Neighborhood Housing Services of New York City

Written Testimony of Sarah Gerecke before the House Financial Services Subcommittee on Financial Institutions and Consumer Credit

Effects of the Subprime Mortgage Crisis in New York City and Efforts to Help Struggling Homeowners
February 11, 2007

To Representative Maloney and the honorable members of the Subcommittee:

<u>Summary</u>

My name is Sarah Gerecke and I am the Chief Executive Officer of Neighborhood Housing Services of New York City (NHS). For 25 years, NHS has provided New Yorkers with the affordable loans and housing education they need to buy, improve and keep their homes and keep their neighborhoods strong. Our nine offices partner with corporations and government to help more than 10,000 people each year. In our efforts to build strong communities, we are led by local residents and guided by local needs. Since 1982, we have invested $2 billion into underserved communities, helping thousands of New York City homeowners.

In 2007 alone, NHS with its corporate and government partners invested nearly $230 million in New York City communities, leading our national NeighborWorks America network. We educated more than 9,700 residents, helping them to build wealth and avoid scams. More than eighty percent of our customers are African-American, Asian or Latino; most are first-generation immigrants; and most have critical jobs like bus drivers, health aides, teachers and police officers. And I'm sorry to say that last year we had more than 2,000 people contact our offices for help in avoiding foreclosure, many more than we could serve with existing resources.

The high rate and geographic concentration of mortgage defaults and foreclosures in certain neighborhoods will exacerbate the already severe effects of the current economic recession. This testimony outlines some of the devastating consequences of recent mortgage lending on New York City neighborhoods. In addition, it documents the widening circle of the economic costs of foreclosure and default affecting individual homeowners, neighboring homes, local businesses, municipal government and the local and regional economy.

We propose several types of intervention to stem the continued decline and boost the local economic base. Using existing and new tools, a vibrant network of nonprofits, governments, private sector and philanthropies is poised to tackle the problem, building on lessons learned from the successful resurgence of New York City from the 1977 fiscal crisis.

Federal tools can be a powerful source of leverage and stability. We recommend the following:

- Increased support for pre-purchase counseling, foreclosure prevention counseling and legal services, including funding to increase capacity of counseling organizations;

- Greater consumer protection during the mortgage origination, refinancing and loan modification process;
- Flexible federal funding for innovative programs targeted to help affected homeowners and stabilize neighborhoods

<u>Overview</u>

Commentators will say that the foreclosure situation is not as bad in New York City as it is in Las Vegas or Cleveland. But the situation here is very grave; the condition of some neighborhoods has declined dramatically even in the last three months and we think it will be much worse in 2008 and 2009. Sarah Ludwig of NEDAP will tell you that more than 14,000 homeowners faced mortgage default in 2007. NEDAP maps show the strong correlation between subprime lending, mortgage foreclosures, race, and the lack of bank branches. NHS neighborhoods in four counties are hardest hit: Southeast Queens, Northeast Bronx, Central Brooklyn and the north shore of Staten Island. And the data reporting does not keep up with the rapid changes taking place today.

I think it's important to remember the role that the home plays in a family and in a neighborhood. The traditional 30-year, fixed rate mortgage—invented in the Great Depression—is a beautiful thing. A family gets started and learns to save in order to afford the 20% down payment and closing costs. By their mid-30s, they are ready to buy a house; their family size and income are stable, and they do not expect to move. They purchase with a prime loan and pay a fixed amount that provides certainty and stability to the family as they plan for college, a rainy day fund for home repairs or illness, and eventually for retirement. At age 65, just when they need it, the home is paid off and the cost of housing drops dramatically as they transition to a fixed-income from their pension or social security.

Until a few years ago, this was the model for working class New York City neighborhoods. Most families lived in their home until they passed away. Turnover was very rare, and often the estate sold the home or it was passed to a family member as a form of intergenerational wealth. Fewer than two or three homes on a block in NHS neighborhoods were sold in any given year before the late 1990s.

I think it's important to remember this in order to understand the impact that subprime lending is having on NYC neighborhoods today. You are familiar with the primary impact of foreclosures on a family: the loss of savings, equity, and ultimately a home. But the collateral damage is worse, frankly, and it is taking two forms:

<u>Collateral Damage to Families</u>

The families who come from us for help are struggling to keep up with unaffordable loans. They take on two or three jobs, leaving children unsupervised and unsupported emotionally. They burn through their savings, using credit cards to pay for necessities, and causing their credit scores to plummet as a result. They have less disposable income for food or health care. A City University study documented that "People experience a range of intense emotions such as depression, anxiety, hopelessness, confusion, fear, and victimization when they are behind on their mortgage payments."[1] They are targets for many scams the minute their house appears on lists of mortgages in default.

If they have to leave the home through foreclosure or distress sale, their lack of savings and poor credit limits their options in the New York City rental market which still has only a 3% vacancy rate.[2] Children are pulled from school mid-year, and it may be harder to maintain employment while looking for a new place to live. They worry about becoming homeless, and some of them do. A bankruptcy or foreclosure remains on the public record for years, limiting choices in employment, housing and education. Regardless of the reasons that the family loses the home, the entire family and especially the children bear the costs for many years to come.

<u>Collateral Damage to Neighborhoods and the Local Economy:</u>

Many others are deeply affected by a family in distress. For families renting units in 2-4 family homes (the predominant ownership form in New York City), a foreclosure imposed on the building's owner (their landlord) results in the termination of the renter families' underlying leases; lenders usually insist on vacating an entire building following foreclosure.

[1] Desirèe Fields, Kimberly Libman, Susan Saegert, PhD, Heléne Clark, PhD, & Fran Justa, PhD, "*Understanding Responses to the Threat of Foreclosure Among Low-Income Homeowners*" (City University of New York: July 2007).

[2] New York City Housing and Vacancy Survey (2006).

These homes are not scattered evenly throughout the city. Studies conducted by NHS indicate the tremendous concentration of subprime lending in target neighborhoods. Our research shows that 50% of the homes on some blocks in South Ozone Park or Bedford-Stuyvesant or Williamsbridge, for example, have mortgages with features most likely to result in default: 2/28 ARMs, prepayment penalties, piggybacks, high loan-to-value ratios and/or investor-owned homes.

And the signs of distress are quite visible now. Formerly pristine blocks in Corona or Bushwick are showing signs of deferred maintenance. For sale signs – ten on some blocks—are distress sales, not the normal desire to retire and relocate. Saddest to me are the "for rent signs" on the windows as homeowners take in boarders to help make ends meet. More tragic for neighborhoods are investor-owned properties. Some remain vacant—four or five on a block—and some are stuffed with renters who are living in dangerous and sometimes illegal conditions. The vacant homes do not always show up as recorded foreclosures. It is difficult for nonprofits to identify the servicer so that we can intervene and get the properties into the hands of qualified owner-occupants rather than speculators.

The impacts are not always predictable. "Many times, if there's a foreclosure, people just walk away," said Mark Loffredo, president of Post Exterminating Co. in Tompkinsville, Staten Island. "The yards get overgrown and rodents find it conducive to habitation. If they recognize that there's nothing to stop them getting in, they will nest in the house. They do search for habitat and they're always searching for food."[3]

Districts that finally emerged from the blackout of 1977 such as Broadway in Bushwick or White Plains Road in Williamsbridge are now seeing the "broken teeth" effect where three or four businesses on the strip are suddenly shuttered. The New York Times[4] documented the hardship faced by commercial strips where stores have gone out of business for lack of customers. In some areas business was off by 50% or more, as strapped homeowners cut costs. Infill construction sites have become ghost towns, scattered with abandoned construction equipment as buildings languish on the market without sale. The latter problem is particularly dangerous, as the sites invite criminal activity and safety risks, and deplorable as New York City still faces a major housing shortage.

Once the bank moves to foreclose, short-term investor interest continues to outweigh the local neighborhood interests, and can lead to accelerated declines in property values. While some servicers take their obligation seriously to maintain the property and find a responsible new buyer, others let the properties fall into disrepair and sell to speculators. Moreover, the ownership of defaulted and foreclosed property is fragmented among different servicers and investors, and difficult to ascertain from

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[3] Glenn Nyback, "Slumping Real Estate Market a Boon for Rodents" (Staten Island Advance, January 26, 2008)

[4] David Gonzalez, "Holidays Find Loan Crisis Spreading to Businesses and Neighbors" (New York Times, December 17, 2007)

public data. The current system of default and foreclosure is wreaking havoc on the neighbors: responsible homeowners who are paying their loans but watching their home become devalued because of their neighbor's default.

The end result is a massive damper on the regional economy that is affecting the entire nation. A November 2007 report prepared for the US Conference of Mayors identifies the New York City Metropolitan Area as facing the highest projected loss of Gross Metropolitan Product during 2008 of any city they studied… more than $10 billion relating to the mortgage crisis, taking into account losses from employment, taxes, spending and property values. The same report estimates New York State losses due to reduced tax revenue of nearly $900 million.[5]

Resources Available and Needed:

NHS has been providing foreclosure prevention services since 1996, when we first noticed abusive lenders coming into our communities. In addition to providing one-one-one counseling, loss-mitigation counseling and education seminars on the issues at hand, NHS provides outreach to its communities. Our grassroots techniques will continue to include a massive educational effort to empower consumers to ask questions before borrowing and seek assistance when necessary.

Last year NHS received additional funding from local and state government to add more foreclosure prevention counseling staff, so that today we have five counselors and two

[5] Global Insight, "US Metro Economies: The Mortgage Crisis; A Report for the US Conference of Mayors" (November 2007).

support staff. It's not nearly enough to handle the 10 or more customers asking for help every day, and my fellow counseling agencies throughout the city feel similarly overwhelmed. Our toolbox is limited to providing unbiased advice, connecting borrowers to servicers, and providing referrals to legal or social services where appropriate. We don't really have the tools to stabilize families or target entire blocks for the long term.

We have received assistance at all levels of government that is helpful. The money that Congress appropriates for Neighborhood Reinvestment Corp. (d/b/a NeighborWorks America) is by far the most useful, and comes to us in several forms: both direct financial support and technical assistance to help us with best practices and maximizing our impact. Congressional appropriations for housing counseling will let us recover some of the direct service costs we can't cover otherwise. We are extremely grateful for Congress' recent increased funding of foreclosure prevention counseling (through NeighborWorks America) in FY 2008. This additional money for foreclosure prevention counseling will enable NHS of NYC and the hundreds of HUD-certified counseling agencies citywide and nationwide to assist the rising number of families facing default. However, additional federal investment is still needed.

The national partnerships with the HOPE hotline and the HOPE NOW alliance benefit our customers directly, and we have seen some increased flexibility from those lenders; however I must say that servicers vary widely in their willingness or ability to help. We use state Housing Finance Agency and the Federal Housing Administration refinancing products wherever possible. HUD-insured reverse mortgages can also be helpful tools in some situations.

At the state and local level, we have been involved in the launch of the Center for New York City Neighborhoods, a new organization to create a comprehensive, coordinated, citywide network to respond to the threat of foreclosures. The Governor's HALT (Halt Abusive Lending Now) initiatives have been creative and effective. At the neighborhood level, NHS has developed with key partners several innovative programs, including neighborhood outreach collaborations, a Rescue Loan Fund, a nonprofit mortgage brokerage, and limited charitable funding to assist families facing immediate hardship. Some foundations and corporations have begun to provide support for these innovations.

However, all of these resources available to fight the problem are a fraction of the need. Funding for additional counselors is helpful, but we also need funding to build capacity: data systems, management expertise, research, policy, program design and evaluation, etc. We need mental health support for our counselors. They are burning out and taking work home and giving out their personal cell phone numbers because the needs are so heartbreaking and urgent. For a nonprofit, funding for increased capacity is extremely difficult to come by yet it is essential for creating an effective, efficient and quickly scalable program. Finally, none of these tools allow us to target an entire block or neighborhood to stop the downward spiral and help the market to stabilize.

What Can Congress Do?

Our traditional sources of funding—charitable contributions from the financial services industry—are at great risk this year, at the time of our greatest need. As banks post record losses, they are also cutting back substantially on their foundation contributions which provide one-third of our operating budget. Investment banks and hedge funds do not participate in our programs right now and perhaps some federal incentive funding or expansion of the community investment act requirements could attract these entities. We desperately need support to build our organizational capacity to do what is asked of us: provide unbiased counseling on a large scale, match borrowers to their servicers, and quickly refinance those who qualify into responsible loans. Our partners providing legal services, outreach and education need similar support to build their organizational capacity.

Support for pre-purchase counseling should also be widened; prevention is much cheaper and more effective than loss mitigation. Studies show that borrowers who receive qualified pre-purchase counseling have 34% fewer mortgage delinquencies than borrowers who received none.[6] People are still buying homes today, and they need the knowledge to make homeownership a success. And strong consumer protection standards are needed in the lending process, for mortgage originations, refinances and for loan modifications too.

[6] Harad,Abdighani and Peter Zorn, "A Little Knowledge is a Good Thing: Empirical Evidence of the Effectiveness of Pre-Purchase Counseling" (Harvard Joint Center for Housing Studies, 2003)

Congress can provide a quick win through an emergency allocation of Federal funds to stabilize the worst-hit blocks. As demonstrated by The Enterprise Foundation and others, direct federal investment through the Community Development Block Grant (CDBG) program would allow existing partnerships to work effectively with investors, lenders, servicers and government to immediately address neighborhood impacts. CDBG flexibility is particularly useful to generate the maximum leveraging of private resources, encouraging servicers to negotiate with borrowers and to quickly mark loans to new market values. This temporary investment will thus stop the overcorrection of the market that is currently occurring.

Each community is different, and CDBG is flexible enough to meet a wide variety of conditions and markets. Federal funding could be used to purchase foreclosed property, or promote the purchase or restructuring of marked-down loans, or develop a model response to buy properties prior to foreclosure in order to avoid investor ownership. And direct federal funding can encourage innovation and unique solutions for unique markets, leveraging local and private resources as it has for decades. There are too many actors, and too much disruption in the market, to stop the downward spiral of default, foreclosure, vacancy, lower values, job loss and re-default. A targeted and coordinated response on the hardest-hit blocks would provide the confidence and tools to restore economic health. Any Federal funds that are needed to address particular neighborhood conditions would be recycled as properties are developed and sold and values are stabilized.

For New York City, some CDBG rules should be streamlined or waived. Many families targeted for abusive loans earn more than current CDBG income limits, especially if they are receiving rental income from any of the units in a 2- to 4-family home. Geographic targeting to mortgage default hot zones would allow for the most effective forms of intervention.

NHS and similar organizations have the experience and the infrastructure to restructure mortgages and to purchase, repair and resell foreclosed property to responsible owner-occupants. For twelve years we have renovated and sold HUD- and HPD-foreclosed properties. A model program targeted to hardest-hit areas, working with investors, servicers, government and nonprofits, could acquire, rehab and resell the properties quickly and efficiently—as we did during the New York City fiscal crisis of the 1970s. Properties would be repaired to meet HUD housing quality standards, and sold to counseled buyers who could afford them for the long term.

Conclusion

We are deeply grateful to Representative Maloney and the Subcommittee Members for focusing attention on this terrible problem. The conventional wisdom is that New York City is not as hard hit as other parts of the country. My organization believes that this conventional wisdom is wrong. Our neighborhoods and local businesses are in desperate trouble today. An immediate, significant and geographically targeted intervention is needed to staunch the flow of equity and investment that is draining New York City neighborhoods of their hardworking residents and draining them of hope. NHS is eager to join our colleagues and partners to address the current crisis quickly, creatively and energetically to restore healthy communities and stable homes to the neighborhoods that are the backbone of the city, regional and national economy.