

HERA Funds Could Reduce Foreclosures and Rebuild Distressed Neighborhoods

On July 30, President Bush signed the Housing and Economic Recovery Act of 2008 (HERA 2008 [H.R. 3221]). The Act is designed to help at-risk households from going into foreclosure through FHA refinancing; stabilize the housing market; strengthen regulations and oversight; and repair the damage in communities hardest hit by foreclosures. The bill has several provisions that will significantly impact the housing industry. Among those provisions are opportunities for state and local governments to strategically curb foreclosure growth and rebuild distressed neighborhoods.

Implementation of this legislation will largely be the responsibility of the federal government, but state and local governments and local nonprofits will play critical roles. In addition to homeowner counseling, these organizations can influence the important task of rebuilding communities devastated by foreclosures. Judicious use of new federal funds could stem the tide of foreclosures, repair distressed neighborhoods, strengthen the housing market in Indiana, and even improve the tax base.

A total of \$4 billion of federal funding will be distributed among states and cities to redevelop abandoned and foreclosed homes (\$3.92 billion) and provide counseling to households threatened by foreclosure (\$180 million). The \$180 million dollars dedicated to pre-foreclosure counseling will be distributed by the Neighborhood Reinvestment Corporation by the end of 2008. The \$3.92 billion to redevelop abandoned and foreclosed homes will be distributed by the U.S. Department of Housing and Urban Development (HUD) as a supplement to Community Development Block Grants. Units of government receiving the funds will have 18 months to purchase and redevelop properties.

Like every state, Indiana will receive a minimum of \$20 million in supplemental funds. But since Indiana has been one of the states hardest hit by foreclosures, it could receive four to five times that minimum amount. The exact amounts are still to be determined, but will likely depend on the numbers of foreclosures, subprime mortgages, and homes in default or delinquency in cities and states.



Determining Indiana's Share of Supplemental Grants Received through HERA 2008

HUD is responsible for establishing the funding allocation formula for the \$4 billion. The resulting allocations will be highly dependent on the data sources used to measure need, since no federal agency directly tracks all foreclosures. Some private organizations (e.g., Mortgage Bankers Association, Foreclosure.com, and Realty Trac) provide counts and estimates, but the methods for collecting data vary and can lead to discrepancies. This is an issue HUD will address when determining the distribution of funds.

However, it is reasonable to assume that Indiana will receive well over the \$20 million state minimum for foreclosure assistance from the federal government.

According to Realty Trac, nearly 53,000 new foreclosures were filed in Indiana in 2007. This is about 2 percent of all new filings in the nation.¹ Indiana ranked 10th among all states in the number of foreclosures filed per household (1 foreclosure per 100 households in the state). In a recent press release, Realty Trac reported that the number of new filings in Indiana is increasing at a slower rate than in the nation as a whole. However, while much attention has been focused on the rapid foreclosure and mortgage delinquency growth



in western states (such as California, Nevada, and Arizona) and Florida—the Midwestern states of Indiana, Michigan, Kentucky, and Ohio still have relatively high proportions of all delinquent loans.

The Mortgage Bankers Association reported that these four Midwestern states were all in the top 10 states with the highest overall delinquency rates.² Indiana, Michigan, Kentucky, and Ohio accounted for about 9 percent of all loans in the nation. Yet these four states have about 13 percent of delinquent borrowers, subprime loans, and subprime delinquencies. Indiana alone accounts for 2 percent of all outstanding loans, nearly 3 percent of all delinquent loans, and almost 2.5 percent of all subprime loans and delinquent subprime loans.

California and Florida have been receiving a great deal of attention due to rapid increases in foreclosures. However, California has less than 14 percent of all loans nationally, but their proportion of delinquencies and subprime loans is only about 12 percent. Florida has 8 percent of all loans, and 9 to 10 percent of all delinquencies and subprime loans.

We cannot know at this point the exact formula and data that HUD will use to distribute the 2008 supplemental emergency assistance. But how the formula is developed and the funds allocated to both cities and states will further complicate the issue. Among many possibilities, the formula may include the number of new filings over a given time period, proportions of housing stock in foreclosure at a given point, delinquencies, subprime loans, and/or delinquent subprime loans. Greater weight placed on any of these measures may significantly affect how much funding each state receives. However, based on recent data from the Mortgage Bankers Association and Realty Trac, it is reasonable to assume that Indiana could receive between \$80 and \$100 million from HERA 2008.

The Benefits of HERA 2008 for All Hoosiers

Title III of HERA 2008 will enable the state and local governments, with the help of nonprofit organizations, to counsel families and purchase and repair foreclosed properties. The bulk of these funds may be used to:

- establish financing mechanisms to purchase and redevelop residential properties;
- purchase and rehabilitate foreclosed or abandoned homes to sell or rent;

- establish land banks for foreclosed homes;
- demolish blighted structures; and
- redevelop demolished or vacant structures.

As a result, strategic use of these funds can not only help families facing foreclosure, but lead to significant benefits for all Hoosiers, especially households located in concentrated areas of foreclosure.

Abandoned and foreclosed homes are bad for neighborhoods, especially when they are highly concentrated in a single neighborhood. The yards and exteriors of these houses may fall into disrepair and they may become targets of vandalism and other types of crime. The presence of foreclosed properties depresses market demand for all houses in the area, leading to lower sales prices and diminishing the home equity positions of nearby residents.

The Center for Urban Policy and the Environment, part of the Indiana University Public Policy Institute, conducts ongoing research on foreclosures in Indiana. Our research on foreclosures listed for sale³ between 2002 and 2005 shows that foreclosures are highly concentrated in central Indiana and a few other urban areas, including Gary, South Bend, and Fort Wayne. The area in Indiana with the greatest concentration and most rapid growth of foreclosures is Marion County and the surrounding counties.

Research focused on central Indiana has allowed us to identify “hot spots” of foreclosures.⁴ This analysis shows that foreclosures are more likely to be concentrated in neighborhoods with lower-income households, middle-to-lower priced homes (less than \$120,000), and where sale prices have been stagnant or declining. Foreclosures also tend to be concentrated in neighborhoods where households are spending more than 30 percent of their incomes on housing costs. But foreclosures are not just a central city problem. Many central Indiana suburban communities experienced rapid growth of foreclosures and had high concentrations of them during 2002 to 2005.

Our research also demonstrates the negative effects of foreclosures on housing prices in the neighborhoods where foreclosures are located. Using a statistical modeling technique, we estimated the effect of foreclosures on housing values in Marion County during 2004. We found that each additional foreclosure within a one-mile radius may reduce the sales price of the average house by as much as 3 to 4 percent, or by about \$3,200.



Our analysis also shows that foreclosed properties sell at margins of 26 to 29 percent less than non-foreclosed properties. When foreclosed properties are concentrated in a particular area and used as comparables for future listings, the 26 to 29 percent “foreclosure discount” may exacerbate the negative impact on the value of other homes in the area. We estimate that foreclosures reduced the value of total sales by 9 percent in Marion County during 2004. To the extent that assessed values are tied to market values and foreclosures are accurately reflected in those values, foreclosures may also contribute to higher tax rates in the future as a result of decreases in assessed values.

Capitalizing on the HERA 2008 Grant in Indiana

The state and its localities will need to monitor the nature of the foreclosure problem so they can most effectively target HERA dollars to produce the greatest benefits.

The cost of foreclosures to all homeowners justifies collective efforts to address the problem. Strategic planning should involve all parties dealing with housing—city governments, nonprofit housing organizations, and the private sector—to develop a comprehensive approach for using federal funds and addressing the foreclosure problem.

Counseling for defaulting households is a necessary step and is built into the funding allocation. This emergency funding will help build the capacity of these efforts in Indiana. It is important to target funds for areas with the highest concentrations of foreclosures and to bring more households into the system—especially homeowners who may be unaware of the service or hesitant to discuss their situation.

We need a strategic plan to effectively address the blight of abandoned, foreclosed properties left behind. These funds give the state an opportunity to address the foreclosure problem in declining neighborhoods and provide quality, affordable, income-building housing opportunities for Indiana households. The focus should be on purchase and rehabilitation of the homes that will have the greatest local impacts. A comprehensive neighborhood approach for the areas hardest hit is needed.

Preparing for the Future

Over the next several months, state and local governments will be working to understand guidelines for how the new federal funds may be used, as those guidelines are made available. Some of the emergency assistance will be directly allocated to larger cities and counties, with further allocations to the state for distribution to other areas. The governments receiving funds will then need to develop plans for using them. There will likely be a significant impact if a comprehensive and strategic approach is taken. Steps should be taken by government units to maximize the investments made through the emergency assistance and to plan for the future, for the period after all funds have been expended.

As part of this process, Indiana should build its capacity to monitor foreclosures. Currently, it is difficult to fully understand

the nature of the foreclosure problem because of a lack of information. A loan-level database available to the state would allow the state and local governments to monitor foreclosures and proactively address problems. The construction of such a database could begin with a standard data collection protocol for all counties to electronically submit to a designated state agency.

Indiana ranked 10th among all states in the number of foreclosures filed per household (1 foreclosure per 100 households in the state).

Strategies for allocating HERA funds should include plans for evaluation. An evaluation of what went well and what did not go well can help to continue and build successful programs in the future. In addition to evaluating those programs, states and localities should continue to look for additional funding opportunities to leverage against this major investment before the end of the funding cycle.

¹Realty Trac. (January 28, 2008). *U.S. Foreclosure Activity Increases 75 percent in 2007*, Press Release.

²Mortgage Bankers Association. (December 31, 2007). *National Delinquency Survey, Fourth Quarter 2007*.

³Data were provided by foreclosure.com.

⁴Data include all Real Estate Owned properties listed by the Metropolitan Indianapolis Board of Realtors

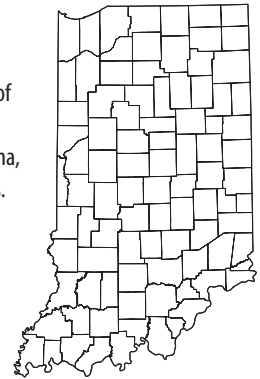


Indiana's Future: Identifying Choices and Supporting Action to Improve Communities

This project, funded by an award of general support from Lilly Endowment, Inc., builds on the Center's research to increase understanding of Indiana. The Center's faculty and staff work to identify choices that can be made by households, governments, businesses, and nonprofit organizations to improve the quality of life. The Center's goal is to understand the people, economics, problems, and opportunities in Indiana, and to help decision-makers understand the impact of policy decisions. The Center also works to mobilize energy to accomplish these goals.

The Center does ongoing research on housing in Indiana and issues that affect local communities. This issue brief focuses on the Housing and Economic Recovery Act of 2008. This bill has provisions that will offer opportunities for state and local governments to strategically curb foreclosure growth and repair the damage from foreclosures in distressed communities.

The Center for Urban Policy and the Environment is part of the Indiana University Public Policy Institute and the School of Public and Environmental Affairs at Indiana University-Purdue University Indianapolis. An electronic copy of this document and other information about other community issues can be accessed via the Center Web site (www.urbancenter.iupui.edu). For more information, visit the Web site or contact the Center at 317-261-3000.



State of Indiana

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