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Purchasing Properties at Scale

Lessons on Acquiring REOs During the Foreclosure Crisis from Pioneering Projects in New Jersey, Phoenix and the Twin Cities

About Living Cities

Founded in 1991, Living Cities (www.LivingCities.org) is an innovative philanthropic collaborative of 21 of the world's largest foundations and financial institutions. Living Cities members are not simply funders. Member organizations participate at the senior management level on the board of directors, and contribute the time of 80+ expert staff toward crafting and implementing the Living Cities agenda, which focuses on improving the lives of low-income people and the urban areas in which they live. Over the past 18 years, Living Cities has invested more than $540 million in American cities, making a demonstrable difference in neighborhoods throughout the nation.

About this Case Study

The foreclosure crisis is threatening to reverse the progress made by the forces that have helped revitalize low-income neighborhoods around the country including community development organizations, funders and policymakers. In 2008, responding to this threat, Living Cities launched an initiative to catalyze, test and learn from 10 of the most promising local pilot efforts to return foreclosed properties to productive use[1]. *Purchasing Properties at Scale,* the third in a series of studies published by Living Cities, offers the community development field lessons learned from these 10 pilot programs.

[1] The pilot sites are Boston, Chicago, Cleveland, Dallas, Detroit, Los Angeles; Minneapolis/St. Paul, New York, Providence, R.I., and Washington, D.C.

Overview

The wave of foreclosures created by the subprime crisis and exacerbated by the current recession has swept through many cities like a hurricane — leading to vacancies, abandonment and economic decline. Although cities and community-based organizations have mounted an all-out response, the sheer scale of the problem has overwhelmed available resources. Many economists are predicting that foreclosures will continue at the current level for at least another year or two; their fallout will last much longer.

In many communities, growing numbers of vacant, foreclosed homes pose substantial threats to stability and quality of life for residents. These conditions create blight and drive down housing values in adjacent areas. Moreover, local governments face huge bills for maintaining vacant properties and removing hazards. In communities with only a few foreclosures and where real estate markets remain strong, buyers will often purchase distressed properties and return them to productive use. However, as the number of foreclosed and vacant properties grows, this becomes increasingly difficult, especially in cities where real estate markets have long been stagnant.

As the scale of the current foreclosure problem became apparent in 2008, many believed that the appropriate response would be a "bulk purchase:" Holders of foreclosed homes, also referred to as "real estate owned" (REO) properties, would transfer packages of these assets to cities and responsible developers. Unfortunately, several significant challenges, detailed later in this case study, have prevented bulk purchases from going forward in more than a handful of locations.

To address these challenges, four of the country's largest affordable housing intermediaries — Local Initiatives Support Corporation, Enterprise Community Partners, Housing Partnership Network and NeighborWorks America — created the National Community Stabilization Trust (NCST). NCST was established to negotiate with REO holders at a national level, in order to create local opportunities for property acquisition, renovation and disposition.

NCST's results so far are promising, according to the organizations interviewed for this report. "The scale and complexity of the REO problem far exceeds the capacity for nonprofits to handle them," says Harold Simon, President of Community Asset Preservation Corporation, a New Jersey-based nonprofit that specializes in acquiring and rehabbing foreclosed and vacant properties. "However, NCST has done a great job of negotiating these deals and created a system that is beneficial to all players."

While NCST provides one means to acquire REO properties, it is still evolving, and other strategies have emerged as well. In places with less severe concentrations of foreclosed properties, organizations are marketing homes, establishing mission-driven real estate brokerage operations[2], and matching new homebuyers or landlord-investors directly with vacant properties. Some are lining up favorable financing for prospective buyers. Finally, some sites have been successful in acquiring properties in bulk when a package of loans is owned by a single lender.

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[2] An approach to the buying and selling of real estate in which a nonprofit broker focuses on making the best match between client and home, rather than pressing clients to buy as much house as they can in hopes of getting the biggest possible commission. See "Using Mission-Driven Real Estate Brokerage in Foreclosure Mitigation: A Case Study of Los Angeles, CA and New York, NY," by Kevin McQueen, BWB Solutions LLC, January 2009.

This case study discusses these and other strategies for acquiring REO properties and examines the factors and conditions that influence cities' and nonprofits' success in REO acquisitions. Each approach presented below shares the goal of balancing publicly subsidized interventions and free-market forces. These strategies ideally will help other cities acquire properties successfully, maximizing their use of capital through sources such as the federal Neighborhood Stabilization Program[3].

Challenges to Acquiring Foreclosed Properties in Bulk

When cities and community-based organizations seek to purchase significant numbers of foreclosed properties, they encounter challenges. One seems simpler than it actually is: Getting accurate, comprehensive, and timely data about units that are in, or are about to enter, foreclosure. Such information includes the current status of an REO property, the identity and contact information for those with ownership or control of the property, and information on its physical condition. Most cities lack systems to efficiently gather and share this information. In such cities, the only source of information is costly, privately-owned databases.

Another barrier is the difficulty of unbundling mortgage-backed securities[4], the pools of mortgage-backed debt that have become the legal owners of these properties. In most cases, the securities have hired servicers to manage their assets. Working with many servicers — finding out the status of a property; negotiating a purchase — has proven difficult for many local groups. One point of contention is whether servicers can accept a bid from a group which is less than the property might fetch on the open market — even if that buyer would just let it rot or flip it.

"Servicers fear being sued by the investors in Mortgage-Backed Securities, which requires them to try to maximize the prices they can obtain at REOs property auctions," says Andriana Abariotes of Twin Cities LISC. New legislation offers legal guarantees to servicers that should alleviate this fear. Unfortunately, servicers remain reluctant to share information on securitized loans, which is having a chilling effect on the number of properties made available to cities and their nonprofit partners.

A third significant barrier is the challenge of assembling sufficient financing and capacity to address the problem at scale. In communities with fewer foreclosures, buyers may be able to move quickly and effectively to return properties to the market. In communities with high concentrations of foreclosed or vacant homes, private investors or developers will purchase only a few of the very best properties at a time, which is not likely to produce a significant stabilizing impact. Federal funding programs (such as the Neighborhood Stabilization Program) are intended to help address this issue. But even these funds are relatively modest compared to the overwhelming scale of the foreclosure problem in many cities.

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[3] Authorized under the recently enacted Housing and Economic Recovery Act of 2008, this emergency funding program will enable states, cities, and their partners, including nonprofit organizations, to acquire and rehabilitate foreclosed homes for homeownership or rental. This funding is administered by HUD and treated as Community Development Block Grant (CDBG) funds, though with differences from the normal CDBG provisions.

[4] A mortgage-backed security is an asset-backed security or debt obligation that represents a claim on the cash flows from mortgage loans, most commonly on residential property. To create these securities, mortgage loans are purchased from banks, mortgage companies, and other originators by entities like Fannie Mae and Freddie Mac, as well as investment banks and other specialized financial institutions. Mortgage-backed securities. Then, these loans are assembled into pools and sold as a single security (usually as bonds) to investors, who have a claim on the principal and payments on the loans in the pool.

Presented below are four examples of national and local responses to the challenges of acquiring foreclosed properties in bulk. First is the NCST, which is facilitating the sale of foreclosed and abandoned properties to cities and nonprofits across the country. Next, the accomplishments of a cross-sectoral partnership in Minneapolis are highlighted to illustrate a successful "property-flow" approach. The third example focuses on Phoenix, where a coalition of nonprofit organizations created a "consumer-driven" response to the city's foreclosure problem. Finally, this study highlights a local bulk purchase in New Jersey.

The National Community Stabilization Trust (NCST)

Formed in 2008, NCST is a nonprofit that facilitates the transfer of foreclosed and abandoned property from national financial institutions to localities in order to promote neighborhood stability. It was launched by four national community development organizations — Enterprise Community Partners, the Housing Partnership Network, LISC, and NeighborWorks America — which came together to explore how their local and regional affiliates could address the foreclosure crisis. NCST seeks to directly address key property acquisition challenges via the following services:

- Transfer Agent/Intermediary — facilitating the cost-effective transfer of foreclosed and abandoned properties to cities or their designated partners
- Financing — providing debt and equity financing to support local and statewide acquisition efforts
- Capacity Building — organizing and facilitating local collaborations working through the four sponsors in order to build a more effective vehicle for acquisition, renovation and disposition
- Focal Point — serving as an industry "voice" for neighborhood stabilization to the media and the general public

NCST tries to help cities and community-based organizations acquire properties, to help fight off decay in foreclosure-affected neighborhoods and to keep properties out of the hands of irresponsible or unscrupulous speculators. It also tries to move quickly, transferring properties within 90 days of a completed foreclosure. This approach minimizes the opportunities for vandalism and property stripping.

One of NCST's programs aimed at achieving these goals is its First Look program. This program was built on the Minneapolis experience (described below), in which NCST's sponsors participated closely. Through First Look, NCST ensures that cities and nonprofits have a brief exclusive access to a limited number of foreclosed properties.

Here is how the First Look program works:

1. A city or its intermediary provides NCST with a list of the zip codes in which it wants to acquire properties.
2. NCST provides those zip codes to servicers, which agree to show the city any foreclosed properties as they become available.
3. The servicer provides the buyer with the addresses, and the city or group has 10 days to inspect the property and decide whether it is interested.

4. The servicer has up to 14 days to establish a listing price through a Broker Price Opinion (BPO)[5].
5. The servicer will take its list price and apply a Net Realizable Value (NRV) discount to it and offer the resulting price to the city (see below for more on NRV).
6. The purchaser has 48 hours to take the property at that price or to counter offer if the servicer has missed a key factor.
7. If the city passes on the property, then the servicer can try to sell it on the open market.

The Net Realizable Value pricing model is a key lever in making REO deals happen. It overcomes a hurdle based on different interpretations of what constitutes a fair price for a foreclosed home. REO sellers have to demonstrate to their investors that they have sold properties for the highest possible price, while socially motivated buyers need "discounts" in order to keep homes affordable and prepare properties adequately for their buyers — priorities other buyers, such as speculative investors, often do not share. The result is often an irreconcilable impasse over pricing.

The NRV formula helps to reconcile these differences by accounting for buyers' pricing needs in market terms. In distressed markets, the longer an REO property is left on the market, the greater the chance its value will decrease, particularly due to vandalism and stripping. To provide an incentive for REO holders to sell their assets rather than holding onto them, NCST needed to quantify the benefit of taking action quickly. NCST's NRV formula, developed by the Resolution Trust Corporation during the savings and loan crisis in the 1980s, takes an estimated market value based on a traditional real estate valuation model. The formula then considers how much the servicer would save by not having to pay for maintenance, construction and transaction costs. It also factors in how much value the property would lose while held in foreclosure.

First Look thus offers a rational mechanism for selling packages of discounted properties, in a way that benefits both the servicers and the community development sector. It allows lenders and servicers to reduce their REO inventories via sales to cities and community-based organizations that fit into their overall REO disposition guidelines. The staggered nature of the process is also a benefit: It is easier for community-based organizations to manage the purchase and rehab of five to ten units at a time rather than hundreds all at once.

Another key activity within NCST's Transfer Agent role will be bulk purchase. NCST is developing a process whereby REO servicers will provide cities access to aged inventory (60 to 90 days on the market). This process will allow the buyers to "cherry-pick" assorted individual properties that fit their neighborhood development strategies and financing modes. NCST's sponsor organizations will also offer financing and technical assistance to affiliated buyers. This bulk purchase strategy can benefit nonprofit and governmental development entities that have the capacity to take on larger portfolios of properties.

Bulk purchase also helps work around potential impasses over how acquisitions occur. Servicers generally prefer to sell a large number of properties quickly through subcontracted local brokers on a "take-it-or-leave-it" basis; socially motivated local buyers, however, want to carefully identify the properties most appropriate to their mission and budget. NCST serves, in effect, as a large-scale broker, which simplifies the sale process for the servicer.

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[5] The estimated value of a property as determined by a real estate broker or other qualified individual or firm, based on the characteristics of the property being considered.

NCST also plans on providing capital to support local and state efforts. NCST will provide financing for REO purchases using a $50 million Program-Related Investment pool obtained from philanthropic investors led by the Ford Foundation. The final design of this financing vehicle is projected to roll out in the fall of 2009.

NCST still faces some challenges rolling out its program throughout the country. It will likely have to renegotiate local agreements to go with its national accords with servicers and lenders. For example, disagreements have arisen over the use of non-local title companies, which provide financial protection against hidden defects or adverse title claims that might arise during the transfer of property. Also, the valuation methodology agreed on nationally will be unfamiliar to local servicers.

In addition, the NCST faces the challenge of negotiating agreements on the required NSP discount at the national level with Mortgage-Backed Securities trustees like Wells Fargo, who remain concerned about being sued by investors if they sell properties below their appraised value. In order to demonstrate a fulfillment of the fiduciary responsibilities, the trustees believe they must adhere to the practices of the marketplace. The federal government recently reduced its discount requirement, giving buyers more leeway to negotiate.

Lastly, national REO holders don't always control significant inventory in neighborhoods targeted by NCST's buyers. Local servicers may not have the same motivations as the larger ones to move properties quickly. For example, they may not have the same financial interest in taking losses on properties at one time, and they often don't have the same public relations concerns that national institutions have. NCST continues to work on addressing all of these issues, and to expand its program to cities and regions across the US.

Local Acquisition Strategies

Although many cities have sought to acquire properties in bulk from REO holders, only a handful have been successful to date. Key components of success have included: exclusive access to properties, sufficient capital, and superior development expertise among a city's nonprofit partners. Profiled below are two examples of direct negotiations with REO holders that succeeded in significant asset acquisitions. The first example is Minneapolis, where the city and the nonprofit community worked together to help create a system for capturing a "flow" of REO units in a compressed timeframe, a model which is being replicated nationally. The second example is Phoenix, where a coalition of nonprofit development organizations facilitated the purchase of foreclosed properties through a "consumer-driven" process.

Minneapolis

Minnesota ranks 18th among states in the number of foreclosures, according to RealtyTrac. The city of Minneapolis has concentrated foreclosure problems in specific neighborhoods, such as in North Minneapolis. As the problem has intensified, the city and its nonprofit sector have been in a race against unscrupulous investors, who are acquiring and reselling foreclosed properties without making necessary improvements.

The foreclosure crisis is not the first time low-income neighborhoods in Minneapolis have been threatened. In the 1980s, the Savings and Loan crisis ravaged these communities. This time, regional stakeholders recognized that a key to avoiding this same devastation would be tight collaboration.

Starting about three years ago, stakeholders across the region convened a meeting to address the foreclosure crisis and soon formed the Minnesota Foreclosure Partners Council, a statewide public, private, and non-profit collaborative. It endorsed a systemic approach to neighborhood recovery as the best way to help communities prevent foreclosures. The council has developed a legislative agenda to stem predatory lending practices and enhanced the counseling capacity of local organizations.

Yet, at the beginning of the foreclosure crisis, Minneapolis nonprofits and other affordable housing developers had little experience in acquiring homes, either from REO holders or the open market. At the time, they were negotiating with two large local banks, Wells Fargo (headquartered regionally in Minneapolis) and US Bank, both of which were willing to sell properties at a discount. Negotiating with other REO holders was more difficult, given the time-consuming process for tracking down decision makers. Additionally, Minneapolis could not use NSP funds when buying properties on the open market because it couldn't obtain the discount that program requires.

To address these challenges, the city and its partners started working with the NCST on foreclosure recovery. NCST established relationships with REO holders, which agreed to give the organization access to 80% of the properties in the market, through an early version of its First Look program. Exclusive and early access to these properties gave the city a critical advantage over investors.

Additionally, the city engaged as its development partner the Greater Metropolitan Housing Corporation (GMHC). This partnership was crucial because GMHC had the necessary expertise in scattered site acquisition and rehab projects to reclaim the foreclosed properties that dotted its target area. The Minneapolis business community formed GMHC in 1970 to preserve, improve and increase affordable housing for low and moderate-income individuals and families. Since its inception, the organization has built over 7,000 single-family homes and rehabbed an additional 900 properties.

Lastly, the Minnesota Housing Finance Agency supported the foreclosure recovery efforts in Minneapolis by loaning $10 million to a local community development financial institution, the Family Housing Fund (FHF). FHF obtained an additional $25 million of capital from private sources, to provide interim financing for acquisitions. In total, foreclosure recovery partners in Minneapolis were able to raise over $70 million through private sources (banks and for-profit developers) and the philanthropic community (McKnight and General Mills). The availability of these resources gave GMHC the capital necessary to compete with speculators and investors.

After inspecting nearly 600 foreclosed homes, the city and GMHC has acquired 240 properties to date — at a significant discount. GMHC is doing some development on its own and is also selling properties to other nonprofit developers. The city is not scrutinizing every purchase by GMHC (an impasse in some other cities), but it is allowing the organization to acquire properties in pre-identified "cluster" areas. For properties that aren't sold to developers, the city plans to demolish the houses and place the vacant land in a land bank, which is being established separately by FHF. So far, the city's overall effort has been mostly funded by private and philanthropic sources. Public resources like NSP account for only a small portion of the capital resources at this point.

In conjunction with the foreclosure recovery efforts, the city of Minneapolis bought 10 to 20 properties at a time, most of which were abandoned and had multiple code violations. Given the physical condition of many of these properties, most were demolished and land-banked. The city has also engaged in litigation to gain control over more properties. To date, it has successfully sued one investor, seizing 150 properties.

The Minneapolis example demonstrates the roles of several critical factors in successful REO acquisition. The strong capacity of GMHC and other nonprofit developers has allowed the local community development system to reclaim a large number of properties quickly and smoothly. That capacity played heavily into NCST's decision to pilot First Look in Minneapolis, leading to still faster and more efficient REO sales. The city has been able to leverage local resources (banks, for-profit sector), utilize regulatory tools (remove blight, demolition of dilapidated properties), and focus on reinvestment beyond its most difficult properties, in order to encourage private sector investment and provide incentives for bringing homebuyers back into the market.

The collaboration demonstrated by the Partners Council enabled all of this to happen in a coordinated way. Andriana Abariotes sums it up this way: "The subprime crisis has left neighborhoods in a state similar to where they were during the '80s. Except this time, in the Twin Cities, there is a built-out, experienced and coordinated community development system in place that can work on a larger scale than it did before."

Phoenix

According to RealtyTrac, Arizona ranks fourth among states in the number of foreclosures. The Phoenix area accounts for more than four in five of those foreclosures and ranks seventh among the nation's cities in the number of foreclosures. To address this challenge, Phoenix LISC began discussions with its nonprofit partners about a year and a half ago. Beyond merely addressing vacant housing, the nonprofits saw the REO crisis as an opportunity to make affordable housing available to low and moderate-income buyers, who wanted to live near work or school. Yet, the organization lacked access to the properties, and the banking community wasn't making the acquisition of foreclosed properties easy.

As Paul Harris of Phoenix LISC pointed out, "One of the challenges of working in the Phoenix market is dealing with the multitude of mortgage lenders that are not the major REO holders. These regional servicers don't have the same motivations or capacities to respond as the larger ones." Moreover, Phoenix LISC's nonprofit partners lacked the capacity to undertake large-scale REO acquisitions. Even if they had the capacity, they lacked the capital. In addition, local nonprofits were concerned about acquiring properties before first lining up buyers because property values were still declining. Facing these challenges, LISC sought another strategy for addressing foreclosures in Phoenix. The key to the new strategy were potential buyers who had gone through local nonprofits' homeownership counseling programs. These programs had access to HOME funds and private loans through relationships with the city and local financial institutions, respectively.

Out of this experience, LISC and a 14-member coalition developed a "consumer-driven model." Buyers who completed the homebuyer-counseling program would choose their own REO properties. The LISC team would then facilitate the acquisition and rehab financing. LISC negotiated agreements with the major REO holders in Phoenix (Fannie Mae, Freddie Mac, Citibank, Wells Fargo, and Countrywide / Bank of America) who agreed to provide a response within five days on offers from pre-qualified homebuyers. These buyers would not have to engage in a bidding war over REOs with speculators and investors. The take-out financing was provided by local banks, which have strong relationships with the counseling agencies.

Moreover, area property values had declined significantly, with the median sales price on foreclosed homes in the inner city hovering around $48,000. Consequently, banks were able to provide smaller

mortgages, which made them more comfortable making loans during the credit crunch. Also, most of the buyers qualified as low-income, so public subsidies also supported their purchases. In a nine-month period, the Phoenix coalition facilitated the acquisition of 337 REO units, as of the end of June 2009.

Going forward, the Phoenix coalition will gear up for neighborhood-level acquisitions, in order to utilize new resources available through NSP. Seven jurisdictions within the Phoenix metro area received nearly $70 million in the first NSP allocations. Separately, the city of Phoenix received $39 million. At the time of this writing, the coalition was in talks with NCST and the city about NSP-II, and the city expressed interest in using the consumer-driven model developed by LISC and its partners.

A key distinction between the foreclosure recovery strategies in Phoenix and those in Minneapolis is the focus on the end-user of the REO properties — the homebuyer. In Phoenix, prospective homebuyers lead the acquisition efforts, while a nonprofit intermediary directs the activities in Minneapolis. Phoenix's success in addressing scattered site foreclosures depends on building partnerships with nonprofit and for-profit developers in order to quickly facilitate the acquisition of REO properties by qualified homebuyers. Lastly, the coalition in Phoenix made sure that the prospective homeowners would have access to financing through local banks. With assistance from nonprofit development organizations, homebuyers in Phoenix could identify REO properties, get an accurate estimate of renovation costs, and move quickly to purchase an affordable home.

The Phoenix example also highlights a key difference between their goals as a "strong-market" city and those goals of mixed- and weak-market cities like Minneapolis. While Twin Cities LISC and its partners sought to stabilize communities, the primary concern of the groups in Phoenix was to create greater affordable housing opportunities for its clients. This difference in goals enabled Phoenix LISC to pursue a model that bypassed many of the inefficiencies that First Look was designed to address.

Lastly, this example illustrates the fact that a successful foreclosure mitigation strategy depends on local nonprofit capacity to organize, execute and fund it. The Phoenix effort is probably more difficult to pursue using NSP because its regulations require the grantee to concentrate on the acquisition of key properties, a challenge for a program based on allowing homebuyers to choose where they live.

Bulk Purchase

To date, the NCST has focused on creating controlled access to a modest number of REO properties within a specified time period. But as the foreclosure crisis continues, there is greater interest in creating mechanisms that transfer larger portfolios from servicers to for-profit, non-profit and/or public sector buyers. As a result, HUD, Fannie Mae and Bank of America have established bulk sales programs.

For a bulk purchase strategy to be effective, cities need to form partnerships with nonprofit and for-profit developers. Also, given the risks of buying REO in an unstable economy, cities and their nonprofit partners have to formulate their disposition strategies upfront. In developing this strategy, they must ask: What are we going to do with the properties? Which will we sell, lease or demolish? How confident are we that our disposition strategy will yield revenues that meet their costs? What will the costs be (for example, how long will we have to hold the property?) To examine these points, this case study turns to an example of an acquisition of a portfolio of 47 mortgages by a New Jersey-based nonprofit development organization.

New Jersey

New Jersey ranks 22nd among states in the number of foreclosures, according to RealtyTrac. Essex County, in the northeast corner of the state, is one of the hardest hit areas. Within the city of Newark alone, there are an estimated 2,500 REO properties. To address these challenges, Housing and Neighborhood Development Services, Inc. (HANDS), a 23-year old community development corporation operating in the cities of Orange and East Orange, launched Operation Neighborhood Recovery (ONR) to acquire 47 abandoned properties.

HANDS saw an opportunity to help stabilize neighborhoods in some of the state's older suburban communities, when it discovered that a number of foreclosed properties in its market area were owned by Washington Mutual Bank. The bank had acquired a mortgage portfolio from an organization (New Jersey Affordable Homes) whose management was accused of fraud. The FDIC subsequently took over Washington Mutual, creating a unique opening for HANDS.

The 47 properties, vacant and abandoned, and many deteriorated, were spread out, but more than 70% were concentrated in Newark and the surrounding area. Although the properties were vacant, none had completed foreclosure due to legal entanglements that had beset the original REO holder. HANDS created a protocol for evaluating the properties in order to determine the price they were willing to offer for each. They assessed the rehab costs (some units needed gut rehabs, some just cosmetic work) by obtaining two estimates from contractors, who would not necessarily be hired to do the work; a reliable REO broker supplemented these estimates with a market assessment. Using this information, HANDS modeled three scenarios for property disposition: "fire sale," "some modest rehab," and "best case," to help them assess financial risk and determine an acceptable purchase price.

HANDS negotiated a purchase price of roughly $2.4 million for the 47 properties, which included acquisition, maintenance, and all other costs necessary to obtain clear titles. The additional costs that HANDS would incur during foreclosure proceedings (NJ is a judicial foreclosure[6] state) were added into the purchase price, as well as legal, taxes and insurance. The average purchase price including all costs was approximately $50,000 per unit. HANDS obtained financing from New Jersey Community Capital, Prudential Social Investment, NeighborWorks America, LISC, and Enterprise Community Partners. HANDS financed approximately 80% of the total cost, and used some of its own resources to provide a portion of the equity.

Legal complications around title issues slowed the completion of the transaction. Also, the financing structure presented underwriting issues for the lenders. Nonetheless, HANDS overcame these hurdles and succeeded in completing the first true bulk purchase of foreclosed homes by a nonprofit in the country.

After acquiring the mortgages, HANDS proceeded with the foreclosure process. A significant number of owners agreed to transfer their titles to HANDS, thereby avoiding the judicial foreclosure process. As a result, a clear title was obtained sooner. HANDS handled its new properties in six different ways: demolition, rental, sale to CDCs, redevelopment by HANDS, direct sale (some as-is, some with rehab) to homebuyers at market-rates and direct sale (some as-is, some with rehab) to investors at market-rates. Additionally, HANDS developed a collaborative relationship with organizations doing neighborhood

[6] A foreclosure that results from a court action rather than from the power of sale given to a trustee.

stabilization work in the cities where the properties were located.[7] One noteworthy tactic that HANDS employed: It used the proceeds from the sale of the market-rate properties, located outside of HANDS' target area, to subsidize the affordable housing units and pay down its debt quicker. Also, local governments played a key role in this transaction by committing funds and other assistance.

Going forward, HANDS plans on additional acquisitions of scattered site REOs properties, using the bulk purchase model developed above. The CDC helped organize a separate company, Community Asset Preservation Corporation, to do similar work on a statewide basis. In addition to purchasing packages of mortgages and REOs properties, the new company will also serve as a transfer agent for the National Community Stabilization Trust, providing a local intermediary function in New Jersey to identify the developers who want access to REOs through the First Look program.

As this bulk purchase example shows, buying a mortgage portfolio is complex. It will most likely succeed when a single entity owns a portfolio of whole loans, rather than when a servicer owns loans that have been repackaged into mortgage-backed securities and sold among multiple parties. For many cities and groups, the approach of creating a city-wide, regional or national intermediary such as NCST may be preferable. It can help spare local CDCs from the costs and challenges of having to negotiate separately for properties. An intermediary can also provide them with key details about those assets before they take ownership.

Conclusion

The strategies highlighted in this case study offer key lessons for a city or nonprofit group building a REO acquisition plan. It is important to distinguish between the approaches utilized by NCST and HANDS. NCST's First Look program employs a strategy that can be called "flow," which facilitates the steady transfer of REO properties. This approach can be an effective means of targeting key properties to help restart a neighborhood's housing economy. NCST's strategy differs from the "bulk" approach adopted by HANDS, which offers the group more flexibility in how they dispose of the acquired assets.

The case study also presents three types of buyers of foreclosed properties -- intermediaries that buy in flow (Minneapolis), buy in bulk (HANDS), and facilitate direct sales to end users (Phoenix). Each of these approaches shares the goal of creating a unique, locally driven balance between public and nonprofit action and free-market forces. In each case, the ultimate objective is to return foreclosed properties to productive use by private owners.

The three approaches differ in how they will effect neighborhood stabilization. The Minneapolis foreclosure recovery partners targeted their REO acquisition efforts on specific neighborhoods, and are likely to have some impact on stabilizing those areas. Conversely, Phoenix's consumer-driven approach and the bulk purchase transaction completed by New Jersey's HANDS did not focus on specific areas. As a result, both of these cases are less likely to produce the same neighborhood results as the work in Minneapolis.

Furthermore, cities have different market dynamics that interact with the strengths and challenges of each community — as a result, neighborhood recovery looks different in different places. Newark, N.J., a

[7] La Casa de Don Pedro, Unified Vailsburg Services Organization, Brand New Day, HomeCorp, Newark Housing Partners, and the Episcopal Diocese of Newark

city that has lost a significant chunk of its population and industrial base over several decades, will have different goals than Phoenix, which continues to grow.

Success is also shaped by local nonprofit capacity and the ability to raise funds locally. None of these models would have succeeded without a dynamic organization driving their efforts. Not all cities have such a resource — or at least they will need help in developing one. Another key factor is the availability of local private capital, essential to augment the growing, but limited, federal pool of funds.

The presence of nonprofit developers at the center of each of these models reinforces the notion that cities themselves are not set-up to acquire real estate in an efficient manner, particularly in an active market. According to Harold Simon of Community Asset Preservation Corporation, "Cities need to understand the scattered site nature of the foreclosure problem, which requires them to build partnerships with nonprofit and for-profit developers in order to negotiate a bulk purchase." This is one reason NCST is valuable: It facilitates the design of systems that bring together key stakeholders — cities, the nonprofit sector and the REO managers. It helps create relationships among stakeholders in which each plays a specific role — providing access to properties, sorting out potential acquisitions, and amassing capital.

The biggest challenge for cities and their allies during this foreclosure crisis — and almost certainly for years to come — is to drive community revitalization at a broad scale. That will involve not just examining and identifying which property acquisition tactic outlined in this case study may work best, but developing longer-term strategies about returning foreclosed properties to productive use. The work is not easy, and given growing unemployment and a still-startling foreclosure rate, conditions on the ground may in fact worsen.

But as this case study shows, dedicated professionals in cities across the country are responding. In particular, nonprofit housing organizations have had to rethink their ways of doing work, evolving from first-homebuyer educators to loss-mitigation providers to strong acquisition /rehab developers. Perhaps the greatest hope is that this foreclosure crisis may create a lasting infrastructure that will prepare the country to face the next challenge down the road.