



## **Developing Comprehensive Foreclosure Prevention and Stabilization Approaches: Connecting the Homeownership Affordability and Stability Plan to the**

### **Neighborhood Stabilization Program**

#### **Introduction: Linking Foreclosure Prevention and REO Disposition**

A foreclosure prevention campaign must involve two primary components: a proactive approach to keep people in their homes and a plan to rehabilitate foreclosed and vacant homes into stable reoccupied properties. The glut of foreclosed homes that plagues many neighborhoods is accelerating the decline of housing prices and worsening the national economic crisis. As homes are foreclosed upon, neighboring home values decline, leading to additional foreclosures. This vicious cycle will continue unless we systematically address both problems facing neighborhoods: properties already foreclosed upon and families at risk of foreclosure.

The Administration's Homeownership Affordability and Stability Plan is clearly focused on addressing the problems that families face in affording their mortgage payments. Helping families avoid foreclosures is critical, and all efforts to bring mortgages to affordable levels must be pursued. However, to complement these efforts, more must be done to address the rising number of foreclosed upon homes, which become real estate owned properties (also known as REOs), in neighborhoods across the country. This will ensure that a floor to the housing market is quickly established, allowing communities and families to be stabilized.

#### **REO Properties and Foreclosures**

Homes that have been foreclosed upon greatly contribute to neighborhood blight and disinvestment. For every foreclosure, neighboring homes lose approximately \$6,000 in value, resulting in lost equity to all homeowners in the neighborhood. In some neighborhoods, families can avoid foreclosure through short or conventional sales. But in others, home values have dropped so dramatically that borrowers are simply walking away, leaving empty homes with few would-be purchasers. In such neighborhoods, where there are high concentrations of vacant homes, there is almost no resale market.

As a result, the properties are severely hurting businesses and neighborhoods. They have tied up bank capital, in turn restricting the availability of needed credit to households and businesses. Meanwhile, concentrations of REOs in vulnerable communities are feeding a downward cycle of property abandonment, increased crime, declining property values, shrinking tax bases and community asset deterioration. Without aggressive intervention, heightened concentrations of REOs threaten to undo much of the tremendous progress made in the last few decades to revitalize low- and moderate-income communities.

Recognizing the need for assistance in these targeted neighborhoods, Congress established the Neighborhood Stabilization Program (NSP) in July of 2008. The NSP provides funds to states and localities (and now nonprofits) to work in the areas most affected by foreclosures to purchase and rehabilitate foreclosed upon homes. These funds are being used in communities such as Cleveland, Ohio, and Los Angeles, California, to purchase homes at a discount, sell them to income-eligible



buyers, use them for rental housing or turn them into community space in order to lessen blight and improve neighborhood well-being.

While many localities and nonprofits are working with communities and servicers to purchase REO properties, it is difficult to implement a neighborhood strategy on a house-by-house basis. Even with the additional resources provided to the NSP in the recent economic recovery bill, the amount of funding to deal with foreclosures is not sufficient to the scale of the problem as the economy worsens. In order to address this difficulty, a number of national nonprofits have created the National Community Stabilization Trust (NCST), which is working to consolidate resources to maximize impact and thus help localities and states make best use of their NSP money.

### **Current Obstacles to Successful NSP Strategies**

Attempts to defuse the toxic impact of REOs on financial institutions and communities face significant challenges. Such obstacles include:

- ***Access to REOs.*** A successful local program must include a willingness of financial institutions to establish an efficient, standardized mechanism for transferring REOs from bank balance sheets quickly and in bulk. Additionally, for the program to have a meaningful local impact, it must secure access to a substantial proportion of all REOs in the targeted area. Some (but not all) servicers have been hesitant to sell REOs at discounts, as required by the Neighborhood Stabilization Program, due to fear that investors will sue because the property is being sold too quickly, at too low a price, or without adequate time to expose it to the market. These fears are directly parallel to the concerns of the servicers regarding loan modifications that have been addressed in the Homeownership Affordability and Stability Plan.
- ***Access to Capital to Purchase REOs in bulk:*** Local communities and nonprofits seeking to purchasing REOs in bulk in order to quickly put the vacant homes back into productive use are a critical element to keeping the homes from being sold to speculators and vulture funds. These groups also must obtain the best possible REO price from the servicers so as to make redevelopment feasible on a limited budget. Affordable prices and available capital will allow REOs to be introduced to the market in such a way as to not drive down housing values even further. However, the current crisis in the credit markets has made it impossible to access financing for this activity.
- ***Access to Capital for Renovation and Interim Holding.*** The amount of short- and intermediate-term capital available to facilitate acquisition and renovation of REO properties and leverage the NSP funds must be sufficient to successfully tackle the national scale of the problem.



## Solutions that Help Stabilize Communities

Congress should complement the foreclosure prevention legislation and the recent efforts to expand NSP funding by including provisions to:

- ***Expanded Safe Harbor for Servicers:*** HR 1106 proposes a safe harbor for servicers participating in loan modification. This protects servicers from investor lawsuits and should be expanded to include the sale of REOs to participants in the NSP.

Proposed language: *In addition, the safe harbor created pursuant to Section 201 this provision shall also apply to the disposition of real property resulting from the foreclosure of a mortgage to a not-for-profit organization, state or local government entity or in connection with the Neighborhood Stabilization Program or for any other charitable purpose, provided that the servicer reasonably and in good faith believes that the anticipated recovery from such disposition will exceed, on a net present value basis, the anticipated recovery from an alternative disposition.*

- ***Target Foreclosure Prevention and Loan Restructuring Activities to NSP Areas:*** There will be a positive reinforcing effect on real estate markets if vacant homes are treated simultaneously with loan restructures in nearby and adjacent areas. This can be accomplished through outreach and targeting efforts of homeownership counseling programs.
- ***Encourage FHA and the GSEs to take leadership roles:*** A significant amount of REOs and troubled loans are directly held by FHA, Fannie Mae and Freddie Mac. These institutions have much greater flexibility in how they treat the assets. They should be industry leaders in developing flexible, comprehensive, integrated and targeted disposition programs that meet local NSP goals, including price concessions for dispositions that are part of the NSP, bulk offering and favorable terms and conditions for sales of REOs.
- ***Three Mechanisms for TARP Investment in Neighborhood Stabilization Efforts:*** TARP funds should be allocated to neighborhood stabilization efforts so as to ensure that the foreclosure prevention efforts outlined in the Homeownership Affordability and Stability Plan are effective. TARP funds can be funneled into neighborhood stabilization efforts in various ways: (1) direct investment of TARP funds in the NSP or NCST; (2) investment from the proposed Public-Private Investment Fund or (3) incentives for institutions that receive TARP assistance to invest in the capital corporation of the NCST. Two specific uses for TARP funding are:
  - ***TARP Investment in the NCST to make NSP work well:*** Additional investment in the NCST is needed to ensure the NSP funds are leveraged and executed in the most effective way by state and local governments. The NCST can function as a short-term, interim and specialized lender to assist neighborhood stabilization efforts and to assure



successful implementation of the NSP. Investment in the NCST capital program will help localities finance the acquisition, rehabilitation and disposition of foreclosed properties on a larger and more impactful scale. This will enable the same amount of NSP funds to be leveraged to deal with more foreclosed properties.

- ***TARP Investment in the Creation of a Bulk REO Financing Facility through the NCST:*** In localities with large volumes of REOs, a bulk financing facility can assist in maximizing NSP funds by purchasing properties in bulk. Such a financing facility would quickly move REOs off investor and bank balance sheets and into responsible hands.

*Revised March 4, 2009*

*For more information, contact:*

*Dvora Lovinger, Senior Director of Government Affairs, Enterprise Community Partners*

*Phone: 202.649.3920 or [dlovinger@enterprisecommunity.org](mailto:dlovinger@enterprisecommunity.org)*