

Policy Lessons from the Neighborhood Stabilization Innovations Initiative

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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/nfmcnp/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 Rebuild³ 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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