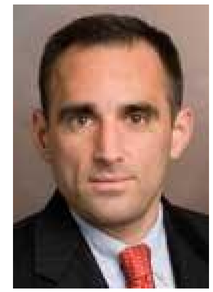

Don't Take a 'Katrina' Approach

Be Ready for a Flood of Mortgage Foreclosures

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The coming rush of foreclosures will have far reaching negative effects on local governments. Commercial and residential mortgage foreclosures create gaps in property tax collection. In turn, long-term vacancies in foreclosed commercial and residential property hurt the values of neighboring properties and decrease traffic to local businesses. The diversion of $700 billion in bailout funds to Wall Street banks reduces the likelihood that federal aid will be available to municipalities, at a time when New Jersey towns face the perfect storm of a national recession, reduced state aid, gaps in property tax collection, and a staggering increase in each town's COAH-mandated affordable housing obligation.

Experts predict home loan defaults will get much worse. Moody's economy.com estimates 1.9 million foreclosures in 2009. Waiting until the tsunami waters recede to take action is a Hurricane Katrina approach. Instead, municipalities must prepare for the coming foreclosure damage now, while there is time.
Organize a Team The first action that should be taken is to convene a group of municipal employees that will share information across departments so as to coordinate the town's approach to foreclosures.

The Foreclosure Team should be chaired by the Mayor or his designee, and include the municipal attorney, the Business Administrator, the Tax Collector, the Director of Community Development, the affordable housing "Municipal Liaison," the COAH "Administrative Agent" (if different from the Municipal Liaison), the Director of the Building Department, and the heads of all municipal utility authorities (if any).

Expect to encounter some resistance. After all, participating in the Foreclosure Team will divert them from their core, non-foreclosure activities. Additionally, the "newness" of both the foreclosure problem and the town's approach to the problem will unavoidably involve some confusion and disagreement among team members, which will make sitting through team meetings seem unproductive.

But it is critical that the department heads (or their senior assistants) actively participate in the Foreclosure Team. If the municipality is prepared for the onslaught of foreclosures, it may actually experience a net benefit in a climate of increased mortgage defaults.

Mayors, Business Administrators, and municipal attorneys should become familiar with the legal consequences of the town's approach to foreclosures. This author identified methods of obtaining new COAH credits, and preserving existing COAH units from foreclosure, in the November 3, 2008 New Jersey Lawyer (Municipal Supplement). Additionally, the importance of preserving affordable units from foreclosure was covered in New Jersey Municipalities' January, 2008 issue.

COAH Credits and Foreclosure In this housing market, municipalities will need magic to create as many units of affordable housing as the Council on Affordable Housing (COAH) requires.

Purchasing homes at foreclosure sales can be that needed magic. By keeping abreast of foreclosures within the municipality, the Foreclosure Team can use the Affordable Housing Trust Fund (AHTF) to purchase suitable properties at a discount, deed restrict the properties as affordable, and then sell the properties to either qualified buyers, or to an entity that will rent to qualified renters.

The City of Lancaster, California is doing just that. Similarly, a municipality can give homeowners money to bring their mortgage payments current and avoid foreclosure, in exchange for executing a deed restriction that converts the recipient's home from market rate to affordable. Last year, Toms River Township began planning to use its AHTF for such a program.

Thus, a municipality may receive a net benefit from the foreclosure firestorm. Although the town has to expend funds if it buys a property at sheriff's auction, (a) it can use money from its AHTF, and (b) the money used to buy the property will be reimbursed when the municipality re-conveys to a qualified affordable family.

Protect Affordable Units COAH has mandated that municipalities create affordable units at four times the rate as in the past. Thus, it is imperative to preserve the affordable units that already exist in the town. If an affordable home owner defaults on their mortgage, the foreclosing mortgagee will want to strip the affordability status from the property at the foreclosure sale, so as to recoup as much of its debt as possible. When the affordability status is stripped from a property, the town's COAH credits decrease. Participation of each member of the municipal Foreclosure Team is needed to prevent this.
The tax collector and the heads of all municipal utility authorities can alert the Foreclosure Team to affordable properties that have accrued municipal

liens, which will usually signal a

contemporaneous mortgage default. Reports of property deterioration from the Building Department may also aid the detection of an imminent mortgage default. When it knows of the imminence of a foreclosure action, the Team is forearmed to save the affordable unit from loss at sheriff's sale.

The affordable housing Municipal Liaison and Administrative Agent, and the Director of Community Development are indispensable in identifying both qualified affordable families to take affordable properties that will otherwise be lost to foreclosure, as well as the town's inventory of affordable housing units that need to be preserved from foreclosure. Additionally, where foreclosure is inevitable, these personnel can leverage their relationships with affordable housing non-profits to purchase foreclosed properties where the town cannot. Lastly, these personnel should direct the team's efforts to ensure that every single affordable home has a properly-recorded deed restriction to cement its status as a COAH-credit property.

Prevent a Ghost Town Despite your best efforts, there will be foreclosures in your municipality. Success will be graded in terms of slowing the rate of foreclosures so that the municipality does not become a vacant ghost town.

The phenomenon of widespread mortgage default increases the number of vacant and abandoned properties. After a foreclosure has occurred, a municipality must prevent the vacant, foreclosed property from deteriorating. Initially, the collapse of the real estate market triggered this overall crisis. If property values continue to plummet, more homes will be worth less than their mortgages.

Towns should use the Abandoned Property Rehabilitation Act ("APRA") to compel the owners of vacant, foreclosed properties to maintain their appearance so they do not cause further decline in neighboring property values. The risk of absentee banks allowing foreclosed properties to deteriorate into nuisances will increase with the rate of foreclosures. Based on the premise that run-down properties infect a neighborhood, APRA grants municipalities broad powers to compel maintenance of vacant properties. The Act enables a municipality to seize buildings that remain nuisances after proper service of notice upon the owner(s).

In light of recent jurisprudence in the area of acceptable means of serving notice of public seizures of property, it is absolutely critical to consult counsel before proceeding under APRA. However, the experiences of such towns as Hackensack demonstrate that a well-publicized APRA program will spur a high degree of compliance, such that nuisance properties will be resolved promptly.

While a municipality cannot prevent all foreclosures, it can mitigate the effects of the coming wave of mortgage defaults, and preserve its character as a living, thriving town.

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