

Seminar Summary

CLEVELAND FED HOSTS RESEARCH SEMINAR ON VACANT AND ABANDONED PROPERTIES

The toll of the housing crisis is no more evident than in the boarded-up homes and overgrown lots that pock neighborhoods across the country. Dealing with the problem requires careful planning informed by careful research. Toward that end, on August 27 the Federal Reserve Bank of Cleveland hosted “Moving Toward Solutions: Research and Policy on Vacancy and Abandonment” in Columbus, Ohio. (This seminar was part of the Federal Reserve System’s national foreclosure series, which culminates on October 20 with a capstone meeting in Washington, DC, that will yield a set of policy recommendations to address this issue.) The Cleveland Fed seminar aimed to highlight the contributions of recent research to the policy discussion about the causes and impacts of foreclosure and vacancy, with an emphasis on the implications and solutions for “weak market cities,” defined by Brookings’ Metropolitan Policy Program as those large and medium-size.

“An evidence-based approach, based on solid research, leads to the best policy,” Mark Schweitzer, senior vice president and director of Research with the Cleveland Fed, said when opening the seminar. “Vacant and abandoned properties is arguably one of the most important issues in community development we’re facing in our district. Research provides the first step in understanding the issue. Once you have an in-depth understanding of an issue, that’s when you can develop effective policy.”

Research presented at the seminar tended to fall into one of three categories, as summarized by discussant Christopher Walker, director of research and assessment at Local Initiatives Support Corporation (LISC). First, there are research activities tied to market diagnosis—explaining the patterns in loan performance and their policy implications. Second, there is research that provides directly actionable information, such as identifying specific properties and areas to be addressed, and where precisely to direct financial support. Third, there are impact studies that analyze the degree to which foreclosures and abandoned properties can affect other properties and development in their neighborhoods and beyond.

UNDERSTANDING PATHWAYS TO FORECLOSURE AND IMPACTS OF VACANCY

Foreclosure rates in Cuyahoga County, home to the city of Cleveland, have passed historic levels, rising from 3,345 in 1995 to almost 15,000 in 2007. In **Pathways to Foreclosure: A Longitudinal Study of Mortgage Loans**, Cleveland and Cuyahoga County, 2005-2008, Case Western Reserve University researcher Claudia Coulton and her co-authors studied the connection between foreclosures and mortgage loan types and borrowers.

Here’s what they found: The No. 1 predictor of whether a Cuyahoga County property purchased in 2005 and 2006 ended up in foreclosure by early 2008 was whether it was financed with a high-cost, or subprime, mortgage loan. According to the study, subprime loans were eight times more likely to go into foreclosure than other loans and accounted for 84 percent of the foreclosures for the study period. The second-highest risk factor was the race of the borrower—black borrowers had foreclosure rates of 28 percent, compared with just under 8 percent for whites. (Racial differences were not particular to low-income borrowers, as 60 percent of loans to high-income blacks were subprime compared with less than 20 percent to high-income whites.) Coulton’s team used statistical techniques to match local mortgage documents and foreclosure filings with Home Mortgage Disclosure Act (HMDA) records.

Another finding that stood out was the small concentration of financial market players involved in the region’s foreclosures. Out of 128 subprime mortgage lenders, the top 20 accounted for 82 percent of the foreclosures on high-cost subprime loans originated in 2005 and 2006. Similarly, the top five plaintiffs (who are seldom the original lenders) accounted for 70 percent of subprime foreclosure filings during the study period.

The extent of the subprime lending problem was particularly evident in data Coulton analyzed showing the number and prices of properties that end up in so-called “real-estate owned,” or REO, status. REO refers to foreclosed homes that, having failed to sell at an auction, go back to the mortgage holder (usually the bank or company that serviced the loan). In 2007, properties in Cleveland that sold within a year of being in REO status did so at about only 30 percent of their estimated market value. In 2000, such properties sold at 80 percent of their estimated market value.

“It’s been reported anecdotally, but quite visible [in the data] is the fact that many homes that get to REO status are going for less than \$10,000,” Coulton said. “It’s kind of startling to see that in the Cleveland suburbs.”

The effects of foreclosures and vacant and abandoned properties are often lumped together, but what if it’s not so simple? In

Emerging Threats to Community Stability: A Spatial Hedonic Model, Cleveland State University researcher and Cleveland Fed visiting scholar Brian Mikelbank disentangled the effects of those two groups of properties with an analysis of 2006 housing data from Columbus.

“We often talk about vacant/abandoned and foreclosed properties together in the same sentence as being so strongly related,” Mikelbank said. “But in Columbus, the spatial effects are really different.”

As is standard in housing market research, Mikelbank used a “hedonic” model, which means that a house’s characteristics are used as independent variables in a regression model to explain or predict the sales price of that house. Mikelbank analyzed the impact of vacant and foreclosed properties on neighborhood property values, both individually and jointly. For every property sale analyzed, Mikelbank considers the number of foreclosed and vacant properties within a specific buffer, or perimeter surrounding the property. This allows him to measure the general impact of foreclosure and vacancy on property values in an area.

One of his key findings was that the pecuniary impact of foreclosures tended to be stronger than the impact of vacant and abandoned properties. According to Mikelbank, that’s because foreclosures were distributed more widely across Columbus, leading to an aggregate negative impact of \$97.5 million when analyzed together in the spatial model. By comparison, vacant and abandoned properties had a negative \$16.9 million “neighborhood effect,” owing to their concentration in the city center. He concluded that modeling the two outcomes separately may overstate the impact of foreclosures on nearby housing market prices. Although it’s true that the negative impact of vacant and abandoned properties is significant, the effect diminishes quickly the farther one goes from those properties.

Wrapping up the Coulton–Mikelbank session, discussant Mark McDermott, vice president with Enterprise Community Partners, noted that \$3.9 billion has been set aside in the Housing and Economic Recovery Act of 2008, or HR 3221, for grants to heavily impacted neighborhoods. “We need to show that we can use those dollars wisely,” McDermott said. “We need research to back that up.”

REGIONAL DIFFERENCES IN FORECLOSURE TRENDS AND VACANT PROPERTY DISPOSITION

The involvement and effectiveness of nonprofit community groups in redeveloping vacant properties varies by region. **Incentives for Redevelopment of Vacant Land: A Cleveland and Detroit Comparison** examined the legal structures and political relationships in those two cities. Margaret Dewar, a professor of urban and regional planning at the University of Michigan, observed that Cleveland and Detroit have experienced similar population and manufacturing employment declines and poverty rates, but have seen much different results in their respective efforts with vacant and abandoned properties. Dewar found that 79 percent of Cleveland’s community-based developers who purchased city-owned property for redevelopment reused almost all of the land, compared with 36 percent in Detroit. In Cleveland, community development groups tended to take the role of facilitator, not taking title to the properties, while in Detroit the groups owned the properties. This difference may be important in understanding the faster pace of reuse in Cleveland.

Dewar also attributed the differing results to political and working relationships. In Cleveland, for example, city council members are elected by ward, whereas in Detroit they are elected at-large. Having council members dedicated to specific swaths of land may help in assembling funds for those areas, Dewar reasoned, instead of having the funds distributed city-wide in smaller block grants.

Researchers like Dewar face several challenges related to data collection, among them limited access to data, inconsistent formats for data collection, and affordability of data. One case in point was the experience recorded in **Foreclosures and Neighborhood Impacts in New Jersey** by Rutgers University Professor of Urban Planning and Public Policy Kathe Newman. In producing a dataset of Essex County, NJ, foreclosure filings for 2004, Newman’s team immediately had to answer the question of “when” a foreclosure is a foreclosure. In practice, a foreclosure goes through several stages, from filing to sheriff sale. In their study, the Rutgers researchers focused on “pre-foreclosures,” to capture the process at the start. They combed through paper documents at the county courthouse to gather data points.

According to their research, pre-foreclosure filings doubled to more than 6,000 annually from 2006 to early 2008. In Newark alone, 13 percent of mortgage loans originated in 2005 are in foreclosure, a figure that Newman expects to rise through the remainder of this year. And specific data relating to foreclosed loans can be difficult to obtain. One barrier to more in-depth analysis of foreclosures is that the plaintiffs in foreclosure filings aren’t usually the mortgage servicers. Identifying the mortgage

servicers requires going through filings one by one, while learning about abandoned properties often requires on-site visits to the properties.

Sizing up Dewar's and Newman's work, discussant Christopher Walker, research director with the Local Initiatives Support Corporation, said making up-close distinctions and observations about the localized effect of the subprime housing crisis is critical. "Understanding the different ways the phenomenon plays out in different neighborhoods is important for framing an appropriate response," Walker said.

REDEFINING ABANDONMENT AS AN OPPORTUNITY FOR REDEVELOPMENT

City agencies tend to bear the largest burden in dealing with vacant and abandoned properties, which are quite literally symbols of deterioration and decline. In **Seizing City Assets: Setting an Agenda for Urban Land Reform**, former Enterprise Foundation President Paul Brophy recast abandoned and vacant properties as hidden positive assets. He listed 10 steps to urban land reform, such as creating a sound legal framework for vacant land reclamation and finding finance for redevelopment.

Michael Pagano, dean of the College of Urban Planning and Public Affairs at the University of Illinois, Chicago, took a comprehensive look at the characteristics of vacant and abandoned properties in **Terra Incognita: Vacant Land and Urban Policy**. In 1998, Pagano's team surveyed 198 U.S. cities with populations over 100,000 to learn more about why certain parcels stand vacant and others are redeveloped. Twenty-five cities identified disinvestment as the leading cause of increased vacant land, followed by 24 saying suburbanization was the culprit. Cities with growing populations actually reported more vacant land than cities with declining populations, a counterintuitive finding that Pagano attributed to annexation, which leads to development on city edges while city centers sometimes decline.

Cities' strategic behavior in promoting certain types of development at certain locations appears to be related to tax revenue structures. Though it might seem that property- tax-dependent cities would have a greater incentive to redevelop more vacant land than sales- or income-tax dependent cities, an analysis of Pagano's data does not support that conclusion. The most significant factor in explaining the amount of vacant land in cities is a municipality's ability to expand its boundaries, Pagano found.

GENERAL DISCUSSION ON LEVERAGING RESEARCH INTO PUBLIC POLICY

Ruth Clevenger, vice president and Community Affairs officer at the Federal Reserve Bank of Cleveland, asked whether the "underlying assumption that homeownership is the cornerstone of wealth creation" needs to be revisited. In all, Clevenger described the seminar as part of the Fed's ongoing outreach and information-gathering efforts as it tackles problems in the housing and credit markets.

Some other key themes that participants raised during the discussions:

- Problems with vacant and abandoned properties are almost always inextricably linked with the current credit crisis. Research that fails to acknowledge this component may fall short.
- Research helps local community development leaders gain an important sense of perspective in dealing with the problem. Some solutions may be more easily identified from a bird's-eye view.
- Small cities often lack resources, such as nearby research universities, to assist in everything from data collection to policy formulation.
- Lack of uniformity among records systems makes comparing data across municipalities difficult.
- There is a need among researchers for more data for analysis. A useful step was the 2005 inclusion of high-cost loan information in HMDA data; more such "opening up" of data sources should occur.
- An interdisciplinary approach to research on this issue is critical. Work that doesn't cross several academic fields—from economics to political science to sociology—may not fully capture causes and effects of the vacant and abandoned property problem.

Along with interdisciplinary research, moderator Joe Schilling, professor in practice at the Metropolitan Institute, Virginia Tech, and head of the National Vacant Properties Campaign, noted the need for broad partnerships to address vacant and abandoned properties. Multiple agencies are involved at one level or another with the problem. Linking them together so that none work in isolation may be crucial in achieving an effective response.