



# DISCUSSION PAPERS

COMMUNITY AFFAIRS DEPARTMENT

**HOW TO SPEND \$3.92 BILLION:  
STABILIZING NEIGHBORHOODS BY ADDRESSING  
FORECLOSED AND ABANDONED PROPERTIES**

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## OVERVIEW

The Housing and Economic Recovery Act of 2008 created the Neighborhood Stabilization Program (NSP), under which states, cities, and counties will receive a total of \$3.92 billion to acquire, rehabilitate, demolish, and redevelop foreclosed and abandoned residential properties. These funds can stabilize hard-hit neighborhoods, putting them on the path to market recovery. This will only happen, however, if they are used in ways that are strategically targeted and sensitive to market conditions. This paper outlines 11 key principles that states, counties, and cities should follow as they plan for and use NSP funds.

- Principle 1. Understand the local housing market.*
- Principle 2. Think strategically about how to use NSP funds.*
- Principle 3. Target property acquisition to maximize neighborhood impact while reflecting realistic resource and capacity constraints.*
- Principle 4. Develop multiple acquisition strategies to reflect different property ownerships and conditions.*
- Principle 5. Develop ground rules to determine when to demolish and when to rehabilitate foreclosed or abandoned properties.*
- Principle 6. Design financing strategies for property reuse to reflect program and policy goals.*
- Principle 7. Build the capacity to hold and maintain properties until reuse.*
- Principle 8. Establish sound ground rules for disposing of properties.*
- Principle 9. Integrate acquisition and rehabilitation strategies with other neighborhood stabilization strategies.*
- Principle 10. Create a coordinated, effective local government management structure for neighborhood stabilization.*
- Principle 11. Form partnerships with other public, private, and nonprofit entities to maximize capacity and resources.*

By focusing on these principles, government and its partners, including CDCs, Realtors, developers, and others, can bring about sustainable neighborhood stabilization and market recovery. Despite the short time frame that states and localities have to submit action plans and spend NSP funds, strategic targeting is critically important. If the NSP funds are scattered about rather than used strategically, at the end of the day some properties will be rehabilitated or demolished, but cities and towns are unlikely to see any sustained improvement in their neighborhoods, their quality of life, or their fiscal condition.

## INTRODUCTION

In July 2008, Congress enacted P.L.110-289, the Housing and Economic Recovery Act of 2008 (HERA), arguably the most complex and ambitious housing legislation to come from the federal government since the Cranston-Gonzalez Act of 1990 – which created the HOME program – or even the Housing and Community Development Act of 1974. Primarily directed at ameliorating the foreclosure crisis and re-energizing the slumping housing market, the act contained a major initiative designed to help stabilize towns, cities, and neighborhoods affected by subprime lending and foreclosures.

Title III of HERA appropriated \$3.92 billion for the Neighborhood Stabilization Program (NSP), which will provide grants to states and units of local government to acquire, rehabilitate, or demolish foreclosed and abandoned properties. These funds are allocated to states and local governments under a formula developed by the Department of Housing and Urban Development taking into account the number of foreclosures, sub-prime loans, and defaults in each jurisdiction.<sup>1</sup> Funds will be distributed early in 2009 and must be obligated by the recipient within 18 months of receipt. This is the first time that the federal government has provided funds explicitly for property acquisition and demolition and for the creation and operation of land banks, entities created for the purpose of acquisition and disposition of problem properties.

The need for these funds is clear. Millions of properties are going into foreclosure, with widespread vacancy and abandonment appearing not only in struggling cities such as Detroit, Cleveland, or Newark, but also in booming Sunbelt communities in the Las Vegas or Phoenix areas. While the need for acquisition, demolition, or rehabilitation will vary widely from one area to the next, reflecting the underlying market conditions of each area, almost any community receiving funds under the act can find legitimate opportunities to spend them in ways that both meet the statutory criteria and benefit the public.

The stakes are high at all levels—state, local, and national. Hundreds of communities are reeling from the effects of defaults and foreclosures. Will they use these funds strategically, in ways that put them on the path to recovery, or will they use the funds in a haphazard, opportunistic fashion, leaving behind only scattered improvements without broader change? State and local governments, by using NSP money effectively, could lay the groundwork for continuing federal support for these activities, particularly in the struggling communities that need it most. If they do not, and these funds are used ineffectively or wastefully, additional funds are unlikely to be forthcoming on the heels of this initial \$3.92 billion, and it will remain hard for advocates to make the case for similar assistance again in the future.

The potential pitfalls are many. Many of the state and local jurisdictions that will receive funds have had only limited experience with the activities for which these funds must be used and – to the extent that they have – are likely to have pursued them only on a modest scale. While the funds will often be passed through to sub-recipients, such as community development corporations (CDCs) and other nonprofit entities, many states and counties – particularly those in the Sunbelt and outside large central cities – may have little CDC or nonprofit infrastructure to call upon. Even in cases where they do, both the capacity and the will to do the scattered-site rehabilitation called for in the act may be far less than needed.

Where cities have acquired, demolished, or rehabilitated properties, those activities have typically been transactional in nature, rather than strategic. A city may have acquired a handful of properties to make possible a particular project or demolished some to remove neighborhood eyesores, actions very different from those contemplated by the act. The goal of stabilizing neighborhoods from the impacts of foreclosure requires a strategic approach, integrating use of NSP funds with other legal and financial tools, many of which may be new to many local governments as well as CDCs. Although a handful of cities and counties around the country have

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<sup>1</sup> The regulations and fund allocations are available online at <http://www.hud.gov/offices/cpd/communitydevelopment/programs/neighborhoodspg/nspnotice.pdf>.

established land banks to permit strategic acquisition and disposition of problem properties, far more have – up to now – avoided such steps. Finally, acquisition of REO properties<sup>2</sup> in an unsettled and in many cases still declining market is a delicate process, requiring not only strong negotiating skills but also a sensitivity to conditions and trends in the local housing market.

This paper is designed to help state and local governments skirt the pitfalls and think through effective, strategic ways in which to use NSP funds to yield the greatest benefits to their residents and their communities while recognizing the time pressures, both with respect to preparing action plans and then spending the NSP funds, under which states and localities are operating. While not a detailed guidebook, it identifies the key issues, strategies, and linkages that should be considered in figuring out how these funds should be used, provides basic information about each, and tries to point the readers in the direction of more detailed information as well as good practices in each area. It includes cross-references to the author’s book, *Bringing Buildings Back: From Abandoned Properties to Community Assets*, published in 2006 by the National Housing Institute and Rutgers University Press, where readers will find a much more detailed discussion of many of the specific issues addressed in this paper.

The paper begins with two fundamental issues: the role housing market conditions play in creating the conditions for successfully fostering recovery of destabilized neighborhoods and how to think strategically about bringing about neighborhood recovery. Market conditions, more than any other single factor, set the framework for making rational decisions about which properties to acquire, which to rehab, and which to demolish. Further sections explore the issues associated with acquiring properties; deciding when to demolish and when to rehabilitate properties; holding and disposing of properties; linking the acquisition and disposition program to other stabilization activities; and, finally, how to organize government functions and partner with nongovernment entities for the best results.

## THE BIG PICTURE

### *Principle 1. Understand the local housing market.*

Local housing market conditions will largely determine whether the public sector should be in the business of acquiring foreclosed or abandoned properties and, once having acquired properties, what it should do with them. This is not only a question of whether to demolish or rehabilitate them but also of deciding to what use to put the buildings — or the resulting vacant parcels — after that initial decision has been made.

Foreclosures and abandoned properties destabilize neighborhoods, undermining the neighborhood’s housing market. Fewer people — particularly people with enough money to choose between neighborhoods — choose to buy homes in the area, and the value of the area’s homes drops. As housing demand declines, the area sees less investment in new construction or rehabilitation and increases in deferred maintenance and abandonment.

Stabilizing a neighborhood involves fostering market recovery. Market recovery leads to increased demand for

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<sup>2</sup>REO properties stands for “real estate owned properties.” It is the standard term used to refer to properties owned by a lender and taken back through foreclosure.

housing in the area, reflected in more people buying homes and the homes commanding higher prices.<sup>3</sup> Thus, if NSP funds are to be used effectively to stabilize a neighborhood, the strategy for using those funds needs to focus directly on how it will affect the neighborhood's market conditions and lead to market recovery. In order to do that, one must first thoroughly understand the local housing market and how public action can influence that market.

- *To acquire or not to acquire.*

Demand determines the extent to which houses, including foreclosed and abandoned ones, will be absorbed by the private market with no need for government to acquire and dispose of them. If, for example, in a particular city the area's vacant, foreclosed houses are likely to be absorbed through increased housing demand as a result of job growth and in-migration over the next couple of years, it may be wasteful for government to buy those houses. The role of government might better be to use its police powers, such as code enforcement and nuisance abatement, to keep these properties from doing harm to their neighbors while waiting for them to be absorbed by the market. Such steps, by preserving the value of the area, are also likely to increase the speed with which the market absorbs those properties. Since NSP funds do not have to be used for acquisition, cities can use their funds for other purposes permitted in the act.

This scenario may apply in some Sunbelt communities such as Las Vegas, where casino and other projects may bring tens of thousands of new jobs to the area over the next few years. It does not apply to cities such as Detroit or Cleveland, where market failure is pervasive and the supply of housing far exceeded the demand even before recent foreclosures expanded the number of vacant properties and diminished the number of potential homebuyers in the marketplace. Other locations, such as California's Central Valley, fall in between. Some areas may recover on their own, but others, particularly those with heavy concentrations of foreclosures, may require public money to jump-start the market recovery. In these regions, careful analysis will be needed to determine which areas are likely to recover without a direct governmental role, in order to concentrate on those areas in greater need of intervention.

Cities such as Philadelphia and Baltimore have developed market-based *neighborhood typologies*, using data on housing market activity and other factors to assess the relative market strengths and weaknesses of the city's neighborhoods, reflecting the fact that neighborhoods tend to fall into a limited number of discrete market categories, from those with thriving markets and strong demand to those, often with large numbers of abandoned properties, with weak markets and little demand. This approach, applied in a framework that takes into account overall regional growth, can be used as a "market screen" to evaluate which areas affected by foreclosures and vacancy are more or less likely to need direct governmental intervention to bring about market recovery.

- *To rehabilitate or demolish.*

Understanding market conditions can help determine not only whether and where to acquire properties but

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<sup>3</sup>When we refer to demand, we mean *unsubsidized* demand, that is, demand from people who have enough money to buy the houses on the market at the prices they command.

also what to do with them. While market conditions are not the only factors that determine whether one should rehabilitate or demolish a property — a subject addressed further below — they are an important factor. Market conditions will determine how many people are likely to be interested in buying rehabilitated houses in a particular area and how much they are likely to be willing to pay for them. If the number is very large and the amount they will pay very high, there may be no need to use public funds for rehabilitation.

In the opposite situation, where few people want to buy in an area, and those few have little money or are unwilling to pay the full cost of acquisition and rehabilitation, the combination of limited demand and the large amount of public money likely to be needed for each house means that rehabilitation should only be undertaken carefully and selectively. In some cases, demolition may be preferable, to remove blighted buildings that may be driving down the neighborhood and to reduce the supply of housing so that it bears a better relationship to demand.

The question of to whom to target houses that are acquired or rehabilitated with these funds also requires sensitivity to market conditions. Buyers or renters of homes where NSP funds are used must earn no more than 120 percent of the area median income (AMI), while one-quarter of the funds must be used to benefit households earning no more than 50 percent of AMI. This range offers considerable scope for public action, since in many metropolitan areas, 120 percent of AMI can exceed \$80,000.<sup>4</sup> Selecting the most appropriate target income mix should take account not only housing need but also how targeting to different income levels can potentially affect the economic health and stability of the neighborhood to which the NSP funds are directed.

***Principle 2. Think strategically about how to use NSP funds.***

While understanding the market is a critical starting point for a strategic approach to neighborhood stabilization, it is not enough. Ultimately, a strategic approach can emerge only where one first has a clear understanding of one's goals and, second, where one mobilizes multiple resources, programs, and activities to achieve those goals. In most cases, the NSP funds will not be enough in themselves to achieve sustainable neighborhood stabilization, particularly in a city with weak demand and many problem areas. To gain the greatest benefit from these funds, cities should take five steps:

- *Leverage NSP funds with other funds from public and private sources.* This can include other grant funds such as CDBG or housing trust funds, as well as private or loan capital.
- *Target NSP and other resources to where they are needed most or where they can achieve sustainable neighborhood stabilization.* Concentrating on a few key areas is likely to be far more beneficial than scattering acquisition or rehabilitation funds around a city or county while leaving large numbers of problem properties untouched.
- *Integrate NSP activities with other strategies that further neighborhood stabilization,* in particular, code enforcement and nuisance abatement.
- *Leverage implementation capacity through partnerships with other public agencies, nonprofit organizations, and businesses.* Local governments are under severe constraints in terms of the capacity they have available for

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<sup>4</sup> For example, based on HUD 2008 data, 120 percent of AMI for a family of four was \$77,000 in Phoenix, \$86,200 in Denver, \$100,900 in Orange County, California, and \$141,400 in Stamford, Connecticut.

neighborhood stabilization efforts and can benefit by building connections to other entities in the community and region with additional capacity and shared goals.

- *Establish benchmarks based on outcomes, not inputs.* Counting the number of properties acquired, demolished, or rehabbed measures neither the extent to which markets have been stabilized nor the grounds laid for market recovery. Cities need to adopt outcome-oriented measures, such as changes in market values or the volume of real estate activity and track progress on those measures as they move forward.

All of these principles apply to states as well as cities or counties. States must make a further decision, specifically, whether to sub-allocate funds on a formula basis to local jurisdictions within the state, or to oversee use of the money directly, through contracts with local or regional public or private sub-recipients. While both alternatives have merit, the state has an overarching responsibility to make sure that its NSP funds are, in fact, used strategically to stabilize neighborhoods. While states may be under strong political pressures simply to pass their NSP funds on to cities and counties, to do so without making sure that the funds are used strategically is irresponsible. Rather than simply sub-allocate funds, states should consider issuing requests for proposals and awarding funds to projects in areas that meet need criteria and demonstrate the capacity to carry out effective neighborhood stabilization efforts.

The above principles should guide public action, whatever specific strategies a state or city may follow. In the following section, we will explore specific questions of how to organize and conduct property acquisition activities. Although not all states or cities may end up using NSP funds for acquisition, where they decide to do so, complex issues arise.

## ACQUIRING PROPERTIES

Property acquisition is a complex process. For acquisition to be carried out successfully, decisions must be made about which properties to acquire, how to negotiate the price, and which legal tools should be used, particularly where dealing with difficult property owners or uncertain economic conditions. While some local governments or allied entities such as redevelopment authorities are experienced in property acquisition, many others have done so only rarely if at all. It is important to move carefully in order to avoid pitfalls and ensure that public funds are used responsibly.

Foreclosure is only one of many ways by which once-sound properties have been rendered unproductive and harmful. Congress recognized this when it authorized NSP funds to be used not only for foreclosed properties but also for other abandoned properties, whatever the circumstances that led to their being abandoned. In an area with large numbers of vacant properties, an acquisition strategy that focuses solely on buying REO properties, ignoring other problem properties in the same area, will be ineffective.

***Principle 3. Target property acquisition to maximize neighborhood impact while reflecting realistic resource and capacity constraints.***

We have already mentioned briefly the importance of targeting resources where dealing with problem properties. When it comes to trying to stabilize an area, it is critical to understand that even one vacant, boarded-up property can undermine the vitality of an entire city block. The harm done, whether measured in the impact



on property values or the effect on neighbors' health and safety, does not increase linearly with each additional vacant property – the first few do nearly all of the damage.<sup>5</sup>

The lesson from this is that a strategy that concentrates on acquiring — or otherwise putting back into productive use — all or as many as possible of the unused properties in carefully selected neighborhoods is likely to be a more effective stabilization and market recovery strategy than one that scatters its acquisitions more widely.

There is no one “right” targeting strategy. At least three distinct approaches may be appropriate:

- Focus on neighborhoods that are close to market recovery, and move the recovery forward by buying and restoring a small number of properties, where costs or other factors make it impossible for the private sector to do the job.
- Target neighborhoods with significant market weakness, but with an intact but frayed physical and social fabric, and build a functioning market by eliminating blighting problem properties or by reducing housing supply to reflect realistic levels of demand.
- Target severely distressed neighborhoods, and acquire properties in order to create potential land assembly, reduce housing supply, or stabilize remaining occupied areas.

In most cases, however, the most effective strategy is likely to involve targeting those areas where small numbers of foreclosed or abandoned properties are undermining the vitality of otherwise viable communities and where a modest investment can have a major impact.

In each case, the acquisition strategy complements market activity or takes place in settings where the market effectively does not exist. An approach that should not be pursued is to acquire properties that are likely to be reused by the market, either with no government intervention at all or with less intrusive government actions, such as code enforcement or pressure on absentee owners, through such measures as vacant property registration ordinances.<sup>6</sup>

A targeting strategy must not only decide what types of areas to target but how many are realistic, given the level of resources available. It is better to do three neighborhoods right, than six or 20 inadequately. While political considerations might suggest that a large number of different areas should be targeted simultaneously — particularly in cities with ward- or district-based city councils — this is not necessarily the case. As was true for Richmond, Virginia's Neighborhoods in Bloom strategy, a solid data-driven planning process can often convince elected officials as well as citizens of the merits of targeting limited resources.<sup>7</sup>

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<sup>5</sup> A study of the impact of abandoned properties on sales prices of neighboring properties found that one abandoned property on a block reduced sales prices by \$6,468. As the number of abandoned properties on the block rises to five, their effect on the value of other properties grows gradually; further increases in the number of abandoned properties result in no statistically significant change. *Blight-Free Philadelphia: A Public-Private Strategy to Create and Enhance Neighborhood Value*, Eastern Pennsylvania Organizing Project and Temple University Center for Public Policy, 2001.

<sup>6</sup> Wilmington, Delaware, enacted a vacant property registration ordinance that imposes a graduated fee on all such properties; that is, for every year a property remains vacant, the fee increases, going in steps from \$500 in the first year up to \$5,000 if the property has remained vacant for 10 years, with an additional \$500 for each year after 10 years.

<sup>7</sup> A case study of Richmond's Neighborhoods in Bloom strategy can be found at <http://www.knowledgeplex.org/showdoc.html?id=333>.

Just as the number of neighborhoods that can be targeted simultaneously must reflect resource constraints, so must the number of properties that are acquired. In any community, the capacity to rehabilitate and resell properties, from both a technical and financial standpoint, is not unlimited. Most developers, both for-profit and nonprofit, have little interest in rehabbing scattered-site properties, a complicated, labor-intensive, and unpredictable task. Particularly where the goal of acquiring properties is to return them speedily to occupancy and reuse, the city and its partners must be careful not to get too far ahead of themselves, acquiring more houses than they are capable of putting back to use.<sup>8</sup>

**Principle 4.     *Develop multiple acquisition strategies to reflect different property ownerships and conditions.***

Current market conditions demand that anyone acquiring properties, particularly those in foreclosure, be a savvy purchaser and obtain a price that truly provides for public benefit rather than bailing out owners or lenders.<sup>9</sup> While most public acquisitions are at fair market value, Sec. 2301(d)1 of HERA specifically provides that:

Any purchase of a foreclosed upon home or residential property under this section shall be *at a discount from the current market appraised value of the home or property*, taking into account its current condition,<sup>10</sup> and such discount shall ensure that purchasers are paying below-market value for the home or property.

The buyer, whether a public agency or a nonprofit entity acting as a sub-recipient of NSP funds, must be prepared to document that it paid less than what would be considered fair market value. In many areas where prices are still moving downward, a price that may be considered a discount from the market value today may no longer be a discount six months later. The NSP regulations provide guidance on the minimum discount that will be required for individual properties and for each city’s overall acquisition portfolio.

Many cities, as well as the CDCs that are likely to be NSP sub-recipients, have only limited experience in land acquisition. Acquiring mortgages or foreclosed properties may involve negotiating with sophisticated entities with access to experienced professionals. The need to comply with the discount requirement of the act adds a further complication. As a result, any state, city, or county planning to use NSP funds to acquire property needs to assemble a strong negotiating team, including:

- An experienced appraiser with a solid understanding of the market factors affecting properties in the neighborhoods where acquisitions are planned;

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<sup>8</sup> This issue is discussed further below under Principle 8, dealing with property disposition.

<sup>9</sup> In this paper, as a shorthand, we have used the term “lender” to refer to the entity that holds the mortgage or is pursuing the foreclosure and ultimately taking title. In reality, as is well known, because of the complex structure of many of the mortgages being foreclosed — particularly subprime mortgages — the entity is likely to be a third party acting on behalf of the investors that hold a pool of mortgages, rather than the initial lender, who is likely to be long out of the picture by the time foreclosure takes place.

<sup>10</sup> This language would seem to imply appraisals do not take the current condition of the property into account, which is not usually the case. A responsible appraiser will adjust his appraisal on the basis of the condition of the property.

- A lead negotiator with experience in real estate transactions;
- An experienced real estate attorney.

The status of different properties — who owns it, where it might be in the foreclosure or tax foreclosure process, whether it is occupied or vacant — strongly affects how one may go about trying to acquire it. Table 1 shows the principal types of properties that might be acquired by public bodies or sub-recipients and the important features of each.

**TABLE 1. PROPERTY TYPES AND KEY FEATURES**

	<b>Properties in foreclosure process</b>	<b>REO properties</b>	<b>Other vacant or abandoned properties</b>
<b>What is being acquired?</b>	Mortgage giving buyer right to gain title through foreclosure	Title	Title
<b>Occupancy status of property</b>	May be occupied or vacant	Usually vacant	Vacant
<b>With whom does one negotiate?</b>	Lender or servicer	Realtor for individual properties, lender, or servicer for bulk purchases.	Usually owner, sometimes Realtor
<b>Other issues</b>	Local properties may be part of a larger pool, making selective acquisition difficult	Realtor may need approval of lender to sell below listing price.	Owner may have liens and judgments that may exceed value of property

*Acquiring mortgages.* From the standpoint of both neighborhood stabilization and protecting current homeowners, there are often compelling reasons to acquire mortgages rather than properties. In many states, the foreclosure process is a lengthy one, and properties may become vacant and deteriorate well before foreclosure has been finalized and title passed to the lender. The earlier a state or municipality can gain control of the property, the better the chances of preventing further deterioration and loss of value. Furthermore, where the owner is still on the premises, it may be possible to restructure the mortgage to allow her to retain ownership or, if not, to stay as a tenant. Since NSP funds cannot be used to acquire mortgages — as distinct from title to properties — cities or counties need to look for other funding sources to complement NSP funds.

Acquiring mortgages, however, is often difficult, particularly with respect to paper that has been securitized and is now held in investment pools in which mortgages from all over the country are combined. It may be difficult to find individuals with whom to negotiate; even then, it is unlikely that they will have an interest in selling properties except in bulk. Both mortgage and REO property purchases may be more feasible at the state or regional level, through a state or regional land bank entity that can then pass the mortgages or foreclose and convey title to local entities.

*Using multiple acquisition tools.* A public agency or CDC can acquire properties from private owners in many different ways. While HERA clearly contemplates that NSP funds will be used to acquire properties through negotiated arm’s length transactions with their owners, other strategies — which may or may not involve use of NSP funds — can complement negotiated arm’s length acquisitions.<sup>11</sup> These tools include:

- *Tax foreclosure.*

When property owners fail to pay their property taxes, a lien is created on the property. If the taxes remain unpaid, the property can be foreclosed either by the city or county or by a third party who has acquired the lien. While tax foreclosure laws vary widely from state to state, in most states some procedure exists by which a city or county can gain title to properties this way. This is a particularly valuable way of acquiring properties, particularly in weak market areas, since the only costs involved are the transaction costs associated with conducting the foreclosure. Stabilization strategies can be vastly enhanced by an aggressive effort to gain control of problem properties through tax foreclosure to ensure that they are put back into productive use. In the long run, cities gain far more fiscally as well as socially from such a strategy than by selling liens to investors for short-term fiscal gain.

- *Gift.*

Where market conditions are weak and some owners are contemplating walking away from their properties, cities as well as nonprofit organizations can often obtain properties by gift. Gifting to a public or nonprofit entity allows the owner to take a deduction on his income tax, while, under most state laws, the city can forgive the property tax arrears when it takes title. Gift property programs, carefully managed, can help complement other more large-scale acquisition strategies.<sup>12</sup>

- *Eminent domain.*

Using eminent domain to acquire property to be reconveyed to a private party is highly controversial. Section 203 of HERA prohibits recipients from using eminent domain to fund any project using NSP funds.<sup>13</sup> It is important, however, to distinguish between using eminent domain to take occupied properties for profitable redevelopment and using it to take vacant properties that are doing harm to their neighbors and where the absentee owner has rejected reasonable offers for the property. This use of eminent domain, often known as “spot blight” eminent domain, is permitted under the laws of a number of states, including Iowa, New Jersey, and Ohio, as well as the District of Columbia. Spot blight eminent domain is a limited tool, most likely to be used as a last resort in situations involving a single property or at most a handful of strategic properties. Since NSP funds cannot be used to acquire properties through eminent domain, a city or county will need another source of funds to draw upon for this purpose.

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<sup>11</sup> Tax foreclosure is discussed in detail in Chapter Seven of Alan Mallach, *Bringing Buildings Back: From Abandoned Properties to Community Assets*, National Housing Institute and Rutgers University Press, 2006, pp. 75-85. Other acquisition strategies are discussed in Chapter Eight, pp. 86-102.

<sup>12</sup> In contrast to tax foreclosure, which wipes out other liens on a property, liens remain in place if a municipality takes a property by gift. As a result, before taking any gift property, the city must determine either that the property has no other liens on it or that the liens are modest enough that the city is comfortable assuming them.

<sup>13</sup> The act reads “No State or unit of general local government may use any amounts received pursuant to section 2301 to fund any project that seeks to use the power of eminent domain.” This could be construed to bar use of eminent domain with respect to projects using NSP funds, even if the funds used to acquire a particular property might be from a different source. The HUD regulations fail to clarify this question.

- *Vacant property receivership.*

Receivership is a tool used to take control of, but not necessarily title to, a building where the owner has allowed it to fall into disrepair and abandonment and where the city wants to see it restored to productive use. If the owner fails to rehabilitate the property after having been ordered to do so by the city or a court, the city can ask the court to be appointed receiver of the property, in order to restore the property to use. While acquisition is not the goal of receivership, it is often a by-product. In either case, the outcome of a successful receivership action is that the building is in fact restored to use, either by the owner, by the city, or by a CDC. Thus, its value can lie as much in its ability to motivate owners to restore their properties as in its use as a tool to gain title to the properties. As such, it is most valuable in what might be called intermediate market environments, where properties have enough value that owners will not lightly allow them to be lost but not enough necessarily to motivate owners to put them to use without the added pressure of the receivership action.

## REUSE, REHABILITATION, AND DEMOLITION

*Principle 5. Develop ground rules to determine when to demolish and when to rehabilitate foreclosed or abandoned properties.*

While a few of the vacant houses that a city, county, or sub-recipient is likely to acquire may need only cosmetic work, many will have undergone serious damage while they have stood vacant. These houses will need substantial time and money to be restored to sound, habitable condition. As a result, cities will find themselves regularly confronting a key question: demolish the house and create a vacant lot, or rehabilitate it for a new owner or tenant?

We have already touched on the threshold issue: will there be a market for the house after rehabilitation? What is considered a reasonable market may vary from area to area. At best, it means that the house, after rehab, will find a buyer willing to pay a price that covers the cost of both acquisition and rehabilitation. In other cases, even if the resale price is less than the cost, and some subsidy is needed, rehabilitation may be justified, because there is a demand for affordable housing that is not met by the housing available in the private market, or because filling the house with a new owner will help stabilize the neighborhood.

In other cases, rehabilitation may not be justified. This could be true if the subsidy cost to bring the price down to where the house can find a buyer exceeds the cost of providing affordable housing through other means or where the supply of houses for sale in the area already exceeds the demand. In the latter case, the house may not find a buyer at any price or may find a buyer only at the cost of dooming another house in the area to abandonment. This is true of many neighborhoods in older cities with weak housing markets. The cost of rehab is also relevant. Depending on a house's size, features, and condition, rehab may cost less than \$10,000 or more than \$150,000. While cost should not in itself drive the decision, it must be given considerable weight.

The decision should also weigh planning and community impact considerations, summarized in Table 2.<sup>14</sup> These factors can be integrated into a "decision tree" that can be used by local officials or CDCs to make decisions about individual properties. It may make sense to preserve a building that might otherwise be demolished if its

loss will create a gaping hole in an otherwise intact block. Conversely, it might be necessary to demolish a building that might otherwise be preserved if it has become a nuisance and threatens to further destabilize its surroundings. In some cases, it may make sense to stabilize and “mothball” a building that may not have an immediate reuse but which has architectural or historic value. In making these decisions, different perspectives should be at the table, including code enforcement, planning, community development, and historic preservation staff within city government, as well as individuals from the neighborhoods where the properties are located.

**TABLE 2. PLANNING/COMMUNITY IMPACT CRITERIA FOR EVALUATING WHETHER TO DEMOLISH OR PRESERVE ABANDONED BUILDINGS**

	DEMOLISH	PRESERVE
<b>Quality of building</b>	The building is obsolete, by virtue of small size or physical character.	The building is attractive, of high quality, or of architectural or historic value.
<b>Neighborhood fabric</b>	The building is located in an area where the neighborhood fabric has largely been lost through incompatible land uses and demolitions.	The building is located in an area where the neighborhood fabric is still strong, and its physical presence contributes to that fabric.
<b>Reuse potential of lot created through demolition</b>	Demolition will contribute to the opportunity to carry out a comprehensive rebuilding or revitalization strategy of the area.	The demolition of the building will result in a potentially unusable vacant lot, rather than an opportunity for redevelopment or revitalization.
<b>Nuisance level of property in present condition</b>	The nuisance impact of the building and the harm that it is doing in its present condition, in the absence of immediate reuse potential, outweigh the benefits of saving it for possible future reuse.	The reuse potential of the building, even if not immediate, outweighs the current harm that it does in its present condition, particularly if enhanced efforts are made to secure or stabilize the property.

**Principle 6. Design financing strategies for property reuse to reflect program and policy goals.**

Part of many cities’ NSP spending is likely to include some form of financing assistance to end buyers of properties, whether they will be owner-occupants or entities who will maintain the houses as affordable rental properties. HERA specifies that one use of the funds is to “establish financing mechanisms for purchase and redevelopment of foreclosed upon homes and residential properties,” including “soft-second, loan loss reserves and shared-equity loans” (Sec.2301(c)(3)(A)). As long as the end-user falls within the income limits of the act, as mentioned earlier, cities are given much flexibility as to how NSP funds are put into any particular transaction.

NSP money can be used in many different ways. Many cities and CDCs, particularly those in the NeighborWorks America network, are familiar with many of the specific financing mechanisms that are used, such as soft second mortgages to fill affordability gaps<sup>15</sup> or seed money loans to cover predevelopment costs. Some ba-

<sup>14</sup> Table 2 comes from Mallach, *Bringing Buildings Back*. A detailed discussion of demolition strategies, including model decision trees applying the criteria in the table, can be found on pp. 175-82.

<sup>15</sup> Soft second mortgages can play an important role in bringing down the effective carrying cost of a home so that a household with a lower income can afford it. At the same time, the use of soft seconds to relieve prospective buyers of all down-payment and closing cost obligations is both risky and questionable public policy. Buyers who do not have a personal financial investment in their property are significantly more likely to subsequently go into foreclosure. Many would-be buyers who lack the ability to make a meaningful financial contribution to the purchase of their home may more appropriately remain renters while building up financial resources through individual development accounts, lease-purchase programs, or other means.

sic guidelines that should be followed in designing how funds should be used are as follows:

- *Leverage NSP funds as much as possible, using them to complement less flexible affordable housing or other funds.*

Many jurisdictions have access to other funds, including HOME, CDBG, and state or local housing trust funds, that can be used to build or rehabilitate affordable housing. Similarly, a variety of mortgage programs, including programs from local lenders under CRA agreements and programs from state housing finance agencies, may be available to finance purchase of new or rehabilitated housing. These programs may be subject to limitations that can be overcome by using NSP funds selectively.

Many such programs are subject to income ceilings lower than the 120 percent of AMI permitted for NSP funds, often set at 80 percent or less of AMI. Using NSP funds, for example, to fund acquisition and rehabilitation of housing to be sold to households earning between 80 and 120 percent of AMI, and then recapturing all or most of those funds from the buyer's purchase mortgage may be an effective approach. If there is a need for a continuing subsidy, the NSP funds can be left in as a soft second mortgage, to be recaptured on resale or used to maintain long-term affordability controls. NSP funds could also potentially leverage additional resources by being used for loan guarantees or loan loss reserves, to help people get mortgage financing, including people who may have lost their homes in the past to foreclosure but represent reasonable credit risks for less burdensome mortgages.

- *Make NSP revolve.*

Using NSP funds for short-term activities that address the immediate need for funds, and which can then be recovered from long-term public or private financing, allows the funds to have an impact beyond the initial 18 months during which the funds must be used. The act explicitly authorizes states and local governments to reuse recaptured funds for up to five years, with language suggesting the possibility of extensions beyond that time. Where funds are being used for acquisition, for example, it is important to have an end game in mind where possible, that is, to have at least a preliminary idea of what the reuse will be and where the funds for that reuse are likely to come from. *In areas with relatively healthy housing markets, acquisition programs should be designed so that all or nearly all of the money used revolves back to the city or sub-recipient for reuse.*

Other uses of NSP funds might include pre-development loans to CDCs rehabbing vacant properties or building new housing on vacant lots created through demolition. The funds would be repaid to the city when the CDC receives approvals and obtains a construction loan from a private lender. Where NSP funds are used to demolish vacant buildings, the city should place a lien on the property and/or, where permitted by statute, file a judgment against the owner to recover the funds expended.

- *Build in effective long-term affordability controls.*

HERA specifically provides that "...to the maximum extent practicable and for the longest feasible term, that the sale, rental or redevelopment of abandoned and foreclosed upon homes and residential properties under this section [shall] remain affordable to individuals or families described in subparagraph (A)" (Sec. 2301(f)(3)(B)).<sup>16</sup> As noted earlier, this means that *all* properties must remain affordable to households earning 120

percent of AMI or less, and that certain properties — those for which the set-aside funds have been used — remain affordable to households at 50 percent of AMI or less.

There are many different vehicles through which affordability can be preserved on a long-term basis, including contractual agreements, deed restrictions or covenants, or land leases such as those used by community land trusts (CLTs). During the past decades, with the growth in CLTs, and even more through the increased use of inclusionary zoning to create affordable housing in states such as New Jersey, California, and Massachusetts, a solid body of tools has been created that can be used by cities and sub-recipients to ensure that affordable housing, once created, can stay affordable for an extended period, even permanently.

Many states and cities, however, have had little experience with long-term affordability controls. Many local programs that use CDBG or other funds impose controls for at most five or 10 years and often provide for recapture of subsidy funds rather than keeping the actual house or apartment affordable, as required by the act. Such communities must first educate themselves about the legal and operational mechanisms available to administer and enforce affordability controls,<sup>17</sup> and then they must set up a public or private nonprofit entity that will take responsibility for administering the controls.

*Long-term affordability controls, particularly with respect to owner-occupied housing, are not self-administering.* Someone must be in place to set resale prices and monitor transactions, qualify new buyers and tenants, and develop waiting lists of pre-qualified buyers to fill properties as they become available.<sup>18</sup> Given the need for longevity and the benefits of operating at scale, these functions can best be housed in a citywide or even regional body, rather than handled by individual small CDCs or local governments. Where a strong, large-scale CLT or CDC already exists, of course, it is reasonable to have that entity administer the controls rather than create a new entity from scratch.

## HOLDING AND DISPOSING OF PROPERTIES

### ***Principle 7. Build the capacity to hold and maintain properties until reuse.***

Property acquisition programs, particularly in struggling housing markets, all require that properties be held for some length of time. How long that may be will depend on market conditions, the condition of the properties, funding availability, and reuse plans. It can be as little as a few weeks or as long as many years. Even where the city wants to reuse the properties as quickly as possible, *some* holding period will usually be inevitable. Where

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<sup>16</sup> While the regulations permit this requirement to be satisfied by compliance with HOME program standards for affordability controls, they encourage states and cities to adopt controls for longer periods than those required by HOME.

<sup>17</sup> An excellent guide to the full range of issues associated with long-term affordability-controlled housing, with particular focus on homeownership options, is John Davis, *Shared-Equity Homeownership: The Changing Landscape of Resale-Restricted, Owner-Occupied Housing*, National Housing Institute, and available at [http://www.nhi.org/research/522/shared\\_equity\\_homeownership/](http://www.nhi.org/research/522/shared_equity_homeownership/).

<sup>18</sup> A good introduction to these issues is Rick Jacobus, *Delivering on the Promise of Inclusionary Housing: Best Practices in Administration and Monitoring*, PolicyLink, 2007, and available at [http://policylink.org/documents/IZadminarticle\\_color\\_web.pdf](http://policylink.org/documents/IZadminarticle_color_web.pdf). While specifically focusing on inclusionary housing, this material applies to managing any program that involves maintaining long-term affordability controls on housing.



a city or county expects to hold large numbers of properties or hold them for extended periods, an entity dedicated, in whole or part, to acquiring, holding, and disposing of properties is likely to be needed. Such entities, known as land banks, can be created within a line agency of local government, can be private nonprofit entities, or, as in the case of the Genesee County Land Bank, can be a public authority created under state enabling legislation.<sup>19</sup>

One of the most challenging tasks facing any land bank is maintaining its inventory of properties. Vacant properties are inherently risky for the neighborhoods in which they are located. Unless the entity responsible can maintain properties well while holding them for future reuse, these properties may do great harm to their neighbors. If that happens, it will also inevitably impair the credibility and legitimacy of the program and the public agency or nonprofit organization responsible. While no maintenance program can completely prevent negative impacts, a well-run, effective program will significantly reduce the potential harm that might otherwise take place. Although the basic guidelines involved are similar, vacant structures and vacant lots on which structures have been demolished raise different maintenance issues.

- *Build maintenance capacity.*

Properties need to be maintained. Lots have to be cleaned and houses cleaned and secured. This requires money, and it requires people to do the work. They can include employees of a public agency, a nonprofit organization, a contractor, or, in some cases, volunteers from community organizations or service clubs or involuntary helpers, such as inmates in minimum-security prisons. Land banks should develop business plans, based on the anticipated number and type of properties likely to be held in its inventory and the maintenance requirements of that inventory. This should be done as early as possible in the process, so that the entity has the capacity in place as its inventory begins to grow.

Finding resources for property maintenance is not easy, but it is critical. Some NSP funds can be used for this purpose. Other resources can be leveraged through partnerships. City or county public works crews may be able to add some vacant lot maintenance to their workloads, while community organizations and businesses may be willing to help with properties in their neighborhoods. Flint, Michigan's Genesee County Land Bank runs a number of programs to get neighbors involved, including an Adopt-A-Lot program and a Clean and Green program.<sup>20</sup> For activities requiring more specialized skills or equipment, such as boarding and securing properties, cities can contract with companies, including national companies such as Safeguard, to provide that service, unless or until the size of the city's inventory justifies building that capacity in-house.

Scale offers significant advantages in vacant property maintenance. A single full-time crew can maintain a large number of lots or buildings, and a centralized computer-based scheduling system can help organize their

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<sup>19</sup> For an overview of land banking and specific land bank entities, see Mallach, *Bringing Buildings Back*, Chapter 11, pp. 128 -42. For a more detailed discussion and analysis of the legal and administrative issues involved with land banks, see Frank Alexander, *Land Bank Authorities: A Guide for the Creation and Operation of Local Land Banks*, Local Initiatives Support Corporation, 2005, and available online at <http://www.lisc.org/content/publications/detail/793>.

<sup>20</sup> The Genesee County Land Bank is an outstanding example of an effective land banking program. For more information, see <http://www.thelandbank.org/programs.asp#one>.

work efficiently. Similarly, a two-person boarding crew made up of a trained carpenter and an assistant can secure large numbers of properties; if the number is large enough to keep the crew busy, it is likely to be more cost-effective than paying an outside contractor on a per building basis. A city or county with a large vacant property inventory should either create a central maintenance entity, either public or private, or a central management system to coordinate maintenance resources. Solid maintenance capacity, coupled with good procedures to address recurrent issues with vacant properties, can mitigate many of the risks associated with managing a vacant building inventory and minimize the city's liability exposure.

- *Develop standardized property maintenance protocols.*

As important as having adequate resources is having efficient systems for using those resources. These systems can take many different forms. They include what are known as protocols, which are standardized procedures that are regularly followed in particular situations. For example, a city could have one protocol that establishes how buildings are secured, and another for maintaining sidewalks in front of city-owned properties, and so forth. Similarly, a vacant lot cleaning system, using computerized workforce management systems to promote the most efficient use of resources, should be established to ensure that all lots are cleaned regularly, as well as ensure that personnel are available to deal with urgent matters, such as illegal dumping.<sup>21</sup>

- *Encourage interim treatments and uses of vacant properties.*

Land banks that expect to hold vacant properties for extended periods should encourage interim treatments and uses of those properties, particularly vacant lots. Organizations around the United States have created green spaces and community gardens, and in some cases even more substantial agricultural operations, on urban vacant lots. While some of these are designed to be permanent uses of the lots, many are designed to serve as interim uses until a permanent reuse is feasible. The Pennsylvania Horticultural Society and the city of Philadelphia have developed a series of inexpensive vacant lot treatments, involving simple plantings and fencing, that discourage illegal dumping and make the lots a more attractive part of the neighborhood.<sup>22</sup>

**Principle 8.     *Establish sound ground rules for disposing of properties.***

The final goal for any acquisition and reuse strategy is to dispose of properties to end-users. A city or county may sell properties directly to end-users, such as home buyers, but is more likely to sell them to entities such as CDCs or for-profit developers who will subsequently build or rehabilitate them as housing for end-users. Cities, therefore, need to have clear policies for both the sale of properties by the city to redevelopment entities and for sale of rehabilitated or newly constructed homes by those entities to home buyers.

Market considerations play a major role in a sound disposition process. In some cases, it may be desirable to sell

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<sup>21</sup> See Mallach, *Bringing Buildings Back*, pp. 166-75, for further information on vacant property maintenance, including ways to deal with illegal dumping on vacant lots.

<sup>22</sup> For further information, see *Reclaiming Vacant Lots: A Philadelphia Green Guide*, Pennsylvania Horticultural Society, 2002. Additional information about PHS's greening programs can be found at <http://www.pennsylvaniahorticulturalsociety.org/phlgreen/index.html>. *Reclaiming Vacant Lots* can be downloaded from the PHS website.

off properties as quickly as possible, to create homeownership or rental opportunities, and even jump-start a depressed neighborhood market. In others, it may be preferable to hold onto properties, either because no market exists or because the only market that exists is for uses that may not be in the area's long-term interest, such as subsidized housing in a neighborhood where private market housing is over-supplied at prices or rents comparable to or lower than the subsidized housing would be. In such cases, making properties available for subsidized housing can further destabilize the area's private housing market, and the properties should be banked for future use. The NSP regulations permit land banks to hold properties for up to 10 years before reuse.

*Pricing.* The first issue that must be addressed, therefore, is when to dispose of properties acquired by the city or county. The second issue is *how much* they should be sold for. HERA sets an upper bound on price by requiring, with respect to sales to individuals for use as their primary residence, that the sale "shall be in an amount equal to or less than the cost to acquire and redevelop or rehabilitate such home or property up to a decent, safe and habitable condition" (Sec. 2301(d)(3)). Thus, if the cost is less than full market value, the home must be sold below market value, which is consistent with the income targeting of the act. Pricing, however, is not that simple. The city should take three factors into account:

- *Market conditions in the area or neighborhood, and the extent to which the city is seeking to stabilize or strengthen the market in that area.*

In an area where the city is actively trying to build a stronger housing market, it may want to sell the house for the highest price consistent with the statutory pricing and income targeting requirements. In an area where housing is already expensive, it may want to sell houses for a substantially below-market price, in order to create or preserve housing opportunities for low- or moderate-income households in the area. In either case, the pricing of properties should reflect both an understanding of market *conditions* and a sound market-related *strategy*.

- *Housing needs and priorities.*

The city may have adopted or may want to adopt priorities for assistance, particularly with respect to homeownership, based on local housing needs and the availability of housing at different income levels in the city and region. While in high-cost areas such as the San Francisco Bay area a household earning 120 percent of AMI will have a hard time finding affordable housing, in Indianapolis or Cincinnati such a household has a wide variety of houses and neighborhoods at its disposal. Similarly, some cities may have particular policy reasons to prioritize one demographic or economic segment of the population, such as a particular household type or income range.

- *The extent to which the city is looking to recover NSP funds for future reuse.*

Finally, the price will be influenced by the city's desire and ability to recover and recycle NSP or other funds used to acquire or rehabilitate the property. If a city or CDC has access to other subsidy funds for housing rehabilitation or for home purchases by income-eligible households, it may want to use these funds in order to recover as much of the more flexible NSP money as possible. In areas where other housing subsidy funds are in short supply, it may be necessary to allow the NSP money to remain in the project as a soft second mortgage or similar instrument, which may or may not be recycled in the future.

While HERA does not impose limitations on the price at which a city may sell vacant houses or vacant lots acquired with NSP funds to a developer or CDC for rehabilitation or redevelopment, prices should be realistic both in terms of market conditions and the availability of other subsidy sources. Too high a purchase price for the property will put undue pressure on the CDC either to raise more subsidy money from other sources or to price the unit for sale to an end-user more aggressively than may be appropriate.

*Capacity.* As a general rule, public bodies are not likely to engage directly in rehabbing or building houses. This is a task for which most local governments are not well-suited, and most recognize that fact. As a result, where the city or county acquires properties, it will usually sell them to a private entity such as a CDC or a for-profit developer for rehabilitation or redevelopment. The city must weigh the capacity of potential redevelopment entities to ensure that the number of properties they take on is realistic in light of their development capacity and financial resources. A city trying to unload as many properties as possible can kill a small developer or CDC with kindness, by pressing them to accept more properties than they can realistically handle.

In evaluating potential redevelopment entities, the city or county should look at some key features of those entities:

- *Track record.* While a new organization can assemble financial and technical resources, there is no substitute for experience.
- *Capacity of staff and consultants.* Although an organization can hire consultants to carry out many technical tasks, a competent full-time staff dedicated to the organization and its mission is needed to direct consultant efforts. Consultants' qualifications and experience should also be carefully assessed.
- *Working capital.* An entity that takes on the rehabilitation or redevelopment of scattered-site properties must be able to deal with many uncertainties during the development process. If it lacks adequate working capital to carry it through an uncertain development timetable, it will either fail or will come back to the city for additional funds that may not be available.
- *Construction capacity.* The entity should either have in-house construction capacity or a relationship with a competent, experienced contractor.
- *Marketing capacity.* The entity should have the ability to effectively market the finished houses. While one may be able to rely on local Realtors in a strong market, the same is not always true where the market is weak or where the city and a CDC may be trying to use the sale of new or rehabilitated houses as a way of moving the market. In those conditions, the redevelopment entity must be able to show that it can actively move properties in the areas where it is rehabilitating or building housing.

*Terms.* The terms of sale that a city uses to sell property to development entities must carefully balance protecting the city's interest with the need to avoid imposing unrealistic burdens on redevelopers. Selling properties with unrealistically short timetables or with unreasonable conditions can impede the ability of the redeveloper to carry out the project. Moreover, to the extent that the city requires specific performance or sets benchmarks for results from redevelopers, the city must be prepared to monitor and enforce those provisions. If the city fails to do so in a timely fashion, it may be legally barred from doing so at some later date.

*Procedures.* One basic rule should govern all property sales by government entities: they should be *fair, consistent, and transparent*. Secretive land deals to favored parties on unduly generous terms are a common transgres-

sion of local governments. Even when such actions are not illegal, the perception that properties have been steered by a mayor or council member to a favored developer or that certain developers get terms not offered to others can undermine the credibility of a city's revitalization efforts.

This does not mean that all sales must be on the same terms or at the same price. "One size fits all" procedures may appear to be a simple way to achieve consistency, but they do not take into account very real differences between redevelopment entities, market conditions, and policy goals. A city may want to adopt different rules for for-profit and for nonprofit entities and should adjust its prices both to reflect market variation as well as variation in its target end-users. Similarly, while there are good reasons in most cases for sales to be competitive, even that should be carefully evaluated. Where the goal is to put well-built or rehabilitated houses back in the hands of qualified end-users, an auction that disposes of city-owned properties on the basis of the highest bidder is most likely not the best approach. An auction may lead to seriously undesirable outcomes, as speculators and flippers are often able to outbid conscientious redevelopers. Most cities have alternative routes, such as selling properties on the basis of requests for proposals, in which they can consider factors other than price, or on a negotiated basis to pre-qualified buyers. In all cases, however, it is important that the ground rules be clear and in writing and readily available both on the web and in print to all interested parties.<sup>23</sup>

## ORGANIZING FOR SUCCESS

***Principle 9. Integrate acquisition and rehabilitation strategies with other neighborhood stabilization strategies.***

Acquiring and reusing abandoned properties is at most only one part of a strategy that will restore stability to neighborhoods destabilized by foreclosures and abandonment. Acquiring and rehabilitating properties is often the most expensive strategy and should be seen as a last resort, to be used only where the market will clearly not work unaided and where less expensive public-sector strategies are not available or not useful. Within a neighborhood at risk of destabilization, the impact of vacant and abandoned properties interacts with other factors. Potentially destructive chain reactions, in which vacancies trigger other vacancies and lead property owners to give up on their properties, can often be forestalled by programs that help those owners maintain their properties, while other efforts, such as neighborhood clean-ups or community policing, can help build neighborhood confidence. All of these neighborhood stabilization strategies should be carried out in a coordinated fashion in tandem with the acquisition, demolition, and rehab strategies being pursued with NSP funds.

- *Use proactive regulatory strategies to minimize neighborhood destabilization.*

Property ownership carries with it responsibilities as well as rights. Property owners must maintain their property to state or local codes and not allow their property to become a nuisance to its neighbors. If they do not, local officials have the power to enforce the codes and to abate nuisances by entering properties to make necessary repairs or to demolish the property. Code enforcement and nuisance abatement are an important part of any neighborhood stabilization strategy.

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<sup>23</sup> For a more extended discussion of disposition terms and procedures, see Mallach, *Bringing Buildings Back*, Chapter Nine, pp. 103-16.

Areas with many foreclosures raise complicated enforcement issues. Homeowners often abandon their homes before foreclosure takes place. The foreclosure may not happen for months or years and, in some cases, never.<sup>24</sup> If a sheriff's sale does take place, the creditor — now the owner — may or may not take responsibility for the property. If the property falls into limbo, it may be many years before it is recaptured, usually through tax foreclosure. By that time, it is likely to have been stripped or vandalized and done untold damage to its neighbors.

The city of Chula Vista, California, has established an abandoned residential property program under which mortgage lenders must regularly inspect defaulted properties, prior to their taking title, and take responsibility if the property becomes vacant.<sup>25</sup> Similar ordinances have been enacted in other California cities, as well as elsewhere, including Coral Springs, Florida.<sup>26</sup> In many states, however, state statutes may bar cities from enacting such an ordinance.

Where the municipality cannot compel the owner or other party in interest to take responsibility for the property, it can use its nuisance abatement power to take action, which can range from modest measures such as lawn mowing or removal of yard debris to stabilization, or, in extreme cases, demolition of the property.<sup>27</sup> In many states municipalities can also use receivership to restore a property to active use. In most states, cities can recover their costs by placing a lien on the property and, in some, can collect those costs through a judgment on other assets of the property owner.<sup>28</sup> Cities and counties should explore creating revolving funds for nuisance abatement and vacant property receivership, possibly using some of their NSP funds for this purpose. Where the city or county mounts a determined collection effort to recapture funds through liens and judgments, a large part of this money will be recaptured, particularly in areas where foreclosed properties still retain value.

The more value the area's vacant properties have, the more likely regulatory action is to be effective, since their owners or other parties in interest are likely to be motivated to maintain them, in order to preserve their asset. Chula Vista has found that almost all lenders can be motivated to take responsibility for properties even before they take title. The city uses its own resources sparingly, and when it does, it can generally recover its costs.

Code enforcement and nuisance abatement in weak market areas are much more difficult because owners may

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<sup>24</sup> In areas with weak housing markets it is not uncommon for lenders to notify homeowners that they are in default but not to proceed with actual foreclosure actions. Or if they initiate the action, they never finalize it through a sheriff's sale.

<sup>25</sup> The lender must exercise the abandonment clause in the mortgage, register the property with the city, and immediately begin to secure and maintain the property to the neighborhood standard. It must also hire a local company to inspect the property weekly and handle maintenance and security of the property. The company must have a 24-hour contact number, which must be posted on the property. The program, which is similar to that in other California cities, was established pursuant to Ordinance No. 3080, adopted August 7, 2007. See [www.chulavistaca.gov/City\\_Services/Development\\_Services/Planning\\_Building/Default.asp](http://www.chulavistaca.gov/City_Services/Development_Services/Planning_Building/Default.asp).

<sup>26</sup> Ordinance No. 2008-109, adopted June 3, 2008.

<sup>27</sup> For a more detailed discussion of using nuisance abatement to address vacant property issues, see Mallach, *Bringing Buildings Back*, pp. 150-57.

<sup>28</sup> The strongest such state statute is that of New Jersey, which provides that the municipality shall have recourse to collect for the costs of nuisance abatement or receivership against "any asset of the owner of the property if an individual, any asset of any partner if a partnership, and against any asset of any owner of a 10% interest or greater if the owner is any other business organization or entity recognized pursuant to law" (N.J. Statutes Annotated 55:19-100).

walk away from properties rather than comply with orders to repair or demolish their properties. While these are still important tools in the municipal arsenal, cities must be realistic about their limitations. In such areas, though, the importance of obtaining legal authority to hold lenders liable for property maintenance or to place judgments on other assets of the property owner to recover the costs of nuisance abatement become critically important, since they represent ways in which to gain access to resources that go beyond the market value of the properties.

While vacant properties tend to be the most problematic ones, code enforcement and nuisance abatement should not neglect occupied properties showing signs of disinvestment. In high foreclosure areas, this is likely to include many one- to four-family rental properties bought by absentee owners for speculative purposes. These properties are not only at particularly high risk of abandonment, but they often represent an important resource of affordable rental housing in the community.

- *Keep people in their homes: stabilize and improve occupied properties.*

Neighborhoods with large numbers of foreclosed or abandoned properties are also likely to have many occupied properties at risk of foreclosure or abandonment. In addition to rental properties often owned by short-term speculators, a particular source of problems in Sunbelt states such as Florida and Arizona, they are likely to include many owner-occupied properties where the owners are facing potential foreclosure or where they may lack the resources to properly maintain their homes. With the housing market still heading downhill in most parts of the United States and large numbers of existing owners still at risk, a strategy that focuses exclusively on houses that are already vacant may end up restoring some properties but failing at the larger goal of stabilizing the neighborhood.

Many communities and regions have created assistance programs for homeowners facing potential foreclosure, including counseling, intervention with lenders to restructure problematic loans, and, in some cases, financial assistance to tide owners over financial difficulties caused by temporary problems such as layoffs or health problems. Nationally, the Hope Now Alliance offers a clearinghouse for information and assistance. In addition to funds for acquisition, rehabilitation, and demolition, HERA appropriated an additional \$180 million to support foreclosure counseling services.

States and local governments developing plans for their NSP allocations should make sure both that adequate foreclosure-prevention resources are available for homeowners in the neighborhoods being targeted for use of NSP funds and that an outreach program is set up to make owners aware of those resources. Other program resources, such as home improvement assistance for financially strapped owners and assistance to help renters stay in foreclosed properties, should be included in a comprehensive neighborhood stabilization package. Responsible renters are often the innocent victims of foreclosure, with few protections under many state laws.<sup>29</sup>

- *Address other factors destabilizing the neighborhood.*

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<sup>29</sup> New Jersey law does not recognize foreclosure as grounds for eviction of tenants. Unfortunately, while few states offer comparable tenant protection, some require advance notification, and California requires that lenders give tenants 60 days after foreclosure to vacate. Many states, however, still permit summary eviction of tenants after foreclosure.

Finally, vacant properties can be as much a symptom as a cause of neighborhood destabilization and decline. As a city figures out how and where to target NSP funds, it should identify what other factors are interwoven with the foreclosure and abandonment problems of the neighborhood and which of them it might be able to address as part of a larger stabilization or revitalization strategy. Existing neighborhood stabilization or revitalization plans that have been prepared by local CDCs can often be a good framework for the larger strategy.

To the extent that foreclosures and vacancies are linked to other dimensions of market failures, strategies to overcome those problems may be appropriate, such as efforts to market the neighborhood to prospective home buyers or offering incentives to motivate would-be owners to buy and rehabilitate vacant properties, by filling the gap between the cost of rehab and acquisition and the market value of the property. Cities may want to consider using NSP funds for this purpose, for buyers earning less than 120 percent of AMI.<sup>30</sup> Elsewhere, other strategies may be more appropriate, from community policing to improving recreation facilities or enhancing the neighborhood's "curb appeal" by sprucing up vacant lots, front yards, and streetscapes.<sup>31</sup>

**Principle 10. Create a coordinated, effective local government management structure for neighborhood stabilization.**

Many cities' ability to carry out an effective neighborhood stabilization strategy may be hindered by how they are organized to carry out the different functions involved.<sup>32</sup> Rehabilitation may fall under community development, but demolition is controlled by the department of buildings. Maintaining the property inventory may fall under public works, while property sales may be the purview of the city clerk. Some cities are further hindered by balkanized systems that give city council members the power to make decisions about property acquisition and sales in their districts. Before the city begins to assemble the outside partners it needs for its neighborhood stabilization effort, it should first get its house in order. Three basic steps are likely to be involved in this process.

- Fully understand the current system.

The first step is for the city to assess the different functions likely to be involved in the neighborhood stabilization strategy and how they are currently organized within city government, including:

- Neighborhood planning
- Tax foreclosure

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<sup>30</sup> See Mallach, *Bringing Buildings Back*, Chapter 16, pp. 217-32, for a discussion of home buyer incentives. Where other incentives are already available, such as historic rehabilitation tax credits, they can be leveraged with HERA funds.

<sup>31</sup> An overview of potential strategies and how they connect to the larger goal of building a stronger housing market in a neighborhood can be found in Alan Mallach, "Managing Neighborhood Change," National Housing Institute, 2008, available from the National Housing Institute at [www.nhi.org](http://www.nhi.org).

<sup>32</sup> The discussion of cities in this section applies to some counties as well in those states where they perform the range of government functions described in this section in unincorporated areas. These include some areas with major foreclosure problems, such as Clark County, Nevada, or Riverside County, California.



- Other property acquisition
- Affordable housing and rehabilitation financing
- Demolition
- Code enforcement and nuisance abatement
- Homeownership counseling and foreclosure-prevention assistance
- Property maintenance
- Property disposition
- Outreach and engagement with neighborhood and civic organizations

The assessment should include not only where these functions are housed but also who is responsible, and what ground rules guide their actions, including both legal — state statutes and local ordinances — and practical constraints.

- *Put someone in charge.*

Somebody has to be able to provide overall direction, with enough authority to ensure that all of the departments and agencies involved work together toward common goals. The leader can be a department director or someone in a central management position, such as a deputy city manager. Someone below that level is unlikely to be able to effectively coordinate the activities of people senior in the city bureaucracy. Whoever is given the authority to direct the strategy, the city’s mayor or city manager should make it clear that the strategy is a matter of priority for the city and that her authority is real.<sup>33</sup>

- *Establish internal systems for better coordination and communication.*

Along with putting one person in charge, the city must establish systems or procedures to ensure that information is shared and that the necessary decisions are made to further the strategy. The specific systems and procedures can vary widely, depending on the structure and political culture of the city. While some cities, such as New Haven, Connecticut, have created “super-agencies” to handle neighborhood revitalization activities, putting housing, planning, code enforcement, and property management under one administrative umbrella, other cities have opted for less drastic change, including creating task forces or working groups, bringing people from the different departments and agencies together to share information and coordinate efforts.<sup>34</sup>

**Principle 11. Form partnerships with other public, private, and nonprofit entities to maximize capacity and resources.**

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<sup>33</sup> Where line responsibility or control of matters having to do with vacant properties, such as decisions about property disposition or reuse (as distinct from policy-setting), is divided not only within the city administration but between the administration and city council members (particularly with respect to individual wards or council districts), establishing the strategy can be a delicate matter but is nonetheless essential. To the extent that reorganization may demand that council members relinquish cherished prerogatives, a thoughtful, and possibly extended, process of explanation and negotiation may be needed.

<sup>34</sup> For a more extended discussion of how municipalities can organize effectively to address vacant property issues, see Mallach, *Bringing Buildings Back*, Chapter 10, pp. 117-27.

No city or county can go it alone. All cities are limited by financial constraints and shortages of qualified personnel, particularly poorer and smaller cities. Legal and procedural obstacles, such as public bidding laws, make it difficult if not impossible for municipal governments to carry out many redevelopment tasks in an efficient or cost-effective manner. Even where cities have the capacity to execute programs, they may lack critical legal powers and must work cooperatively with other cities, the county, and the state. Private partners can bring the financial and technical capacity to plan and execute neighborhood stabilization efforts, carrying out many tasks that cities are ill-suited to perform, while public partners can ensure that the tools exist to do the job.

- *Public sector partners.*

Partnerships between public agencies can take many forms, sometimes involving formal cooperative or other agreements, and sometimes simply being a matter of being on the same page. Where strong regional bodies such as councils of governments or metro planning agencies exist, they may be able to further inter-municipal or city-county agreements. Three different kinds of relationship may be required to create the most effective neighborhood stabilization effort:

*Inter-municipal cooperation.* In many metropolitan areas, particularly in the Northeast and Midwest, the problems of foreclosure and abandonment are not limited to a single local jurisdiction. In Buffalo, Cleveland, or Newark, the problems spill over from the central city to the suburban inner ring, and some inner ring suburbs have foreclosure problems as serious as those of the central city but with less financial or managerial capacity to address them.<sup>35</sup> Relationships between municipalities with shared problems, often with at-risk neighborhoods straddling municipal boundaries, can benefit all parties.

*City-county cooperation.* In many states, important responsibilities are divided between cities and counties. While cities deal with most matters involving vacant properties, counties are often responsible for foreclosing on tax liens and holding any properties taken as a result. This has created problems and, at times, open conflicts between cities and counties around the country. The city may want tax delinquent properties for redevelopment or rehabilitation, while the county may prefer to sell tax liens to investors in order to help balance the county budget, often putting the properties in a legal limbo. Developing a cooperative partnership between the city and the county with respect to tax-delinquent properties, including when to take properties and who will take responsibility for the property inventory, can be a crucial element in forging an effective neighborhood stabilization strategy.

*City-state cooperation.* The city-county issue highlights a second important one. The ground rules for tax foreclosure are set by neither the city nor the county but by the state. State enabling legislation establishes the procedures that must be followed by the county and often limits its ability to use its authority in ways that will further revitalization, rather than revenue generation. The Genesee County Land Bank Authority could not be established until Michigan tax foreclosure statutes were revised to permit, among other things, a fast-track process for foreclosing on tax-delinquent vacant properties.

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<sup>35</sup> Arguably the most daunting foreclosure problem in the Cleveland area is in the small suburb of East Cleveland, where, by mid-2008, one out of eight properties in the community had already gone through foreclosure and become REO property.

The power of the state to set the ground rules for local action goes far beyond tax foreclosure. Matters such as the extent to which creditors can be required to maintain vacant properties before the foreclosure sale, the scope of nuisance abatement actions, and the manner in which cities can recover the cost of those actions are all regulated by state statute. While some states have delegated some authority to select local governments, generally known as “home rule” cities, most local governments can act only within the parameters of state statutes. The current crisis has made clear that state legislatures need to give local governments the tools to act effectively to stabilize their neighborhoods. Cities, through ad hoc coalitions or through established state-level organizations such as municipal leagues, should work to get state government to enact the legislation and adopt the policies and procedures that will enable them to do the job.<sup>36</sup>

In addition to providing local governments with tools, states can become directly involved in neighborhood stabilization. States may be in a stronger position to negotiate with lenders or Realtors for REO portfolios and may be able to create land bank entities that can act as “wholesalers” in support of local efforts. State housing finance agencies may be able to leverage NSP funds by linking use of housing trust fund money or bonding capacity to local programs that effectively target NSP funds strategically.

- *Private-sector partners.*

Private-sector partners can bring financial resources and technical capacity to the table. Every region has a private-sector infrastructure that can potentially be engaged in working with local government to implement its strategy. Since capacity is likely to be a significant limiting factor for many local efforts, cities and counties need to do whatever they can to mobilize the capacity that exists in the community. While capable CDCs, where they exist, are critical players, local for-profit developers, contractors, Realtors, and lawyers can also play important roles.

Some private partners such as foundations, local banks, or corporations can be looked to largely for financial resources to leverage public funds. CDCs, Realtors, attorneys, appraisers, and contractors are “capacity” partners, in that they bring people with specific technical skills and capacities to carry out the tasks inherent in any strategy using NSP funds – acquiring, rehabilitating, building, and marketing residential property. A few may be both financial and capacity partners.

To get the most benefit out of private-sector partners, they must be genuine partners in the effort. They need to be brought into the process of developing the NSP action plan early, in ways that they understand that their voices are being heard and their ideas reflected in the final product. In the final analysis, the success of any community’s NSP strategy, however solid its planning, will depend on the extent to which it can leverage additional financial resources as well as the time and energy of skilled individuals to perform the complicated tasks that make up the strategy. Doing so should be a high priority for every state, city, or county engaged in using NSP funds to address its foreclosed and vacant property concerns and stabilize its neighborhoods.

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<sup>36</sup>An overview of the actions states can take to address the foreclosure crisis, including addressing its neighborhood impacts, can be found in Alan Mallach, *Tackling the Mortgage Crisis: Ten Action Steps for State Government*, The Brookings Institution, 2008.