, Georgia's foreclosure rate remained the fourth highest in the nation–in fact, banks took back more homes in Atlanta than in any other major metropolitan area in the country.[1] For the Atlanta Neighborhood Development Partnership, Inc. (ANDP), the challenge has been to innovatively address the range of housing needs of lower-income households. Using NSP funds, ANDP has redeveloped over 350 units, and has resold the majority of them to lower-income families ready to buy a home. ANDP has been particularly successful finding buyers as a result of an innovative marketing program that targets real estate intermediaries rather than the buyers themselves. However, the tight mortgage credit environment, coupled with the financial instability of many lower-income households, also led ANDP to consider rental and lease-purchase options for Atlanta's hardest hit markets.

One of ANDP's main concerns at the start of its NSP work was whether or not it would be able to find low- and moderate-income families ready to buy REO properties after rehab, especially given the tight credit market. One of the keys to success was hiring an experienced consultant who restructured ANDP's marketing efforts. Originally, ANDP had focused its strategies on reaching homebuyers directly–for example, attending housing fairs, advertising via newspapers and radios, and holding open houses. Unfortunately, some of the potential buyers they managed to reach through these efforts were not necessarily ready to actually buy a home or to qualify for financing. Under its new marketing strategy, ANDP added a specific focus on reaching the organizations that serve consumers: real estate agents, lenders, and housing counselors. ANDP made a concerted effort to publicize its rehabbed for-sale homes by attending lender and agent meetings, giving presentations, and holding monthly webinars. It found that these intermediary organizations were more likely to have a pipeline of borrowers who were ready to buy, and so it became easier to close on property contracts.

In addition to improving its marketing, ANDP has also been working to secure FHA financing to expand its pool of capital for acquisition and rehab. When the NSP first began, it was challenging to find commercial banks willing to originate loans for neighborhood stabilization work; indeed, much of ANDP's original funding for this work came from national nonprofit intermediaries, including HPN through the National Community Stabilization Trust's REO Capital Fund, Mercy Loan Fund, and Self-Help.

ANDP believes that FHA financing through the Section 203(b) and 203(k) loan programs could be an important new source of renewable, flexible capital for redevelopment work. These programs have been open to nonprofit borrowers for decades and have many important features: loan terms are 30 years; interest rates are low; and the Section 203(k) program offers insurance specifically for acquisition-rehabilitation of properties containing four or fewer units. However, accessing these programs and using them to their full potential has historically been a challenge. The 203(b) and 203(k) products are not actively marketed by lenders to nonprofit borrowers, and they require HUD approval of both the lender and borrower in the transaction. In mid-2013, ANDP was approved as a HUD mortgagor, and it continues to seek an originating lender to pilot the program. FHA-approved lenders accustomed to underwriting individual buyers may find methods for underwriting nonprofits

1 Core Logic, Inc. National Foreclosure Report, December 2012

daunting. However, HUD and FHA both recognize the importance of scattered-site redevelopment, and have been working to provide the guidance that lenders need.

As another strategy, recognizing that not everyone is ready for ownership, ANDP is also exploring the feasibility of developing "hybrid-tenure" strategies such as lease-purchase. While some low-income households are able to purchase rehabbed REOs, would-be buyers with tarnished credit histories need an option that will allow them rebuild their credit and "grow" into ownership. However, hybrid-tenure models are challenging to implement. First, hybrid-tenure models require flexible financing. Conventional funding sources for affordable housing are rarely flexible enough. For example, commercial loan products cannot be assumed by the homeowners when they are ready to buy. This means that the nonprofit also needs to ensure that there is a network of lenders that can provide end mortgages to borrowers. Furthermore, federal sources, such as HOME, have requirements that make them inappropriate for properties which may be either sold or rented, dependent on the market demand, and with tenure arrangements that might change over ensuing years.

In addition to the financing challenges, nonprofits pursuing lease-purchase must also address borrower-level considerations. For example, ANDP realized that many families may need a longer period of time to get their finances back in order, well beyond the terms of the lease. In addition, some of the renters may not necessarily be committed to or interested in their rental property—once they're ready to buy, they may have a wider range of homes available to them. That said, ANDP continues to believe that having hybrid-tenure strategies and tools in place can contribute to neighborhood stabilization by ensuring that there is a solution for every type of property and household.

Twin Cities Scattered Site Rentals

Since the start of the foreclosure crisis, color-coded maps of North Minneapolis have shown a patchwork of foreclosed properties, with concentrations located in predominantly African-American and immigrant communities. In addition, a tornado in 2011 damaged hundreds of homes, further limiting the number of affordable rentals in an already tight market. Neighborhoods are struggling with an aging, often vacant housing stock that is vulnerable to vandalism and damage. Vacant units quickly become uneconomical to repair as they lose value, which can then lead to further neighborhood deterioration as blight spreads through the community.

Project for Pride in Living, Inc. (PPL), a 40-year-old nonprofit housing developer in Minneapolis, committed to responding to the challenge of these vacant and REO properties, many of them small two- to four-unit buildings. Unfortunately, the typical "buy, rehab, sell" model for these properties wasn't feasible, since unlike in Connecticut, owner-occupant demand for these houses in North Minneapolis was low. PPL was faced with a particularly difficult set of options. Ignoring these properties would likely lead to further neighborhood destabilization—the only interest in these properties was from speculators looking for deals. From a community development perspective, having these properties vacant or bought by outside investors would do little to restore the vibrancy of the neighborhood. Demolishing these properties–another option–would lead to a decline in the supply of affordable rentals, since changes in zoning restrictions made it unlikely that there would be one-for-one replacement with new units. PPL decided that the best solution would be to own and operate these buildings as high-quality, affordable, scattered-site rentals, despite the fact that a scattered-site model is inherently more expensive and less efficient than larger family rentals.

Luckily, PPL already had experience with scattered-site rentals, having owned and operated 62 units in ten small rental buildings in North Minneapolis since the 1980s. There have been pressures over the years to change PPL's portfolio mix away from scattered-site rentals due to their higher operating costs and management challenges, but in the wake of the foreclosure crisis, PPL made the strategic decision to focus on these two- and four-unit buildings.

As with any housing development intervention, PPL had to be creative in developing the financing for its scattered-site rental program. In 2010, PPL consolidated and recapitalized its scattered-site portfolio using Low Income Housing Tax Credits (LIHTC). While LIHTC can be used for multi-site development, this rarely occurs due to the higher risk investment associated with managing multiple buildings. PPL was able to do so because its limited equity partner was willing to take the risk as a result of its longstanding relationship and trust in PPL's capacity to manage the project.

Since then, PPL has been involved in the redevelopment of 60 additional rentals in smaller buildings in North Minneapolis. Acquiring, rehabbing, and ultimately managing these properties has required complex funding strategies that mesh funds from multiple federal, state, and local sources. PPL is using local and neighborhood connections, as well as the First Look program of the National Community Stabilization Trust, to acquire properties. The average acquisition price is $25,100 per unit, which is much lower than the metropolitan-wide median sales price of $170,000.[2] PPL is then spending an additional $85,000 per unit to fix the buildings by using funds from NSP, the Affordable Housing Trust Fund of the City of Minneapolis, the State of Minnesota, and Hennepin County. Of the 60 units, 21 carry project-based Section 8 subsidy in a partnership with Minneapolis Public Housing Authority to support foreclosure recovery. Additional rental assistance for disabled and formerly homeless individuals will be used in 28 more units. Thus, 49 of the 60 units in PPL's stabilization program will be serving very low-income renters while reoccupying property that would otherwise be at high risk of vacancy and blight.

PPL has also learned important lessons about how to manage scattered-site rentals. First, PPL selects properties in proximity to one another, or properties that are close to other PPL assets. This strategy amplifies the impact of PPL's investments and establishes a critical mass of well-managed properties that contribute to the quality of life in the area. This geographic concentration also reduces transit time for management staff. Second, the human side of PPL's property management strategy is also important. Residents in the rental properties are

2 Minneapolis Area Association of Realtors. http://www.mplsrealtor.com/downloads/market/MMI/mmi.pdf

screened carefully, and contact with tenants is regular and frequent, either through property management personnel or social service providers. PPL also cultivates a strong presence and relationship with the community so that neighbors always know who to call if they observe something that concerns them. Off-duty police officers are hired to help keep an eye on the scattered-site properties. Third, PPL raises funds up front to invest in capital improvements, since small buildings cost more to maintain.

While PPL still has not achieved unit by unit efficiency of its scattered-site portfolio, it has enough experience and capacity to make the operations sustainable. Importantly, it sees its role not only as a "housing developer," but also as a "community developer," which means that it will continue to focus on strategies that are right for the neighborhood, rather than those that are the most cost efficient.

Common Challenges and Recommendations

The experience of the three programs affirms that stabilizing and revitalizing neighborhoods requires a spectrum of tenure options. To be viable, new streams of financing need to be created and adapted to existing resources to better serve communities. Developers and owners of rental and hybrid-tenure properties need better availability of tools to finance their investments as portfolios, over a long term, at scale. They also need regulations that better support targeted investment in hard-hit neighborhoods. Finally, individual households need better access to training and asset building services, as well as financing, advising and training to support their successful transition as homeowners or owner-occupant landlords.

On the policy front, a key recommendation is that the field needs more flexible forms of capital that can be used to support multiple tenure approaches and neighborhood stabilization goals. For all three of these nonprofits, the primary challenge is not operating capacity, even though rental, lease-purchase, and owner-occupied housing programs all require skilled approaches.[3] The largest obstacle has been–and continues to be–finding appropriate capital sources. Each of these case studies provides examples of innovative financing approaches. In Connecticut, HDF is assembling a new pool of capital to leverage state homeownership subsidies to develop a new loan product. In Atlanta, ANDP is seeking financing and public partners to create a range of tenure options, including lease-purchase, with long-term financing. In Minneapolis, PPL is pushing the flexibility of old (LIHTC, HOME, CDBG, Section 8) and relatively new (NSP) public sources for rental tenure.

Going forward, lenders and mortgage insurers like FHA should follow the lead of CDFIs and philanthropic social investors by offering scalable financing products that are designed

3 Property and asset management inefficiencies of multiple-roof/scattered-site portfolios are sometimes daunting, although high-capacity nonprofits like PPL, do have a good track record. Advances in communication technology offer new promise for bringing efficiency to managing a geographically scattered portfolio. Members of the Housing Partnership Network have been engaged in ongoing discussions through the International Housing Partnership with UK-based housing associations, which offer interesting examples of integrating logistics software, call centers, and mobile communications to manage very large scattered portfolios effectively.

for flexible tenure and lease-purchase strategies. There is a gap in the system of financing single-family rental property. It is difficult to raise flexible capital for rental and mixed- or hybrid-tenure single-family portfolios.[4] FHA 203(b) and 203(k) loans show particular promise as they can be adapted and made more flexible for use in support of neighborhood stabilization efforts. However, very few lenders are currently offering these products, and the approval process can be cumbersome.

Lenders and mortgage insurers should offer nonprofit investors better tools to assemble "horizontal multifamily" portfolios of scattered-site properties in order to meet neighborhood stabilization objectives. NSP funding provided a unique opportunity to assemble portfolios over time, without having site control up front. A new private-sector portfolio-level debt product that does not require site control at closing would allow nonprofit buyers to compete fairly for properties in markets now dominated by cash buyers.

State HFAs can play an important role in supporting innovation by targeting public subsidies to approaches that leverage private capital, like LEAP in Connecticut. Since they are similarly mission driven, state HFAs can serve as a very important resource for capital. In addition to helping to fill financing gaps, they can also play a valuable role as convener, bringing different partners together to create a delivery system for affordable housing.

Other federal policies may also make it more difficult for nonprofits to pursue scattered-site rentals, especially in weak markets. Concentrating scattered-site rental properties is vital to reach a critical mass for both operating efficiency and neighborhood impact. However, public programs often impose disincentives on concentrating affordable housing in particular neighborhoods. For example, HUD project-based Section 8 regulations prohibit new contracts in high-poverty or majority-minority areas. Such rules have created obstacles for efforts designed to maximize neighborhood stabilization impact. Similarly, targeting can conflict with strategies that aim to increase mixed-income communities. For PPL, navigating the regulations associated with divergent goals has added complexity in identifying properties for acquisition and piecing together financing sources. Public agencies should revisit their well-intentioned disincentives to concentrating investments in high-poverty neighborhoods. Revisions should allow public investment to play an important role in highly targeted redevelopment strategies, catalyzing neighborhood revitalization before the private market will jump in.

Finally, there is strong alignment of social and financial goals when housing counseling and training is integrated into consumer financial products, as LEAP is demonstrating in its integrated program. These services should be incorporated and compensated in loan transactions. Similarly, nonprofits have an important opportunity to play a role in homebuyer education in lease-purchase models. They can also be crucial in preparing renters for ownership responsibilities and in training owner-occupants to be landlords. Nonprofit stewards have the unique commitment and skills to work directly with people in ways that improve outcomes for investors and communities alike.

4 Housing America's Future: New Directions for National Policy, Bipartisan Policy Center, February, 2013, pp.76 through 78.

The long-term success of any of these strategies has a lot to do with innovation, flexibility and commitment. High-capacity nonprofits are poised to build on their innovative post-NSP approaches to invest at larger scale in the long-term vision of stable, vibrant neighborhoods and successful households. The opportunity now is to build more effective systems that support a wider range of tenure options for single-family housing stock, as part of broader neighborhood stabilization strategies.

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Strengthening Neighborhood Stabilization: Refining Business Models for Housing Counseling

Danielle Samalin*

Housing Partnership Network

The connection between property acquisition and housing counseling in neighborhood stabilization efforts may seem obvious in 2013, but in the early years of the housing crisis, it was not. Even within organizations that provided both housing development and counseling services, there was often little or no interaction between the two departments. But if the last five years have taught the affordable housing industry one thing, it is that there is immense value both for homeowners and for the broader mortgage market in embedding nonprofit housing counseling into neighborhood stabilization efforts.

Since 2007, housing counselors have served as trusted advisors for millions of troubled borrowers. Through targeted outreach programs, counselors have helped public entities and private mortgage lenders reach distressed borrowers and improve loan outcomes. Indeed, a suite of new academic and practitioner studies documents the economic and social value of housing counseling.[1] In its evaluation for Congress, for instance, the Urban Institute found that borrowers who received counseling under the National Foreclosure Mitigation Counseling Program were twice as likely to obtain a loan modification and 67 percent as likely to remain current on the mortgage nine months later, compared with counterparts who received modifications without the assistance of a counselor.[2]

Although the value of counseling is often acknowledged, the notion of fully integrating housing counseling into neighborhood stabilization efforts is not typically part of the conversation. During the past few years, the Housing Partnership Network's (HPN) Innovations in

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1 NeighborWorks America, "National Foreclosure Mitigation Counseling Program: Congressional Update" (Washington, DC: NeighborWorks America, June 2012), available at www.nw.org/network/nfmcp/documents/2012CongressionalReport.pdf; J. Michael Collins and Maximilian D. Schmeiser, "Effects of Foreclosure Counseling on Distressed Borrowers," Journal of Policy Analysis and Management 32:1, 2013; U.S. Department of Housing and Urban Development, "Foreclosure Counseling Outcome Study: Final Report, Housing Counseling Outcome Evaluation." (Washington, DC: HUD, Office of Policy Development and Research, May 2012), available at: www.huduser.org/publications/pdf/foreclosure_counseling_v2.pdf ; J. Michael Collins, "The Role of Default Counseling for Mortgage Borrowers in Financial Distress," *Consumer Knowledge and Financial Decisions,* International Series on Consumer Science, Douglas Lamdin, ed. (pp. 165-82) (Rueil-Malmaison, Germany: Springer, 2012); Neil S. Mayer and Kenneth Temkin, "Pre-Purchase Counseling Impacts on Mortgage Performance: Empirical Analysis of NeighborWorks® America's Experience." (Albany,CA: Neil Mayer and Associates, 2013), available at www.nw.org/network/newsroom/documents/ExperianMayer_FullReport.pdf.

2 NeighborWorks America, "National Foreclosure Mitigation Counseling Program."

Neighborhood Stabilization and Foreclosure Prevention Initiative has been piloting new models that have taken the idea further by embedding counseling directly into new models, and engaging housing counselors as essential partners, rather than adjunct social service providers. The implications of this are significant; to capture the full economic and social benefit of housing counseling (both to the homeowner and the asset holder), it is essential to reframe and refine the counseling business model and delivery system to reflect the full value of the services. What's more, in the wake of severely constrained and diminished public funding for the industry, this kind of business model transformation may be key to sustaining the housing counseling industry going forward.

This article begins by reviewing the evolution of the housing counseling industry and discussing the opportunities and challenges of adopting a "fee for service" model of housing counseling. We then highlight two recent business model innovations that have emerged in response to the foreclosure crisis–the Mortgage Resolution Fund in Chicago and the Occupied Homes Program in New York City. Through HPN peer exchange, nonprofit organizations working on both the supply and demand sides of stabilization efforts–including developers and housing counseling providers–were able to better understand how their efforts were intertwined. The discussions led to new, more collaborative social enterprise models for neighborhood stabilization. In the Mortgage Resolution Fund and the New York Occupied Homes Program, housing counseling is explicitly incorporated to fully capture the value and expertise that counselors bring to the loss mitigation process. Moving forward, developing new methods of delivery to bring the industry to scale may be an essential component of long-term housing market sustainability.

The Evolution of the Counseling Industry

Counseling programs have long been part of homeownership and foreclosure prevention strategies. The U.S. Department of Housing and Urban Development (HUD) began funding housing counseling organizations through the Housing Counseling Assistance Program 50 years ago. When the program was enacted in 1974, the focus was on home retention. This shifted in the late 1980s and early 1990s as lenders began to use pre-purchase homeownership education and counseling to screen individuals and reduce risk.[3] Pre-purchase counseling thus became part of a menu of services and innovations designed to improve access to credit for historically underserved populations. Nonprofits that provided housing counseling services helped to build a pipeline of mortgage-ready borrowers for down payment assistance and other affordable homeownership programs. Inherent in the move to expand pre-purchase counseling programs was the recognition that they reduce risk and add value to the mortgage market. However, there was still no definitive proof that counseling "worked." Or, at least, there was not enough proof to justify paying for the cost of counseling as part of a mortgage contract.

3 Steven Hornburg, "Strengthening the Case for Homeownership Counseling: Moving Beyond a Little Bit of Knowledge." (Washington, DC: NeighborWorks America, 2004).

The housing crisis that began in 2007 precipitated rapid changes in the counseling industry. Once the magnitude of subprime delinquencies became apparent, the demand for foreclosure prevention counseling skyrocketed. In December 2007, Congress authorized $180 million for a National Foreclosure Mitigation Counseling (NFMC) Program, which enabled local agencies to ramp up staff and resources to respond to the demand for their services. Organizations that had established homeownership counseling programs to help people purchase homes had to retool quickly to advise clients on how to pursue loan modifications and prevent default.[4] These organizations have since been at the front lines of myriad public programs, particularly federal initiatives, related to loss mitigation and neighborhood stabilization. They include:

- In 2008, the Housing and Economic Recovery Act, which authorized an additional $180 million for NFMC and $3.9 billion for the Neighborhood Stabilization Program;
- In 2009, the Financial Stability Act, which created the Making Home Affordable Program that included the Home Affordable Modification Program (HAMP);
- In 2010, Hardest Hit Funds, which provided $7.6 billion to 18 "hardest hit" states, plus the District of Columbia, to support locally tailored programs to assist struggling homeowners;
- In 2011, the Emergency Homeowner Loan Program, which provided funds similar to the Hardest Hit Fund in the remaining states; and
- In 2013, the Making Home Affordable Outreach and Intake Program, which provides funding to housing counseling organizations for HAMP outreach and packet submission.

HUD also began to prioritize loss mitigation efforts in its Housing Counseling Assistance Program, first by allocating increased funding to foreclosure prevention, and then by implementing the Mortgage Modification and Mortgage Scams Assistance program. Through these initiatives, counseling agencies became the go-to providers for services ranging from outreach for at-risk borrowers, to document collection and modification package submission, to connecting clients to emergency, legal, and employment services. The new resources were instrumental in enabling counseling organizations to meet increasing demand for foreclosure counseling.

However, these programs also introduced new challenges for the industry. For example, each program had its own reporting and filing requirements. In addition, there were significant prohibitions against combining funding sources. Although the funds from the NFMC program were never intended to cover the full cost of service provision, and were instead

4 As the first national HUD Housing Counseling Intermediary, designated as such in 1994, the developments of the last five years have directly affected the Housing Partnership Network and our 30 members who provide housing counseling services. The infusion of NFMC funds into our network increased foreclosure counseling production by 200 percent.

intended to supplement other funding sources,[5] HUD nonetheless prohibited leveraging NFMC funds to cover the cost of providing foreclosure counseling services with HUD Housing Counseling funds. The impact of this prohibition on counseling organizations was significant. As a program director at one HPN member expressed, "Counseling is a loss leader. We have to constantly supplement the program with profits from our other programs to keep it running while at the same time we leave money on the table with our federal grants. For a foreclosure counseling case that took us 40-plus hours to complete, the [NFMC funds] only cover the first 10 hours. The federal funds we were not able to [leverage] could have covered the cost."

In addition to inefficiencies in the myriad grant rules, the new programs were challenging to manage because each program depended heavily on housing counselors to understand—and explain to borrowers—its unique requirements, all the while negotiating with servicers who were often responding to a different set of incentives and constraints.

Moreover, and perhaps more important, even in the midst of an unprecedented housing crisis, federal funding for housing counseling has been precarious at best. The HUD Housing Counseling Program was zeroed out of the 2011 Continuing Resolution, temporarily cutting off funds to the program entirely. Sequestration has further threatened the viability of housing counseling programs, and it is unclear whether the current Congress will further cut HUD's counseling budget going forward.

The fact that an essential funding source could be eliminated in the middle of a crisis underscored the need for the counseling industry to diversify and lessen its reliance on federal grants. Public funding is unlikely to remain high enough to support the growing demand for counseling, which remains strong as the foreclosure crisis continues and aspirations for homeownership remain strong.

Fee-for-Service: A Step in the Right Direction

These three challenges—multiple grant revenue streams, programmatic inefficiencies, and insecure funding—underscore the need for the counseling industry to decrease its reliance on federal grants and generate new revenue sources. The fee-for-service model—or, paying a fee per service provided—has long been discussed as a potential route for the housing counseling industry, rather than continuing to rely on grant funding. However, until recently, this model has been difficult to implement.[6] This changed when the American Securitization

5 National Foreclosure Mitigation Counseling Program, Round 7 Funding Announcement, page 3: "The intent of NFMC Program funding is to expand and supplement counseling services available to families facing default and foreclosure. It is expected that eligible Applicants will make every effort to receive reimbursement for counseling services from other sources, such as investors and/or servicers, to increase the sustainability of these services. NFMC Program funds are not meant to replace current or future fee-for-service arrangements between counseling agencies and servicers, lenders, or other interested parties." http://nw.org/network/foreclosure/nfmcp/documents/I.FundingAnnouncement-Round7_001.pdf

6 The original concept for the NFMC program was a fee-for-service model. Although it was ultimately funded through federal grants, via NeighborWorks America, the NFMC program built the substantial evidence that the counseling industry needed to secure fee-for-service contracts.

Forum announced that counseling fees could be reimbursed from securitization transactions in appropriate circumstances.[7] As a result, several small fee-for-service relationships emerged between investors, servicers, and housing counseling intermediaries. In a typical fee-for-service arrangement, servicers agree to pay a flat fee to agencies for counseling their borrowers, identifying specific reimbursable services such as helping the borrower complete an application package for a loan modification.

The emergence of fee-for-service arrangements led to several improvements in the counseling process. Throughout the crisis, the relationship between counselors and servicers tended to be antagonistic rather than collaborative. Under fee-for-service contracts, these relationships improved, given that participating counselors were more likely to have access to an identified contact person at the servicer to provide training and answer questions regarding an application for a loan modification. In addition, contracting with servicers has required some counseling organizations to improve their business functions, such as information technology and insurance, to comply with bank rules. Servicers have also improved systems to enable better exchange of information. For example, many counselors are now able to use electronic portals to directly submit borrower applications rather than using cumbersome and unreliable faxes that previous servicers required. In certain markets with limited grant funding, fees have also served to support growing counseling efforts.

However, the structure of fee-for-service contracts has its limitations, both in achieving borrower outcomes and in generating revenue for a counseling organization. Despite often having a better relationship with the servicer, counselors' effectiveness is limited because they remain detached from the actual business transaction and modification decision. For instance, privacy laws prevent counseling agencies from conducting direct borrower outreach. In addition, once a borrower is contacted, the counselor does not have access to investor guidelines that dictate the terms that would be acceptable for loan modification. As a result, counselors may be unable to negotiate effectively on behalf of the client to find a solution that is preferred for the investor. Moreover, if the loan modification is denied, the counselor cannot explain the reason for the denial to the borrower, as they are only told that the denial is "due to investor guidelines" without further explanation.

It is also unclear whether current fee structures are sufficient to support the wide range of services the nonprofit organization provides. Even if a borrower is granted a loan modification, the fee paid by the servicer generally does not cover the intensive financial counseling, budgeting, and follow-up needed to ensure that the homeowner stays current with his or her mortgage payments. When families are unable to remain in their homes, housing counselors still shoulder the burden of finding alternatives after foreclosure. The contract fee does not cover these services. In fact, the flat fees often do not cover the full cost of counselor time for even the most straightforward loss mitigation transaction. Although counseling agencies will continue to form strategic relationships with servicers, fee-for-service arrangements have not proved the cure-all the industry imagined.

7 For full Alliance Action Plan, see http://www.hopenow.com/alliance-statement.php

The Mortgage Resolution Fund: Linking Counseling to the Value of the Asset

Lessons learned from fee-for-service relationships have led to innovations in response to the foreclosure crisis. One key innovation is integrating the housing counseling model more deeply into the mortgage transaction by creating a direct link between the benefits of counseling and the returns to the investor. The model is based on the principle that preventing default is more efficient and cost-effective than allowing the foreclosure to take place. In this model, rather than the counselor contracting with the servicer–who is in fact just a middle man in the transaction–the counseling agency is directly linked to the investors through the loss mitigation process. This model is being piloted as part of the Mortgage Resolution Fund (MRF), which was founded in March 2011 by Mercy Portfolio Services, the National Community Stabilization Trust, Enterprise Community Partners, and HPN.

Using Hardest Hit Funds and leveraged pools of capital, MRF purchases delinquent notes from the investor at a discount, right-sizes the mortgages, and offers genuine principal reduction in conjunction with intensive financial coaching. As a nonprofit, mission-driven investor, MRF can control the loss mitigation process, ensuring that families who are underwater (owing more than their home is worth) but who could otherwise afford their mortgage are able to do so. Both borrowers and lenders benefit from reduced financial loss, as do neighborhoods.[8]

MRF is innovative from a variety of perspectives, but one key to its success is the full integration of housing counseling into the program through the Resolution Specialist model. Resolution Specialists are employees of a nonprofit organization with a history of providing a range of homeowner supports, affordable lending, and other related services. The Resolution Specialist is directly linked to the "asset" side of MRF; the counselors have access to loan data before they even speak with a client, and they are able to initiate direct contact with both the investor and a designated team at the servicer. In contrast to a traditional loss mitigation model, Resolution Specialists do not have to wait until a client contacts them. In addition, because Resolution Specialists screen applicants and explain eligibility criteria, they have direct access to investor guidelines that dictate eligibility. This is unprecedented for the counseling community. If an aspect of eligibility is unclear, Resolution Specialists can call a MRF team member at the servicer or investor staff to gain clarification. Resolution Specialists also participate in weekly calls with the servicer and MRF staff to review the case pipeline.

In spring 2012, MRF partnered with the Illinois Housing Development Agency (IHDA) to develop a pilot program in the Chicago area.[9] Using Hardest Hit Funds, IHDA agreed

8 Geoff Smith and Sarah Duda, "Left Behind: Troubled Foreclosed Properties and Servicer Accountability in Chicago." (Chicago: Woodstock Institute, January 2011).

9 Illinois was a logical place to pilot MRF for a variety of reasons. In August 2012, Illinois posted the highest rate of foreclosure in the country—one in every 298 houses was in foreclosure. Unlike many other parts of the country, foreclosures had actually increased by 33 percent over the previous year. Strong local capacity also exists in Chicago. Neighborhood Housing Services of Chicago has served thousands of homeowners at risk of foreclosure in the Chicago region through its homeownership counseling services. Working to revitalize Chicago communities since 1975, the organization has a track record of achieving excellent outcomes for its clients.

to provide an initial investment of up to $100 million to purchase delinquent mortgages and improve borrower and neighborhood outcomes. In Illinois, Resolution Specialists are employed by Neighborhood Housing Services of Chicago, a local community development financial institution (CDFI) that has long provided homeownership counseling services. Under contract with MRF, the Resolution Specialist is responsible for building and implementing an Individual Program Plan for each borrower using MRF guidelines. MRF looks to the expertise of the Resolution Specialist to determine the plan for each borrower and to assist in bringing secondary debt under control.[10]

In summer 2013, the Mortgage Resolution Fund expanded to purchase mortgage notes in Northeast Ohio, bringing the total pool to 1,350. The mortgages in the Ohio pool are up to three years delinquent. Some borrowers had already received foreclosure notices at the time that MRF acquired the note.

Despite the odds stacked up against preventing foreclosure for these borrowers, initial results from the loan pool purchases have been extremely encouraging. Homeowners respond in higher numbers to the MRF Resolution Specialists than to traditional loan servicers who may have contacted them in the past. Of the total pool of families holding delinquent notes in Illinois and Ohio, nearly 70 percent have had contact with a Resolution Specialist, compared to an industry standard in the range of 30-40 percent. Results also suggest that the MRF loan modification rate is higher when a Resolution Specialist is involved in the process. Of the MRF households contacted, nearly 80 percent have modified their loans, entered into short sales or deeds in lieu, or relocated to more appropriate housing options.

The individual anecdotes coming out of MRF in Illinois and Ohio tell an even more compelling story than the statistics alone. One MRF borrower was previously unable to establish a modification with her servicer despite several attempts to do so, after she was hospitalized and her son became ill. As a MRF client she was eligible for a "right-sized" mortgage that she could afford and entered into a modification, which brought stability to her life and allowed her to remain in her home. A second MRF borrower suffered from the loss of her spouse's income after a divorce, and had only child support as her income. She was repeatedly denied modification approvals and lost $1,500 to a loan modification scam. Eager to put her financial troubles behind her, with MRF she was able to work with a Resolution Specialist to voluntarily enter into a deed in lieu of foreclosure. Relieved of her mortgage obligations, she was able to move forward with her life after this crisis.

One of the most promising outcomes of the MRF program thus far is the true sustainability of the restructured mortgage. As of November 2013, 91 percent of MRF borrowers

10 The standard is a 31 percent/45 percent front-end/back-end debt ratio that will support the homeowner's ability to stay in the home with a new mortgage at the reduced principal. Once MRF owns the note, the Resolution Specialist can recommend a trial modification or alternative disposition depending on the household's financial situation. Options may include a short sale or deed in lieu of foreclosure, with foreclosure only as a last resort. If borrowers are approved for a trial modification, they receive an action plan to reduce back-end (non-mortgage) debt and financial coaching during a 6- to 24-month period until the household is eligible for a permanent loan modification. Borrowers become eligible for a permanent modification after making on-time payments and by bringing down back-end debt to an affordable level. If a borrower's financial situation does not allow for a trial modification, the Resolution Specialist will work through the transition to more affordable housing.

approved for a trial modification in Illinois are sustaining their mortgage payments, including 14 percent who have already converted to a permanent modification. The ability to sustain homeownership once a mortgage is right-sized is an outcome that has implications beyond the MRF model, for the broader mortgage industry.

The Occupied Homes Program: Embedding Housing Counselors

Another new model is the Occupied Homes Program (OHP) in New York. This program is composed of the Neighborhood Housing Services of New York City, the New York Mortgage Coalition, and the Long Island Housing Partnership. Its goal is to help underwater homeowners who have endured a recent hardship to stay in their home. The consortium of New York area organizations has created a pilot project to keep families in place while converting nonperforming assets to affordable and viable mortgages. Specifically, the program encourages servicers to offer structured short sales or identify candidates for principal reductions that could be offered under mortgage settlement agreements.

The program purchases the note at the current market rate and rents the home back to the household. The family is able to stay in the home while they receive intensive financial coaching from a HUD-certified housing counseling agency. The rent is equal to the new principal, interest, taxes and insurance of the newly adjusted mortgage. The family demonstrates they are able to afford the new mortgage with this new payment history. If the household meets underwriting criteria and makes 12 consecutive on-time payments, they may repurchase the home under the program's mortgage terms.

As in MRF, housing counselors play a critical role in the OHP model. They identify potential participants from existing client pipelines, and counselors work to determine if a current homeowner can afford the adjusted mortgage payment. Once a participant enters the program, housing counselors seek to resolve financial issues impeding sustainable homeownership. Counseling services are critical to ensuring loan performance, thereby providing significant value to both the investor and the homeowner.

Conclusion

It is unclear what the future of the housing counseling industry will look like, but increasingly, there is recognition of its value. For example, in its 2013 report, the Bipartisan Policy Center's Housing Commission called for an "entirely new system of housing finance," and declared that housing counseling and education must be central to any sustainable homeownership strategy. The report stated that more could be done in the pre-purchase counseling arena to build on models of lender-counselor partnerships. "Lenders, investors, and regulators could provide counseling incentives for borrowers on the margins of creditworthiness."[11] In addition, the Consumer Financial Protection Bureau in its new rules regarding high-risk mortgages has underscored the importance of counselors to the industry. Starting in January 2014, before lenders make a high-cost loan, they must certify that the consumer has received

11 Bipartisan Policy Center, "Housing America's Future: New Directions for National Policy" (Washington, DC: Bipartisan Policy Center, February 2013), p. 35.

"homeownership counseling" that specifically discusses the high-cost product the lender is offering the consumer.[12] HUD is also exploring strategies to integrate housing counseling into FHA lending.

What is harder to foresee is how the counseling industry will evolve given fiscal constraints, and how it can be structured to achieve greater scale. The Commission posited that the stakeholders who benefit from counseling should pay for it.[13] However, this means that the industry must improve its ability to identify and market to customers, whether they are homeowners, lenders, servicers, or rental property managers, as well as demonstrate its return on investment. Efficiencies in the way products are delivered must be created.

One solution may be to take advantage of technology to increase scale and maximize efficiency. HPN, together with its member the Minnesota Homeownership Center, has developed and recently launched Framework®, an online homebuyer education tool that is interactive, fun, and adheres to the National Industry Standards for Homebuyer Education curriculum. Framework is an example of a low-cost approach to providing counseling services, and the online platform may be more effective at reaching populations who face challenges attending in-class sessions.

But the hope is that the Mortgage Resolution Fund and the Occupied Homes Program in New York will also demonstrate the value of embedding counseling into all of the steps of a mortgage transaction. By fully integrating counseling into relevant financial products and social enterprise models, the scale of counselors' impact is vastly increased, leading to better outcomes for individual households, investors, servicers, and communities.

Danielle Samalin, Vice President of Homeownership Initiatives at the Housing Partnership Network, oversees the Network's housing counseling and foreclosure prevention efforts, with a specific focus on new business innovations in counseling such as the Network's online homebuyer education tool, FRAMEWORK®, and the Resolution Specialist component of the Mortgage Resolution Fund.

12 Consumer Financial Protection Bureau, "What the New High-Cost Mortgage Protections Mean for Consumers" (Washington, DC: CFBP, January 2013), available at http://files.consumerfinance.gov/f/201301_cfpb_high-cost-mortgage-rule_what-it-means-for-consumers.pdf

13 Bipartisan Policy Center, "Housing America's Future," p. 10.

The Federal Housing Administration's Distressed Asset Stabilization Program: An Innovative Solution for Addressing the National and Local Impacts of the Recession

Carol Galante
Federal Housing Administration

The housing market and the nation's economy have come a long way over the past year. Construction is growing faster than at any time since the crisis began in 2008 and 2012 was the strongest year of home sales since the beginning of the recession. Rising home values have lifted millions of families back above water on their mortgages, foreclosure starts are down, and unemployment rates continue to fall, putting communities and the national economy on the road to recovery.

Although we are seeing signs of economic rebound, we must remember that the crisis was truly disastrous for many families and communities. When President Obama spoke recently about the role that housing plays in creating a better bargain for the middle class, he was clear that one of our priorities must be rebuilding the communities that were hardest hit by foreclosure. And while the housing market and the economy have continued along the path to recovery, that recovery has been uneven–some areas continue to lag behind. Those places are being held back by high foreclosure rates and vacant properties that drag down home values and slow growth. We need to rebuild these local economies if we want to create opportunities for everyone to reach or remain in the middle class.

Throughout the recession, the Federal Housing Administration (FHA) played a vital role in preventing a larger housing crisis. By providing much-needed liquidity and credit access when the private market contracted severely, FHA has kept the housing market functioning. However, this crucial countercyclical role came at a cost in the form of added stress to FHA's insurance fund. We continue to deal with a sizable portfolio of seriously delinquent loans and, because we could not rely solely on FHA's traditional real estate owned (REO) disposition mechanisms to handle this influx of loans, our team looked for innovative ways to address the challenge associated with nonperforming assets. In addition to seeking higher recoveries for FHA's insurance fund, we also considered ways we could leverage these assets to achieve broader goals, including reducing the concentration of vacant foreclosed properties and contributing to stabilization in areas hit hardest by the recession. These efforts resulted in the development of the Distressed Asset Stabilization Program (DASP).

An Innovative Solution to a Lingering Problem

DASP, which builds on an existing program known as the 601 Accelerated Claims Disposition note sales program, is an innovative strategy to sell severely delinquent loans before they go into foreclosure. Under FHA's traditional claim payment process, foreclosed homes are conveyed to the Department of Housing and Urban Development (HUD) as REO properties. Under DASP, however, FHA-insured loans are sold prior to foreclosure through a competitive bidding process in which loan pools are sold to the highest bidder, including nonprofit and community-based organizations. Once the note is purchased, foreclosure is delayed for a minimum of six additional months, giving the new servicer a chance to work through possible alternatives with the borrower, one of which may be to find an affordable solution to allow the borrower to remain in his or her home. Because the purchaser is able to buy the mortgage notes at the prevailing market rate–which is generally below the outstanding principal balance–they often have an increased ability and incentive to help borrowers prevent foreclosure. If that isn't possible, the purchaser may be able to help the borrower sell the property through a short sale or find some other alternative preferable to foreclosure. Purchasers are required to report on final resolutions of the loans purchased, including the level of loan restructuring received by a borrower. While it is still early in the process of working through loans purchased through DASP, preliminary indications are that many borrowers who would otherwise have faced foreclosure are indeed finding alternative solutions.

DASP also serves an important role in our efforts to increase recoveries on defaulted loans. To achieve higher recovery rates than those associated with FHA's traditional REO disposition process, we have worked to increase the share of loans directed to pre-REO alternatives. As a result of these efforts, our alternative disposition programs have increased recovery rates on defaulted loans by seven percentage points since January 2013. This improvement has had a direct, significant impact on FHA's insurance fund.

In effect, DASP creates a win-win-win situation for all involved. It enables FHA to avoid the carrying and maintenance costs associated with REO disposition while achieving material reductions in FHA's delinquent loan portfolio. For small servicers, assigning eligible loans to HUD through this program reduces the costs of carrying them through foreclosure, benefitting both the servicer and FHA. DASP also provides many borrowers better alternatives than the foreclosure that would be almost certain otherwise, and it contributes to more stable communities as cities and towns work to emerge from the effects of the recession.

Targeted Support Where It Is Needed Most

Some communities need even more help in addressing the high concentrations of seriously delinquent properties, and we wanted to ensure that these communities experienced the stabilizing and revitalizing effects of FHA's distressed asset programs. In the hardest-hit areas, vacant and abandoned properties hurt the community's economic recovery, significantly lowering surrounding home values. For these areas, HUD created specialized pools of loans within DASP called neighborhood stabilization outcome (NSO) pools. These pools carry additional safeguards to ensure that the program contributes to revitalization and stabilization in communities struggling to rebuild from the effects of the recession.

NSO pools require that at least 50 percent of the loans within a purchased pool achieve "neighborhood stabilizing outcomes," which may include resolutions such as holding the property as a rental unit for at least three years or executing a short sale to a new owner-occupant. The six-month delay for foreclosure proceedings applies to the NSO pools as well. Selling these significantly distressed loans located in areas hardest hit by the crisis can encourage investment in these communities, potentially breathing new life into these loans and facilitating proactive steps to make sure homes are occupied.

Parties seeking to bid in the NSO pools are required to meet additional criteria beyond what is required for bidders in national pools to ensure they will comply with the program's goal that fewer homes end up as vacant REO properties. In some of these hard-hit communities, state and local leaders are already acquiring these loans and using HUD tools to offer workable solutions for homeowners and communities. Nonprofit and for-profit investors have shown great interest in using this program to help families in their community find affordable housing options quickly and sustainably. Some have had great success in partnering with state and local government entities to acquire assets through DASP, leveraging their expertise to achieve government goals in targeted areas. Early indications are that some of these nonprofits are achieving strong borrower contact rates and substantial effectiveness in helping homeowners avoid foreclosure, resulting in the positive individual and community outcomes DASP was created to deliver. Because of this success, FHA is working with local leaders to create additional smaller pools to fit their targeted neighborhood strategies.

DASP sales brought an enthusiastic response from the marketplace in fiscal year 2013. FHA sold more than 40,000 notes nationwide, with targeted NSO pools in Chicago, Illinois; Tampa, Florida; Phoenix, Arizona; Newark, New Jersey; the greater Orlando area in Florida; southeastern Florida; Southern California; Cleveland, Ohio; southern Ohio; Atlanta, Georgia; and North Carolina.

Innovation for Restoration

The recent signs of recovery from the worst economic downturn since the Great Depression are promising, largely due to the decisive and aggressive action the Obama administration has taken during the last five years. FHA answered the call to ensure liquidity in a disrupted market, and protected access to homeownership for millions of American families. As a result, FHA has contributed significantly to stabilizing the nation's housing market and to promoting a speedier recovery from the recession. No program or policy will solve all of the problems in a $9 trillion housing market, but as the country emerges from the recession, we must continue to seek out new and innovative ways to strengthen communities and help families while we work to restore FHA's insurance fund. The Distressed Asset Stabilization Program is one way we do just that.

DASP is an important example of how the federal government can work with private and public partners to facilitate greater stabilization in local and national markets and assist hard-hit communities as they recover. DASP is also an example of how we can use existing tools to help better manage the fund, securing it for future generations of homeowners. With DASP and other innovative efforts, HUD is committed to ensuring that the nation's housing market and the broader economy return to full health, and that the American dream of homeownership remains alive and well.

The United States Senate confirmed Carol J. Galante to serve as the Assistant Secretary for Housing/Federal Housing Commissioner on December 30, 2012. Prior to her confirmation, Ms. Galante served as the Acting Assistant Secretary for Housing/FHA Commissioner, having first joined HUD in May 2009 as the Deputy Assistant Secretary for Multifamily Housing programs. Prior to her appointment at HUD, Ms. Galante was President and Chief Executive of BRIDGE Housing Corporation, the largest non-profit developer of affordable, mixed-income and mixed-use developments in California.

Reflections on the Crisis: The Need for Public Sector Entrepreneurialism

Mercedes Márquez

Los Angeles Housing + Community Investment Department

In 2012, I left my post as the U.S. Department of Housing and Urban Development's (HUD) Assistant Secretary of Community Planning and Development to return to Los Angeles and resume my role as the head of its Housing Department (LAHD). By virtue of these dual roles, I had the unique opportunity to see the foreclosure crisis and the response from both the local and federal policy perspective, and to reflect on what we've learned about community development as a result. Through my experiences, I have come to believe that it takes a real commitment to the spirit of introspection and innovation to confront challenges, particularly in the realm of neighborhood stabilization and development. Like entrepreneurs who find and assess opportunities, identify and manage risk, track and value process(es), locate and manage resources, and anticipate and measure benefits and outcomes, my team and I have consistently sought the spaces across and between sectors that represent fertile ground for innovation and success.

I share some of these successes here to show how the practice of stabilizing and developing thriving neighborhoods is evolving for the better. The Los Angeles experience with the Neighborhood Stabilization Program (NSP) and Consolidated Plan (ConPlan), for example, provides valuable insights into how a spirit of entrepreneurship and a commitment to placemaking can contribute to community revitalization. I also describe how a culture of technical assistance and data-driven planning is emerging at the federal level, bringing with it the promise of better targeting of public funds and greater transparency. This is not to suggest that any of these efforts are without their challenges (indeed, often large and frustrating ones!). However, I also believe that the last five years have fostered incredible innovation within the community development field, and that these innovations should be shared and celebrated.

Reflections on Los Angeles and NSP

As I look in the rearview mirror, I am still staggered by how badly Los Angeles was hit by the foreclosure crisis. Between September 2006 and October 2009, the Los Angeles area saw more than 206,000 homes go through foreclosure, 32,000 in the city of Los Angeles alone. The Northeast San Fernando Valley and South Los Angeles areas were the hardest hit, but in very different ways. In the Valley, the impact was felt primarily in single-family homes. In contrast, in South Los Angeles foreclosures struck many more multifamily housing properties. The foreclosure crisis contributed significantly to declines in the city's economy as well. Los Angeles relied heavily on the real-estate industry as a driver of its local economy, and the collapse of the housing market decimated the employment base. Residential unit development activity fell off a cliff, and with it, all the jobs that supported that development activity.

By necessity, the ethos of "doing more with less" took hold within LAHD and fundamentally shaped how we approached our NSP program. We leveraged existing legislative and government infrastructure, data resources and tools (e.g., mapping), and cross-departmental and cross-jurisdictional relationships forged before NSP to expand the breadth of the NSP dollar. Plainly speaking, the City stretched and strategically used every dollar, bolstering as many policy priorities as possible.

Some examples:

Job Creation - Bridges to Business. The Bridges to Business Success (B2BS) is a collaboration of Citi Community Development, the City of Los Angeles' Housing and Community Investment Department, the University of Southern California Minority Business Development Agency, and the Southern California Minority Business Development Council. B2BS provides minority small business owners with professional training to build capacity to effectively compete for public and private contracting opportunities. Graduates of the program successfully completed nearly $4 million of contracted NSP work in Los Angeles; NSP was responsible for creating or retaining more than 4,700 full- and part-time jobs. Jobs ranged from accounting and other administrative positions to construction and real estate professionals, the fields most acutely affected by the economic downturn. Linking NSP to employment goals also provides training opportunities for career advancement. Contractors learned energy efficient construction techniques in order to work in an emerging, "green" economy.

Transit-Oriented Development. One of the key concerns for me and my staff has been how to promote equitable transit-oriented development and ensure that we preserve affordability near public transit routes. We decided to use NSP to help achieve this goal, and directed NSP funding toward projects located on or near transit stops. One example of this is the Metro@ Chinatown Senior Lofts. This property is a transit-oriented development that encompasses the adaptive reuse of two delinquent, vacant, blighted office buildings into 123 affordable rental live/work units. Located about a block away from the Chinatown stop of the Gold Line, this Enterprise Green Communities-certified project has significantly enhanced the image, livability, and economic vitality of the Chinatown community.

Addressing Chronic Homelessness. The City, working in partnership with the Los Angeles County Department of Health Services (DHS), has set aside 15 NSP properties, totaling 56 housing units, to provide permanent supportive housing opportunities for homeless individuals with disabilities or chronic health conditions who are frequent users of DHS hospital services.

Creating Green Spaces - Parks Initiative. NSP enabled the City to convert blighted and vacant properties into community parks. Working in NSP neighborhoods and leveraging both NSP1 and other public and private funds, the City converted nine blighted and vacant foreclosed properties (acquired with NSP1 funding) into new community parks. The parks are designed with sustainable landscapes and water and energy-conserving elements, such as smart irrigation systems and solar-powered lighting.

Preservation of Valuable Housing - RSO Acquisition Strategy. The data and mapping performed by the City revealed that foreclosures in South Los Angeles consisted of a mix of single-family homes and smaller rental properties that were subject to the City's Rent Stabilization Ordinance (RSO). The RSO protects tenants from excessive rent increases in multifamily properties built and occupied prior to October 1, 1978. In many submarkets in the city, rents charged for rent-stabilized units are the more affordable options for tenants. NSP provided the resources to acquire RSO buildings in foreclosure and that were in significant disrepair. Funds were used to invest in substantial rehabilitation. Thereafter, rehabbed properties were transferred to mission-driven organizations with the capacity to own and manage them as affordable rental housing for very low-income households. To date, NSP funds have been used to acquire 46 RSO properties containing more than 150 housing units.

Affordable Housing Trust Fund. The Affordable Housing Trust Fund (AHTF), established in 2000, creates affordable rental housing for low- and very low-income households in Los Angeles. The AHTF emphasizes projects that keep per-unit costs as low as possible, as well as projects that have a demonstrated high level of leverage. However, the foreclosure crisis required that we think innovatively about how to leverage NSP dollars to fund large, catalytic projects that would otherwise have difficulty scoring competitively in the AHTF NOFA process. We decided to target NSP investment to developments that would offer rental opportunities at deeply affordable levels. To date, nearly one-half (47 percent) of combined NSP1 and NSP2 expenditures in Los Angeles have been on projects to assist households with very low incomes, greatly exceeding the minimum requirement of 25 percent. The values of nimbleness and flexibility proved instrumental here. Los Angeles did not originally contemplate using NSP2 funds to acquire and rehabilitate large, multifamily developments, but we nevertheless saw this as an opportunity to meet various goals, such as reviving catalytic projects in areas of need and creating and preserving deeply affordable, multifamily rental units.

The implementation of NSP in Los Angeles was neither easy nor perfect, but we did embrace the spirit of entrepreneurialism as much as possible. We researched, mapped, reviewed, reconsidered, changed direction, adapted, argued, and collaborated, with measurable benefits to the low-income communities we care about.

Los Angeles Beyond NSP

Now, after my stint at HUD (more on that below), I find myself back in Los Angeles, confronting both new and old challenges. While the LA housing market is recovering, many neighborhoods still struggle with foreclosed properties, and affordability remains a perennial concern. With no federal financial commitments (like NSP) in the foreseeable future, Los Angeles has had to consider how it will continue the work begun with NSP.

Encouragingly, the values and systems we put into place with NSP are proving to be very helpful as we move forward, as evidenced by the work on the City's consolidated plan (ConPlan). First, NSP required that we develop significant data analysis and mapping expertise to identify our target neighborhoods. This expertise has been critical to our ability to develop a strategic ConPlan that dovetails transit investment with other community development goals. Showing the power of data in place-based planning and investment, through maps, unleashed opportunities for transformative neighborhood stabilization and development not seen before in Los Angeles.

Second, the idea that singular funding streams should serve multiple goals has really taken root, and we have made the goal of truly comprehensive community development a linchpin of our ConPlan. Given that transit infrastructure funding will entail $40 billion of investment in the region, it made sense to direct those investments in a way that also connects residents to human services, affordable housing, jobs, neighborhood amenities, as well as the rest of the city. We are really proud of the work we've done on the ConPlan, and feel honored that Federal Reserve Chairman Ben Bernanke singled out the Los Angeles approach as a model plan that "calls for a multifaceted approach" to "build healthy communities by integrating community, economic, and housing development investments with transit opportunities to increase their positive impact on neighborhoods."[1]

Third, our work on NSP highlighted the need to build the city's own institutional capacity–to think strategically about the structure of our departments, to create new organizations, and to work collaboratively to effectively coordinate efforts and maximize impact. We've taken the bold, yet necessary, step of consolidating the former Community Development Department's human service functions with the portfolio of programs and services provided by the former Housing Department. Tellingly, the new Housing and Community Investment Department (HCIDLA), which I now lead, is actively implementing the strategic plan articulated in the transit-oriented ConPlan. We also remain committed to undertaking place-based planning in partnership with the private sector, nonprofits, and other government agencies. For example, both LISC and Enterprise have committed to Los Angeles by providing technical assistance to inform the process for targeting the investment of scarce federal housing and human services dollars. In addition, Enterprise will undertake outreach campaigns such as a transit-oriented development university, where community stakeholders will be given the tools to participate in the planning and decision-making process to ensure equitable transit-oriented development.

The Importance of the Federal Role

In addition to my experiences in Los Angeles, my vantage point from my HUD tenure taught me another important lesson: there is a powerful role for the federal government in

1 Ben Bernanke, "Creating Resilient Communities." Federal Reserve System Community Affairs Research Conference. Washington, D.C. April 12, 2013. http://www.federalreserve.gov/newsevents/speech/bernanke20130412a.pdf

helping municipalities respond to the foreclosure crisis and neighborhood redevelopment going forward. While nearly every corner of the country was negatively affected by foreclosures, the exact nature and effects of the crisis were very local. The investment plan set in motion in Los Angeles, through NSP, did not necessarily guarantee success in a rust belt city, a rural county in the southwest, a New England township, or a village in the Pacific Northwest.

For me and my team at HUD, the key question guiding our work was always "what is it that only the federal government can do?" Certainly, federal funding and a public commitment to place-based investments are critical, and I am proud to have been part of the Obama administration where place-based planning was not only encouraged, but backed by clear funding preferences. But I also realized that a key role that HUD can play is one of technical assistance and building the capacity of local municipalities to develop their own innovations.

Let me provide just one example. In Los Angeles, I learned first-hand about the power of data to map needs, shape investments, and build political consensus. But while I was at HUD, it became evident that many localities lacked or had very limited access and ability to use geospatial, analytical tools to assess the breadth and depth of their foreclosure crisis. In fact, we found that only 30 percent of grantees had any mapping capacity.

In response, HUD launched the eCon Planning Suite, a set of data and technology tools to help communities make sure scarce federal dollars were targeted to where they were needed most and could achieve the biggest impact. In addition to improving the effectiveness of public funds, this approach to planning can save state and local communities at least 65,000 staff hours each year and thousands of dollars in consultant fees. HUD Secretary Shaun Donovan put it this way, "We know that in a time of huge budget cuts at the state and local level, it's harder and harder to have the resources to bring that information together. This technology that we're providing is going to be really revolutionary in helping all of our grantees work smarter."[2] It also empowers the public in a way never before offered. Anyone can log on to the mapping tool and see precisely where the need is in their neighborhood, where investments have been made, and they can be more informed when they argue for their vision of where federal tax dollars ought to be targeted. This is democracy in data!

Concluding Thoughts

My experiences as a policymaker and practitioner at the local and national levels have afforded me the unique insight into the absolutely critical nature of espousing a sense of introspection and innovation. At both the local and federal levels, my team and I strove to implement key tenets of entrepreneurialism: we engaged in constant self-assessment and a regular review of real-time data, understanding that the economic and fiscal realities of the

2 U.S. Department of Housing and Urban Development, "HUD Launches Overhaul Of Consolidated Planning Process," Press Release HUD No.12-077. http://portal.hud.gov/hudportal/HUD?src=/press/press_releases_media_advisories/2012/HUDNo.12-077

housing crisis and the government's response were fluid. And I'm proud to say we're already seeing the manifestations of this "public sector entrepreneurial spirit" taking hold today. We are not planning for it, we're doing it!

Most important, what has been impressed upon me is the absolute need to innovate despite adversity, and to maximize limited funding by aligning local and federal resources, combined with private and philanthropic partners, to have a positive impact on communities.

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Affirmatively Furthering Fair Housing in REO-to-Rental Programs

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In July of 2013, the Department of Housing and Urban Development (HUD) released a new proposed regulation entitled "Affirmatively Furthering Fair Housing" (AFFH). The purpose of the proposed regulation is to modernize and clarify a component of the 1968 Fair Housing Act, which requires the government to avoid policies that perpetuate or increase residential segregation, and to undertake affirmative steps to promote residential integration and fair housing choice. At their core, the Fair Housing Act and the obligation to affirmatively further fair housing were designed to undo the government sponsored segregation that had emerged in the years after World War II.

Since its passage, HUD has implemented the AFFH provision with varying levels of enthusiasm, depending on the Administration in power. But it has consistently recognized the obligation in the law and its applicability to all HUD programs. However, in contrast to HUD, the Treasury Department, the Internal Revenue Service (IRS), and the Federal Housing Finance Agency (FHFA) have not formally acknowledged their civil rights responsibilities under the Fair Housing Act, despite the fact that they oversee many important housing initiatives, including the Low Income Housing Tax Credit (LIHTC), Government Sponsored Enterprise (GSE) receivership and reform, the Home Affordable Modification Program, and the Real Estate Owned (REO)-to-Rental program.

The REO-to-Rental program is particularly intriguing from a fair housing perspective. In January 2012, the FHFA launched its REO-to-Rental program, which converts pools of foreclosed REO properties held by the government-sponsored enterprises into affordable rental properties.[1] The program targets metropolitan areas hard hit by foreclosure and requires investors to rent them out for a specified number of years. Fair housing advocates viewed this program as a new opportunity for affordable rental properties in less-segregated, low-poverty communities–that is, until they discovered that the FHFA and the Department of the Treasury had made no effort to conform the new program to the requirements of the federal Fair Housing Act. This article discusses how the federal agencies responsible for the REO-to-Rental program can take advantage of this opportunity in the future, even if it has so far eluded them.

The "Affirmatively Furthering Fair Housing" Regulation

The stated purpose of the proposed "Affirmatively Furthering Fair Housing" regulation is to "improve fair housing choice through fair housing planning, strategies and actions." It sets forth a regulatory framework designed to clarify and systematize the standards for identifying and addressing patterns of housing segregation, provides uniform national data and improved technical assistance to grantees, and strengthens the role of community and resident input into the fair housing planning process.

The new HUD proposal is grounded in the 1968 Fair Housing Act, the legislative capstone on a series of extraordinary civil rights laws that included Title VI and Title VII of the Civil Rights Act of 1964, as well as the Voting Rights Act of 1965. The Fair Housing Act (also known as Title VIII) not only banned private discrimination but it also sought to undo patterns of racial segregation that had emerged in the years after World War II, driven largely by government policy. The Act thus emerged as a response to what the Kerner Commission famously described as "two societies, one black, one white–separate and unequal."

The provision of the Act that addressed the government's role and responsibility for undoing segregation was Section 3608, which provides that "all executive departments and agencies shall administer their programs and activities relating to housing and urban development (including any Federal agency having regulatory or supervisory authority over financial institutions) in a manner affirmatively to further the purposes of this subchapter."[2] The courts and HUD have consistently interpreted this provision–the duty to affirmatively further fair housing–as requiring federal, state, and local governments to avoid policies that perpetuate or increase residential segregation and to undertake affirmative steps to promote residential integration and fair housing choice.[3] The new proposed regulation is HUD's latest effort to modernize and clarify the AFFH obligation.[4]

AFFH at the Department of the Treasury

The Department of the Treasury, through the IRS, administers the LIHTC, the nation's largest low-income housing development program.[5] Since the beginning of the foreclosure crisis, the Department of Treasury, in conjunction with HUD, has also overseen two new housing initiatives designed to reduce the number of foreclosed properties: the Home Affordable Modification Program (HAMP) and the REO-to-Rental Program (also in conjunction with the FHFA). HAMP, which began in 2009, offers reduced monthly mortgage payments to homeowners who are at risk of foreclosure. Since its inception, more than 1.2 million homeowners successfully modified the terms of their mortgages to reduce their monthly payments.[6] The REO-to-Rental Program is designed to reduce the number of vacant, foreclosed properties by enabling investors to purchase pools of these properties for rental housing.[7]

In contrast to HUD, however, the Treasury has not yet officially acknowledged its civil rights responsibilities under Section 3608 of the Fair Housing Act.[8] Treasury's housing programs are clearly "programs and activities relating to housing and urban development," and the Department has been put on notice of its obligations repeatedly,[9] yet it has continued to postpone compliance. Fair housing advocates have argued that in many states, the failure of the Treasury to adopt fair housing rules has contributed to a pattern of segregated development in the LIHTC program, administered by the Treasury and the IRS in cooperation with state housing finance agencies.[10] The lack of civil rights guidance for the LIHTC program has led to litigation in several states, including cases in South Dakota, New Jersey, Connecticut, and Texas. Most recently, a federal district court in Dallas ruled that a civil rights organization had established a prima facie case of discrimination in the tax credit allocation practices of the Texas Department of Housing and Community Affairs.[11]

AFFH in the Federal Housing Finance Agency and the REO-to-Rental Program

Similarly, the FHFA has no rules or procedures to affirmatively further fair housing. The FHFA, created by the Housing and Economic Recovery Act of 2008, is the regulator and conservator of Fannie Mae and Freddie Mac and the regulator of the 12 Federal Home Loan Banks. The FHFA is advised by the Federal Housing Finance Board, composed of the secretaries of Treasury and HUD, the chair of the Securities and Exchange Commission, and the FHFA director.[12] As a federal agency "administer[ing]…programs and activities relating to housing and urban development (including any Federal agency having regulatory or supervisory authority over financial institutions),"[13] the FHFA is clearly covered by the affirmatively furthering fair housing obligation.

In January 2012, the FHFA launched the REO-to-Rental Program, which was jointly developed and implemented by the Department of the Treasury and HUD.[14] Under the program, qualified investors would bid and purchase pools of foreclosed properties from Fannie Mae or Freddie Mac or the FHA, located in areas with high foreclosure rates that would be rented for a specified number of years. The goals were to reduce the inventory of unsold homes, help stabilize housing prices, support neighborhoods, and provide sustainable rental housing.

Ideally, REO-to-Rental programs could acquire properties for low-income rental in high-opportunity communities that would provide new, racially integrated housing choices for low-income families currently living in high-poverty, segregated neighborhoods. However, the current policy approach auctions single-family properties in higher-income areas for homeownership, while single-family properties in lower-income neighborhoods are directed towards affordable rentals. This approach reinforces existing patterns of segregation and contributes to the lack of affordable rental properties in economically diverse neighborhoods.

Prior to the launch of the federal REO-to-Rental program, fair housing groups had documented disparate maintenance and marketing practices between privately held REO homes in white neighborhoods and those in communities of color. The National Fair Housing Alliance conducted an examination of more than 1,000 REO properties and found that those in African American and Latino neighborhoods were more consistently vacant and in substandard condition than those in white neighborhoods, resulting in further harm to communities of color.[15] The failure of lenders and servicers to provide equal maintenance and marketing practices to their portfolio of REO properties is also an act of housing discrimination and a violation of federal law. There was hope that the launch of the REO-to-Rental program would enable mission-driven nonprofit organizations to both acquire and improve properties in distressed communities and acquire properties for low income rental in thriving middle-class communities to promote fair housing goals.

When FHFA and HUD issued a "Request for Information" to solicit ideas for disposition of REO properties held by Fannie Mae, Freddie Mac and the Federal Housing Administration, fair housing advocates across the country submitted their proposals in a letter to Edward DeMarco, acting director of the FHFA.[16] The Housing Partnership Network also submitted a detailed proposal, and several national civil rights groups submitted a supplemental statement on the request for information in February 2012.[17]

The key concern among advocates was that the request for information did not include any aspect of the AFFH mandate in the goals and objectives of the disposition strategy. [18] This AFFH obligation involves not only protecting vulnerable communities of color; it also requires the federal government to expand housing opportunities for low-income families of color in higher-opportunity communities outside traditional "areas of minority concentration." The absence of any mention of this obligation is indicative of the approach of both the Treasury and FHFA to date. While REOs are disproportionately located in minority communities, a significant number of properties are located in job-rich communities with low poverty rates and high-performing schools. Maps prepared by the Kirwan Institute in four metropolitan areas demonstrate the enormous fair housing potential of FHFA's REO inventory.[19]

The key elements of the civil rights groups' proposal included:

- ***Geographical distribution.*** Pools of rental properties in the auction should not be concentrated primarily in low-income neighborhoods and should include properties throughout a metro area with at least an equal number of properties in communities of opportunity.
- ***Improving the bidding process to empower nonprofits.*** Currently, Fannie Mae and Freddie Mac "First Look" programs provide select nonprofits the opportunity to purchase REO homes during the initial 15 days of a property's listing. The proposed REO-to-Rental program should extend this time period to 45 days for REO properties in low-poverty, high-opportunity communities. The right of first refusal should be extended to qualified nonprofit organizations and public housing authorities in high-opportunity areas, as well as other entities that commit to maintaining the property as long term, income-targeted rental housing.
- ***Bulk purchase program.*** The Administration's plan should include an aggressive pre-retail bulk purchase program limited to the acquisition of properties for rental in low-poverty, high-opportunity communities. These properties should be prioritized

for families using Section 8 vouchers to cover the higher purchase price and to ensure strong affirmative fair housing marketing goals.

- ***Nonprofit partnerships.*** Incentives should encourage partnerships with nonprofits that have experience in affordable housing development and management.
- ***Scattered-site property and asset management.*** Disposition of REO properties through bulk sales will create some economies of scale and potentially lower management costs. However, too much aggregation of properties may make it difficult for nonprofits to compete. There must be a balance between volume and feasibility for nonprofit partners.
- ***Financial incentives.*** The government should offer financial structures like seller financing and joint venture arrangements that increase the ability of nonprofits to participate in the purchase of the properties.
- ***Affirmative marketing.*** REO properties and property managers should be subject to affirmative marketing requirements to ensure that families living in segregated, high-poverty neighborhoods have priority access to units in safer and higher-opportunity areas. This program should be viewed by the government as an opportunity to expand opportunity for low-income families, particularly through the use of both tenant-based and project-based vouchers in REO properties in high-opportunity, low-poverty communities. A strict source-of-income nondiscrimination policy should be established for REO rental properties (similar to requirements in the HOME and LIHTC programs)[20] to ensure that Section 8 voucher holders have access to REO rental units in high-opportunity areas. Affirmative fair housing marketing should target households least likely to apply in the area where each property is located and ban discriminatory local residency preferences.[21]

The first bulk sale began in February 2012 with 699 Fannie Mae–owned properties in Florida. Two other bulk sales–one in the Chicago area and one in the Southwest, including Arizona, California, and Nevada–resulted in 1,763 properties sold through this pilot program.[22] The disposition of this inventory represented a once-in-a-generation opportunity to advance fair housing goals. This opportunity was lost in the first round of the REO-to-Rental program because of the absence of affirmative fair housing goals; we hope that low-income renters get another chance in the next round.[23]

Conclusion

The foreclosure crisis was built on a segregated housing market, and had a disproportionate impact on families of color.[24] The government has an obligation to ameliorate these disparities in its disposition of government-owned foreclosed homes. The REO-to-Rental program provides an opportunity to add thousands of additional rental housing units that are particularly well suited for families. Many of these units are located in lower-poverty, low-crime neighborhoods with above-average schools. If the Treasury and the FHFA had been conforming their policies and practices to their basic legal obligations under the Fair

Housing Act, patterns of segregation in government-supported housing would be noticeably different today. We hope that the federal Administration, including the Treasury Department and the FHFA, recognize that there is still time to act in support of fair housing goals.

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Endnotes to article: Affirmatively Furthering Fair Housing in REO-to-Rental Programs

1 The REO-to-Rental program included properties held by the GSEs under the receivership of the FHFA (Fannie Mae and Freddie Mac), as well as properties held by the Federal Housing Administration (FHA), which is part of the Department of Housing and Urban Development. See www.fhfa.gov/webfiles/22367/FHFARFIReleaseFinal.pdf.

2 42 USC §3608(d).

3 The AFFH obligation was expressly extended to state and local grantees in 1983 in an amendment to the Housing and Community Development Act of 1974, Pub. L. No. 93-383, 88 Stat. 633, consistent with court precedent interpreting the Fair Housing Act. See Otero v. New York City Housing Authority, 484 F.2d 1122 (2d Cir 1973). Congress also required that state and local grantees certify their compliance with the AFFH obligation in the Cranston-Gonzalez National Affordable Housing Act of 1990, 42 USC §12705(b)(15)-(16) (2006).

4 The AFFH proposed regulation is also a response to a report of the Government Accountability Office critical of HUD's oversight of the AFFH process, though HUD had begun the development of the rule well before the GAO Report was issued. See US Government Accountability Office, "Housing and Community Grants: HUD Needs to Enhance Its Requirements and Oversight of Jurisdictions' Fair Housing Plans," report to congressional requesters, September 2010. www.gao.gov/assets/320/311065.pdf.

5 26 USC §42. Between 1987 and 2011, there were 37,506 projects and almost 2,318,000 housing units placed in service (see HUD USER at http://www.huduser.org/portal/datasets/lihtc.html).

6 12 U.S.C. §5219(a)(1). See also number of homeowners assisted at http://portal.hud.gov/hudportal/HUD?src=/press/press_releases_media_advisories/2013/HUDNo.13-139.

7 http://www.fhfa.gov/Default.aspx?Page=360.

8 To date, the only step taken in any Treasury housing program related to fair housing is the so-called general public use rule at work in the Low Income Housing Tax Credit program. The rule imposes penalties for acts of discrimination against individual renters of tax credit units. It fails to address the obligation of the IRS to take steps and to require housing credit agencies to take steps to avoid racial segregation and promote integrated housing choices for low-income families of color. In 2000, the Treasury also

entered into a "memorandum of understanding" with HUD and the Department of Justice to explore the implementation of fair housing standards, but to date, little has emerged from this collaboration beyond the original memorandum.

9 For a sample of civil rights coalition letters directed at the Treasury, see www.prrac.org/projects/lihtc.php. In addition to its failure to adopt rules to implement the AFFH obligation, the Treasury does not have the basic nondiscrimination rules required of all federal agencies under Title VI, which explicitly directs all federal agencies to adopt regulations barring discrimination and segregation based on race and disability in programs of federal financial assistance (and an administrative complaint process to be followed in cases where discrimination is alleged). 42 USC §200d-1 (Title VI); 29 USC §794 (§504). The Department of Justice is charged with the responsibility of coordinating agency compliance with this mandate by executive order (Executive Order 12250, Leadership and Coordination of Nondiscrimination Laws). To our knowledge, neither the Treasury, the IRS, nor the FHFA have adopted rules, policies, or procedures complying with the rulemaking mandate of Title VI for recipients of assistance under the programs they administer. It seems clear that the Treasury's housing programs are subject to Title VI and §504 as "federal financial assistance" under the act. The Low Income Housing Tax Credit–enabling statute, §42 of the Internal Revenue Code, allocates credits equal to a specified financial value to state credit agencies within an annual housing credit ceiling. State agencies then grant credits to project owners who sell them to raise capital to pay for construction costs. Low Income Housing Tax Credits are a "thing of value . . . extended by the grant statute" and are thus governed by Title VI and §504 (U.S. Department of Transportation v. Paralyzed Veterans of America, 477 U.S. 597, n. 11 [1986]). The few courts that examine this issue within a tax context distinguish between deductions generally available to taxpayers and tax benefits that provide direct subsidies in order to carry out regulated public purposes. See, e.g., McGlotten v. Connally, 338 F. Supp. 448 (D.C., 1972). However, regardless of the Treasury's obligations under Title VI in regard to "federal financial assistance," it is bound by the AFFH requirements of the Fair Housing Act, which have no such limiting language.

10 See generally publications and advocacy documents collected at www.prrac.org/projects/lihtc.php. Research documenting the extent of racial segregation and concentration of Low Income Housing Tax Credit units in high poverty locations includes, among other studies, Ingrid Gould Ellen and Keren Mertens Horn, Poverty and Race Research Action Council, "Do Federally Assisted Households Have Access to High Performing Public Schools?" *Civil Rights Research*, November 2012, www.prrac.org/pdf/PRRACHousingLocation&Schools.pdf; "Are States Using the Low Income Housing Tax Credit to Enable Families with Children to Live in Low Poverty and Racially Integrated Neighborhoods?" (Abt Associates, 2006), and "Assessment of the Economic and Social Characteristics of LIHTC Residents and Neighborhoods" (Abt Associates, February 28, 2000). For additional research, see, e.g., William Callison, "Achieving Our Country: Geographic Desegregation and the Low-Income Housing Tax Credit," *Southern California Review of Law & Social Justice* 19 (Spring 2010): 213; Myron Orfield, "Racial Integration and Community Revitalization: Applying the Fair Housing Act to the Low Income Housing Tax Credit," *Vanderbilt Law Review* 58 (November 2005): 1747; Florence Roisman, "Mandates Unsatisfied: The Low Income Housing Tax Credit Program and the Civil Rights Laws," Miami Law Review 52 (1998): 1011; PRRAC and Lawyers' Committee for Civil Rights, "Building Opportunity: Civil Rights Best Practices in the Low Income Housing Tax Credit Program," 2008, www.prrac.org/projects/LIHTC.php. Some defenders of the program's demographic characteristics argue unconvincingly that because the LIHTC program is "less" segregated than other segregated housing, it is not perpetuating segregation—even when most family units are being placed in higher poverty, racially concentrated neighborhoods. See, e.g., Keren Horn and Katherine O'Regan, "The Low Income Housing Tax Credit and Racial Segregation," *Housing Policy Debate* 21 (3) (2005): 443–473.

11 Inclusive Communities Project v. Texas Dept. of Housing and Community Affairs, 2010 WL 3766714 (N.D. Tex., September 28, 2010).

12 See Federal Housing Finance Agency, Strategic Plan 2009–2014. www.fhfa.gov/webfiles/14476/FHFA_StrategicPlan_2009-2014n.pdf.

13 42 USC §3608(d).

14 See Federal Housing Finance Agency, US Department of the Treasury, and US Department of Housing and Urban Development, "FHFA, Treasury, HUD Seek Input On Disposition Of Real Estate Owned Properties." Press release (Washington, DC, August 10, 2011). fhfa.gov/webfiles/22367/FHFARFIReleaseFinal.pdf.

15 See National Fair Housing Alliance, The Banks Are Back–Our Neighborhoods Are Not (Washington, DC: National Fair Housing Alliance, April 4, 2012). www.nationalfairhousing.org/LinkClick.aspx?fileticket=sNHLaQE4WSw%3d&tabid=3917&mid=9405.

16 Philip Tegeler et al., "Re: Affirmatively furthering fair housing in the disposition of REO properties," letter to Edward DeMarco, acting director of the Federal Housing Finance Agency, September 15, 2011. www.prrac.org/pdf/REO_civil_rights_comments_9-15-11.pdf.

17 National Urban League et al., "Proposal to Incorporate an Opportunity Framework to Transition REO Property into Rental Housing," February 2012. www.prrac.org/pdf/AFFH_in_REO_properties_Feb_2012.pdf.

18 See also Stella J. Adams, "The Fair Housing Act Implications of the Emerging REO-to-Rental House Market," August 13, 2013. http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2309182. Adams discusses concerns about compliance with other nondiscriminatory laws, such the Equal Credit Opportunity Act and Unfair and Deceptive Practices laws.

19 See maps of Cleveland, Columbus, Cincinnati, and Seattle at the Poverty & Race Research Action Council. www.prrac.org/full_text.php?item_id=13398&newsletter_id=0&header=Current%20Projects.

20 42 USC 12745 (a)(1)(D); 24 CFR 92.252(d) (HOME); 26 USC §42(h)(6)(B)(iv) (LIHTC).

21 For an overview of affirmative marketing requirements and best practices, see Megan Haberle et al, Accessing Opportunity: Affirmative Marketing and Tenant Selection in LIHTC and Other Housing Programs (PRRAC, December 2012), at www.prrac.org/pdf/affirmativemarketing.pdf.

22 Federal Housing Finance Administration, "Fannie Mae SFR REO 2012-1: Highlights of the REO Pilot Transactions," November 2012. www.fhfa.gov/webfiles/24720/SFREO2012DealTermF0.pdf.

23 This proposal has taken on additional urgency now that President Obama has called for the eventual winding down of Fannie Mae and Freddie Mac as quasi-public agencies. See White House, Office of the Press Secretary, "Remarks of President Barack Obama on Responsible Home Ownership–as Prepared for Delivery." Press release (Phoenix, AZ, August 6, 2013). www.scribd.com/doc/158529513/Remarks-of-President-Barack-Obama-on-Responsible-Homeownership.

24 See Jacob Rugh and Douglas Massey, "Racial Segregation and the American Foreclosure Crisis," *American Sociological Review* 75 (2010): 629; see also Debbi Gruenstein Bocian et al., "Lost Ground, 2011: Disparities in Mortgage Lending and Foreclosures" (Center for Responsible Lending, 2011); Derek Hyra et al., "Metropolitan Segregation and the Subprime Lending Crisis," *Housing Policy Debate* 23 (1) (2013).

Foreclosure Recovery: The Work That Remains

Paul Staley

Self-Help Foreclosure Recovery and Asset Building Project

The house on 40th Street in Richmond, California, was just one of millions of homes that were lost during the foreclosure crisis. The husband got sick and the couple fell behind on their payments. He died and the bank foreclosed. Right around the same time, the Gomez family (not their real name) moved from Texas to San Francisco, where they, along with their two sons, moved into a one-room basement apartment with no kitchen and only a shared bathroom. Both husband and wife were employed as janitors and they set about shopping for a house to buy.

They looked and made offers, over and over again, but they never succeeded in getting to the contract stage. By their estimation, they made more than 40 unsuccessful offers during 2011 and 2012. Time and again they were told that they had lost to an all-cash offer from an investor. They were about to give up when their agent came across a listing for the house on 40th Street. It had been purchased and remodeled as part of the Foreclosure Recovery and Asset Building Project, an effort created and funded by the East Bay Community Foundation and managed by the Self-Help Community Development Corporation, for which I serve as Project Manager. The program provides homeownership opportunities to low- and moderate-income families by buying, fixing and re-selling foreclosed homes.[1]

Their offer was one of 25 submitted. It was not the highest, but project managers selected it because their predicament symbolized one of the great dislocations of the housing collapse and recovery: families with steady employment and good credit were continuing to live in substandard housing because of competition from well-funded investors.

Diagnosing the Bubble

The housing bubble, its collapse, and the subsequent economic decline have been diagnosed and analyzed from a variety of angles. We have also spent a great deal of time worrying about a recurrence of those events: Are we seeing another bubble in home prices? Will prices fall again when the dreaded shadow inventory hits the market? But we should also examine how the response to the foreclosure crisis has changed the residential real estate landscape and how that response has sown the seeds for the next set of housing policy challenges.

One can, to a certain extent, view the housing bubble and ensuing debacle as the result of an epidemic of misunderstanding throughout the U.S. housing market. Subprime lenders misled borrowers about the risks embedded in the mortgages they were taking on, and at the

1 Debt financing for the project is provided by One PacificCoast Bank and homebuyer education and counseling is provided by the Community Housing and Development Corporation of North Richmond and the East Bay Asian Local Development Corporation.

other end of the financial spectrum, financial analysts and investment managers seriously underestimated the risks in their investments in the securities backed by those misunderstood mortgages. An entire edifice of credit was built on this web of misunderstanding, and eventually it collapsed.

But what about now? What are we potentially not seeing properly right now as the housing market and the entire economy continue to recover? In particular, what has been the impact on low- and moderate-income communities, and what are the policy implications of that impact?

Is It Still the American Dream?

One major misunderstanding may be the belief that the foreclosure crisis will produce a lasting change in Americans' desire to own a home. I recall a conversation with a Wall Street banker whose breezy interpretation of the bubble and its aftermath was that a lot of people who shouldn't have bought homes had done so, and the ensuing deluge of foreclosures meant that two things were going to happen: the first was that a lot of those people would never be owning homes again, and the second was that their foreclosed homes would become a new asset class of detached rental housing. In this particular instance, his analysis was more than slightly self-serving since he was trying to arrange financing for one of the larger regional buy-and-hold funds that was acquiring and then renting out a substantial number of single-family homes. But he was hardly alone in seeing the market in this light.

As a matter of public policy, there has been a debate in some quarters over what constitutes the "right" level of homeownership, despite the numerous studies that have demonstrated its benefits. But while economists debate the after-tax costs of shelter, they fail to recognize the noneconomic factors that drive the urge to own one's home. Renting may make more financial sense than ownership for many households, but that does not provide very good guidance as to how those households will behave, precisely because deciding to buy a home is not an entirely financial decision.

For people for whom certain levels of educational and professional achievement are not attainable, owning a home offers a significant and tangible sense of accomplishment. For the immigrant, it signals arrival. For those who have faced discrimination, it represents release from the sometimes arbitrary authority of a landlord. Finally, in the eyes of many working-class families, owning a home offers a degree of control and safety that their rental housing choices cannot provide.

Here in California, home prices in communities with "good schools" have increased well above those with inferior school systems as public funding of education is spread thinner across the state. Housing prices in those fortunate communities capture the premium homebuyers are willing to pay in order to get an increasingly scarce commodity: good public schooling. Less well appreciated is that a similar premium exists for single-family homeownership in low- and moderate-income communities. As people feel less safe in public space–the streets where they and their children walk, their parks, and even their schoolyards–they will increasingly seek out the safety of a home where a sturdy fence protects a yard where their children can play, and a private driveway and garage provide a safe place to park their cars. In both instances–the suburban house in a good school district and the tidy bungalow in an urban neighborhood–the price of the house represents demand not just for shelter, but for other benefits as well.

As a result, if we continue to underfund the public realm, lower-income households–the people who experience a disproportionate share of the violence and crime that develop in the wake of that depletion–will strive even harder to find shelter where they will feel safe. This, in turn, will add even more demand for what passes as affordable housing in already expensive markets. This also explains the counter-intuitive outcome of rising property values in areas where other indicators of quality of life are declining.

Carpe Domus

One of the great clichés of the real estate market is the old chestnut, "Cash is king." But if so, never has royalty been so eager to insert itself into our less well-heeled neighborhoods. An equally apt description of what has happened can also be found in the adage that "nature abhors a vacuum." In late 2008 and early 2009, there were lots of homes available but not that many buyers. There was an eerie post-neutron bomb feeling to the neighborhoods where subprime lending had been most prevalent. House after house stood vacant, sometimes stripped of all appliances and plumbing. The houses were there, just barely, but the people had disappeared. There were houses, but no buyers.

Into this void stepped pools of private capital that scooped up houses at prices not seen for more than a decade. Some investors were flippers–i.e. they fixed and resold the homes–while most were building portfolios of rental properties as a longer-term investment. Viewed from one perspective, these investor groups were performing the classic function of speculative capital in a depressed market: absorbing excess supply, thereby stabilizing the market.

But over time a different dynamic began to emerge. As the economy recovered, households returned to the market, hoping to take advantage of cyclically low prices and historically low interest rates. But at the same time, the success of the initial investor groups had spawned further growth of that business. In a low interest rate environment, the prospect of 6-8 percent annual returns plus future capital gains from sales of the homes was a very attractive proposition. Furthermore, these investment groups had made major strides in creating operating platforms that could analyze, acquire, lease, and manage a large number of homes spread across a wide area.

Thus the stage was set for the story that has been repeated thousands of times in the past year. A family finds a house and tries to buy it, only to have the seller accept an all-cash offer from an investor group. The Foreclosure Recovery Project was designed to break this pattern. The Project is an all-cash buyer with a difference: after the houses are remodeled, we market them exclusively to potential owner-occupants. All offers must include a letter from the buyers explaining their situation and background. The Gomez family's situation is repeated in most letters, and it is not uncommon to hear from families who have submitted 20 or more unsuccessful offers.

Furthermore, the evidence suggests that the impact of investor acquisitions has been disproportionately greater in low- and moderate-income neighborhoods. This is not merely a result of limited financial resources and restricted access to credit. As a general rule, rental yields–net income divided by the cost of the house–are higher in lower-priced neighborhoods, making investments there potentially more profitable. The sweet spot for investors was at the lower end of the market, especially given the substantial decline in valuations in those neighborhoods in the aftermath of the collapse of the subprime lending market.

Most press accounts about investor involvement in the market have focused on either the aggregate numbers–investors are playing a large role–or this "crowding out" phenomenon. Less attention has been paid to the longer-term impacts of this significant redistribution of homeownership. The most critical is the substantial appropriation of income and potential wealth that will take place over the coming years. Ever since the bubble burst, it has cost far less per month to own than to rent a house in the working-class neighborhoods of the Bay Area. Quite simply this is what made buying and renting out those homes such an attractive investment. But this also means that there are thousands of households that could have afforded to buy a home but instead are paying more each month as rent, and that excess cost of shelter flows right out of their neighborhoods. An even more significant impact is the lost opportunity for lower-income families to realize substantial increases in household net worth as the houses they couldn't buy appreciate in value over the coming years. The scale of this transfer of wealth will ultimately be measured in the billions of dollars.

Slumlord or Merely Absentee?

Every investor-owned home represents an ownership opportunity that has been delayed indefinitely. This has implications in addition to the income and wealth effects discussed above. The first is that community stability may be compromised in these neighborhoods. This is not merely the result of the displacement of long-term residents through foreclosure. Rental properties turn over at a faster rate than owner occupied homes. Neighbors have less time to get to know one another, and in certain respects, less incentive to do so. This can erode neighborhood cohesion, particularly if mobility is high in and out of poorly maintained or otherwise inadequate rental units.

The second impact is more qualitative. Some community leaders have expressed concerns that these investor groups will become the new breed of slumlord. But there is no evidence that these new investment groups will be any worse at property management than smaller "mom and pop" operations. In fact, one could argue that these larger, better-capitalized groups have the resources and management capacity to provide a superior level of property management. But there is still an unavoidable aspect to their dominance in certain markets:

they may never be slumlords, but they will also never be occupants. As a result, neighborhoods where most houses were once occupied by owners are now communities of predominantly renters.

There is no denying that very few absentee owners will do the extra embellishment or landscaping that an owner would. Pride of ownership is evident at every address in a wealthy neighborhood, but it plays a potentially even greater role in lower-income neighborhoods. The well-maintained yards and homes of owner occupants are statements that life, even in dangerous surroundings, does not have to be ugly or degraded. Quantifying the impact of this is difficult, but sadly, the possibility exists that crime could follow in the wake of this erosion of community identification and appearance.

The third and most significant impact is simply this: a substantial portion of the single family housing stock in our low-to-moderate income neighborhoods is "off the market" for purchase by households. When these homes become available for purchase and at what price is anybody's guess. Many of these investment funds have fixed maturity dates, at which point they are obligated to sell their portfolios and return capital and accrued profits to their investors. The largest funds are exploring the possibility of becoming REITs (Real Estate Investment Trust) in which case their inventory of homes would not necessarily need to be sold. (In the REIT scenario, the funds convert their investors' ownership interests into stock; the newly formed REIT continues to own the houses, but any investors who need or wish to cash out would sell their stock in the public markets.) Regardless of which course of action these funds pursue, the facts on the ground as of fall 2013 remain the same: We have constrained supply in our lower-priced neighborhoods in the face of sustained strong demand from households who are interested in and capable of becoming owners.

Conclusion and Policy Responses

A crisis, even one as long-standing as this, is a fluid situation. Although foreclosure and delinquency rates are still high by historical standards, they are trending lower. Prices have increased dramatically from the trough. In the meantime, a new set of players, the investment funds, has a significant role in lower priced single-family markets. Now seems like the appropriate time for thinking about the next phase of this housing cycle. While the work on loan modifications and other resolutions of individual hardships must continue, the new and important challenge in this next phase will be to recapture investor-owned housing units in low- and moderate-income neighborhoods. A sample of ideas provides a starting point for developing possible programs, including:

- Down payment assistance and housing and credit counseling to help tenants rebuild their credit scores and purchase the houses they are currently renting. This would help neighborhood stability by allowing tenants to stay in place.
- Tax incentives for investors to transfer their houses to nonprofit ownership and management. Tax credits plus Community Reinvestment Act financing could provide

a low cost capital structure for these nonprofit entities, or tax incentives could be used to encourage sales by investors directly to low-income families.

- Expanded down payment assistance or shared equity programs to bridge the affordability gap for low-and-moderate income buyers. Such a program could provide an inflation hedge for socially minded capital by allowing invested dollars to earn a return based on home price appreciation.
- A nonprofit, single-family REIT that could acquire and control investor portfolios of homes. Property management for such a venture could be outsourced to one of the private platforms that have been developed in the wake of the housing collapse.

The foreclosure crisis was a devastating experience for the millions of families who lost their homes. But at the same time it offers an opportunity for other households to buy homes at cyclically low prices and historically low interest rates. Sadly, many of these potential buyers have been unable to take advantage of these circumstances. The Foreclosure Recovery Project is a modest attempt to help low- and moderate-income households become homeowners. But there is much work remaining. The nation's recovery from the foreclosure crisis will be a challenge for years to come as we work to restore homeownership in our communities.

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