EVALUATION OF THE LIVING CITIES FORECLOSURE MITIGATION INITIATIVE

Final Interim Report

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Executive Summary

In response to the foreclosure crisis, Living Cities developed the Foreclosure Mitigation Initiative (FMI) in late 2007. Under this initiative, Living Cities made $5.25 million worth of grants to organizations in 10 locations: eight cities and parts of two states. The purpose of these grants was to support new efforts to stabilize neighborhoods facing large numbers of foreclosed, often vacant housing units. FMI was developed with the expectation that the federal government would provide funding for the acquisition and resale of foreclosed properties. Therefore, as initially conceived, FMI funding was to support innovative local neighborhood stabilization pilots that would be implemented quickly and so be able to serve as models for replication when federal funds became available.

Living Cities asked the Urban Institute to conduct an evaluation of the FMI effort. The Interim Report presents preliminary findings for each of the following eight research questions on the FMI program:

1. How did the FMI pilots fare against their expectations for becoming fully operational and for achieving acquisition, rehabilitation, and disposition goals? For testing innovative approaches to foreclosure mitigation?
2. What factors influenced their successes?
3. What were the major obstacles to successful implementation, and what are the potential and the known solutions?
4. How did federal funding (through the Neighborhood Stabilization Program [NSP]) affect the initiatives, and how did the initiative affect federal funding?
5. What early sense, if any, can we get of the impact of this work?
6. What conclusions can we draw about what did and did not work?
7. What can we learn about the role of different players (nonprofits, banks and servicers, state and local governments, philanthropy) in this process?
8. What are the implications of the Living Cities initiative for how philanthropy responds to crises?

This summary briefly highlights some of the key findings discussed in the Interim Report. A final report, based on further research, will be prepared for March 2010.

Local FMI efforts generally proposed to establish new partnerships and financing or other arrangements, broadly defined, to purchase foreclosed homes, rehabilitate them, and put them back to use in rental or homeownership status. Grantees' proposals described how they would design, structure, and move to implement such strategies, and they identified quantitative housing unit production goals for the first year or more of that work. Most grantees were successful in making their programs operational during the grant period, assembling needed collaborations and financial commitments, and designing new or retargeted programs. They made significant innovations in structuring new institutions and partnerships and on focusing programmatically on foreclosed structures and stricken neighborhoods. But in most cases they were significantly slower in actually putting housing back to use than they and Living Cities had anticipated.

The four main reasons for the lag were beyond the control of national and local FMI actors: (1) difficulty in putting together financing in the chaotic lending environment of 2008; (2) a much harder time than expected acquiring foreclosed properties from reluctant (or disappearing) servicers; (3) competition from other purchasers of foreclosed homes; and (4) slow rollout of federal NSP dollars. While in general FMI deliberately chose grantees that were among the farthest along in this work in the country, the grantees had in most instances not yet tested their markets when they received their awards; and none could know the eventual timing of federal assistance.

Local and state governments often played key roles in progress. Their imprimatur made assembling collaborations much easier, and they allocated significant amounts of NSP funds to about half the FMI grantees, positioning those recipients well for larger-scale action now that first-round NSP money is flowing. A history of cooperation and trust among key actors and getting all the major players to the table early on also contributed in important ways to the progress of many FMI pilots. Some combination of the public role and an existing practice of collaboration smoothed the process of allocating stabilization-program responsibilities and resources efficiently.

FMI's early grant dollars appeared to play important roles in success in at least two ways: paying for staff at various levels (intermediary grantees, community development corporations) to carry out the detailed design and early testing of the local initiatives and reducing risk for other investors and lenders in loan pools for acquisition, rehabilitation, and resale. FMI support seemed to play a significant part in directing NSP dollars to the programs piloted by the Living Cities grantees, as hoped, because the pilots were among the earliest efforts toward neighborhood stabilization to be up and running in the face of foreclosures. The effect of FMI on federal policymaking that led to the creation of NSP is less clear, although it may have helped identify reoccupancy of foreclosed homes as an issue worth addressing.

The least-anticipated challenge has been the difficulty in acquiring properties. The National Community Stabilization Trust (NCST), itself in pilot operation, offers one hopeful approach. NCST has agreements with some major holders of foreclosed properties to give nonprofit developers and intermediaries, including FMI pilots, a limited "first look" at properties before going fully to market. If the tight restrictions of "first look" can be handled and more lenders and servicers involved, grantees may have access to a larger number of REO (that is, "real-estate-owned," which are owned by lenders as a result of a foreclosure) homes to purchase, thereby making it easier to achieve production targets.

It is too early to tell how much impact the FMI-supported efforts will have on stabilizing the pilot communities. Most of the grantees have yet even to acquire a significant number of properties. We are just now seeing some examples of acquisitions of key problem properties and initial small clusters of buildings, including acquisitions in subneighborhoods in which participating nonprofit community development corporations had previously made major investments in properties abutting foreclosure sites. These are candidates for impact, but it is too soon to see results. Living Cities had also intended to help create lasting structures that would address problems of foreclosures, vacancy, and blight and to put into place broader revitalization strategies. It is also too early to judge success of that goal.

The response of Living Cities to the crisis in high-foreclosure neighborhoods suggests some preliminary lessons. The Living Cities effort to jump-start a response to foreclosed properties demonstrated the ability of a large collaborative of philanthropic actors to identify a crisis, select an aspect on which to focus, devise an approach to dealing with it, and move quickly to making grants. Its willingness to take some risk of failure with investments in nascent local initiatives allowed it to act swiftly and to pursue a stated objective of enabling good strategies for dealing with an emerging problem. FMI's flexibility in the use of grant funds and in the grant-period timing, as the systemic reasons for delays became clear to grantees and grantor, accommodated to the evolving circumstances in the initiative's national and local environments. The decision to fund operating costs for core staff, data, and program development matched well the existing status of new and innovative efforts on the ground.

However, the question of whether the structures and mechanisms created with FMI support will soon produce larger-scale housing and neighborhood stabilization results remains open. There are hopeful signs in some of the pilot sites and surges of activity using newly arriving NSP funds. But issues remain in key areas, including access to and competition for foreclosed properties for acquisition. Even substantial NSP and other capital dollars may be insufficient for the scale of the task. Operational support, post-FMI, may be inadequate for sustainability, especially if production is not rapidly scaled up. Transfer of FMI pilot program approaches and lessons to other locations may be difficult. If FMI fails to have the expected impact, then the question will be raised about what more could have been done—more accurate advance information, greater resources, increased cooperation from other stakeholders?— to improve an already seemingly well-designed effort.

I. Introduction

In response to the foreclosure crisis, Living Cities developed the Foreclosure Mitigation Initiative in late 2007.[1] Under this initiative, Living Cities made $5.25 million worth of grants to organizations located in 10 cities. FMI was developed with the expectation that the federal government would provide funding for the acquisition and resale of foreclosed properties. Therefore, as initially conceived, FMI funding was to support innovative local neighborhood stabilization pilots that would be implemented quickly and so be able to serve as models for replication when federal funds became available.[2]

This Interim Report on the FMI program uses data collected through two case studies (Neighborhood Progress, Inc. [NPI] in Cleveland and Twin Cities Local Initiative Support Corporation [Twin Cities LISC] in St. Paul), key informant interviews,[3] and documents from all 10 pilot sites and their Living Cities contact staff and consultants. In this report, we present preliminary findings for each of the following eight research questions on the FMI program:

1. How did the FMI pilots fare against their expectations for becoming fully operational and for achieving acquisition, rehabilitation, and disposition goals? For testing innovative approaches to foreclosure mitigation?
2. What factors influenced their successes?
3. What were the major obstacles to successful implementation, and what are the potential and known solutions?
4. How did federal funding (through the Neighborhood Stabilization Program [NSP]) affect the initiatives, and how did the initiative affect federal funding?
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By analyzing grantee-provided data, background information collected for each site, an expanded set of key informant interviews, and information collected during a total of four on-site visits, the final report, due in January 2010, will provide more complete answers to the same research questions. In the next

[1] NSI is now referred to by Living Cities as the Foreclosure Mitigation Initiative.

[2] Living Cities. 2008. *Mitigating the Effect of Concentrated Foreclosures on Urban Communities: A Ten-City Pilot to Prove What Can Work: Grant Proposal to the Open Society Institute*. June 19.

[3] About half the total 10–12 key informant interviews were completed by mid-September, just before this report was prepared.

section, we present preliminary answers to each question. The case studies for NPI and Twin Cities LISC are presented in the appendix.

II. Findings

This section presents our preliminary findings for each research question. These answers will be amended as we complete the two remaining case studies and conduct additional key informant interviews before the final report is submitted.

1. How the FMI pilots fared against expectations

Becoming fully operational. As discussed earlier, the FMI's initial objective was to assist grantees in getting their acquisition and rehabilitation programs off the ground so that the programs could potentially be replicated or scaled up once federal funds became available to address the foreclosure crisis. In many cases, the FMI grantees had to establish either new organizations or relationships with other stakeholders to implement programmatic activities. Therefore, a grantee's program could be considered fully operational once the institutional groundwork (creating new legal entities and partnerships) was created. All the grantees, however, expected to start programmatic activities relatively soon after receiving their award and so proposed quantitative production outcomes that, in hindsight, may have been too aggressive. Therefore, this section discusses both the grantees' progress with regard to their ability first to establish the legal and institutional frameworks required to implement their programmatic activities and their infrastructure to implement the program and then to meet quantitative production goals. Over time, it appears that all FMI participants recognized that grantees could not be expected to meet production goals for reasons beyond anyone's control but that the grantees could make satisfactory progress in establishing the required institutional infrastructure.

Overall, the 10 FMI grantees have all made progress in implementing their proposed activities. In some cases, grantees had to work with other organizations to establish partnerships or incorporate a new organizational entity for conducting all or some of the FMI-funded activities. In Cleveland, for example, NPI and the Cleveland Housing Network created a single-purpose limited liability company (Opportunity Homes), which is responsible for acquisition, rehabilitation, and resale of properties acquired, partly with funding secured with the help of NPI's FMI grant. In Detroit, the Office of Foreclosure Prevention and Response was created outside of city government to provide a new locus of focused attention and collaboration on the issue. In Chicago, Mercy Portfolio Services created two new local structures, one to acquire and hold properties and the other to plan and operate the initiative. In New York, the Center for New York City Neighborhoods was established to provide an array of foreclosure and neighborhood stabilization services; it was created quickly, despite the challenges inherent in a city with a host of housing players. In Massachusetts, the Massachusetts Housing Investment Corporation (MHIC) created a new acquisition and rehabilitation loan pool with multiple financing sources and established new collaborations with community development corporations (CDCs) and for-profit developers who are to carry out the acquisition, rehabilitation, and disposition activities in seven cities.

In general, creation of operating structures, partnerships, and mechanisms has been easier to keep on track, including on time, than have other key steps in the process of getting the pilot efforts moving. Indeed, in some cases the organizations have jumped into action and then had to wait for further financing and subsidy components to fall into place.

While each grantee has started FMI activities, these organizations have progressed unevenly in implementing program activities, including acquiring and rehabbing properties. In some cases, FMI grantees took longer than expected to identify partners and finalize the agreements required to initiate program activities. For example, the Community Housing Land Trust of Rhode Island, under its FMI program, established a partnership with two CDCs (West Elmwood and Olneyville Housing Corporation) that operate in Providence. Because such partnerships are relatively rare in Rhode Island, it took longer than expected to get all the partners to reach an agreement on terms. Others benefited substantially from relationships with a history, in which partners had worked together before, developed confidence and trust, and practiced nonterritorial division of responsibilities. In some of the pilot locations, key individual staff members had worked for other local partners previously or served on their boards, in addition to participating in past cooperative efforts.

FMI grantees had other tasks to carry out to get ready to move forward in production and apparently progressed well in pursuing them. An important example was vetting and approving quality developers—nonprofit and for profit—as potential purchasers of individual properties using the mechanisms being developed by the grantees, for the several FMI recipients who were themselves not taking possession of properties.

Achieving acquisition, rehabilitation, and disposition goals. Even in sites that did not require establishing new organizations or partnerships (or where such activities went relatively smoothly), the FMI program grantees have not met quantitative targets for acquisition and rehabilitation activities. The major reason for these delays is that grantees had more trouble than expected in acquiring both financing and properties from servicers and other financial institutions with large REO inventories of properties. In large part, that challenge stemmed from the unprecedented turmoil in credit markets that started in late 2007, which made it difficult for grantees to access private market financing and REO properties held by servicers or lenders. The sharply worsening situation in fall 2008 after grants were underway further confounded expectations. A separate critical element of the financing difficulty was the unexpected length of time that it took until NSP-1 funds were actually released for local use—funds to which some FMI grantees thought they would have access much earlier in their FMI performance period.

Closing on the required financing has been a problem across the board for nearly all FMI grantees. City First Enterprises, in Washington, D.C., expected to raise nearly $18 million through a sale of tax credits through the New Market Tax Credit (NMTC) Program. Unfortunately, City First Enterprises' initial commitment for that funding fell through as credit markets seized up in late 2008 and, according to

Living Cities' staff, will be unable to raise any funds through the program. As a result, City First Enterprises has not been able to move on its plan to purchase 100 REO homes located in the District of Columbia within a year of receiving its FMI grant. In Cleveland, NPI could not close on a $6 million pool of debt capital until May 2009, nearly a year after receiving its FMI grant because the providers of the debt capital had to agree to a relatively complex financing structure (see case study in the appendix). As a result, NPI could not begin acquiring properties until spring 2009 and thus by June 2009 had acquired only 30 of the 50 properties it expected to purchase. In Massachusetts, while there was no real danger that MHIC would fail to put together the Neighborhood Stabilization Loan Fund from multiple sources, the process lasted longer than anticipated because of the number of lenders providing capital and the complexity of arrangements.

A number of the pilots made initial acquisitions at a modest level before NSP funds were available and in some cases before their new financing structures were in place, using existing sources of funds and counting on NSP and finance dollars to arrive in time to take out temporary funds. Continuing delay in NSP release and specification of provisions and revisions in rules for NSP's uses seems to have discouraged grantees from implementing acquisition activities, leaving many FMI grantees (or their partners) with small asset holdings, awaiting further assurance that they would be able to obtain and use the federal funds.

Most of the FMI grantees expected to purchase homes through some sort of bulk-sale agreement that would facilitate access to foreclosed properties in their target areas. This has not been the case: most grantees have acquired properties on the open market, without any type of purchase arrangement with a servicer. EHOP-Dallas's FMI grant proposed, in the first 12 months after receiving its funding, to acquire 30 properties from servicers who hold REO properties.[4] The organization began negotiations with Fannie Mae, but the two parties could not reach an agreement. As a result, EHOP-Dallas had to seek out other potential suppliers of REO properties. Unfortunately, because servicers would not agree to any such arrangements, EHOP-Dallas was unable to acquire any properties with its FMI grant.

An exception is in the Twin Cities, where the Greater Metropolitan Housing Corporation (GMHC) in Minneapolis and Dayton's Bluff Neighborhood Housing Services (DBNHS) in St. Paul acquired properties as part of the National Community Stabilization Trust's prepilot program. Under this program, servicers provide each organization with an opportunity to take a first look at REO homes before they are offered for sale to the general public. (NCST is discussed in the Twin Cities LISC case study in the appendix.)

[4] See page 2 of the EHOP-Dallas proposal. The proposal indicated that the organization would acquire and rehabilitate 345 properties over three years, some of which will be acquired from the Department of Housing and Urban Development under the existing Asset Control Area program (ACA).

In Massachusetts, even with the many challenges in the acquisition arena because of competing bidders for REOs, the MHIC effort has recently moved rapidly to reach about half its production goal of acquisitions now that NSP funds are firmly in place to help pay for the rehabilitation work that the purchased properties will require. That is at least a hopeful sign that the release of federal funds—with program structure, partnering, financing, and operating mechanisms in place—will now allow a rapid increase in production activity. Whether the burst can be sustained in Massachusetts and whether such a surge will occur across the other pilots are key questions to be answered in the near future.

Testing innovative approaches to foreclosure mitigation. FMI supported programs that, as one key informant said, in some cases represented an expansion of an organization's existing activities but that for some grantees reflected new approaches to financing for REO acquisition and rehabilitation or processes for acquiring and selling REO properties. We define innovation to include a broad range of potential new approaches that grantees proposed to implement, for example:

- new sources and mixes of financing
- new and expanded partnering arrangements
- new programming emphasis on acquisition, rehabilitation, and disposition
- creation of new institutions
- development of new tools and processes
- new approaches to geographic and property targeting

FMI grantees are in early stages of testing a variety of innovations in putting foreclosed properties back into positive use. Naturally, because FMI grantees have not fully implemented their activities, there are sharp limitations to drawing conclusions about their effects. City First Enterprises, for example, by using NMTC funds for acquisition and rehabilitation, was perhaps one of the more innovative FMI-supported programs in its original conception. But, as discussed above, because the collapse in the capital markets made it very difficult for City First Enterprises to raise funds, that program is unlikely to meet its production goals. As with City First Enterprises' program, EHOP-Dallas's initiative is an innovative approach: the grantee proposed to apply its Asset Control Area program, under which it purchases Federal Housing Administration properties from the U.S. Department of Housing and Urban Development (HUD) at a discount, to private REO properties. But, as discussed above, EHOP-Dallas was unable to find servicers willing to sell it properties, as HUD does under the Asset Control Area program.

These two programs, which key informants suggested are among the most innovative of the 10 FMI programs, are behind schedule, as they require the grantees to work with third parties to secure either financing or properties to purchase REO homes. Informants suggested that this is not a surprise: there is a correlation between the time it takes to implement an FMI program and the extent to which the programmatic activities are new and innovative.

In contrast, important innovations are moving forward in other pilot locations. The MHIC effort in Massachusetts is addressing the problems of foreclosure among small properties, especially given the presence of three-decker properties.[5] The housing experience of most CDCs in the area is concentrated in developing larger-scale new housing projects or in some cases larger rehabilitation projects. Although learning to deal with small, scattered-site acquisition and rehabilitation and financing in a fast-moving market is very challenging, some progress is now beginning to show in this area of innovation.

Use of mission-oriented for-profit and nonprofit brokers in New York and Los Angeles, aimed at promoting homeownership and housing preservation, is likewise a new form of activity for those grantees. Tight targeting of activity within specific neighborhoods in Chicago, Cleveland, and Massachusetts is a departure from spreading funds throughout political jurisdictions and in line with a central tenet of NSP and stabilization efforts more broadly. Each employs an extensive use of data and mapping to help select key targets. It will be important to see how such concentrated activity contributes to the impact of the foreclosure efforts. Detroit is entering into new territory for a city without a rich community development history in its efforts to corral and put to use data in strategic planning in the face of immense challenges.

Thus, FMI grantees have not yet demonstrated that their innovative approaches work, in the sense of being able to move to scale or create neighborhood impact or models for replication. But they are at work on a significant set of innovations that may prove fruitful as they have time to evolve. It is important to remember as well that improving and reoccupying foreclosures as a focused objective and program is quite a new form of activity, so that the partnerships, structures, and program mechanisms just now moving into significant production are innovations as well.

2. Factors that influenced success

As detailed in the previous section, the most influential factors on the success of a grantee’s program were ready access to financing and the presence of institutional relationships with key stakeholders. These two factors, when present, allowed grantees to implement programmatic activities relatively quickly. Conversely, grantees that had to close on new sources of financing or develop new institutional relationships typically found it more difficult to start their program, as these activities required more time than expected.

FMI usually selected grantees that were among the farthest along in developing responses to foreclosed properties in their neighborhoods. While “farthest along” was in most instances not terribly far, as Living Cities recognized, this choice made for a better chance of programmatic launch and at least some production in the near term than an alternative of seeking to create activity where it had not yet been locally generated. Faced with a sudden emergency and looking for quick action, grantees with an at least partial existing capacity to respond were presumed to have an advantage in moving forward.

[5] These were originally constructed as three-family homes; current owners often rent a portion of the home to generate income that is used to help pay the mortgage on the property.

A major factor that influenced the ability of an FMI grantee to establish partnerships was the organization's existing relationships within its local community development context. For example, Twin Cities LISC was a participant in the Minnesota Foreclosure Partners Council, which was formed in late 2006 to bring together key institutions to coordinate efforts to address foreclosures in the Twin Cities and the state of Minnesota. The council is an example of a strong collaborative culture of community development stakeholders in the Twin Cities. In addition, investors committed $16 million of capital for acquisition and rehabilitation of foreclosed homes in the Twin Cities even before Twin Cities LISC received its FMI award. Therefore, because the FMI grant was made in an environment in which stakeholders were working together to address the problems associated with concentrations of foreclosed homes, implementation proved relatively straightforward.

Having the appropriate state and local governments on board for the FMI-supported grantees and program strategies was also an important contributor to the early accomplishments and augured well for future production. In Massachusetts and Chicago, state and local government both participated in designating MHIC and Mercy Portfolio Services to lead the efforts supported by Living Cities and allocated major shares of NSP funding to them. The New York City effort also involved local government and an allocation of NSP resources from the start. Potential for moving production to scale seems lower in Los Angeles, however, where the Living Cities–supported Neighborhood Housing Services, Inc. lacks tight connections with the mayor and where the city allocated NSP funds in other directions.

Indeed, finding situations in which all the key and necessary players are at the table together is an important part of raising the chances of success. Those players include not only the kinds of organizations FMI supported directly and city or state government but also other local funders (private philanthropy and public agencies), lenders, investors in potential foreclosure responses, developers (both CDCs and for-profit), and representatives of the neighborhood (homeowners, borrowers, and consumers). The Massachusetts task force formed with the support of the governor and other important players is a prime example of community collaboration, identifying strategic and programmatic directions and allocating responsibilities by consensus. In Detroit, where many of the key actors were initially *not* talking with each other, Living Cities wisely supported a new foreclosure-focused institution and its efforts to bring all the players together. It also gave Detroit a different scope-of-work sequence and timeline for its grant to allow discussion and then collaboration before action was expected.

The FMI pilot sites have in general been able to select a primary strategy and program direction at an early stage in their work and to stick with their primary thrust in the face of significant obstacles. Bringing the multiple players to the table at the start and receiving imprimatur from state and local government in many cases are important contributors to identifying one approach promptly and maintaining stable direction.

FMI appears to have been successful in identifying lead nonprofits as its grantees, which are in the main competent, with skilled and experienced staff. Given the many difficult challenges facing the start-up efforts, including creating new systems of operation and adjusting to external factors beyond their control, that competence and experience in similar, related work are critical, as is so frequently the case in other initiatives. In our review to date, the lead nonprofits seem to have connected with strong partners: CDCs (and in some cases for-profits) with a good history in affordable housing that can adapt that experience and skill to the foreclosure responses.

Early grant dollars from FMI appeared to play important roles in success in at least two ways: (1) paying for staff at various levels (intermediary grantees, CDCs) to carry out the detailed design and early testing of the local initiatives; and (2) providing risk reduction for other investors and lenders in loan pools for acquisition, rehabilitation, and resale. We return to the issue of the value of FMI resources in a bit more detail in question 8 below. In addition to grant dollars, participants from the various state and local efforts also seemed to appreciate the "community of interest" that FMI-sponsored meetings provided, as they faced down new and difficult challenges. Early local dollars appeared to play important roles in some cases, including as replacements for stalled NSP dollars, as discussed further in question 3.

3. Major obstacles to successful implementation and potential and known solutions

Delays in receiving federal NSP money, challenges in closing on other financing, and the inability to purchase homes from servicers easily and especially in bulk are the biggest obstacles the FMI grantees face. These challenges delayed implementation at nearly every site, and there is little that FMI grantees could do to overcome these challenges other than seek alternative sources of funding and acquire individual properties on the open market rather than through bulk sales.

The FMI initiative was created with the assumption that grantees would have access to some form of federal program (such as NSP) funding. Although NSP-1 awards were made to all jurisdictions in which FMI grantees operate, little NSP-1 funding has been made available within these areas. For example, Minneapolis selected nine CDCs to receive a total of $6.5 million in grants that the organizations can use for acquisition and rehabilitation of foreclosed properties. As of September 2009, none of the nine CDCs had received their grant, and the organizations are hesitant to start acquisitions until they have formal award agreements with the city. The problem was acute in Chicago, where the FMI program is supposed to administer all NSP-1 funds. Until very recently, because these funds had yet to be disbursed, the FMI grantee could not begin acquisition activities.

In some instances, other players have stepped in with their own resources to get programs moving before the release of NSP funds. In Massachusetts, a commitment of state subsidy funds gave partners the confidence to make some initial acquisitions; and CDCs and for-profit developers advanced their own capital for some purchases and rehabilitation. But these stopgaps had inherent constraints on their scalability. And as restrictive rules emerged for NSP and players became less certain that their properties and work would ultimately be eligible for federal program subsidy, early action slowed until NSP-1 funding was available.

In addition to a lack of NSP funding, many grantees have been unable to close on other sources of financing, or it has taken longer than expected to finalize funding agreements. As discussed earlier, City First Enterprises in Washington, D.C., will likely be unable to raise capital from its allocation of new market tax credits, and NPI in Cleveland took nearly a year to negotiate with funders to establish a $6 million pool for acquisition and rehabilitation of foreclosed properties.

Most of the FMI grantees expected to acquire properties in bulk from servicers, lenders, Fannie Mae, or Freddie Mac. Grantees that started negotiations on multiproperty purchases quickly discovered that servicers were unreceptive to such sales. They had to purchase homes through other channels, generally by private market transactions. In Cleveland, for example, Opportunity Homes is purchasing about a third of its homes by looking at properties on the multiple listing service (MLS). In the Twin Cities, DBNHS and GMHC both thought they could acquire homes through bulk purchases. Because their initial negotiations with servicers did not succeed, they began to acquire properties through private purchases.

To make such acquisitions easier, DBNHS and GMHC participated in a pilot of the NCST. Under NCST, participating loan servicers have zip codes of coverage areas in St. Paul and Minneapolis. (There are between four and five such zip codes in each city.) DBNHS and GMHC receive notifications each day of REO homes within these zip codes, getting, in theory at least, a first look before the properties are available to other potential buyers. The organizations have one day to review the list and tell the servicer whether they want to consider purchasing the properties. The homes must be screened carefully. In some cases, for example, the properties are condominiums and are thus not appropriate as a redevelopment target.

DBNHS and GMHC have five days to request a servicer to appraise a property. Once the request is made, servicers engage an appraiser, who determines the property’s market value. The appraisal process can take anywhere from a week to a month. Once the appraised price is provided to the servicer, the servicer can offer a price to the CDC. In general, servicers initially set prices 25 percent below the appraised value, but the discount now is much less, requiring a higher share of funds be used for property acquisition. Once the price is set by the servicer, DBNHS and GMHC have the option to purchase the property.

Since the program began, DBNHS and GMHC combined have requested pricing information for about 1,200 properties and have purchased 180. The remaining properties were not purchased because they were not located in strategic parts of the organization’s impact area or because there were insufficient gap funds available to make the rehabilitation feasible. Of the 90 homes purchased by each organization, the majority were to be demolished, while about 30 percent were to be rehabilitated and then resold. On average, the total development costs for these properties are estimated between $180,000 and $200,000, and they are expected to be resold for between $150,000 and $160,000**.**

NCST provides a promising model that could help other FMI grantees acquire properties more efficiently and for less than if they purchased foreclosed homes on the open market. In particular, NCST negotiates with servicers so that individual organizations do not have to invest resources in these activities. Furthermore, because NCST is a national organization with more visibility than local entities, it is likely to have more success in working with servicers to make properties available to nonprofits before they are offered to the general public. Nonetheless, based on early experience the set of properties flowing into NCST has been limited so far, with only some lenders and servicers participating and securitized loans not generally flowing through the program. As a result, many FMI grantees are likely to continue to try to acquire properties through other means and on a one-by-one basis.

Aside from cooperation from servicers, acquisition has also lagged as a result of competition for properties in stronger markets. In the Boston area, for example, it has been very difficult for the CDCs to acquire even homes in poor condition in weaker-market neighborhoods. Apparently, speculators anticipating a return to significant home appreciation and owners intending to leave properties in poor condition are outbidding CDCs for properties at prices that do not work out for a strategy of acquisition, rehabilitation, and rental or resale. (Our final report, incorporating the specific lessons from our Massachusetts site visit, will expand on the actions being taken there to deal with this central issue.) In New York, few properties are available as REOs at all. The Center for New York City Neighborhoods effort is therefore centered more on short-sale opportunities designed to increase local homeownership, competing with potential landlord purchasers through the center's new mission-oriented broker system.

4. *Effect of the initiative on federal funding and the effect of federal funding on the initiative*

This section summarizes our assessment of the potential effects of FMI on the use of federal funds for responding to the national foreclosure crisis, as well as the impact of the availability of HUD NSP dollars on the FMI program itself. FMI was developed at a time when national policymakers were formulating responses to the emerging foreclosure crisis. As a result, one of the objectives of FMI was to inform policy discussions about potential federal programs that could be initiated to ameliorate the problems resulting from the spike in foreclosures. At a more local level, FMI was meant to demonstrate models that could be replicated or expanded once federal funds were allocated under what became NSP.

Based on the informant interviews completed to date, opinions about the impact of FMI on the larger national debate on the federal response to the foreclosure crisis appear to be mixed.[6] Some informants

[6] We will be able to provide a more thorough analysis of this question in the final report, once we have completed all our key informant interviews and case studies.

suggested that FMI has helped raise the visibility of the need for federal support of the acquisition, rehabilitation, and resale of REO properties. According to these key informants, the federal response to the foreclosure crisis initially concentrated too much attention on facilitating loan modifications that would, presumably, help prevent foreclosures. However, this strategy did not address the problems associated with properties that did go into foreclosure, including negative effects on the neighborhoods in which such properties are located. As a result, FMI, by targeting its activities on REO properties, may have sharpened the focus of the debate on a broader range of policy interventions.

Other informants, however, suggested that FMI's effect on larger policy decisions was relatively modest. According to these observers, FMI could have had a larger impact if the grantees had made better progress in establishing their programs so that they could demonstrate successful approaches., given the previously-discussed difficulties with rapid program start-up experienced by many FMI grantees, particularly those undertaking more innovative approaches, the policymaking window closed before the lessons learned from FMI grantees could be used to develop NSP-1 and NSP-2 regulations.

There is more solid evidence that FMI has affected the use of federal funds at the local level in the communities where the program has been operating. One of the early objectives of FMI was to have programs up and running to help direct the use of NSP funds into effective channels and to demonstrate successful programs that could be replicated or scaled up with NSP funds. Most concretely thus far, in a number of cities FMI grantees are employing substantial NSP-1 funds in programs that grants from Living Cities helped them develop. The most obvious case is Chicago, where the city's full NSP-1 grant is being administered and allocated to projects by Mercy Portfolio Services.

The Cleveland FMI program, administered by NPI, directly influenced the proposed NSP-2 proposal submitted by that city. County officials asked NPI staff members to participate in developing the area's NSP-2 grant because local officials viewed the FMI-supported program as a model to be replicated throughout the city. After preliminary discussions, representatives of Cleveland and Cuyahoga County decided to establish a collaborative that would submit an application on behalf of the Cleveland area. In response to the NSP-2 program solicitation request, the Cuyahoga County Land Reutilization Corporation, Cuyahoga County, the city of Cleveland, and the Cuyahoga Metropolitan Housing Authority have submitted a consortium application requesting a total of $74,550,000 of NSP-2 funding to implement a revitalization program aimed at market recovery.

Unlike NSP-1, the consortium proposed to target its NSP-2 funds for activities in 20 Cleveland-area neighborhoods: the six Strategic Investment Initiative (SII) neighborhoods, five suburban areas, and nine additional Cleveland neighborhoods. The proposed program requests funding for the following activities: (1) acquisition-rehabilitation for homeownership (415 units), $24,900,000; (2) demolition (1,000 units), $10,000,000; (3) deconstruction (100 units), $1,500,000; (4) long-term acquisition and stabilization (150 units), $2,250,000; (5) land reutilization (150 units), $1,500,000; (6) homebuyer assistance (415 units), $8,300,000; and (7) rental project development assistance (252 units), $18,645,000. As compared to NSP-

1, which allocated nearly two-thirds of its funding for demolition, only 15 percent of NSP-2 funds are to be used for demolition or deconstruction. Moreover, NPI received just over $1 million from the city of Cleveland's NSP-1 grant to provide gap financing that was required after development costs unexpectedly increased by about $30,000 per unit.

In another example, MHIC in Massachusetts is the lead player in a collaborative application for NSP-2 funds there—one of the two in which the state is participating and the prime proposal for its larger-city targets—an example to which we will return in more detail in our final report. We might see further such models as later grant reporting from grantees unfolds and we complete our site visits.

While the FMI program may have influenced decision-making about the use of NSP program funds, the NSP program, when it was finally authorized, also had important consequences for the progress of FMI. We have already discussed some of these effects in reviewing progress of the local FMI efforts in pursuing its production goals (section 1.b.) and in identifying factors in their success (section 2).

In addition, the biggest single impact of NSP funding to date appears to have been to delay the process of acquisition, rehabilitation, and disposition of foreclosed properties. This outcome has resulted from a combination of factors: delays in final release of funds, changes and uncertainties in the rules for use of NSP money, and NSP rules that make it very difficult to use the funds for some of their intended uses—notably property acquisition. To varying degrees and in different ways, FMI grantees relied on the expected availability of NSP money to make up the difference between the costs of acquisition and rehabilitation in the market on the one hand and the market value of the improved properties in which they had invested on the other. They have had to wait with this gap unfilled. The delay in funding in some cases forced deferral of acquisitions directly. In other cases where federal money was not to be used for acquisition itself, the lack of NSP money nonetheless discouraged acquisitions because grantees and their deals depended on NSP to ensure workable rehabilitation and disposition. And uncertainty and change in the emerging details of NSP made grantees wary of acting without final rules in place. They were concerned that the ultimate program specifications might make some of their early acquisitions or other actions ineligible for eventual NSP aid.

Further, once NSP was fully defined, a number of provisions made it difficult to use the money in some instances. An example is the requirement to contact former tenants of vacant properties. FMI grantees and their partners have spent significant time figuring out how to use NSP-1 funds effectively now that the dollars are flowing. We will expand further on these specific issues in our final report.

Finally, an important part of FMI's strategy was to position grantees so that they could use federal money to take their initiatives to significant scale. This goal seems to have been accomplished to a certain extent with about half the FMI grantees becoming major recipients or users of NSP-1 money. The timing of decisions about NSP-1 seems to suggest that FMI resources were not the only or even the primary factor in causing NSP resources to flow through FMI recipients, but they nonetheless seem to have been a factor. Only recently, with the start of the flow of NSP dollars into actual use, have grantees been able to begin pursuing concretely the objective of scaling up production with NSP funds. As noted earlier, however, in some cities and states FMI grantees have not yet completed—or are just completing—their program development activities, which has meant that they have not previously been fully ready to take advantage of NSP money.

5. The early sense of the impact of this work

In this section, we provide a preliminary assessment of the impact of FMI on the local communities in which the grantees operate. (Later in this report, in response to question 8, we discuss the effect of FMI on Living Cities, with a focus on lessons learned for all philanthropic organizations.) Because most of the grantees have yet to acquire a significant number of properties, it is too early to tell the effects of rehabilitation on the stability within the neighborhoods targeted by FMI grantees. We are just now seeing some examples of acquisitions of key problem properties and small clusters of buildings, including acquisitions in subneighborhoods in which CDCs have made major earlier investments in properties abutting foreclosure sites. These activities are candidates for neighborhood impacts, but it is too soon to see any concrete results.

Living Cities also had an FMI objective of helping create lasting structures to address problems of foreclosures, vacancy, and neighborhood blight and to aim for broader stabilization strategies. It is far too early to determine if the partnerships and other types of relationships established by FMI grantees will endure and help these organizations complete other types of neighborhood stabilization projects once the foreclosure crisis has abated. For example, while the partnership between NPI and the Cleveland Housing Network in Cleveland has benefited both organizations, it is unclear if these two groups will continue to collaborate after completing their FMI activities. Nonetheless, it is likely that some of the organizational relationships formed under FMI will continue. At this point, however, it is not possible to know with certainty which partnerships will sustain activity of this kind over time. We plan to revisit this issue in the final report.

6. Conclusions about what did and did not work

As discussed in this report, although Living Cities selected grantees based partially on their ability to begin activities soon after receiving their award, in reality, some grantees had trouble implementing their activities. In general, having financing already in place made it easier for grantees to begin their operations, and grantees that did not have to establish new partnerships also had an easier time getting started. Twin Cities LISC provides a good example of both factors: the FMI initiative was supported by $16 million available from a loan pool administered by the Home Prosperity Fund (HPF). As a result, Twin Cities LISC could work with the fund to develop a contract-for-deeds mortgage product that allows credit-impaired families to purchase a home with a three-year mortgage that is to be replaced with a new loan as the homeowner's credit improves. Moreover, Twin Cities LISC's FMI program helped support an existing organization, the Minnesota Foreclosure Prevention Council, that was actively engaged in bringing together area wide stakeholders for monthly meetings to discuss potential new initiatives for addressing the foreclosure issue.

In contrast, NPI in Cleveland, which moved quickly to establish its program, could not implement activities before closing on all its financing. Rather than close within an anticipated three-month timeframe, NPI took nearly a year to close on all financing. As a result, even though NPI is a highly capable CDC, with a strong track record of successfully developing housing, it fell behind schedule because it could not meet the goal of closing very rapidly on financing. The problem was especially acute for grantees that sought new sources of financing (City First Enterprises in Washington, D.C.) or whose program relied on a fast disbursement of NSP funds (Mercy Portfolio Services in Chicago and MHIC in Massachusetts). Mercy Portfolio Services established an organizational infrastructure in anticipation of administering $55.2 million of NSP-1 funds allocated to Chicago. Because these funds were not made available until very recently, the grantee could not start acquisition activities. MHIC anticipated that NSP funds would finance homebuyers who would purchase homes acquired and rehabbed by organizations it had funded. Without NSP funding, though, these organizations could not acquire homes because they were unsure whether buyers would qualify for permanent mortgages. As indicated above, delay and uncertainty in NSP funding were key constraints, outside the control of local players; and a central question still outstanding is whether the grantees have now positioned themselves well enough to move rapidly as the NSP-1funds are in fact released—simply because there is such limited experience to date.

7. What we can learn about the role of different players

No one stakeholder has the financing capacity or technical skills to conduct all the activities required for a successful REO property disposition program. As a result, FMI programs are implemented with the assistance of, and in some cases in partnership with, local governments, other nonprofit organizations, lenders, and other service providers. Based on our initial case studies, it appears that where stakeholders in a given area have particular expertise or capacity and can successfully divide tasks among local governments, CDCs, and intermediaries, they create a more effective response than any one organization working on its own. In another preliminary finding, how local or state government decides to interact with the nonprofit actors plays a significant role in the allocation of responsibilities and the success of those arrangements in furthering the local FMI efforts. As we complete our case studies, we will be able to identify specific roles that each stakeholder played in the FMI programs at the local level and draw conclusions about the most appropriate division of labor among stakeholders.

The FMI initiative in the Twin Cities is built on a sophisticated collaborative structure that includes local CDCs, intermediaries, and local governments. The role that each type of organization plays is influenced by local governments' attitudes toward partnering with CDCs. The city of Minneapolis is more willing than the city of St. Paul, for example, to include CDCs in its foreclosure response. As a result, GMHC has received support in its purchase and rehabilitation activities from Minneapolis. In contrast, St. Paul's preference is to conduct its own redevelopment activities, and thus DBNHS and other St. Paul CDCs have received very little support for foreclosure responses.

As detailed in the Cleveland case study, NPI has leveraged the expertise and capacity of service providers to create an effective approach to implementing their FMI program. The program relies on six CDCs to provide "on-the-ground" intelligence about their neighborhoods and exploits the capacity of the Cleveland Housing Network to facilitate scattered-site rehabilitation projects across these neighborhoods. For example, Village Capital, with its strong financial expertise, led the negotiations to put into place a complex financing structure that has four tranches of debt and nearly $4 million of grant funding. Because the city of Cleveland responds to requests for demolition within the program's target areas, it has effectively delegated the responsibility of identifying properties for demolition in those areas to the CDCs that participate in the program.

Overall, the above approach creates synergies in which the whole is greater than the sum of its parts. No one organization could have implemented a $10 million project across six neighborhoods by itself. Recognizing capacity issues, the FMI program in Cleveland allows these organizations to have a larger response to the city's foreclosure crisis.

8. The implications of the Living Cities initiative for the response of philanthropy to crises

The effort of Living Cities to respond to foreclosed properties demonstrated the ability of even a large collaborative of philanthropic actors to identify a crisis, select an aspect on which to focus, devise an approach, and move toward making grants relatively rapidly. In our final report, we will examine the benefits of the specific collaborative approach used by Living Cities. But even with the information collected so far, we see that the board and staff of Living Cities recognized early the critical nature of the foreclosure crisis for its own place-based work and that of the nonprofits they support, generating an initial discussion at the Living Cities board meeting in later 2007. Within 90 days, they scoped out the scale and nature of various needs, the kinds of responses required and those already supported by others, and selected a strategy of aiding the return of foreclosed properties to use. In another 90 days, they finished assembling funds, designed the effort in more detail, identified potential grantees, and soon selected grant recipients.

Being willing to take some risk of failure with investments in nascent local initiatives, without waiting for them to be fully structured or launched in many cases, contributed to the speed of getting assistance into the field as well. Many of the funded proposals were to be driven by partnerships not yet formally created, pursuing new lines of work. Living Cities apparently relied on organizations, people, existing cooperative relationships (in many but not all cases), good ideas, and other signs of potential to select promising efforts often not yet off the ground.

Speed appears to matter very much, at least in the foreclosed properties crisis. Even with the swift action by Living Cities, in some of the 10 markets, speculators and property owners with poor histories of repair and management were actively in the market before FMI grantees could put together all the pieces of their efforts.

When Living Cities started FMI in response to the foreclosure crisis that was devastating many neighborhoods, there were a number of potential tactics for supporting the acquisition and rehabilitation of foreclosed properties. Therefore, rather than be prescriptive, Living Cities decided to fund FMI grants to organizations operating in 10 different cities or states, all of which proposed different approaches to financing and acquiring foreclosed homes and getting them reoccupied. The assumptions underlying these grants were that the recipients could ramp up their activities relatively quickly and demonstrate successful approaches that could be models for other locations. This approach of letting state and local initiatives determine the shape of response within the Living Cities–selected strategy area appears to have been appropriate and successful in generating models that may be scalable in their pilot locations and adaptable to others.

Providing flexible basic grant support for staffing, program development, and other core start-up functions in some pilots and key risk-reduction reserves for investors in others, based on information acquired to date, appears to have made strong contributions to getting pilots up and running. Given our observations so far, there is truth in the words of one of our key informants: “A little bit of well-timed, well-targeted money goes a long way.” A notable example, says another informant, is Chicago. FMI provided money the city lacked to get planning and program development moving. As a result, a single well-respected national nonprofit was chosen to receive all the local NSP-1 money and to set up an initiative targeting the funds to a select set of neighborhoods in a city with a strong tradition of spreading its community development money around widely.

Once the FMI initiative got underway, the grantees and Living Cities staff realized that getting the local programs off the ground was in various ways more complicated than expected. On one front, the financial crisis made it difficult for grantees to close on anticipated sources of financing for foreclosed homes. Given the dynamic nature of this environment, Living Cities was flexible in allowing grantees to pursue other strategies and alternative uses of grant funds. For example, in Cleveland NPI used a portion of its FMI grant to support Village Capital in its efforts to secure the $10 million of financing used in the program and to help two partners complete tax credit projects so that the Ohio Housing Finance Agency would fund its commitments of $1.5 million in gap financing and a $1.0 million compensating-balance loan. This use was not anticipated in NPI’s application but was a critical final component in its efforts to secure all its financing for property acquisition and rehabilitation. In another example, in Massachusetts, MHIC was allowed to lend to a loan fund that financed rehabilitation and repair undertaken under receiverships, outside of the original program design, when stabilizing properties acquired by others out of foreclosure proved an important issue and acquisition of foreclosed properties proved more challenging than expected in the Boston area's competitive market for properties.

In many sites, Living Cities has extended the period of performance, recognizing that grantees may require more time to complete their program production, given changes and unexpected forces acting in financial and housing markets. This is another example of the flexibility of Living Cities in administering the FMI program. The FMI program established quantitative production targets, which, for a variety of reasons discussed above, have not been met. From the start, Living Cities has focused a significant part of its attention not so much on meeting quantitative production goals as on creating new partnerships and relationships that will help stakeholders, over time, create more effective responses to foreclosure-related (and potentially other neighborhood stabilization) issues. It recognized that it had intervened so early in the process of dealing with already foreclosed properties and vacancies that someone still had to figure out how to do the acquisitions, financing, integration of (new) public funds with private resources, and share that experience with others. Production was only one concern from the start, with limited expectations in the 100–200 unit range and certainly not significant relative to the scale of the problem. Especially when circumstances outside of grantees' control delayed action or reduced its short-term scale, Living Cities joined with its grantees in identifying and recognizing the causes and gave grantees room to maneuver on the timing of production.

Thus, the FMI program illustrates a major lesson for philanthropic organizations: a new crisis requires flexibility, especially when no one is certain about the most appropriate response and new practices need design and testing. With its board, Living Cities carefully aired different types of interventions that could be funded and decided on supporting the acquisition and rehabilitation of foreclosed homes. At that point, its willingness to limit initial expectations, absorb some risk of failure, accept unproven and diverse programmatic ideas, learn from experience along with its grantees, and adjust expectations at least in the short run seems, in our observations to this stage, to have matched the crisis circumstances and responses well.

Whether the structures and mechanisms now created to address foreclosed properties will eventually allow and provide for larger-scale activities, now that NSP funds are flowing, remains to be seen; issues persist in many areas, including the specifics of using NSP, competition for acquisitions, transparency, and other aspects of servicer and investor sales, among others. If such progress generally fails to occur, the results would then raise a very challenging question about how to make more accurate early assessment of the nature of crises and the potential for a given set of strategies to succeed. In this case, for example, was there a way to assess the difficulties of acquiring foreclosed properties ahead of time and redirect some strategic attention to its problems through other means? We do not yet know whether that question needs to be addressed or whether local problem-solving and systems design experience with the NCST and other parts of the current initiative will, with a bit more time, make it moot.

Appendix A:
Cleveland Case Study

Cleveland: Neighborhood Progress, Inc.

Introduction

In May 2008, Living Cities awarded a $500,000 Foreclosure Mitigation Initiative (FMI) grant to Neighborhood Progress, Incorporated (NPI), to support an initiative that included three elements: (1) acquisition of foreclosed homes for redevelopment and resale; (2) acquisition of foreclosed homes for demolition; and (3) aggressive marketing of foreclosure-prevention services to help homeowners learn about such services and use them to avoid losing their homes.

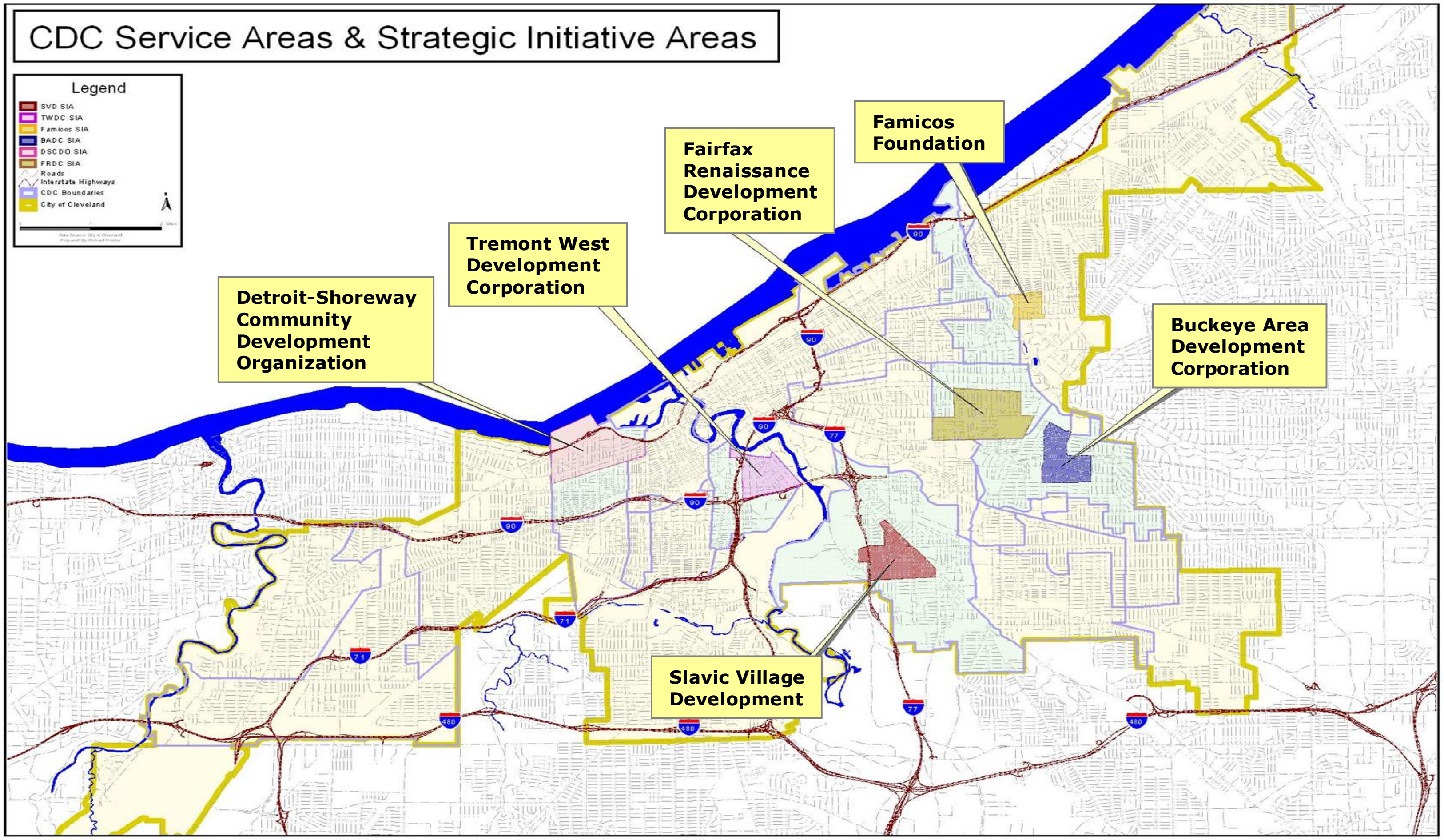
NPI's program builds on its Strategic Investment Initiative (SII), under which NPI selected, in 2005, six community development corporations—Buckeye Area Development Corporation, Tremont West Development Corporation, Famicos Foundation, Fairfax Renaissance Development Corporation, Detroit Shoreway Community Development Corporation, and Slavic Village—to work with so that it could build market value in targeted neighborhoods through comprehensive investment, create "neighborhoods of choice" for current and future residents, and demonstrate significant, measurable increases in population, households, homeownership, housing values, and household income.

Each CDC was selected for the SII because it was a capable organization and as such had a strong track record of development, had identified a large-scale anchor project that was ready for development, and had a clearly articulated vision for its communities. Moreover, in each of the six neighborhoods, the CDC could leverage locational assets (such as cultural and other types of institutions located in the neighborhood) and recent market improvements. The six neighborhoods, then, were not the most distressed areas of Cleveland. Rather, they represented areas that showed evidence of nascent market resurgence, which could be accelerated by the completion of a large anchor project that was ready to be constructed.

The SII areas are smaller than each CDC's coverage area: the SIIs for each of the CDCs typically have between 2,500 and 6,000 residents. Therefore, within this compact area, the anchor project is expected to have a large impact on the quality of the surrounding neighborhood. These anchor projects are not necessarily developed by the CDC within the SII. For example, the anchor project within the Detroit Shoreway CDC's SII is Battery City, a 328-unit, privately funded market-rate housing development located near Lake Eire. (A map showing the location of each SII is presented in figure 1.)

Each of the six CDCs selected model blocks within its SIIs. These areas are very small: in some neighborhoods they constitute a six-square-block area and are typically important

Figure 1: Location of Strategic Investment Initiative Areas



Source: NPI. Used with permission.

entryways into the area that contains the neighborhood's anchor project. For example, the Detroit Shoreway CDC selected model blocks that are just south of the Battery City development.

Residents within model block areas are eligible for programs that provide support to homeowners for repairing and beautifying their homes, including assistance for siding replacement, lawn repair, and other exterior improvements. The key to the model block initiative is that it focuses resources and attention on small areas that are strategically located in a neighborhood's SII.

Consistent with NPI's aim of targeting community development activities in a strategic way, the organization's FMI activities target foreclosure prevention and acquisition, rehabilitation, and demolition activities within relatively small areas that generally overlap with model blocks. Therefore, NPI's initiative recognizes that foreclosure interventions can have the greatest effect on stabilizing a neighborhood when such activities are targeted at a small area with strategic importance to the overall neighborhood quality.

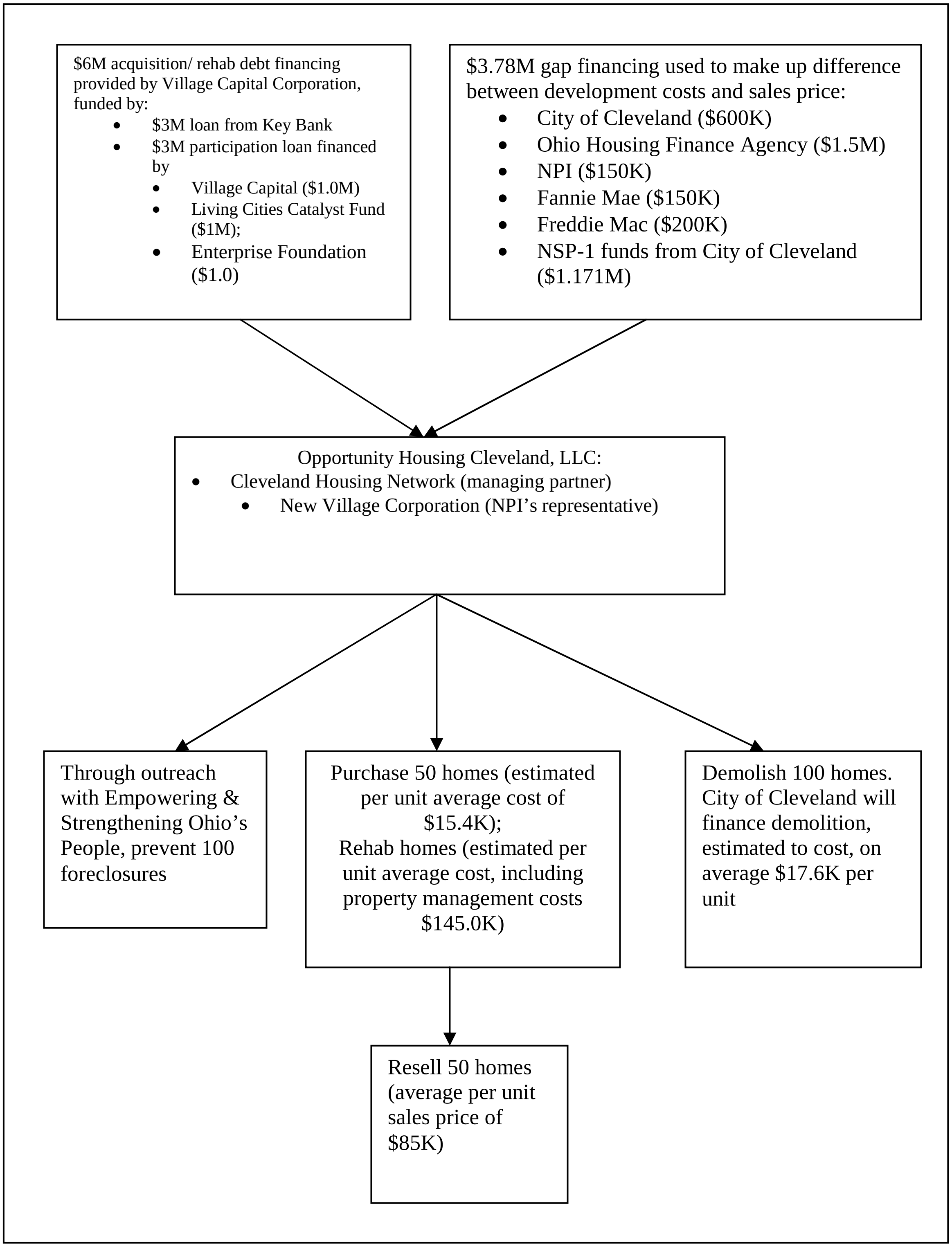
As detailed below, NPI's foreclosure-prevention initiative is operational: the limited liability corporation that administers that program was established in August 2008, and all the acquisition and rehabilitation financing is in place. But the program did not close on all its financing until May 2009, and initial conversations with Fannie Mae on purchasing REO properties did not result in agreements. As a result, the program did not meet its objectives of selling 50 homes, demolishing 100 homes, and preventing 150 foreclosures by the end of the performance period of the Living Cities grant (June 30, 2009). But all the pieces are now in place, and participants expect to reach their production targets within the next 12 months.

1. How the FMI pilots fared against expectations

The following sections describe NPI's progress toward meeting expectations for the implementation and execution of its FMI initiative. As detailed below, the program is behind schedule in meeting its quantitative production objectives but has successfully worked with partners to establish a structure in which all program elements are now underway. Moreover, by targeting foreclosure-prevention and remediation activities strategically, NPI is demonstrating an innovative approach that was the basis of the model included in the NSP-2 application submitted by a collaborative consisting of the city of Cleveland, Cuyahoga County, and the Cuyahoga County Land Bank.

Becoming fully operational and achieving acquisition, rehabilitation, and disposition goals. With its FMI grant, in August 2008 NPI established Opportunity Housing, LLC (also known as Opportunity Homes), which is a single-purpose entity with the Cleveland Housing Network as a managing partner and the New Village Corporation (which is the real estate development subsidiary of NPI) as the other partner. Figure 2 summarizes Opportunity Homes' structure.

Figure 2: Summary of Opportunity Homes' FMI Structure



Source: Author's review of program materials.

Village Capital Corporation, which is the nonprofit lending subsidiary of NPI, manages $6 million of debt financing that can be used for acquisition and rehabilitation of the properties scheduled for resale by Opportunity Homes. The money comes from two sources and is separated into two liens and four tranches (see figure 3):

- Key Bank provided a $3 million first-lien loan that can be used only for construction. The loan has an adjustable rate, which is 300 basis points below prime. The Key Bank loan is first in line to be repaid from the proceeds of sales of rehabilitated homes.

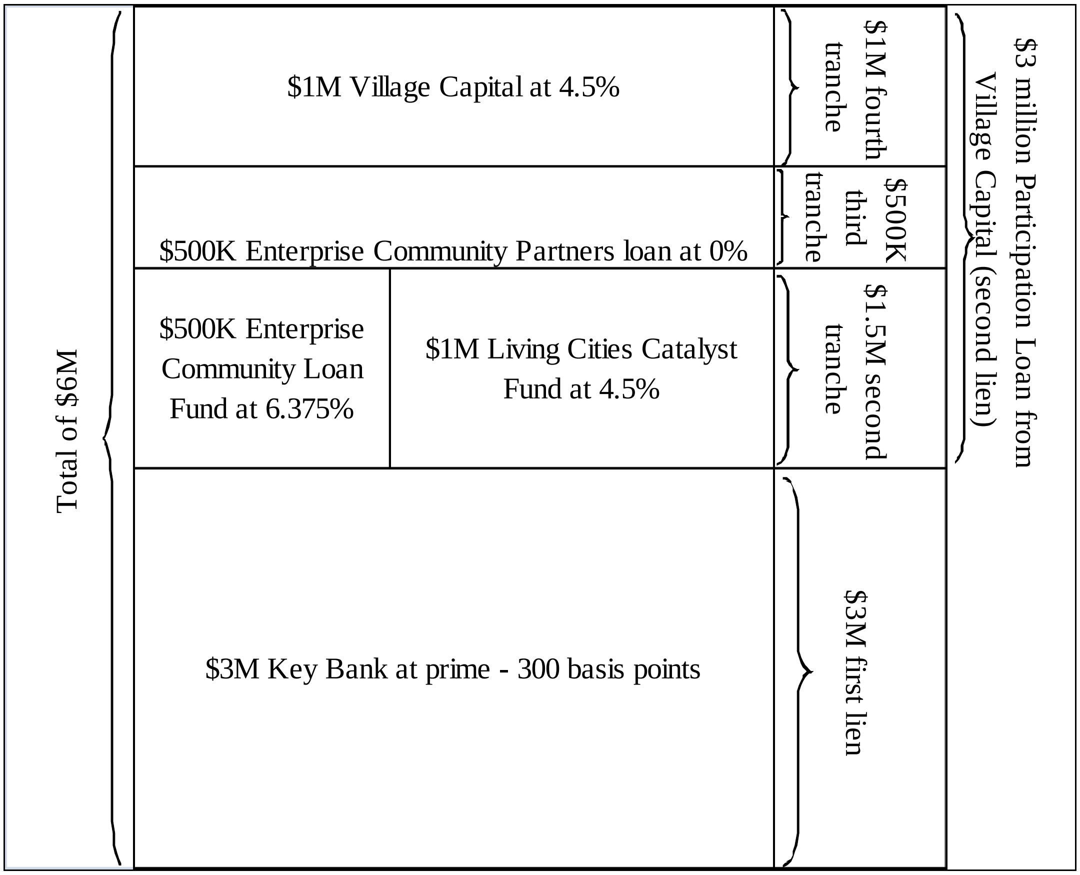
- Village Capital provided a $3 million second-lien participation loan funded by Village Capital ($1 million), the Living Cities Catalyst Fund ($1 million), and the Enterprise Foundation ($500,000 from the Enterprise Community Loan Fund and $500,000 from Enterprise Community Partners). All these loans are subordinate to Key Bank; the loans from the Catalyst Fund loan and Enterprise Community Loan Fund are *parri passu* second in line to be repaid from sales proceeds, and the Enterprise Community Partners Loan is third in line for repayment while the Village Capital loan is fourth in line for repayment.

In addition, Village Capital secured a $1 million compensating-balance loan, with a 0 percent interest rate from the Ohio Housing Finance Agency. The proceeds of this loan are used to purchase a certificate of deposit for Opportunity Homes; the interest earned on the certificate is used to repay the participation loan. As a result, Opportunity Homes pays an effective interest rate of 3.0 percent of funds drawn on the participation loan, rather than Village Capital's cost of capital of about 4.1 percent.

About half ($255,000) the FMI grant is being used as a loan-loss reserve, and another $90,000 of the grant is being used as a debt-service reserve for the $3 million participation loan made by Village Capital that is subordinate to Key Bank's loan. Key Bank, because it has a first lien on the properties financed with the loan and the loan amount is only 50 percent of the total debt structure, did not require a credit enhancement or loan-loss reserve. All the funding for the participation loan would not have been made available, according to NPI staff, without the loan-loss and debt-service reserves funded by the FMI grant. Therefore, the FMI grant was critical for attracting acquisition and construction financing for rehabilitation and demolition. NPI staff said that there were no alternative sources for capitalizing the loan-loss reserve and that they would have been unable to make the initiative work without the FMI grant.

In addition to its debt financing, Opportunity Homes has access to about $3.8 million of grant funds to finance the difference between total development costs for a given home and the sales price paid by the buyer. On average, Opportunity Homes can use its grant funds to reduce the sales price from an estimated total development cost of $162,000 per unit by $77,000 to reach an estimated average per unit resale price of $85,000.

Figure 3: Summary of Opportunity Homes' Acquisition/Construction Debt Structure



Source: Village Capital Corporation. Used with permission.

Note: Interest rates for participation loan do not include reductions resulting from a 0 percent, $1 million compensating-balance loan provided by the Ohio Housing Finance Agency.

Needless to say, the negotiations required to establish a financing structure from five different sources arranged in four tranches were extremely complex and time consuming. Key Bank, for example, initially expressed interest in funding a portion of the participation loan but decided to provide a separate loan, with first-payment priority. In addition, OHFA would not agree to finalize its compensating-balance loan until the Cleveland Housing Network and the Buckeye Area Development Corporation completed open projects that received tax credits from OHFA. Opportunity Homes could not draw on Village Capital's $3 million participation loan until the OHFA compensating-balance agreement was finalized. As a result, Opportunity Homes closed on all of its financing in May 2009, nearly a year later than proposed.

Because Key Bank's loan can be used only for construction, the funds available to Opportunity Homes for acquisition are limited. To resolve the issue, Opportunity Homes used $40,000 of its FMI grant to resolve the outstanding issues with OHFA and closed on this final piece of the financing structure in May 2009. Given the delays in closing on the financing, Opportunity Homes was able to acquire 30 properties by July 31, 2009, which is 60 percent of its goal of 50 homes. But, now that the financing is in place, Opportunity Homes will be able to move quickly and acquire homes to meet the production goal of 50 homes rehabbed and sold.

Opportunity Homes' initiative also includes foreclosure-prevention counseling and demolition. NPI contracted with Empowering & Strengthening Ohio's People, a Cleveland-based organization that works with homeowners and their lenders to obtain affordable resolutions that preserve homeownership. Its staff work with representatives of each of the six CDCs, whose coverage area encompasses the model blocks, to conduct extensive outreach activities that include going door to door.

The demolition component is funded largely by the city of Cleveland. Each of the six CDCs, in conjunction with the Cleveland Housing Network and New Village representatives, identifies properties that are not feasible to rehabilitate because of their condition and rehabilitation costs. New Village staff members send a list of such properties to the city of Cleveland, which then demolishes the property. Once it receives a request for demolition, Cleveland assigns an inspector who determines if the property can be condemned. The city also has to attempt to contact the property's owner. Once the property is condemned and the owner has been contacted (or the city can document its attempts), the city can solicit bids for the demolition. From the time of inspection, it takes at least six months to demolish a property, but the timing can be quicker if the property represents an immediate hazard. Rather than work through the city, NPI staff can file a public nuisance case against the property's owner and obtain an order to demolish the property. This process also takes between six months and a year to complete.

Through July 31, 2009, 52 homes had been demolished within the Opportunity Homes target areas. Forty-four homes had been demolished by the city of Cleveland, 5 were demolished with funds supplied by NPI, and 3 were demolished by private owners. Opportunity Homes proposed to demolish 100 homes within the program's target area. But, given the time it takes to demolish homes (a minimum of roughly six months to a year) it is not surprising that the program is behind schedule. As with the acquisition part of the initiative, NPI staff expect to be able to meet the production target within 12 months, as staff from each of the six CDCs participating in the initiative continue to identify homes for demolition. Opportunity Homes, began its joint outreach activities conducted by Empowering & Strengthening Ohio's People (ESOP) and the CDC that operates within the neighborhood in which the outreach activities take place in December 2008. As part of the outreach, every month the CDC that ESOP works with mails a flyer explaining that a representative of ESOP and the local CDC will distribute information on counseling services offered by ESOP to all addresses within the CDC's SII. In addition, for each parcel within the target area Case Western Reserve uses data to identify whether there is a mortgage on the property with an adjustable rate loan, a high-cost loan, or a loan originated by a subprime lender or whether the property is currently in foreclosure. A week after sending the mailing, a number of two-person teams that consist of an ESOP and a CDC representative go "door knocking." Each two-person team typically knocks on 30–60 doors within a two-hour window. The team will ask the homeowner about his or her mortgage and, if the homeowner wants to attend a counseling session, the team can set up an appointment that takes place at the CDC location.

Opportunity Homes projected that 100 foreclosures would thereby be averted within the initiative's target area. Through July 31, 2009, 18 foreclosures had been averted—meaning that a homeowner in danger of being in foreclosure became current on his or her mortgage. The reason for the relatively small number, compared to the projection, is that the outreach activity started only in December. Therefore, as more outreach is conducted, NPI staff members expect to be able to prevent 100 foreclosures within the Opportunity Homes target area.

Testing innovative approaches to foreclosure mitigation. The approach used by Opportunity Homes to mitigate foreclosures has three innovative features:

- A "division of labor" between CDCs operates within each Opportunity Homes coverage area—the Cleveland Housing Network, which is responsible for rehabilitation, and New Village, which acts as NPI's representative on all program activities—that leverages the capabilities of each partner to increase the overall effectiveness of the initiative.

- All the organizations providing services use data analyzed at the parcel level to assist in decision making so that activities are conducted strategically.

- The targeted area is relatively small, so that activities have a better chance of stabilizing the neighborhood immediately surrounding the target area.

Although the program has just started with its full financing, all the participants interviewed for the case study indicated that the initiative is benefiting from each innovative feature. The division of labor is one of the most compelling aspects of NPI's program. According to NPI staff, the organization did not have much expertise in completing in-fill or rehabilitation development. The SII's main features are to construct new housing and to support large-scale new anchor development projects. As a result, NPI did not want to be responsible for developing properties for rehabilitation and sought a partner that had such expertise. The Cleveland Housing Network, however, had extensive experience in in-fill development, particularly through its scattered-site low-income tax credit (LIHTC) program. The network, though, did not concentrate its activities in any one area of Cleveland and thus did not have a track record of completing projects in an area targeted for more comprehensive community development services.

Once the foreclosure crisis hit Cleveland in late 2006 and in 2007, both NPI and the Cleveland Housing Network realized that continued development of new construction projects made little sense. As a result, each organization sought the other out for potential collaboration. In particular, NPI asked the network to review a potential lease-purchase program that it was developing; it reviewed the proposed model, provided comments, and, based on this initial contact, worked with NPI to develop the FMI grant application.

In addition to NPI and the Cleveland Housing Network, the six CDCs that receive funds through the SII play an important role in the FMI program. Each of the CDCs has staff members who are very familiar with their neighborhood conditions and also have been working in the model block areas for the past four or five years under SII. As a result, the CDC staff members, using parcel-level maps provided by Case Western Reserve University, identify the best properties for potential rehabilitation or demolition. In effect, the CDCs are the "eyes and ears" for Opportunity Homes. The CDCs will then work with the network and NPI to determine if it is financially feasible to rehabilitation potential target property.

Once a property has been selected for demolition or rehabilitation, the CDC does not have to raise funds or manage the rehabilitation of the property. In some cases, a CDC will purchase a property (NPI makes available about $150,000 to each CDC for acquisition), but the CDC will sell these properties soon thereafter to Opportunity Homes. Thus, the CDCs face very little (if any) financial exposure to construction delays. The Cleveland Housing Network, being a seasoned developer, has the expertise and capacity to manage several scattered-site development projects, which makes it possible to rehabilitate more properties than if the six CDCs were responsible for rehabbing properties themselves, with funding from Village Capital. As one CDC director interviewed for this case study pointed out, the CDC would be able to manage only three or four rehabs per year, but now there can be as many as 20 units rehabbed within the CDC's area per year because of the network's capacity to manage multiple rehabilitation projects simultaneously.

The FMI initiative in Cleveland uses data in making a range of decisions but, in particular, to determine which parcels are at risk of foreclosure. The data are collected and available from the Northeast Ohio Community and Neighborhood Data for Organizing (NEO CANDO), which is a social and economic data system of the Center on Urban Poverty and Community Development, a research institute housed at Case

Western Reserve University's Mandel School of Applied Social Sciences. NEO CANDO allows users to access data for the entire 17-county northeast Ohio region or for specific neighborhoods within Cleveland. NPI has contracted with Case Western Reserve to conduct data analysis, which includes generating parcel-level maps of each SII. In these maps, the Opportunity Homes target area is shown so that team members can identify, visually, which parcels are either in foreclosure or in danger of going into foreclosure. This information supplements the "on-the-ground" information collected by CDCs through neighborhood meetings and by walking around the neighborhoods.

The third innovative feature of the FMI program in Cleveland is that services are targeted at very small areas. As discussed earlier, most Opportunity Homes target areas are the same as the model blocks. These areas are usually between 6 and 10 square blocks. Such an approach is consistent with NPI's general community development approach of concentrating comprehensive services in discrete target areas. Indeed, the SII is focused on six Cleveland neighborhoods, and the organization provides support to another eight CDCs in the city.

While it is too early to determine if the FMI program created its intended effect of helping stabilize the target areas, concentrating foreclosure-mitigation services in smaller areas is included in the NSP-2 application submitted by a consortium that consists of the Cuyahoga County Land Reutilization Corporation, Cuyahoga County, the city of Cleveland, and the Cuyahoga Metropolitan Housing Authority. This application requests $74.6 million in NSP-2 funds to provide foreclosure-mitigation services in 20 neighborhoods, including all six SII areas. This approach is different from the NSP-1 funds, which are not geographically targeted within Cleveland. Therefore, the FMI initiative has had an effect on how local policymakers view the best way to allocate foreclosure-mitigation funds even though it has just begun its property acquisition and rehabilitation activities.

2. Factors that influenced success

Cleveland's FMI program is a $10 million effort that involves a number of organizations so that effective foreclosure-mitigation services can be provided to six target neighborhoods within Cleveland. In some cases, the organizations providing services had not formally worked together before. Yet, within a year of receiving its grant, NPI was able to establish a new limited liability company, raise $10 million of funding, and begin rehabilitation, demolition, and foreclosure-prevention counseling services.

The main factor that led to this success is that NPI did not start this work from scratch. Cleveland is well known for its sophisticated community development infrastructure. As a result, all the organizations knew one another, even if they had not formally worked together on specific projects. This made it relatively straightforward for each organization to participate in the initiative, although not without the inevitable problems that arise from establishing new partnerships.

In addition, the FMI initiative in Cleveland builds on an existing program—the SII and model blocks—that targets neighborhoods for comprehensive community development activities. Therefore, NPI had the infrastructure in place (data analysis and CDC partners) to implement a spatially targeted foreclosure-mitigation program.

3. Major obstacles to successful implementation and potential and known solutions

The Cleveland FMI program, based on its proposed quantitative production numbers, is behind schedule. Three major obstacles delayed the program: (1) the expected sources of properties (bulk sales from servicers) did not materialize; (2) it took longer to finalize the $10 million in funding required to finance the program; and (3) actual rehabilitation costs are running at $33,000 more per unit than anticipated. In response to these challenges, Opportunity Homes began purchasing a greater number of homes on the open market and secured more gap financing (primarily from Cleveland's NSP-1 grant) to provide for the higher-than-anticipated construction costs. As discussed earlier, Village Capital successfully negotiated the terms of all debt-financing sources available to Opportunity Homes by being flexible and accommodating each funder's preferences for lien and repayment positions.

NPI originally expected to acquire a relatively large number of properties through bulk-purchase agreements with large servicers or Fannie Mae. These negotiations did not go anywhere, and the initiative had to seek alternative sources for properties. Representatives of the Cleveland Housing Network estimate that the properties acquired to date come equally from three sources: purchases of homes that are listed on MLS, homes recommended from the six CDCs that operate within the program's target areas, and homes acquired from either HUD or Fannie Mae.

Some key informants indicated that they expected a larger share of homes to be acquired from recommendations made by CDCs. This channel, however, has not produced as many potential acquisition recommendations as originally envisioned, in part because some CDCs have been relatively slow in identifying such properties. As a result, Opportunity Homes partners have looked to MLS listings to find potential acquisitions located within the target areas. This strategy has proven effective.

In addition, Opportunity Homes has established relationships with some servicers, typically those with agreements with ESOP. Through these relationships, Opportunity Homes has been able to increase the number of REO homes purchased from servicers before they are listed for sale. Consequently, these homes can sometimes be acquired for relatively lower prices.

Some of the homes purchased under the initiative have asbestos. The Ohio Housing Finance Agency (OHFA), as a condition of its funding, is now requiring that asbestos be removed from all homes. A lower-cost alternative remediation strategy would be to place drywall around the affected areas. OHFA has rejected such an approach, and removing asbestos added about $10,000, on average, to per unit construction costs. In addition, costs for materials are also higher than originally anticipated. In all, total average rehabilitation costs are $33,000 per unit higher than expected. To fund this difference, Opportunity Homes secured $1.17 million from Cleveland's NSP-1 grant. This allocation represents about half the city's NSP-1 funds available for rehabilitation (most of the city's NSP-1 funds are targeted for demolition). The remaining funds required to finance the gap are from grants provided by Fannie Mae and Freddie Mac.

4. *The effect of the initiative on the flow of the Neighborhood Stabilization Program and other federal funds*

The city of Cleveland, under NSP-1, was awarded $9.4 million but received an additional $16 million from the state of Ohio, which recognized that the city's award was too small. The city allocated $14.5 million of the total $25.4 million (65 percent) for demolition of 1,700 homes (Cleveland estimates, as of 2009, that there are 8,000 vacant homes in Cleveland that should be demolished) that are located in neighborhoods with the greatest need and with a median household income of less than 120 percent of area median income. The FMI program influences how some of the NSP-1 demolition funding is spent. As discussed earlier, CDCs, working with Cleveland Housing Network and NPI, identify homes in their respective Opportunity Homes target areas that cannot be rehabbed and need to be demolished.

About $9 million in NSP-1 funding will also be used to assist developers in acquiring and reselling 160 units (as discussed above, Village Capital received $1.171 million for gap financing to support the FMI program). The remaining funds are to be used for program support and to update data systems that provide information about abandoned properties.

NPI did not play a role in developing the list of activities funded by NSP-1, which emphasizes demolition over rehabilitation and does not target specific neighborhoods in Cleveland. In contrast, NPI staff members were asked by county officials to participate in developing the area's NSP-2 grant because local officials viewed the FMI program as a model to be replicated throughout the city. After preliminary discussions, representatives of the city of Cleveland and Cuyahoga County decided to establish a collaborative that would submit an application on behalf of the Cleveland area.

In response to the NSP-2 program, the Cuyahoga County Land Reutilization Corporation, Cuyahoga County, the city of Cleveland, and the Cuyahoga Metropolitan Housing Authority have submitted a consortium application requesting a total of $74,550,000 of NSP-2 funding to implement a revitalization program aimed at market recovery. Unlike NSP-1, the consortium proposed to target its NSP-2 funds on activities in 20 Cleveland-area neighborhoods: the six SII neighborhoods, five suburban areas, and nine additional Cleveland neighborhoods. The proposed program requests funding for the following activities: (1) acquisition-rehabilitation for homeownership (415 units, $24,900,000); (2) demolition (1,000 units, $10,000,000); (3) deconstruction (100 units, $1,500,000); (4) tong-term acquisition/stabilization (150 units, $2,250,000); (5) land reutilization (150 units, $1,500,000); (6) homebuyer assistance (415 units, $8,300,000); and (7) rental project development assistance (252 units, $18,645,000). As compared to NSP-1, which allocated nearly two-thirds of its funding for demolition, only 15 percent of NSP-2 funds are to be used for demolition or deconstruction.

5. The early sense of the impact of this work

Because the FMI program in Cleveland has just started its production, it is too early to determine the effects of its concentrated rehabilitation, demolition, and foreclosure-counseling activities. Its main effect, to date, is the deepened relationships among the service providers (Cleveland Housing Network, NPI, and ESOP) that may be leveraged for future community development activities. Indeed, NPI may use these partners to provide services under NSP-2 that will provide the Cleveland area three times the funding of NSP-1.

In addition, the program (as detailed above) demonstrated a foreclosure intervention approach that was the basis of the Cleveland area's NSP-2 application. In this sense, local officials viewed the program as a success even before it started to produce outcomes: the overall logic of concentrating services in specific neighborhoods was compelling enough to serve as a model of the proposed NSP-2 program.

6. Conclusions about what did and did not work

Although the Cleveland FMI program has just started production, there are some lessons learned for other foreclosure-mitigation programs. In particular, using large servicers as a source of bulk sales is a risky strategy, as these organizations did not follow through with early promises of participating in such transactions. As a result, the program had to use other sources to identify properties for sale, including MLS listings.

In contrast, dividing up the responsibilities for program activities among a set of capable organizations appears to be an extremely effective approach. Some participants indicated that, when more than one organization had a particular expertise in a given area, there were some challenges in establishing which organization would have the lead responsibility. But, after nearly a year, these problems have been ironed out, and all the service providers indicate they have good working relationships with one another.

7. What we can learn about the role of different players

As discussed throughout this case study, the NPI program in Cleveland has a division of labor among service providers, which has been an effective approach to implementing the program. The program relies on six CDCs to provide on-the-ground intelligence about their neighborhoods and then leverages the capacity of Cleveland Housing Network to facilitate scattered-site rehabilitation projects across these neighborhoods. Village Capital, with its strong financial expertise, led the negotiations for putting into place a complex financing structure that has four tranches of debt and nearly $4 million of grant funding. Because the city of Cleveland responds to requests for demolition within the program's target areas, it has effectively delegated the responsibility for identifying properties for demolition in these areas to the CDCs that participate in the program.

Overall, this approach creates synergies in which the whole is greater than the sum of its parts. No one organization could have implemented a $10 million project across six neighborhoods by itself. Recognizing capacity issues, the FMI program in Cleveland allows these organizations to have a larger response to the city's foreclosure crisis.

8. *The implications of the Living Cities initiative for the response of philanthropy to crises*

As discussed earlier, the majority of FMI funds awarded to NPI were used to fund loan-loss and debt-service reserves for Village Capital's $3 million participation loan. According to informants, there were no alternative sources of funding for these reserves, and without the grant the participants would not have agreed to fund the loan. Moreover, Key Bank would have been unlikely to have provided its $3 million loan without the second-lien participation loan.

In addition to funding the reserves, the FMI grant was used to support Village Capital in its efforts to secure the $10 million of financing used in the program and to help two partners complete tax credit projects so that OHFA would fund its commitments of $1.5 million of gap financing and a $1.0 million compensating-balance loan.

The key here is that Living Cities allowed its FMI grant to be used for a range of activities and allowed NPI to determine how to use the grant. The application discussed using the grant for reserves and administrative support but not to assist partners in closing outstanding tax credit transactions. Because Living Cities was flexible, NPI could respond to funders' requests and close on all financing within nine months of the program's start.

In addition to its flexibility, the FMI grant, according to informants, was first-in money that allowed NPI to craft a response to Cleveland's foreclosure crisis. Some people interviewed said that they were like a "deer in the headlights" when foreclosures started to multiply in the city, beginning in 2006. Both the Cleveland Housing Network and NPI were producing new housing and in response to the crisis had to shift their activities to in-fill rehabilitation. The grant from Living Cities, because it was made in May 2008, came early enough to allow these organizations to shift their focus but also to change strategies as needed.

Consequently, a critical lesson for the philanthropy community is that early responses will likely require revisions over time, as market conditions change, potential funders change their minds, and market conditions change. Therefore, funders should allow their grantees to make midcourse corrections so that they can implement solutions to problems as they arise. For example, rather than demand that NPI pursue bulk-sale agreements, LC allowed Opportunity Homes to identify alternative sources of properties for acquisition. Without such approval, Opportunity Homes would not have been able to make any acquisitions and would be even further behind schedule.

Interviews Conducted, September 2–3, 2009:

Eric Hodderson, NPI
Linda Warren, Village Capital
Bobbi Reichtell, NPI
Walter Wright, NPI
Frank Ford, NPI
Daryl Rush, City of Cleveland
Ron O'Leary, City of Cleveland
Marie Kitteridge, Slavic Village Development Corporation
Rob Curry, Cleveland Housing Network
Jeff Ramsey, Detroit Shoreway Community Development Organization
Matt Laska, Detroit Shoreway Community Development Organization
Vickie Johnson, Fairfax Renaissance Development Corporation
John Anoliefo, Famicos Foundation
John Hopkins, Buckeye Area Development Corporation

Appendix B:
Twin Cities Case Study

Twin Cities LISC: Minnesota Foreclosure Partners Council

Introduction

Twin Cities Local Initiatives Support Corporation (LISC) received a $500,000 Foreclosure Mitigation Initiative (FMI) grant from Living Cities in July 2008; the grant's performance period ended June 30, 2009. Twin Cities is administering the grant on behalf of the Minnesota Foreclosure Partners Council, which was formed in late 2006 to bring together key institutions to coordinate efforts to address foreclosures in the Twin Cities and the state of Minnesota.

The FMI grant was awarded to fund three activities: (1) on-going coordination of the council; (2) investment in the Home Prosperity Fund (HPF) for the design and launch of pilot financing initiatives; and (3) the design and support of acquisition and disposition strategies. As detailed below, all three activities have been successfully completed. The FMI award allowed the council to fund a staff person to coordinate monthly meetings, design agendas, and prepare minutes and other follow-up materials for each meeting.

The FMI grant was also used to design and implement acquisition and disposition strategies. As a result, two CDCs—Dayton's Bluff Neighborhood Housing Services (DBNHS) and the Greater Metropolitan Housing Corporation (GMHC)—were selected as prepilot sites for the National Community Stabilization Trust (NCST), under which DBNHS and GMHC receive information about foreclosed homes that are available for purchase in each organization's coverage area. Both DBNHS and GMHC can evaluate these properties and decide whether to purchase them before the homes are available for sale to the general public.

The largest share of the FMI grant ($375,000, or 75 percent) was used to provide a loan-loss reserve for a new loan product that provides a second mortgage for buyers, the contract-for-deeds program. As detailed below, the program is similar to a lease-purchase option: the buyer receives a first mortgage and uses the contract-for-deeds mortgage to finance no more than 20 percent of the purchase price. A private lender (University National Bank) provides a first-lien mortgage for no more than 80 percent of the purchase price. Within three years, the buyer must pay off the existing mortgages with a new loan. Buyers under the contract-for-deeds program have slightly damaged credit and cannot qualify for a mortgage at the time that they purchase the home. The expectation is that, after three years, the owner's credit will be repaired so that he or she can receive a new loan and pay off the existing mortgages.

The informants interviewed for this case study said that the FMI grant provided a critical source of financing for each of the three activities that could not have been funded with other sources of money. Moreover, the grant was made at a critical time: stakeholders in the Twin Cities area were formulating responses to the local foreclosure crisis that, in 2007, resulted in 4,700 foreclosures combined in Minneapolis and St. Paul.

1. How the FMI pilots fared against expectations

Twin Cities LISC met each of the three objectives that it set forth in its grant agreement with Living Cities. As detailed below, the council has met monthly; the staff person funded with the grant has been able to coordinate these meetings, which provide a unique forum for area wide stakeholders to meet and discuss potential responses to the area's foreclosure crisis. The FMI grant has supported two acquisition and disposition initiatives: (1) two local CDCs (DBNHS and GMHC) participated in the prepilot NCST program that makes it easier for developers to purchase homes held by servicers as a result of a foreclosure; and (2) the Twin Cities Community Land Bank, a nonprofit LLC made up of multiple public and private partners that will assemble, manage, and dispose of property and vacant land for the purpose of stabilizing neighborhoods and encouraging reuse or redevelopment of urban properties. Finally, the FMI grant was used to establish a loan-loss reserve that was used to support the contract for deeds program, under which homebuyers can live in a home and have three years to qualify for a mortgage to purchase the property.

Becoming fully operational and achieving acquisition, rehabilitation, and disposition goals. The Twin Cities LISC initiative did not require the establishment of any new organizational entities. Rather, the program built on an existing foundation of collaborative relationships among regional community development stakeholders. The council was established in January 2007, well before Twin Cities LISC received its FMI grant. The council was initially supported by funding from the Family Housing Fund and focused on collecting and analyzing data that could inform responses to the area's foreclosure crisis. The FMI grant was used to fill a staff position for coordinating council activities, including monthly meetings.

According to key informants, the council provides a unique forum for area wide stakeholders to meet and discuss potential responses because it is not a governmental agency nor is does it have a limited geographic coverage. The council's focus has changed over time, from its initial focus on foreclosure prevention to an emphasis on identifying potential options for acquiring and disposing of foreclosed homes.

One of the main benefits of the council is that members can explore potential solutions together. For example, some stakeholders expressed an interest in establishing a land bank based on one in Genesee County, Michigan. The council invited a representative of that land bank to make a presentation about the organization and how such an approach might apply to the Minneapolis area. Based on this initial presentation, a land bank was established in the region. This is one example of the council's ability to provide a "space" in which stakeholders convene to explore potential innovative responses to the foreclosure crisis.

In addition to the council, the FMI grant was used to support the NCST prepilot initiative with DBNHS and GMHC. Both organizations began acquiring foreclosed properties in their coverage areas in 2007. DBNHS, which serves East St. Paul, began acquiring foreclosed properties with funds made available from a Federal Home Loan Bank loan. GMHC, whose coverage area includes North Minneapolis, began acquiring foreclosed homes with a $10 million loan that it received from Minnesota Housing, which is administered by the Family Housing Fund.

Starting in the summer of 2007, both organizations began purchasing homes in their coverage areas, which had very high numbers of REO properties. Using loan proceeds from the HPF, as of June 2009, GMHC had purchased 172 homes in the North Minneapolis neighborhood (see figure 4), an area with the highest share of homes in foreclosure in the city.

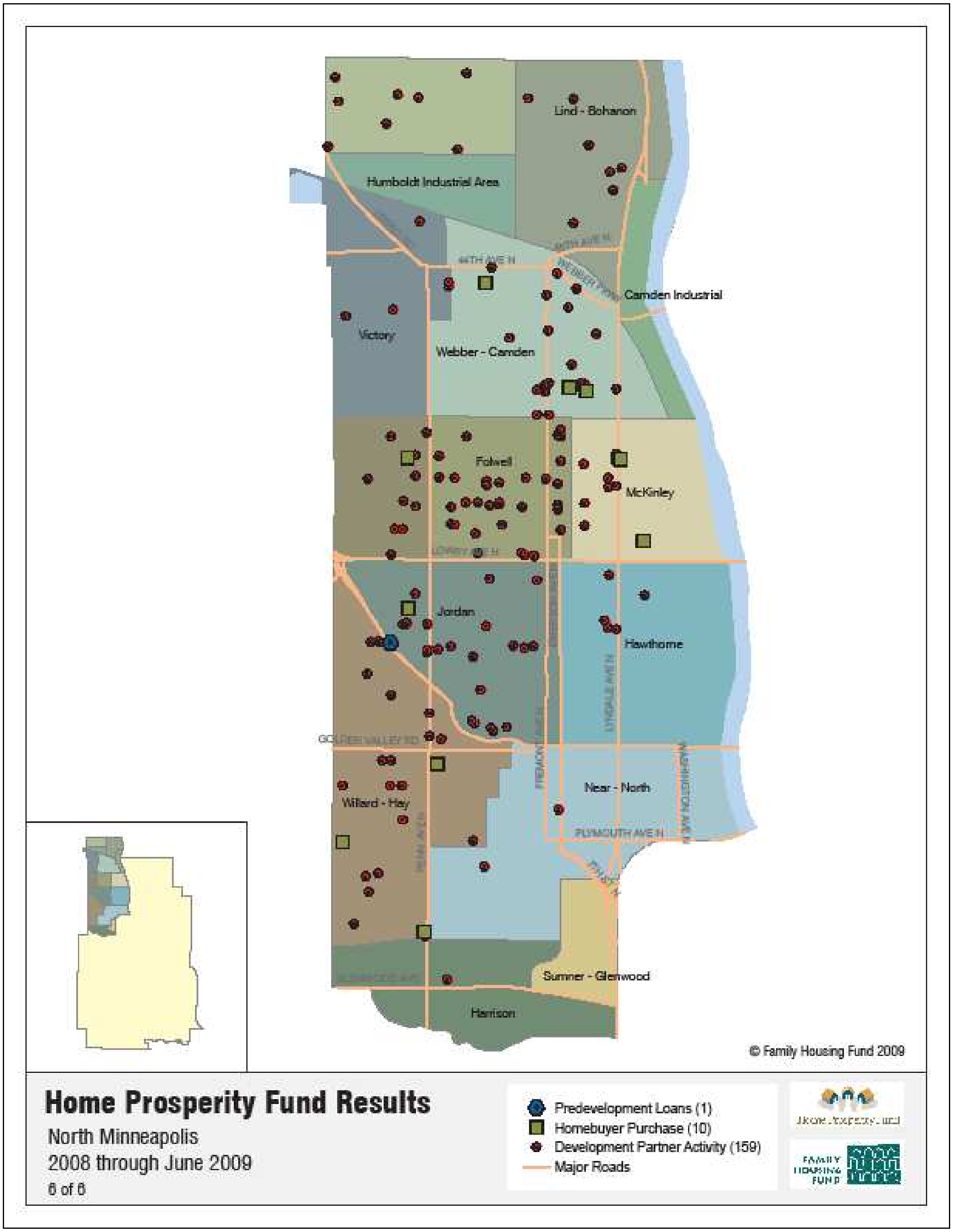
The organizations quickly learned that purchasing these homes was a complex process, because so many of the homes were owned by trusts, as the underlying mortgages were securitized. Nonetheless, DBNHS and GMHC were able to purchase homes. The Housing Partnership Network, of which GMHC is a member, learned of these activities and sought to create a more streamlined mechanism for allowing CDCs to purchase foreclosed homes.

Based on these discussions, DBNHS and GMHC were selected as NCST prepilot sites. Under NCST, participating loan servicers have zip codes of coverage areas within St. Paul and Minneapolis. (There are between four and five such zip codes in each city.) Each day DBNHS and GMHC receive notifications of REO homes that are located within the zip codes selected to be within the prepilot coverage area. The organizations have one day to review the list and tell the servicer whether they want to consider purchasing the properties. In some cases, the properties are condominiums and are thus not appropriate redevelopment targets.

DBNHS and GMHC have five days to request a servicer to appraise a property. Once the request is made, servicers engage an appraiser, who determines the property's market value; this process can take anywhere from a week to a month. Once the appraised price is provided to the servicer, it can offer a price to the CDC. In general, servicers initially set prices 25 percent below the appraised value, but the discount now is much lower. Once the price is set by the servicer, DBNHS and GMHC have the option to purchase the property.

Since the program began, DBNHS and GMHC combined have requested pricing information for about 1,200 properties and have purchased 180. The remaining properties were not purchased either because they were not located in strategic areas of the organization's impact area or because there were insufficient gap funds available to make the rehabilitation feasible. Of the 90 homes purchased by each organization, the majority are demolished. About 30 percent of the properties are rehabbed and then resold. On average, the total development costs for these properties are between $180,000 and $200,000, and they are being resold for between $150,000 and $160,000.

Figure 4: Location of Homes Purchased by GMHC Since January 2008 With HPF Funds



Source: HPF. Used with permission.

The FMI grant has also been used to support the contract-for-deed program administered by the HPF. The HPF, established in 2007, provides long-term below-market interest rate loans to development partners in the seven-county metropolitan area. HPF now has $25 million to lend, at a weighted average cost of capital of 3.0 percent and weighted average term of 12 years. The investors in HPF are Minnesota Housing, Thrivent Financial, TCF Bank, US Bank, and Wells Fargo and the McKnight and Pohlad Foundations.

HPF initially committed $250,000 each to DBNHS and GMHC for the contract-for-deeds program, under which homebuyers with slightly damaged credit receive a first-lien mortgage with an interest rate of 5.5 percent. This loan cannot exceed 80 percent of the purchase price. The mortgage funded by HPF is a second-lien loan for no more than 20 percent of the purchase price and is originated with an interest rate of 3.0 percent. Both loans have a three-year term but a payment based on a 30-year, fully amortizing loan. The expectation is that the homeowner, after a maximum of three years, will be able to qualify for a new loan in the amount of the unpaid principal balances of the first- and second-lien mortgages.

Because the contract-for-deeds loan is a second lien and the combined loan-to-value ratio is above 95 percent, the mortgage represents some risks to HPF investors. As a result, $375,000 of the FMI grant was used as a loan-loss reserve for the contract-for-deed product. Note that the initial commitment from HPF was $500,000, so the loan-loss reserve represented almost 80 percent of potential losses from the first round of contract-for-deeds mortgages. Without this loan-loss reserve, it is unlikely that HPF investors would have agreed to fund this product. HPF has subsequently doubled its commitment for contract-for-deed lending to $1 million but has not been required by investors to increase the loan-loss reserve.

It is important to recognize the leverage created by the FMI grant used for the loan-loss reserve. Because contract-for-deed loans require a first mortgage, each such loan supports a mortgage that is nearly four times as great. In a typical transaction, a purchaser buys a $120,000 home; he or she has a $2,000 down payment and finances the remainder with a $22,000 contract-for-deed loan and a $96,000 first mortgage. Therefore, the $375,000 loan-loss reserve now supports $1 million of funds available for these mortgages. Assuming that each loan averages $22,000, 50 loans will be originated (before the proceeds are recycled) in transactions that will include a total of $4.8 million of first-lien mortgages. Therefore, the $375,000 loan-loss reserve supported a total of nearly $6 million of lending.

Testing innovative approaches to foreclosure mitigation. As discussed earlier, DBNHS and GMHC participated in a prepilot NCST program under which these organizations can purchase foreclosed homes before they are offered for sale to the general public. This makes REO acquisition easier, and the organizations do not have to compete against other buyers for properties and can thus purchase them at lower prices. According to key informants interviewed for this case study, about 180 properties have been purchased by DBNHS and GMHC under the NCST initiative.

2. Factors that influenced success

One of the most important factors that led to the success in the Twin Cities is that the FMI grant did not require the recipient to establish new relationships with third-party organizations or start new activities. One key informant characterized the FMI grant as "amplifying and accelerating" the activities that were already underway in the area. As a result, the FMI grant activities were implemented relatively quickly, and all three of the objectives of the program were reached by the end of the grant's performance period.

As discussed earlier, the council began in January 2007, 18 months before Twin Cities LISC received its award. In addition, the HPF, which funds contracts-for-deeds loans, had $16 million of capital already committed when the FMI initiative began in the Minneapolis area. And DBNHS and GMHC were purchasing foreclosed homes before July 2008. As a result, stakeholders were already acting collaboratively at the time the FMI grant was made, which reduced start-up times.

In addition, the stakeholders who were responsible for implanting the three activities funded by the FMI grant all had strong working relationships with one another. For example, GMHC had already received $10 million in funding from Minnesota Housing administered by the HPF to finance the acquisition of foreclosed properties in North Minnesota before the FMI grant was made. Consequently, it could work relatively easily with fund staff to develop the contract-for-deeds program and assist in the negotiations with the fund's investors to determine the required loan-loss reserve.

This collaborative approach leads to another factor that influences success: stakeholders come together and develop initiatives that spread risk throughout the system. The contract-for-deeds program is one example. The HPF receives funding from a number of sources, all of which are in the same position in terms of repayment. The loans made under contract for deeds are no more than 20 percent of the purchase price of the home, and they are supported by a loan-loss reserve. Thus, no one organization is exposed to an inordinate amount of downside risk, which creates a win-win solution.

3. Major obstacles to successful implementation and potential and known solutions

The FMI program in the Twin Cities reached all its milestones, but any effort to acquire and resell foreclosed properties in the area has been hampered by the slow release of NSP-1 funds by local governments. As detailed below, the city of Minneapolis has selected nine CDCs to receive grants that range between $500,000 and $1 million. These funds come from the city's NSP-1 grant that included $6.5 million for rehabilitation. Although the nine organizations have executed grant agreements with the city, none have received funds. This lack of funding makes it difficult for the CDCs to acquire properties because they cannot be sure of when they will receive the city funds to finance the difference between total development costs of rehabbed properties and sales proceeds. GMHC has sufficient funds to purchase homes and make up some of the gap between total development costs and sales proceeds, but the other eight CDCs do not have sufficient capital to do so. As a result, they are hesitant to acquire properties. So far, St. Paul is not allocating its NSP-1 funds to CDCs. The city's strategy is to acquire, rehabilitation, and resell properties itself rather than use CDCs. But the city has not made any purchases with its NSP-1 funds, thereby complicating the work of any St. Paul–based CDC to coordinate purchase activity with the city.

Unfortunately, there is little that area CDCs can do to move the funding process along. The nine CDCs in Minneapolis will eventually receive their NSP-1 grants and in the meantime are working to line up other sources of financing so that they can acquire properties as soon as the NSP-1 funds are available. In St. Paul, CDCs are working with their existing funding to acquire properties and will continue their attempts to work in areas that St. Paul has determined will be target areas. However, according to key informants interviewed for this case study, St. Paul City Council members are making decisions about which properties should be purchased by the city, and oftentimes such homes are not located within specific target areas outlined by St. Paul.

4. *The effect of the initiative on the flow of the Neighborhood Stabilization Program and other federal funds*

The city of Minneapolis received $14.0 million under NSP-1 and targeted $6.4 million for gap financing. The city, through a competitive process, selected nine CDCs to receive grants of between $500,000 and $1 million. The recipients can use these funds to subsidize a maximum of $25,000 per unit for acquired properties that are either resold or rented. GMHC received the largest award and will use the funds to subsidize the sale of some of the homes it acquired with loans originated by the HPF.

Under NSP-2, a consortium of suburban jurisdictions in the Twin Cities metropolitan area submitted an application, as did a consortium that includes the city of Minneapolis, the city of Brooklyn Park, and Hennepin County. The decision to establish consortia to make NSP-2 applications was made after discussion of the issue at council meetings.

5. *The early sense of the impact of this work*

The FMI program in the Twin Cities helped stakeholders coordinate their activities by participating in the council. As a result, local CDCs, governments, and intermediaries worked through potential responses and helped GMHC secure funding to acquire foreclosed properties in the North Minnesota neighborhoods. In addition, the council offered a forum for stakeholders to explore the potential benefits of establishing a land bank, which was formed on a model loosely based on the land bank in Genesee County, Michigan.

In addition to the council, the funding established a loan-loss reserve, which was essential to the HPF's rollout of the contract-for-deeds loan, the product that enables credit-impaired families to purchase a home. The lack of NSP funding has limited the volume of such loans, but it should increase as NSP-1 funds are made available to nonprofit developers in Minneapolis and, in St. Paul, are used by the city to acquire properties.

Finally, the FMI program in the Twin Cities helped facilitate the NCST prepilot that was tested by GMHC in Minneapolis and DBNHS in St. Paul. This program, which allows CDCs to get a first look at foreclosed homes before they are offered for sale to the general public, has been successful and will likely be replicated across the country.

6. Conclusions about what did and did not work

The main feature of the FMI initiative in the Twin Cities is that it was built on an existing foundation of strong institutional relationships among area stakeholders. As a result, the program was able to start relatively quickly and meet its milestones within the grant's performance period. The stakeholders, however, are limited in their ability to acquire and rehabilitate properties because NSP-1 funds are still not available.

7. What we can learn about the role of different players

The FMI initiative in the Twin Cities is built on a sophisticated collaborative structure that includes local CDCs, intermediaries, and local governments. The role that each type of organization plays is influenced by local governments' attitudes toward partnering with CDCs. Minneapolis is more willing than St. Paul to include CDCs in its foreclosure response. As a result, GMHC has received support for its purchase and rehabilitation activities from Minneapolis. In contrast, St. Paul's preference is to conduct its own redevelopment activities, and thus DBNHS and other St. Paul CDCs have received very little support for foreclosure responses.

The NSCT prepilot demonstrated that servicers can benefit from working with CDCs to dispose of properties in ways that benefit their investors (by reducing holding times) and the neighborhoods in which the properties are located.

8. The implications of the Living Cities initiative for the response of philanthropy to crises

The FMI award helped an existing infrastructure in the Twin Cities respond to the foreclosure crisis. Because Twin Cities LISC did not use the funds to create new institutions, the activities in the grantee's award agreement could be implemented relatively quickly. Because these activities did not include specific quantitative benchmarks, however, it is difficult to establish the extent to which each activity was implemented with the level of intensity contemplated when the award was made. It is clear, however, that the grant funds helped the council by supporting a staff position and helped the HPF develop the contract-for-deeds program and establish the NSCT pilot for GMHC and DBNHS. All these activities have been helpful in the region, but Living Cities cannot get quantitative measures of the progress and impact of these activities.

Interviews Conducted, September 8–9, 2009

Chene Shoquist, City of Minneapolis
Tom Strietz, City of Minneapolis
Cecile Bedor, City of St. Paul
Shawn Huckleby, Faegre and Benson
Becky Rom, Feagre and Benson
Tom Fulton, Family Housing Fund
Elizabeth Ryan, Family Housing Fund
Lowell Yost, Family Housing Fund
Carolyn Olson, Greater Metropolitan Housing Council
Melissa Manderschied, Minnesota Foreclosure Partners Council
Andriana Abariotes, Twin Cities LISC
Jeff Washburn, City of Lakes Community Land Trust
Jim Erchul, Datyon's Bluff NHS
Kristen Fitzpatrick, Metropolitan Consortium of Community Developers

Appendix C:
List of Acronyms and Abbreviations

List of Acronyms and Abbreviations Used In This Report

ACA - asset control area

CDC - community development corporation

DBNHS - Dayton's Bluff Neighborhood Housing Services (St. Paul)

ESOP - Empowering & Strengthening Ohio's People

GMHC - Greater Metropolitan Housing Corporation (Minneapolis)

HPF - Home Prosperity Fund (Minnesota)

HUD - U.S. Department of Housing and Urban Development

LIHTC - Low Income Housing Tax Credit

LISC - Local Initiatives Support Corporation

MHIC - Massachusetts Housing Investment Corporation

MLS - multiple listing service

NCST - National Community Stabilization Trust

NMTC - new market tax credits (New Market Tax Credit Program)

NPI - Neighborhood Progress, Inc. (Cleveland)

FMI - Foreclosure Mitigation Initiative

NSP - Neighborhood Stabilization Program

OHFA – Ohio Housing Finance Agency

REO - real-estate-owned

SII - Strategic Investment Initiative