"If you build in all those costs into market-rate housing, it certainly results in costs more than the market value," said Graziano. "So if we are trying to reestablish a market, then we must have an infusion of capital."

Another difficulty with Section 108 loans, said Graziano, is the requirement to put up collateral equal to the value of the loan.

To get a Section 108 loan, a development agency can pledge up to five times its CDBG entitlement amount, which Graziano said should be adequate since it is unlikely that Congress would stop funding the program.

Under current rules, Baltimore typically must use the land at a project as collateral. This creates a problem during development, Graziano said, since new collateral must be found as portions of the land are released to a developer.

Other Problems

Graziano identified several other technical problems that HUD must deal with in creating Choice Neighborhoods. The use of census tracts to identify neighborhoods could be more flexible, and HUD could allow portions of census tracts to be used, he said.

Graziano also said that HUD often places unrealistic restrictions on multifamily properties it transfers, requiring that HUD receive all future net profits on any resale in perpetuity. This can be a deal stopper, he said, especially for condominium units where the resale restriction affects both the developer and future homeowners.

The restriction on the use of HUD funds in connection with eminent domain is also a big issue, Graziano said. HUD funds can be used if a taking is for a public purpose, but Graziano said the definition is so narrow that the replacement housing must have 100 percent affordable housing units.

"This is antithetical to the notion of eliminating blight and then creating a redeveloped community with mixed-income housing," he said.

AFFORDABLE HOUSING

Reno Housing Authority Uses Neighborhood Stabilization Funds To Buy, Rehab Vacant Properties

The Housing Authority of the City of Reno, Nev., (RHA) has purchased 52 single-family properties to rehabilitate for resale or rental through the neighborhood stabilization program (NSP) and other funding sources to help steady a real estate market troubled by steep price declines and foreclosures during the past two years. RHA also hopes to get additional NSP grant funds to continue these activities.

David C. Morton, RHA executive director, said that the agency has successfully acquired vacant properties because it has its own financial resources that can be used early in a transaction, with subsequent reimbursement with NSP funds. Morton said that RHA's previous experience with single-family purchases has proven useful.

RHA is the subcontractor of a $4.2 million NSP grant made to the Washoe County HOME consortium. As the lead jurisdiction in the consortium, the city of Reno selected RHA to administer the grant, setting aside $1.2 million for low-income renters and designating the rest for the purchase and rehab of homes to families with incomes up to 120 percent of area median income.

RHA has purchased or has sales pending for 31 single-family homes through the NSP and has enough remaining funds to buy two additional houses. RHA also has bought 11 HUD-held homes through the Good Neighbor program and has used non-HUD funds to buy four single-family homes for rent to low-income families.

In addition, six houses were purchased through a $588,000 economic development initiative (EDI) grant sponsored by Sen. Harry Reid (D-Nev.). Five of these homes are being rehabbed with $320,000 in HOME funds and rented to low-income households. These funds were targeted to the low-income Oliver Montello neighborhood. One house, due to its poor condition, was purchased and demolished.

Third-Party Facilitator

RHA has agreed to work with the National Community Stabilization Trust's First-Look program, which facilitates sales of bank-held properties to local nonprofits and for-profit housing groups.

Banks or other lenders with real estate owned (REO) properties notify local buyers of properties within their target areas. The potential buyers must indicate within 24 hours if they are interested and have five days to review and inspect properties and determine their as-is value.

The financial institutions in First-Look calculate the prices for which they are willing to sell, taking into account cost savings realized from the expedited sales process. The Trust also has bridge financing available to facilitate transactions.

Minimizing Costs

To minimize NSP rehabilitation costs, RHA has followed a strategy of buying only houses that are in relatively good condition. RHA bought 15 foreclosed three-to-five-bedroom houses in the Stead development in Reno built from 1999 to 2005.

Near the crest of the market, these homes were valued near $300,000, but the current appraised values are between $82,000 and $173,000. RHA bought them at discounted prices ranging from $73,000 to $161,000.

The purchase prices of older properties in Sparks and Sun Valley have tended to be somewhat lower than at Stead. Rehabilitation costs for all NSP houses have varied from about $15,000 to about $30,000.

Overall, RHA will not break even with the costs for NSP and receives only a small amount for administrative costs. However, Morton said that stabilizing the market and adding to RHA's inventory of affordable rentals have been the overarching goals.

In an indication that the Reno housing market is stabilizing, RHA has encountered competition at the low end of the market from investors and first-time home buyers. This is good for the market, said Morton, but it also means RHA must be nimble and act quickly to compete.

Since RHA must have an inspection, appraisal, environmental review, and, for properties over 50 years old, a historic preservation review, it is difficult to compete for a property on the open market, Morton said. An environmental review takes a week to 10 days, and the historic preservation review takes up to 30 days, and the reviews must be completed before RHA can obligate funds, Morton noted.

Property Search

Morton said that RHA searches for potential troubled properties by, for example, driving through neighborhoods to scout out homes with lock boxes or a notice that that a house has been winterized. At times, RHA has performed an inspection before a property is officially offered for sale.

RHA performs its own inspections, but contracts out most of the rehabilitation work, and the city performs environmental reviews. In this economy, bargains are found for construction and appraisers, said Morton, who added that the business has helped keep some contractors in business.

RHA could purchase additional foreclosed properties if it had more funds, said Morton. RHA may get additional NHP formula funds through a state reallocation this year, and it has been awarded $21.0 million in American Recovery and Reinvestment Act (NSP2) funds as the lead agency for the consortium.

Under the plan it submitted, RHA would purchase about 200 vacant foreclosed homes for rehabilitation, including energy-efficient improvements, over three years. A portion of these homes would be resold at discounted prices with grants and forgivable loans to eligible families.

In addition, RHA would use properties it owns as collateral for a $1 million loan from the Idaho-Nevada Community Development Financial Institution, Inc. to buy additional properties in the NSP2 target areas.

This funding would be used to buy properties at auction when it is not possible to go through the federal requirements for buying homes. In addition, the RHA board has set aside 100 rental vouchers for investors that purchase vacant foreclosed properties in NSP target areas, make energy-saving improvements, and submit them to RHA for designation as project-based voucher dwellings. In return for this private investment, RHA would commit a rental subsidy for 10 years.

AFFORDABLE HOUSING

Los Angeles Finds Problems with Neighborhood Stabilization Program

The Los Angeles neighborhood stabilization program (NSP) has gotten off to a slow start, due in part to competition for properties from investors and high rehabilitation costs, according to a third quarter 2009 report from the city housing department.

The city received a $32.8 million NSP grant and operates a walk-in program that provides purchase and rehabilitation funding to eligible home buyers. Restore Neighborhoods LA., Inc. (RNLA), a nonprofit, also purchases real estate owned (REO) properties for rehabilitation and resale to home buyers.

In some of the lowest-income neighborhoods, there has been unusually high demand for foreclosed properties, with investors who are cash purchasers competing with low- and moderate-income NSP buyers, the city said. Real estate brokers reportedly prefer easy cash deals from sales of "as is" properties that can close quickly.

Rehabilitation Needs

Rehab needs are substantial, and the city has found that many problems are hidden from home buyers. Some NSP sales have been canceled after inspection because the rehabilitation cost exceeded the $75,000 limit the city has set. The city also reports that many listing agents and brokers for REO properties avoid FHA or VA financing because of the inspection requirements.

To address these problems, the housing department has held training sessions with over 700 lending and real estate professionals. The city revised the purchase assistance loan documents to remove reference to the rehabilitation requirements for the property.

Some lenders have refused to fund loans if these requirements are mentioned, believing that their investors will not buy the loans with this documentation. Instead, the city has created separate loan documents to be executed by borrowers after the close of escrow.

The housing department said that if properties in the walk-in purchase program can't be rehabilitated to its standards, it will transition the program primarily to support buyers of properties that have been purchased and rehabilitated by RNLA prior to sale.

RNLA had reviewed over 90 properties referred through the National Community Stabilization Trust and had 17 in its production pipeline in the third quarter. RNLA also has taken steps to obtain properties from other sources, including REO listing brokers and Fannie Mae.

MORTGAGE FINANCE

FHFA Issues Final Rules to Allow Non-Insured CDFIs to Become Federal Home Loan Bank Members

The Federal Housing Finance Agency (FHFA) has issued final regulations implementing Housing and Economic Recovery Act (HERA) provisions authorizing community development financial institutions (CDFIs) to become Federal Home Loan Bank (FHLB) members.

The rules were published in the January 5 Federal Register and go into effect on February 4.

The newly eligible CDFIs include community development loan funds, venture capital funds, and state-chartered credit unions without federal insurance that are certified by the CDFI Fund. CDFIs which are federally insured depository institutions were already eligible for FHLB membership.

In a revision to the proposed regulations published on May 15, 2009, the final rules make clear that CDFIs which are holding companies for insured depository cannot ob-