FURMAN CENTER
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SCHOOL OF LAW • WAGNER SCHOOL OF PUBLIC SERVICE

JANUARY 2010

FURMAN CENTER FACT SHEET

Foreclosed Properties in NYC: A Look at the Last 15 Years

In many parts of the country, the foreclosure crisis has created a glut of properties owned by banks, mortgage companies, mortgage-backed securities trusts and other investors in mortgages (all of which we refer to as "lenders"). These homes, often called "REO" properties,[1] can harm communities in many ways. First, while they are REO, properties are almost always vacant, leaving them vulnerable to vandals and thieves. Furthermore, because large financial institutions or mortgage trusts see the properties as minor assets, they sometimes do not make maintenance of the properties a priority, and the neglected properties then can become neighborhood disamenities. If the condition of REO properties deteriorates, local governments (and their taxpayers) may be stuck with the cost of providing added police and fire protection, code enforcement and, in the worst cases, demolition. In addition, because foreclosing lenders often put REO properties back on the market immediately, these properties can swamp already weak real estate markets, further pushing down home values. Finally, some investors in REO properties let the properties deteriorate further while they hold them for resale, or quickly resell the properties after making cosmetic repairs that may hide the properties' serious defects.

Despite the possible negative impacts REO properties can impose on surrounding neighborhoods, little is known about the nature or size of the stock of REO properties in New York City, in large part because there is no reliable or publicly available source of data on REOs. The Furman Center has analyzed property sales data from the past 15 years to fill this gap.[2] In this fact sheet, we describe what happens to properties that enter foreclosure and provide detailed data about the size of the REO stock, the length of time properties stay as REO, and the sales of properties out of REO. We report on these trends over the past 15 years, paying particular attention to changes in recent years as a result of the current downturn.

1 "REO" stands for "Real Estate Owned," a shortening of the "Other Real Estate Owned" category of assets that appears on the financial statements of mortgage lenders. REO properties are just a subset of vacant properties resulting from the foreclosure crisis; many properties are likely vacant well before they complete the foreclosure process and become bank-owned, because the owners and tenants have left the property.

2 See the Methodology section for more detail on how we identify REO properties.

How does a property become REO?

At the beginning of the foreclosure process in New York, a lender files a notice in the public records called a *lis pendens* (LP). Lenders typically issue an LP after the borrower is more than 90 days behind on her mortgage payments. While the filing of a mortgage-related *lis pendens* is a clear sign that the homeowner is having trouble making her payments, a completed foreclosure is not inevitable. A homeowner behind on her payments may be able to refinance or modify her mortgage to return to good standing with her lender, stop the foreclosure process, and stay in her home. If real estate prices have held up, the owner may be able to sell her home and repay the mortgage with the proceeds. However, if the owner is unable to catch up with her mortgage payments, modify her mortgage, refinance or sell, a mortgage lender in New York will likely move the foreclosure process towards its end: a public auction of the home conducted by a court-appointed referee.[3] From *lis pendens* to auction, the full foreclosure process in New York City typically takes about 12-18 months.

3 In some cases, a homeowner in foreclosure may agree to convey her home directly to her mortgage lender in order to avoid the final stages of the foreclosure process and to be formally discharged from her debt—a transaction known as a "deed in lieu of foreclosure," or just "deed in lieu."

At the auction, private bidders have an opportunity to purchase the house (throughout this paper we refer to such sales as an "auction sale"). But if there are no bids that meet the foreclosing lender's minimum price (typically the amount of the outstanding mortgage balance), the foreclosing lender will acquire the property itself. So, while a foreclosure action is not, technically, a "repossession," because other bidders have an opportunity to buy the house before the lender ever owns it, the foreclosing lender does often end up taking title.

Once a lender owns a property, whether as a result of a foreclosure auction or a deed in lieu, the property is an REO property. Most lenders will evict any homeowners or tenants who are still in a home that becomes REO in order to make the property more marketable.[4] The lender will then inspect the home, make certain repairs, if needed, then list the house for sale. Lenders sometimes rely on large, well-publicized auctions to sell REO properties, but most sell REO properties through conventional real estate brokers, who market the homes on-line and in the print and broadcast media, as they would any other property listing.

4 In May, 2009, The Protecting Tenants at Foreclosure Act (part of SB 896) was enacted, requiring lenders who acquire REO properties to honor existing leases or, in the absence of a lease, to provide at least 90 days notice before eviction.

What are the characteristics of properties that enter foreclosure in New York City?

Of the more than 100,000 New York City properties that entered foreclosure between 1993 and the first half of 2009, the vast majority were 1-4 family buildings: 34% were single family homes and 50% were 2-4 family buildings.

For properties that received an LP between 1993 and the first half of 2009, the median time from when the borrower purchased the home (which we refer to as the "initial sale") to the filing of a *lis pendens* was just under three years. In other words, half of homeowners went into foreclosure less than three years after buying their homes. Beginning in the early 2000s, however, with the rise of subprime lending and the increase in buyers taking out risky (and sometimes multiple) loans, the length of time between an initial purchase and a foreclosure filing became even smaller. Of the foreclosure filings issued in 2007, the median time between the initial sale and the LP was only 1.5 years. In fact, a full 30% of the filings in 2007 were on properties that had been owned for less than one year. Because an LP is filed only after a borrower is delinquent on her mortgage for more than 90 days, this figure represents a troubling number of borrowers that defaulted almost immediately upon acquiring their homes. Fortunately, that trend appears to have slowed: in 2008, 12% of foreclosure filings were issued on properties that had been owned for less than a year. However this is still a much higher percentage than it has been in the past; in 1993, only 3% of foreclosure filings were issued on properties that were purchased less than a year earlier.

What happens to properties that enter foreclosure in New York City?

As discussed above, not every property that enters foreclosure ends up as REO or even makes its way through the entire foreclosure process. Properties that received an LP in 2007, for example, had experienced a wide range of outcomes by the end of June, 2009:

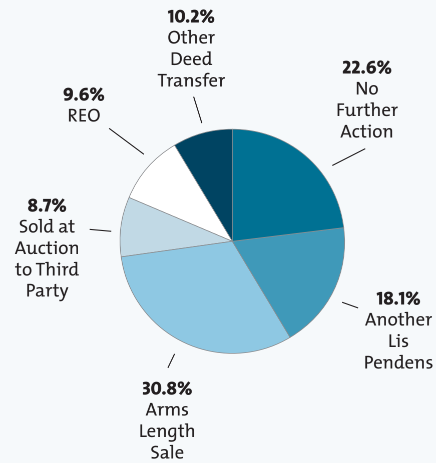
- 14% were sold by the homeowners in arms length transactions;
- 4% of properties transferred ownership through other means (such as divorce settlement or estate sale);
- 2% were sold at auction to third-party bidders;
- 12% of these properties ended up as REO;
- Almost 14% hadn't been sold or completed the foreclosure process, but had received another LP filing; and
- Finally, and perhaps surprisingly, 54% of properties that received an LP in 2007 had not, by the end of June 2009, been sold or completed the foreclosure process, and had not received an additional LP.

For this last group of properties, the fact that we could not identify any other outcome after the initial LP indicates either that the homeowner had become current, refinanced or modified her loan, or that the foreclosure process had not made its way to auction yet. As discussed above, the full foreclosure process typically takes about 12-18 months in New York City (and in some cases, takes significantly longer), so at least some of the foreclosure actions initiated in 2007 were still making their way through the process and ultimately may still end up as REO properties.

For the almost 14% of properties that received a second LP at least 6 months after the first, the additional filing indicates that, at the very least, the owner experienced multiple episodes of mortgage distress, even if she still appeared to own the property as of June, 2009. The borrower may have been able to catch back up with her mortgage payments for a time, but then defaulted again; the borrower may have refinanced, but fell behind on her new mortgage; or the borrower may have fallen behind on a second mortgage on the same property.

To better understand how the outcomes of properties that enter foreclosure have varied over time, we performed a similar analysis on properties that received a foreclosure filing between 1993 and 2005, and calculated the outcomes these properties faced in the three years after the LP filing.[5] Figure A summarizes the results. A sizable share (31%) of the properties that received a foreclosure filing between 1993 and 2005 sold at an arms length sale within three years of receiving an LP filing. In general, this means that these properties were worth enough after the LP that the homeowners could still sell them for more than the outstanding balance of their mortgages and repay the loan. Nearly 23% of properties had no further action in the three years following the foreclosure filing, most likely because the owner either became current on her loan again, modified the loan terms, or refinanced. Finally, 10% of properties that entered foreclosure during this 13-year period ended up as REO within three years.

FIGURE A: Outcomes of properties that received a foreclosure filing between 1993 – 2005 (outcomes as of three years after the LP was issued)



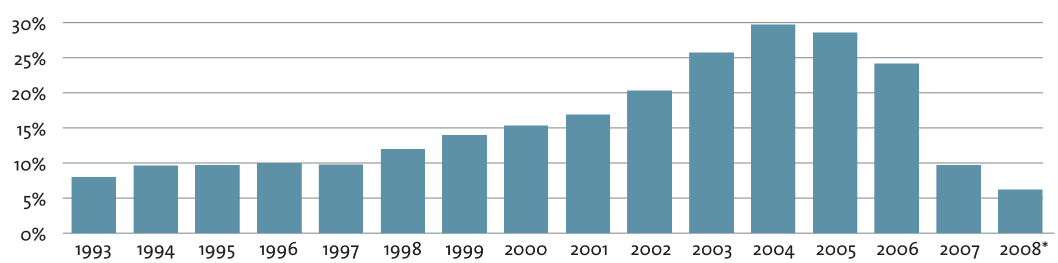
5 Only LP filings through 2005 were used to ensure that there was at least three full years of data after each filing to determine the distribution of outcomes, as 90% of auctions are completed within three years of the initial LP. These figures should not be compared to the outcomes for properties that received an LP in 2007, as there is not yet three years worth of data from which to measure the outcomes of those properties.

How has the current downturn changed the options available to people facing foreclosure?

The real estate bust and subsequent economic downturn of the last few years have changed the face of real estate in New York City and dramatically changed how people who own properties in foreclosure resolve the foreclosure. For example, homes entering foreclosure in recent years are much less likely to sell in an arms length sale. As shown in Figure B, just 10% of properties that received an LP in 2007, and only 6.5% of properties that received an LP in the first three quarters of 2008, were sold in an arms length sale within one year. In contrast, 30% of properties that received an LP in 2004 sold within a year in an arms length sale.

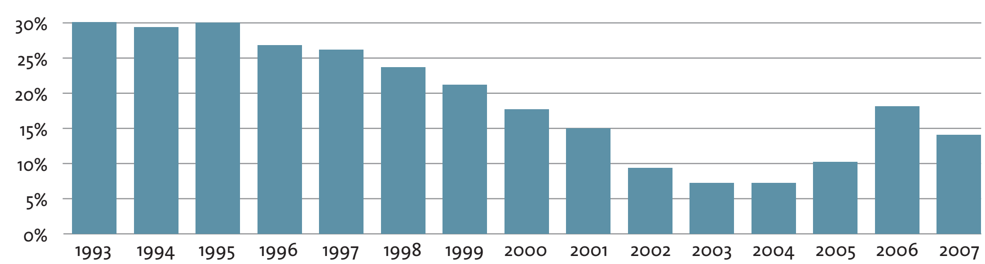
Another sign of how the downturn has changed the outcomes of properties entering foreclosure is the rising share of properties that end up at auction, where they will either be sold to a third-party investor or end up as REO. As shown in Figure C, of properties receiving an LP in 2004, only about 7% went to auction within three years. But, as the mortgage market collapsed and housing prices stopped rising, fewer distressed homeowners could escape foreclosure by refinancing or selling their homes. As a result, for properties receiving LPs in 2006, just two years later, the share of properties in foreclosure that ended up

Figure B: Share of properties that sold in an arms length sale within one year of receiving a foreclosure filing



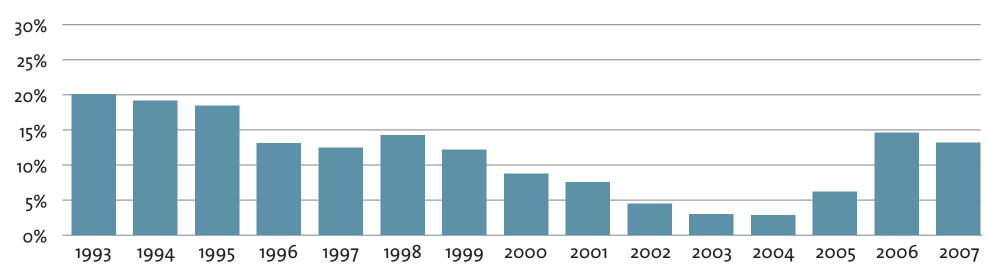
** Only includes LPs issued in the first three quarters of 2008.*

Figure C: Share of properties that went to auction after receiving a foreclosure filing



Note: Given the length of time it can take before a property reaches auction, we expect the 2007 figure to grow as new data become available.

Figure D: Share of properties that end up as REO after receiving a foreclosure filing



Note: Given the length of time it can take before a property reaches auction, we expect the 2007 figure to grow as new data become available.

at auction more than doubled: 18% of properties that received an LP in 2006 made it to auction. Of properties that entered foreclosure in 2007, 14% had already gone to auction by the end of September 2009.[6]

Similarly, in recent years there has also been a significant increase in the share of properties in foreclosure that end up as REO. As shown in Figure D, the percent of properties entering foreclosure that ended up as REO within three years increased from 3% of those that received an LP in 2004 to 15% of properties that received an LP in 2006. Properties in recent years were still not as likely to end up as REO as those that entered foreclosure in the early-mid 1990s, however. As shown in Figure D, in the early-mid 1990s, nearly 20% of properties that received an LP ended up as REO. Over the next decade, as the economy and housing market improved, that share dropped off dramatically, before its recent rise.[7]

6 Given how long the foreclosure process can take in New York, we expect that percentage to be significantly higher once we are able to include all 2009 data.

7 Even though the share ending up as REO is smaller today, the number of properties receiving LPs has increased so much in the last few years that the aggregate number of REO properties in New York City is higher today than in the early-mid 1990s.

How many REO properties are in NYC?

From the beginning of 2007 to the end of 2008, the stock of REO (and likely vacant) properties in New York City increased dramatically. As Figure E shows, in December, 2006, there were approximately 290 REO properties in the City; by the end of 2008 that number had grown to 1,830. The significant increase in the stock of REO properties in recent years was a result of four primary trends:

1. More properties entered foreclosure.
As Figure F shows, 2007 and 2008 had the highest number of foreclosure filings in this fifteen year period, and based on data from the first three quarters of 2009 it is clear that foreclosure filings this year will significantly outpace previous years.

2. Properties that entered foreclosure were more likely to go to auction.
As discussed above, and shown in Figure C, after a large drop-off at the beginning of this decade, the share of properties with LPs that went to auction saw an uptick in recent years; 18% of properties that received an LP in 2006 went to auction, compared to only 7% of properties that received an LP in 2004.

Figure E: Existing stock of New York City's REO inventory

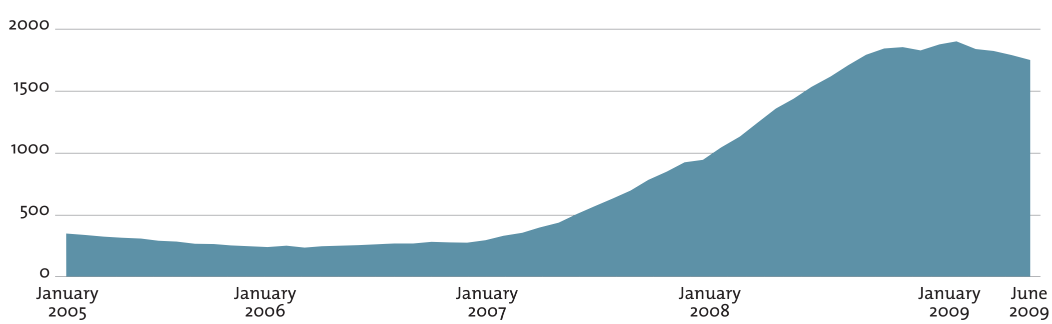


Figure F: New York City Foreclosure Filings on 1 - 4 Family Properties

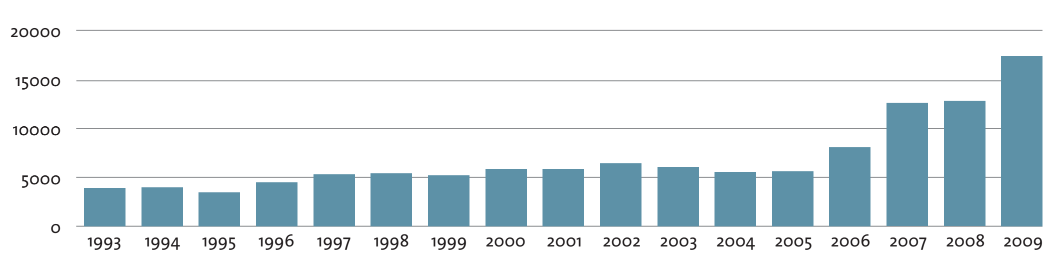


Figure G: Foreclosure auction outcomes

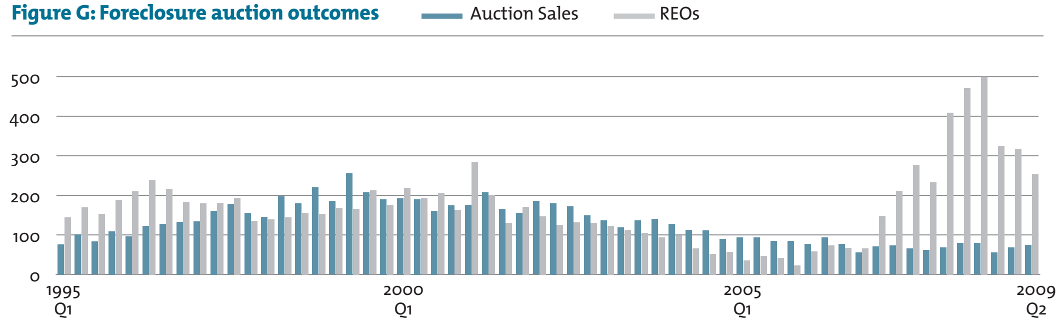
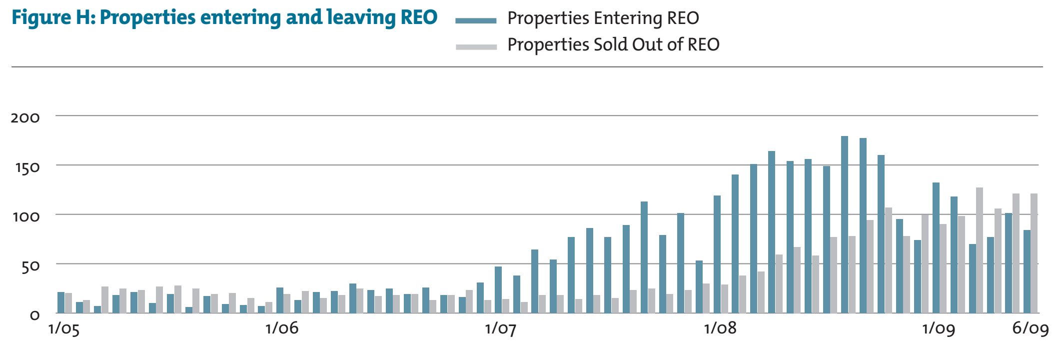


Figure H: Properties entering and leaving REO



3. Properties were less likely to be bought at auction by third parties, and more likely to end up as REO.

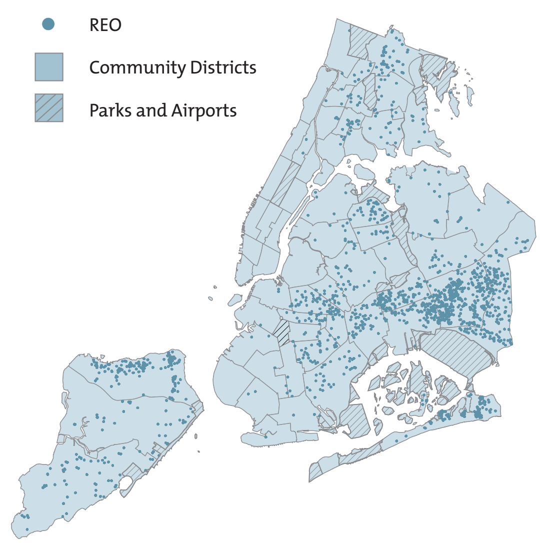
Figure G shows that auction sales to third parties have seen a steady decline since the late 1990s. In contrast, the number of properties that entered REO out of auction increased significantly after 2005. The third quarter of 2008 saw more properties enter REO than any other quarter in our study period.

4. The number of properties entering REO increased more rapidly than the number leaving REO.

Figure H shows the number of properties entering and exiting REO each month. Beginning in early 2007 and lasting throughout most of 2008, the number of properties entering REO far outpaced the number leaving REO, resulting in the significant increase in the total stock of REO properties discussed above. In the first two quarters of 2009, however, this trend has reversed, and more properties sold out of REO than entered.

As one would expect, REO properties are concentrated in the areas of the City that have seen the highest rates of foreclosure. Map A shows the location of properties that entered REO in 2008, and highlights the concentrations of such properties in Eastern Queens, Central Brooklyn, and the North Shore of Staten Island.

Map A: Location of Properties that Entered REO in 2008



Source: Public Data Corporation, NYC Department of Finance, Furman Center

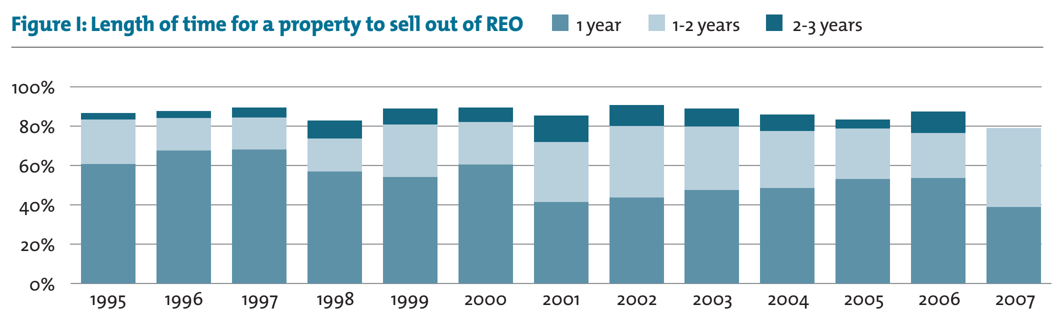
The sharp increase in the number of REO properties in 2007 and 2008 is noteworthy. However, the inventory of REO properties in New York City remains far smaller (both in relative and absolute terms) than the inventory in many other large cities that have seen higher rates of foreclosure and softer housing markets. There are also signs that the REO inventory has reached a plateau, at least momentarily. In the first two quarters of 2009, more properties left REO than entered REO, resulting in a slight decline in the overall size of the stock.

What happens to REO properties?

In 2007, about 880 properties entered REO. Figure I shows that 39% of those were sold in an arms length transaction within one year. While this is the smallest share of REO properties to sell within a year of entering REO for all years studied, it represents a much larger volume than we have seen before. For example, in 2005, 53% of new REO properties sold within a year, but there were only 115 properties that entered REO in that year.

Properties that sell out of REO may be bought by new homeowners who will occupy the house, or they may be bought by investors who will rent the building, warehouse it for future sale, or quickly resell it. It is not possible to track the range of outcomes, but we are able to identify instances in which a property is resold soon after purchase, an activity commonly referred to as "flipping." Properties that have gone through foreclosure and/or have been sitting vacant are likely in need of renovation. If new buyers renovate the property before reselling it, this can have positive benefits for the surrounding neighborhood. But if buyers do minimal work before turning the property around, this could result in reselling a property with defects such as mold that could threaten the health of new homeowners, or structural or mechanical problems that could make it difficult for the new buyers to maintain the property within their budget.

Figure I: Length of time for a property to sell out of REO



Our data show that flipping has been a common outcome of REO sales throughout our study period. Between 1995 and 2007, 44% of properties that sold out of REO were resold within one year. Figure J shows how this has changed over time. Flipping activity peaked in 1998, with 55% of REO sales resold within a year. This decreased to 37% in 2006, and 32% by 2007.

Flipping has been consistently profitable. As Figure K shows, over our entire study period, the median price increase (the percent by which the post-REO sale price exceeded the sales price of the property when it was bought out of REO) has been more than 45%. That means that if an REO property was sold for $300,000, the same property would typically sell within a year for $435,000, representing a much faster rate of appreciation than we would otherwise have expected. Even in the year when we saw the fastest annual rate of house price appreciation, from 2002 to 2003, the average rate of appreciation citywide was only 14%.[8]

This price inflation is one reason that flipping is sometimes viewed as a detriment to the neighborhood. If these rapid price increases do not reflect an increase in the quality of the housing, they may artificially inflate the sales prices of surrounding properties through the comparables appraisers use in setting home values. The artificially high prices may cause even more homebuyers to stretch their finances and take out loans they may not be able to afford, leading to even more foreclosures.

8 This percent is calculated using the Furman Center's index of price appreciation. This index, also called the repeat sales index, measures average price changes in repeated sales of the same properties. Because it is based on price changes for the same properties, the index captures price appreciation while controlling for variations in the quality of the housing sold in each period. Sale prices used in the repeat sales index are adjusted for inflation, thus the index measures the rate of price appreciation above and beyond inflation.

FIGURE J: Share of REO sales that flipped within one year

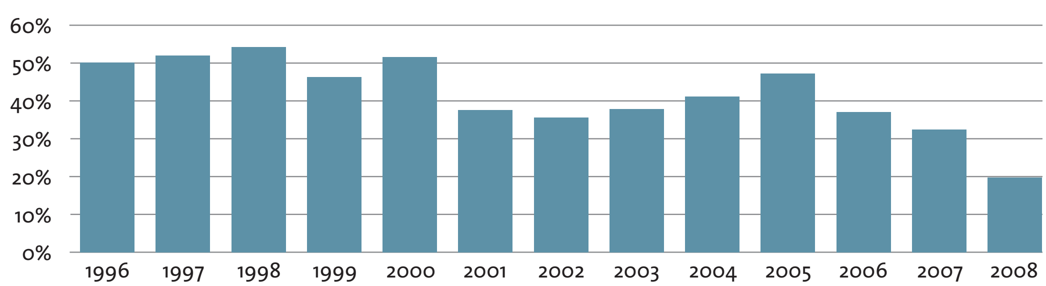
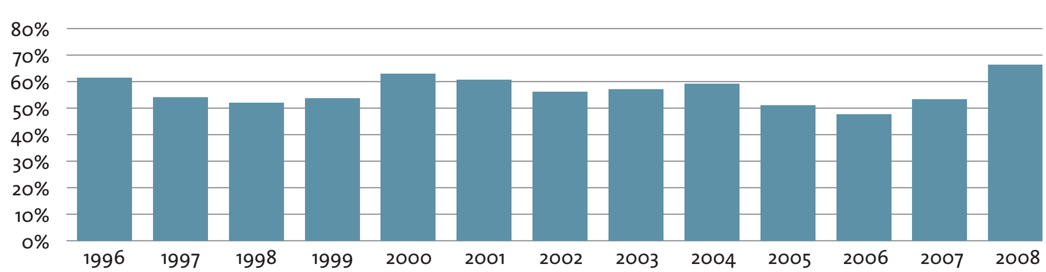


FIGURE K: Median price increase of flipped REO properties (%)



What is next?

While the total number of REOs in New York City remains relatively small compared to many hard-hit cities, the dramatic increase in the overall stock of REO properties in the past few years could still present significant challenges for certain neighborhoods. It is too soon to tell whether the recent increase in sales of REO properties will continue, resulting in a decrease in the REO inventory, or whether sales will slow, and the inventory will rise as the properties currently in the foreclosure process make their way to auction. Either way, we hope this analysis, and our ongoing efforts to understand the impacts of foreclosed properties on surrounding neighborhoods, will be useful to policymakers and the housing community as they refine their strategies to stabilize hard-hit neighborhoods.

In response to the growth of REO and other vacant properties in cities across the country, the federal, state and local governments and a number of non-profit community development and housing organizations have launched a wide variety of initiatives. These initiatives have a variety of goals, including reusing REO homes as affordable or market-rate housing, mitigating the negative impacts of vacant properties, and increasing the accountability of lenders for the maintenance and responsible sale of REO properties. More information about these efforts can be found in the following resources:

- A Furman Center report summarizing strategies to reclaim foreclosed properties: http://furmancenter.org/files/furman.ford_.whitepaper.pdf.
- A comprehensive web site for information about reusing foreclosed properties, sponsored by a consortium of non-profit organizations: www.foreclosure-response.org.
- A resource maintained by NeighborWorks America with information about foreclosure-related neighborhood stabilization efforts: www.stablecommunities.org.

Appendix: Data

The data for this report come from three sources: *lis pendens* filings from Public Data Corporation; residential sales transactions from the New York City Department of Finance; and the Final Assessment Roll from the New York City Department of Finance.

■ ***Lis pendens* filings from the Public Data Corportaion.** This data set includes a record of every *lis pendens* filed in New York City since 1993 (we do not have Staten Island data prior to 2000, but we have checked for robustness and found that this omission does not appear to bias our results in any way). An LP may be filed for a host of reasons unrelated to a mortgage foreclosure, but we have limited this analysis to just mortgage-related LPs. Further, the same property may receive multiple *lis pendens*. In our analysis, about 25% of properties received more than one *lis pendens*. There are at least two unique situations where a homeowner could have multiple LPs filed: i) a homeowner receives a *lis pendens* filing from multiple banks at nearly the same time (perhaps from a first lien and junior lien) or ii) a homeowner receives a *lis pendens*, works something out with the lender or otherwise becomes current, and then falls in to trouble again down the road, receiving a subsequent LP. Because of limitations with our LP data, we cannot distinguish between these situations. As a proxy, in this report we assume that if a second LP is filed within six months of the first LP, it represents the same period of financial distress for the homeowner and base our further calculations (i.e. the amount of time until a sale or auction) on the date of the first LP. However, if the first LP is followed by a subsequent LP more than six months later, we treat the two as separate instances of homeowner distress.

■ **Residential sales data from the Department of Finance.** This data set includes a record of every deed transfer in New York City since 1974, including: the names of the grantor and grantee (multiple names are allowed for each record); the sale price; and one or two flags used to indicate the condition of transfer as reported on the Real Property Transfer Tax Return. We dropped from our analysis any correction deeds or transfers that had no bearing on the status of the mortgage debt. We then used a combination of the condition of transfer flags and text searches to classify sales out of foreclosure. We used the condition of transfer flag to identify debt free gifts, marital settlements, sales per trust agreements or sales that are forced based on non-mortgage related judgments, which we include in our "other deed transfers" outcome category. Similarly, if a deed transfer was flagged as a deed in lieu, we included it in that category. In the case where a sale had two condition of sale flags (e.g. an estate sale and an arms length sale) we prioritized other deed transfer and auction flags before an arms length sale flag.

▸ To identify auction sales, REOs and arms length transactions, we used a combination of the condition of transfer flags, text searches and the sales price. If a sale was flagged as a "transfer by referee or receiver" or if we found the word "referee" or "esquire" in the grantor name field, we classified the sale as an auction.

▸ To identify transfers into REO, we searched the grantee name field for the word "bank" or the name of any large bank or subsidiary. Further, we compared the name of the grantee to the name of the LP servicer and if those names matched, classified the sale as a transfer into REO. If a transaction was flagged as both an auction because of the grantor field and an REO because of the grantee field, we counted its outcome as REO.

▸ Finally, if a transaction had not been classified in any prior categories, had a condition of transfer flag indicating it was an arms length sale or other transfer, and had a sale price of at least $10,000, we classified it as an arms length sale. We eliminated from our sales data the few observations that failed to fit into any of these categories (e.g. when a sale was flagged only as an arms length sale but had a sale price of $0).

■ **Final Assessment Roll from the Department of Finance.** This data set includes building characteristics and geographic information for every property in New York City. We used building class codes from this data to limit our analysis to 1-4 family residential buildings.

Appendix: Methodology

■ **Matching LPs, Sales and Property Characteristics.** Each of these datasets identifies properties using a unique borough, block and lot number (BBL). Starting with the set of all *lis pendens*, we used BBLs to match each *lis pendens* received since 1993 with the most recent sale of that property prior to the *lis pendens* (if the sale happened in 1974 or later).

When measuring the median length of time between an initial sale and an LP filing, we include only those properties with LPs after arms length sales (as we previously defined). Properties that were bought out of auction or were otherwise transferred to a homeowner outside of any arms length transaction were not included in these calculations. We also note that this analysis does not take into account any loan refinancings the homeowner may have obtained between the time of her home purchase and the filing of the LP. So while we are measuring the time between initial sale and LP, if the homeowner refinanced during that time, we may not be measuring the length of time the particular loan entering foreclosure had been held.

We then matched the LP to any sales that occurred within three years after the LP, and assumed that the first such sale was undertaken in response to the foreclosure filing. We limited our universe of outcomes to three years after the initial LP was filed to ensure consistency when comparing outcomes across years (e.g. if a property received an LP in 1995 and did not sell until ten years later, we would classify that LP as not being resolved). For properties that received multiple LPs, we also matched any LPs that were filed after the first LP but before the first subsequent sale. Finally we matched all of these properties to their building characteristics from the Final Assessment Roll to determine the size and geographic location of the building. Thus, we compiled a database where we could track properties from initial sale through the foreclosure process to any subsequent sales. This database includes over 100,000 properties in New York City that have entered foreclosure since 1993, the entire universe of properties that received foreclosure filings.

To track the amount of time properties stay as REO and the outcomes of properties when they leave REO, we added to our database several subsequent sales after the transfer to REO. We disregarded any transfers between banks or governmental agencies and used a strategy similar to that outlined above to identify arms length sales. Finally, if a property had a second arms length sale within a year after the initial arms length sale out of REO, we assumed that the property was purchased the first time by an investor who quickly flipped it.