

***Submitted
By
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Cleveland***

***Domestic Policy Subcommittee
Oversight and Government Reform Committee***

***Monday, December 7, 2009
10:00 a.m.***

Cleveland Strategies for a Housing Recovery

Introduction

Good Morning Mister Chairman and Members of the Subcommittee, fellow panel members and members of the audience. I am honored to be before you to represent the City of Cleveland and our Mayor, Frank G. Jackson, for today's hearing on the ongoing residential foreclosure crisis. It is beyond debate that Cleveland has been hit hard by foreclosures. What is not as well known is that the city – under the leadership of Mayor Jackson – has taken an aggressive posture in responding to challenges.



Cleveland has battled the exploitation of the housing market as it changed from flipping to predatory lending to foreclosure to dumping. It is imperative to acknowledge that the “tricks” deployed for profiteering evolve. Thus, the responses, to be effective, must change as well. My comments herein will describe the local efforts to combat a crisis that has undoubtedly expanded way beyond foreclosures. Corrective measures must, therefore, address weakness along the entire “housing” process.

Since 1995, Ohio’s counties saw a 400% increase in foreclosures.¹ The primary cause for foreclosures in Cleveland was predatory lending.² In 2002, when Mayor Jackson was President of City Council, the city passed legislation to prevent predatory loans, but the city was blocked from enforcement. The waves of foreclosures increased in the early part of the decade and escalated dramatically from 2005 forward.³

Year	Number of Foreclosures Per Year	Number of Foreclosures Per Month (Avg.)
2005	1926	160.5
2006	7369	614.1
2007	7623	635.3
2008	7088	590.6
2009 (Jan-Nov 30)	5555	505
Total	29,561	501

As grim as the foreclosure numbers are, the community is determined to fight back. Today, you will hear testimony from members of the two panels who are involved in what has emerged as an integrated team to coordinate our local response.

The Local Landscape & The Impacts of the Housing Crisis

The City of Cleveland has a slow-growth economy. The population is estimated at 438,403 people.⁴ As the result of the economic recession, the city is wrestling with an unemployment rate that is 2% higher than the state rate, and 4% higher than the national rate. Most of the city’s census tracts meet the guidelines for low-mod census tracts as determined by the Department of Housing and Urban Development (HUD).

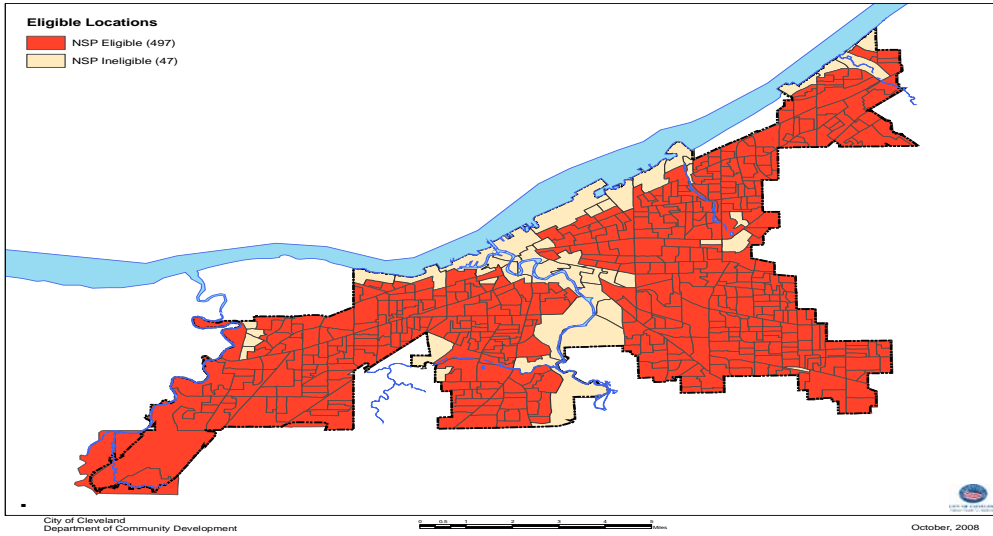
¹ Policy Matters, *Foreclosure Growth in Ohio 2009*, page 6, Rothstein, March 2009. Policy Matters Ohio is a nonprofit, nonpartisan research group in Ohio. It provides real-world policy analysis regarding economic issues that affect low- and moderate-income families.

² See e.g., *Policy Matters, Home Insecurity: Foreclosure Growth in Ohio*, page. 9, Sopko, Oct. 2004.

³ For the escalation of foreclosures see e.g., *Foreclosure Growth in Ohio – 2009*, by Policy Matters. “Housing foreclosures have a detrimental affect on working families, draining incomes and depleting savings. Communities are also negatively impacted as tax revenues are depleted, social services are in higher demand, and dozens of intangible effects ripple outward.” *Testimony to Cleveland City Council, February 2, 2008*. See Policy Matters reports on foreclosure at <http://www.policymattersohio.org/pdf/ForeclosureGrowth2009.pdf>

⁴ *City of Cleveland Community Reinvestment Area Housing Survey*, August 12, 2009, citing statistics from the American Community Survey estimates.

HUD NSP - Low Middle Moderate Eligible

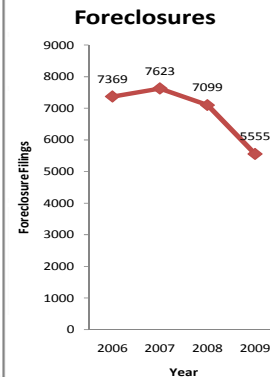
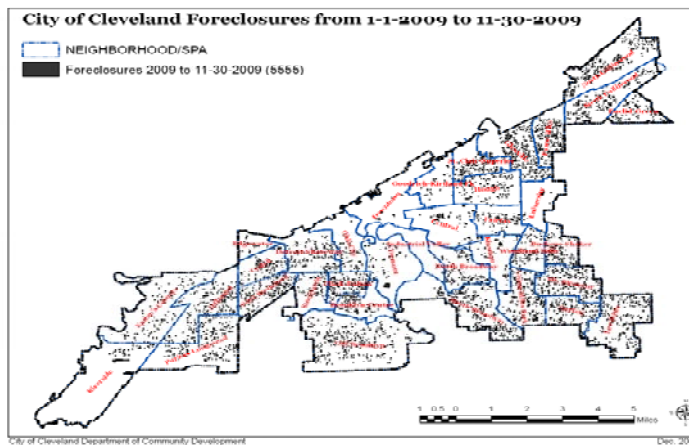


The impact of foreclosures on our communities has significantly undermined our strong history of neighborhood revitalization. Our community development objectives are to develop viable urban neighborhoods that include:

- decent housing
- a suitable living environment, and
- expanded economic opportunities - principally for persons of low and moderate income.

Each of the above elements has been adversely affected by foreclosures. The below map of foreclosure filings demonstrates that none of the 36 neighborhoods in the city have been spared.

City of Cleveland Foreclosures



Virtually every foreclosed house sits vacant at some point during the foreclosure. Once vacant, they are frequently damaged, vandalized or used for criminal activity, resulting in

real and perceived health and safety threats to the surrounding homes. Frank Ford will discuss the devastating impacts in his testimony.

Foreclosures reduce the value of the foreclosed property as well as the value of surrounding properties. The reduced value decreases the assessed property tax value. Seventeen cents of each dollar paid for property taxes supports the city's operating expenses, and 9% of the city's general fund is based upon property taxes. According to Case-Shiller, the property values in the Cleveland area have declined 3.7% over the past year.⁵ While that rate is lower than the decline in value in some cities, the values in Cleveland were not inflated as in cities such as San Francisco, Las Vegas or Phoenix. To make matters worse, the city's Finance Department projects a 12% decline in property value in 2010.

Lower property tax revenues cause a gap in the city's budget that is compounded by the added expenses related to vacant properties such as demolition, debris removal and other nuisance abatement tasks. The city has almost doubled nuisance abatement expenditures from Community Development Block Grant (CDBG) funds to \$890,000 since 2004. That increase in expenditures for vacant properties has come during a period when block grant funds were declining.⁶ The city has also dramatically increased the number of demolitions since 2004 when CDBG funds were used to demolish 225 houses. In 2009, the city expects to demolish 1,700 structures. The amount expended for demolition has increased from \$1.8 million in 2004 to \$6 million in 2008. In 2009, the city committed over \$15,000,000 of its Neighborhood Stabilization Program (NSP) funding for demolition. Even this increase is not capable of addressing the 8,009 structures identified as "vacant and distressed."

As painful as the decrease in revenue coupled with increased expenses are for the city, the dire financial condition of the former homeowner, after suffering through a foreclosure, is worse. Financial counseling agencies have stated that it takes *at least 2* years for a family to restore their financial circumstances and re-build their credit after a foreclosure. This estimate has been corroborated by local financial institutions.

A Comprehensive Local Response

The wave of local foreclosures required that we "re-think" our strategies for community development. The local approach may be described as comprehensive, strategic, practical and designed for the local market. Cleveland has a long history of public-private partnerships, particularly in the realm of community development. The participants include government, philanthropic, non-profit organizations, community development corporations (CDCs) and the corporate community. We have expanded upon that infrastructure to design and coordinate our recovery strategies.

The recovery strategies are comprehensive because they are intended to reinforce threats or weakness in the housing market, including:

⁵ It may also be argued that the decline in the city is greater than the Case-Shiller study area.

⁶ The city received \$30 million of CDBG funds in 2000. The award was \$27.4 million in 2005. The 2009 allocation was \$23.9 million, a small increase over the \$23.6 million allocation in 2008.

1. Data collection & management: data collecting, research, tracking & monitoring,
2. Outreach and intervention with homeowners,
 - a. Foreclosure prevention counseling,
 - b. Financial literacy & home ownership counseling,
3. Code Enforcement,
4. Demolition,
5. Tracking and acquisition of foreclosed and vacant houses, and
6. Rehabilitation.

I will briefly discuss strategies related to each of the categories above and explain its relationship to foreclosures and vacant property. Please note that a common thread to virtually every strategy to combat foreclosures and vacant property is a collaborative effort. There is local coordination between the Mayor and city council, the city and the county, the judiciary, foundations, city-wide non-profit organizations, neighborhood organizations and universities.

For example, for over three years the Vacant and Abandoned Property Action Council (VAPAC) has been convened by Neighborhood Progress, Inc, and includes the City, the County, Housing Court, the Cleveland Neighborhood Development Coalition (the trade association for the local CDCs), the First Suburbs Consortium, NEO CANDO.

Data Collection & Management: We had to first reorganize how we view the city and manage information. There is currently a more robust data collection and exchange structure for information to move from the academic (CWRU, CSU), government (City and County), and non-profit entities.

Claudia Coulton will discuss the significance of aggregating and disseminating data for research, analysis and planning. Her management of the NEO CANDO⁷ system for collecting data and providing broad-based access is important because NEO CANDO serves a central role for accessing and sharing collected data. The NEO CANDO web-based access enables information to flow between the city, county, non-profit development agencies or policy and research organizations, such Policy Matters or The Housing Advocacy & Research Center.⁸

Property data is the lynchpin to the city's Neighborhood Typology, upon which the city as well as non-profit and philanthropic partners have based our programmatic strategies. The typology identifies market conditions based upon 9 real estate related variables in order to ascertain relative strength.⁹ In areas of weak market strength we have adopted a

⁷ NEO CANDO is operated by the Case Western Reserve University, Mandel School of Applied Social Sciences, Center on Urban Poverty & Community Development. <http://neocando.case.edu/cando/index.jsp>

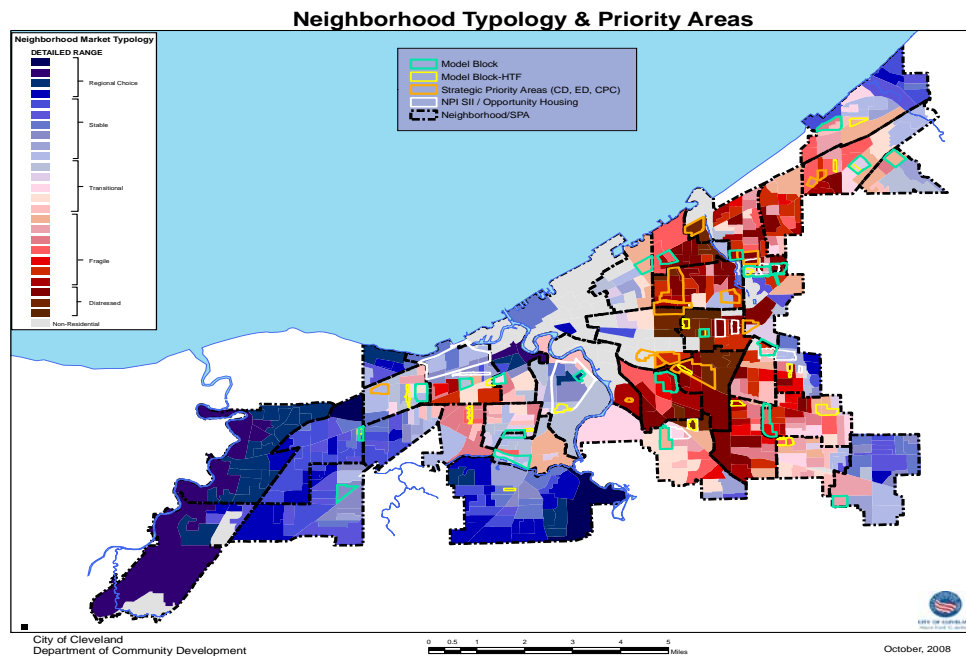
⁸ The Housing Research & Advocacy Center works to eliminate housing discrimination and assure choice in Northeast Ohio by providing those at risk with effective information, intervention and advocacy. The city has used HRAC research for lending analyses. <http://www.thehousingcenter.org/>

⁹ The Neighborhood Typology uses data for 9 variables that is aggregated to a block group level: median assessed value of parcels with 1-3 family structures, change in median value of 1-3 family homes between a baseline (1989-1991) and 2005-2008, net change in the number of 1-3 family homes from 1990-2008, percent of 1-3 family homes transferred by sheriff's deed, homeownership rate, boarded & condemned homes, percentage rated "fair" or worse by the County Auditor in 2007, percentage of homes surveyed as vacant & distressed in 2008, demolition rate from 2006-2008.

<http://cd.city.cleveland.oh.us/>

focused or targeted approach in order to better insure desired outcomes and impact. The targeted areas, called model blocks, strategic investment areas or opportunity housing areas are where programs and investments are more heavily focused. This approach is reflected in the city's NSP and NSP2 applications. The map on the next page reflects the results of the Typology analysis and indicates the priority areas.

The priority area concept is reflected in the Opportunity Housing Program that is central to the Neighborhood Stabilization Program (NSP). Opportunity Housing combines, in 6 neighborhood target areas, demolition of 300 houses, rehab of at least 150 houses for sale, rehab of up to 100 houses for lease-purchase housing for low-income families, and counseling for foreclosure prevention. The effort involves Neighborhood Progress, Inc. Cleveland Housing Network, ESOP, 6 community development corporations, the city, and funding from the State of Ohio and NSP funds.¹⁰ The concept is also reflected in the NSP-2 proposal submitted by a consortium that includes the Cuyahoga County Land Reutilization Corp. (CCLRC), Cuyahoga County, the City, and the Cuyahoga Metropolitan Housing Authority (CMHA).



The table below reflects how program resources would be expected to be distributed relative to the Typology.

¹⁰ The NSP Plans for the NSP awards from HUD and the State of Ohio are available at <http://cd.city.cleveland.oh.us/>

Strategy Matrix

	Regional Choice	Stable	Transitional	Fragile	Distressed
Code Enforcement Action	✗	✗			
Senior Initiative	✗	✗	✗	✗	✗
Rehab – conv. And widely avail	✗	✗			
Rehab - subsidized		✗	✗ target	✗ target	
Exterior		✗	✗	✗	
Vacant Affordable		✗	✗ target	✗ target	
Large scale projects - strengthen asset base		✗	✗	✗	✗
Demo and Landbank			✗ target	✗ target	✗

The growth of our data infrastructure locally is an important tool to identify problems, plan strategies, track activity and to measure impact. While there have been great strides in how data is collected and organized, we continue to seek better ways to collect data and organize it for analysis.

Outreach, Intervention and Counseling: Data has assisted with efforts to assist families threatened with losing their homes to foreclosure. Statistics indicate that time is a factor in avoiding foreclosure. In the Opportunity Homes areas, canvassers from ESOP used data to identify families who have adjustable loans that are about to re-set. Those families were approached and advised to seek counseling to re-work their loans. Mark Seifert will discuss in his testimony, the efforts of ESOP as it has evolved from a local advocacy organization to a state-wide organization with one of the best track records in the country for mortgage loan workouts. ESOP is one of several local organizations that is involved with foreclosure counseling.

The United Way First Call for Help at 211 line can refer homeowners to agencies funded by the county for foreclosure prevention counseling. The State’s Save the Dream effort operates in a similar manner.¹¹ The city also uses an average of \$400,000 per year of CDBG funds to support efforts of the City’s Department of Consumer Affairs and several agencies for counseling services.

As important as foreclosure prevention counseling is, there are other critical counseling needs. We firmly believe that unless people have a greater understanding of financial literacy, wealth building and homeownership counseling, Cleveland residents will have difficulty rising above precarious financial circumstances. This belief compelled the City and the County to initiate what has become the Northeast Ohio Coalition for Financial Literacy.¹² This coalition of over 35 government, non-profit organizations, universities and financial institutions is organized to inform, provide resources and assist people to

¹¹ <http://www.com.ohio.gov/SaveTheDream/>

¹² <http://www.neocfs.org/>

become better educated about making wise financial decisions. The coalition is also evaluating ways to improve the standards and outcomes for people who participate in counseling programs.

While the need for continued foreclosure prevention counseling is important, counseling in wealth building and home ownership is necessary for sustainable improvement in our neighborhoods.¹³

Code Enforcement: Code enforcement becomes a factor after the foreclosure is filed and the resident leaves the premises. In 2008, the city identified 8,009 1 to 3 family properties as vacant and distressed properties. The City's Department of Building and Housing has restructured its code enforcement approach to improve the partnership with CDCs for identification of problem properties. The City is also duplicating the vacant & distressed property survey that was undertaken in 2008. It will be completed by the end of the year. Building & Housing will also use \$350,000 of NSP funds for "Operation Prevent," which will strengthen its efforts to prosecute those responsible for flipping, bulk sales and dumping vacant property. Operation prevent will enable Building & Housing to staff the Vacant Property Unit with additional inspection staff, legal staff and IT staff. The funds will also support strengthening the data system required to track transfers of foreclosed property. The identification of responsible parties is made more difficult by frequent transfers and avoidance of recording of deeds. Housing Court has aggressively fined buyers of bulk sale properties.

Demolition: Demolition is the likely outcome for most of the houses that are vacant. The city surveyed other mid-western and weak market cities and noted that most were able to rehab only 10% of vacant houses. The balance were slated for demolition. While we desire to salvage as many that we can within our strategic framework, we recognize that the volume of demolition will be high.

The Department of Building and Housing has developed strategies for both code enforcement and demolition. Demo priorities are "the worst first," those near schools, parks and playgrounds, houses in strategic areas, and those viable for deconstruction pilot programming. The strategies take into account that the need for demo will stretch the resources.

Tracking and acquisition of foreclosed and vacant houses: The sources of vacant homes are HUD, Fannie Mae, and Bank REO portfolios. That said, identifying the owner or responsible party for a particular house is more complicated. Through the Case Western Reserve University NEO CANDO program, we have improved our ability to track foreclosure filings, ARM resets, vacant property inventories, REO holdings, properties sold from REO, and demolitions on a parcel by parcel basis.

Next, is the task of gaining control of vacant and abandoned property for reuse. The establishment of the CCLRC and the consortium created for the NSP-2 proposal is integral to managing vacant properties. CCLRC will coordinate and fund a regional

¹³ A parallel need is to restrict predatory consumer loans as evidenced by the debate in Ohio over Pay Day lenders. See generally, *Policy Matters & Housing research and Advocacy Center, Trapped in Debt: The Growth of Pay day Lending in Ohio*, Rothstein and Dillman, Feb. 2007

approach to acquire, rehabilitate, demolish and maintain homes left vacant or abandoned because of foreclosure or the weakened market created by the economic crisis. With the substantial increase in real estate holding, REOs, banks and servicers began to dump REO properties on the housing market in Cuyahoga County through bulk sale and auction. Many of these properties were purchased by vacant property wholesalers which sold the property without improvement to other investors. The result is a rapid, well documented decline in average sales prices throughout Cuyahoga County. The table below shows the volume of sales and average prices for the entire county for the years 2000, 2004 and 2008.

Cuyahoga County Total Sales and Volumes

	2000	2004	2008
Number of Sales	23,162	24,734	18,579
Mean Sale Price	126,418	143,732	99,850

The CCLRC brings new resources and capacity to the problem. Specifically, (i) it has a greater ability to acquire, hold and dispose of improved and vacant property than any other consortium member; (ii) it can be the mechanism to drive hard bargains with REO holders and bank servicers and meet the property transaction timetable required by successful negotiation; and (iii) it is able to act quickly to return a salvageable property to productive use.

The CCLRC will strategically acquire and “mothball” housing units. These units may consist of individual houses, or of vacant lots resulting from demolition. Houses will be properly secured and maintained so as not to create damage to the housing market while they are being held. Holding of this real estate will take place with a maximum of ten year disposition strategy.

The CCLRC is a platform for innovation and the most nimble of the NSP-2 Consortium members. It presents the best opportunity to turn policies of the other consortium members into action in a collaborative fashion. County Treasurer Rokakis will provide more detailed testimony about the CCLRC.

Rehabilitation:

The strategy is to use either private and non-profit developers to restore homes. The traditional non-profit partners are participants in planning and implementation. The city has added over 50 re-qualified for-profit developers who have made a commitment to quality rehabilitation of homes. Through NSP funds, the City offers an 80% construction loan to redevelopers of 1-4 family homes in target areas to overcome credit access issues. In addition, the City offers gap support to bridge between the current market and the cost of quality restoration to mitigate developer risk in a fragile market.

It is recognized that houses being brought back onto the market will require additional incentives from the up-front development “gap” financing referenced above. In the NSP-2 proposal, a homebuyer credit enhancement will be provided for each home sold to

income eligible buyers. This is expected to be in the form of a second mortgage of \$20,000 at 0% interest, forgivable over a ten year period.

The strategies outlined today reinforce and advance the plan to create neighborhoods of choice that Mayor Jackson has developed including:

- Varying the development approach in neighborhoods based on the need and market potential of each,
- Jump starting investment in our existing housing stock and communities through expanded rehabilitation and development of model block investment areas,
- Eliminating blighting conditions that should not exist in any community and that threaten , not only the quality of life in an area but the safety of area residents,
- Supporting the markets in stable areas, and
- Redeveloping neighborhoods in a sustainable and environmentally sensitive manner.

I hope that the discussion above frames the extent of the destruction that the crisis has created. I have also outlined that the local partners are working on coordinated approaches to attack each problem area.

Challenges

The overarching challenge we face locally is that the “foreclosure crisis” is broad and changes. We must have a multifaceted response. We must also be nimble in recognizing shifts in conduct that require modification of programs. We are forced to anticipate and respond to problems, and strive to be diligent in preventing further abuse.

In pursuing those ideals, we seek assistance from state and federal policy makers:

1. Financial Counseling: Support for counseling is ongoing. There remains a high volume of loans with suspect terms that threaten borrowers. That is compounded by economic related challenges caused by job loss. The tightening of credit adds to the financial counseling need to help people improve their financial acumen.

As Mike Seiferrt will explain, the HAMP program is hampered by process inefficiencies – even though it is much better than previous programs.

In NSP, counseling was not permitted as a program expense, but was allowed as an admin expense. Counseling is critical to minimize further foreclosures, and is imperative to create pools of buyers for rehabilitated homes. It is a necessary program activity.

2. Property Disposition: The HUD disposition agreement with the city is dramatically better than the previous process. It should be expanded. HUD’s REO contractor needs to improve its management of property in its portfolio. The number of HUD properties in deplorable condition remains too high.

Surrounding homeowners should not be subjected to open and vandalized homes with debris strewn around them.

3. Demolition: The volume of vacant houses tests our ability to find funds for demolition. The availability of NSP funds have allowed the city to significantly increase demolition over levels we had already increased. The newly formed CCLRC creates another resource for demolition, but the volume of deteriorated vacant houses will continue to test local resources. That reality is aggravated when all sources of vacant property attempt to dump deteriorated houses on municipalities.

For example, HUD's agreement with the city is beneficial; however, HUD should assist with the cost of demolition – particularly where the property deteriorated under HUD's control. The same situation exists for HUD financed multi-family properties that default on HUD loans.

The same is true for Fannie Mae, lenders and servicing firms. The city is frequently told “use your NSP money for demo.” That response (1) shirks responsibility – often for weak management of REO portfolios, and (2) overlooks the NSP and NSP legislative intent that preferred to limit the use of funds for demolition – despite statistics that would dictate that most vacant homes should be demolished.

4. Financing: Anyone who gets a loan can get relatively good interest rates. The question is who can get a loan? Financial institutions remain disengaged with prevention and recovery. Loss mitigation efforts leave a lot of room for improved performance. Further, there is little predictability about what is needed for a “yes” decision for a home purchase loan. The same is true for business loans. They are extremely difficult, particularly for construction related businesses. Local contractors attempting to rehab houses wrestle with access to credit.

Credit uncertainty for construction and for buyers tests our ability to rehab vacant houses, even though we are using NSP funds to plug the gap, such a remedy is limited. Limited availability of financing creates the risk of needing to demolish houses that could have been salvaged.

Conclusion

The City of Cleveland, its residents and businesses have been victimized by unscrupulous actors extracting equity and value from our housing market. As the crisis undermined 20 years of progress in community revitalization, we may be bloody but our heads are unbowed. We have coalesced around the shared objectives of creating comprehensive strategies for not only combating the combined foreclosure/housing/economic crisis, but we are determined to re-build and strengthen our communities.

I have discussed issues that may seem to be separate from foreclosure, but they are not. The foreclosure problem infected the entire housing production system - on its way to sinking the economy. Our belief is that the remedy requires reinforcing the housing production system in order to be effective - a challenging task that must engage all

sectors. I hope I have demonstrated that Cleveland area has accepted the challenge. We will continue to need assistance from the State and Federal governments. Thank you again for the opportunity to present my testimony today.