

**Testimony of Frank Ford
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**In Support of House Bill 323
Before the Housing and Urban Revitalization Committee
Ohio House of Representatives
Wednesday, November 18, 2009**

The story of the foreclosure crisis in Ohio begins with abusive lending that was merely negligent at best and predatory at its worst, and climaxing with a wholesale emptying out of homes. But that's not the end of the story. Like a tsunami, each annual tidal wave of foreclosures has left in its wake hundreds of thousands of vacant, blighted, and vandalized properties. The immediate damage—the disrupted lives resulting from the emptying of their homes—has been followed by collateral damage to neighboring homeowners, and their communities at large.



A graphic illustration of this is presented by two houses in Cleveland depicted in the photograph above. The house on the right was built by the Buckeye Area Development Corporation, a local nonprofit community development corporation (CDC), in 2004 and was sold to a homeowner for \$141,000. In 2006 Wells Fargo foreclosed on the house on the left and took the property at a Sheriff Sale, and that house became vacant. Wells Fargo let it sit vacant for two years, while it

was broken into, vandalized and became a public nuisance. Wells Fargo then sold the damaged house to an investor in 2008 for \$1,200.00 and the investor continued to let it sit vacant and deteriorating. The owner of the house on the right, a single mother with two children, could only watch while the value of her home plummeted. If she had to sell her home today she'd be lucky to get \$80,000 for it.

The full measure of the post-foreclosure damage is understood only when one considers that every blighted house could negatively impact five or six other houses near it. In Cleveland today, there are an estimated 11,500 vacant houses¹ so those vacant homes could easily impact the market value of 60,000 occupied homes. So, speaking to scale, if each home lost \$10,000 in value [*a conservative estimate*], it would equate to a \$600,000,000 loss of homeowner equity. But the cost of foreclosure doesn't end there. The decreased market value represented by this loss of equity will inevitably result in a loss of property tax assessment and lost tax revenue for publicly supported schools, police, fire and social services.

The saga is doubly tragic because of how it has undermined, and continues to undermine a highly regarded community development system in Cleveland that was making steady progress through the 1990s and the early part of the 2000s. Unfortunately, while that system injected homeownership equity into the front door of neighborhoods, by way of responsible local lenders, there were irresponsible subprime lenders and Wall Street investment bankers who mined neighborhood equity and extracted it out the back door.

Much of the news coverage over the past several years has focused on the reckless acts of financial institutions that led to wholesale foreclosures—either making bad loans or recklessly buying thousands of those loans without exercising any due diligence to determine what they were buying.

In the case of those financial institutions that bought the mortgages, specifically the servicers and trustees who manage the loan pools, it appears that the same irresponsible decision-making that brought us the foreclosures in the first place is now compounding the problem by the manner in which it's handling post-foreclosure blighted property—what banks refer to as REO property, or “real estate owned,” by the financial institutions.

In this regard, Cleveland may again serve as a useful illustration, and to some extent, as a warning, to other cities that may not yet have experienced a severe post-foreclosure problem. Any city, regardless of how strong its real estate market might appear, could suffer a market failure if it reaches a critical mass of foreclosures. For hundreds of years foreclosures have worked as a successful debt recovery mechanism, when there is but a single foreclosure

¹ Estimate provided by the NEO CANDO data system, Center for Urban Poverty and Community Development at Case Western Reserve University, as of October 1, 2009.

surrounded by otherwise stable occupied homes. The foreclosed home can be quickly re-marketed, re-sold and the loss minimized. But when lenders flood neighborhood markets with bad loans, and then flood the same neighborhoods with foreclosed blighted property, the system breaks down completely. Streets in Cleveland that had no foreclosures five years ago, now have four or five. Streets that had a few foreclosures now have 10 to 20.

The growth of this problem in the past few years, and its impact on foreclosure re-sale, is illustrated by a study recently done by Case Western Reserve University². In 2005 less than 10 percent of REO property in Cleveland was sold by banks for less than \$10,000. By 2008, 65 percent of the REO sales by banks were for less than \$10,000—such as the house in the photo above, sold by Wells Fargo to an investor for \$1,200. A \$1,200 sale would appear to be no bargain for the bank. But consider that the house (pictured) probably has \$50,000 or more in code violations. After sitting for two years and being repeatedly vandalized, the damage could require all new mechanical systems, new plumbing, new wiring, mold remediation and more. Moreover, if the city were to demolish the home, the vacant lot would then have a \$10,000 demolition lien against it. Vacant lots in Cleveland typically sell for \$500 to \$1500, often more than foreclosed homes in poor condition. A vacant lot with a \$10,000 demolition lien against it is a liability with a negative value.

What we now have taking place in Cleveland is an “REO Race” – can the financial institutions “unload” or “dump” their liability for public nuisance property before the local municipal code enforcement officials catch up with them? In their race to dump property, the banks are making no effort to screen the buyers.

So who’s buying these properties and what are they doing with them? The buyers range from inexperienced individuals who watch the late-night infomercials and become captivated by the promise of making millions from real estate, to a new niche industry that seems to have sprung up in the past decade – companies, most of which are out of state, that specialize in making bulk purchases of vacant foreclosed homes. *[A representative list of these companies is attached to my testimony]*. Their business models vary – some merely act as wholesalers and flip the package of 10 to 20 homes to another investor for a small markup; some post them on Ebay without making any repairs; some make a bulk purchase only to acquire one decent prospect, knowing they will abandon the other properties. The best of them actually do some renovation, but usually cosmetic only without addressing more serious issues before putting the house back on the market. This was made clear to me last Summer when I had the opportunity to join with other colleagues to spend a day meeting with two out of state investors to discuss their business goals and objectives. One of the most striking admissions came when one of them said “if we

² “Beyond REO: Property Transfers at Extremely Distressed Prices in Cuyahoga County 2005-2008”, Center on Urban Poverty and Community Development, Case Western Reserve University, December 2008.

had to bring these properties up to code, our business model won't work." In other words, they were saying "we're going to come into your community and we plan on violating your housing codes".

Evidence of intent to evade local housing laws is made abundantly clear by the docket of the Cleveland Municipal Housing Court. In the period beginning January 1, 2009 through October 23, 2009, the Court levied \$1.5 million in fines to 11 corporate REO investors for failing to show up for court hearings. *[The Court's list of fines is attached to my testimony.]*

Foreclosures per se are not the true cause of damage to neighborhood markets. The real damage is being done after tens of thousands of homes are emptied out, and those doing the emptying take no responsibility for the physical condition of the vacant home.

The vast majority of foreclosures are being initiated by out of state financial institutions. They want the privilege of using the state's legal apparatus to bring foreclosure actions, but they don't want to be held accountable for state and local laws pertaining to health and safety codes. Moreover, foreclosing financial institutions want the privilege of offloading their liability for public nuisance property by dumping those defective assets to investors who are demonstrating the same disdain and contempt for Ohio's laws.

With House Bill 323 the Ohio legislature has an opportunity to take important steps toward 1) halting the ancillary public nuisance damage from foreclosures and 2) protecting the assets of homeowners throughout Ohio. I strongly support this bill and urge you to give it full consideration.

Thank you,
Frank Ford

Additional Documents Submitted

List of Buyers Purchasing From Banks Out of REO [City of Cleveland]

List of Per Diem Fines Levied By Cleveland Municipal Housing Court

Power Point – Cleveland Properties Owned by Interstate Investment Group

Housing Market Facts and Trends

Digital Video – Foreclosed Wells Fargo Property (2 minutes, 45 seconds)