

Research Brief

OFFICE OF THE NEW YORK STATE COMPTROLLER

DIVISION OF LOCAL GOVERNMENT AND SCHOOL ACCOUNTABILITY

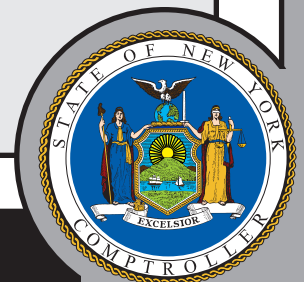
Foreclosure Update From a Local Government Perspective

A recent report from the Office of the State Comptroller (OSC) showed that residential property foreclosures continue to pose a serious challenge for New York's local governments. New filings continue to rise in many parts of the State, making it difficult for the courts to make headway in reducing caseloads.¹ New York State has the fourth-slowest foreclosure process in the nation, averaging over 2.5 years per property.² It is not surprising, then, that New York has a disproportionately high share of mortgages in foreclosure, relative to the rest of the country. As of the 3rd quarter of 2015, the State had the second-highest home foreclosure inventory in the nation with 4.77 percent of mortgages in foreclosure. New Jersey led the nation at 6.47 percent.³

Prolonged foreclosure activity is taking a toll on local governments and communities. Borrowers facing foreclosure sometimes abandon their properties, which fall into disrepair. In some cases financial institutions, faced with a long and potentially costly foreclosure process, decide not to foreclose immediately, even after properties are abandoned—particularly in the case of low-value properties in economically distressed neighborhoods.⁴ This leaves some local governments with high concentrations of such properties, along with the associated challenges of trying to ensure that they are maintained while vacant and returned to productive use as soon as possible.

Summary

- **Statewide, 1 in 21 home mortgages (4.77 percent) are in foreclosure.**
- **Certain State measures, with the worthy intent of consumer protection, may have lengthened the time required to complete foreclosures and caused some cases to get stuck in the foreclosure process.**
- **Foreclosures create a number of issues for local governments, including shrinking property values, higher crime rates, and increased costs for code enforcement.**
- **Vacant abandoned “zombie properties” are of particular concern to local governments.**
- **Land banks are a relatively new mechanism that may help local governments return zombie properties to productive use.**
- **Other responses include increased efforts to expedite cases, agreements by lenders and servicers to maintain vacant properties throughout foreclosure and the creation of a statewide registry of zombie properties. However, it is too soon to know how successful these measures will be.**



Until recently, much of the policy response to foreclosures has focused on financial institutions and consumer protection. In general, the banking regulators' primary concerns are the health of the nation's financial system and of banks and lenders, as well as protecting the interests of those who invest in mortgage-backed securities or purchase other financial services and products. The consumer protection agencies' primary focus generally is the borrowers and their interests, rights and well-being. Local governments—and thus the residents of their communities—are generally underrepresented in the policy decision making. However, communities and residents can experience negative consequences—including higher crime rates and lower property values—when borrowers and financial institutions or mortgage loan servicers abandon properties.⁵ Taking the impact on local governments and communities into account when crafting measures to tackle foreclosures could help mitigate these concerns. The local government perspective is the focus of this research brief.

Financial Institutions and the Foreclosure Crisis

Mishandling of mortgage activity by some financial institutions has contributed to the foreclosure crisis.

Some lenders contributed to the crisis by loosening lending standards enabling borrowers to obtain mortgages they could not afford.

When the crisis began, some banks failed to follow due process in filing for foreclosure using “robo-signed” documents (foreclosure documents signed by employees without reviewing them).⁶

Some banks were criticized for insufficient efforts to implement the federal government's Home Affordable Modification Program (HAMP). HAMP was intended to promote loan modifications that would enable borrowers to keep their homes.⁷ Even when lenders participated in court-mandated settlement proceedings, anecdotal reports indicated that lender representatives were sometimes unprepared to proceed in good faith.⁸

Foreclosure Process Tradeoffs

New York is a judicial foreclosure state, which means that bank foreclosure cases are resolved through the State's court system. Processing foreclosures through the courts can help protect the interests of both borrowers and lenders; however, it can also lengthen the foreclosure process. On average, foreclosures take over one year longer in judicial foreclosure states compared to other states.⁹ Increased foreclosure activity and changes to the foreclosure process in response to the financial crisis that began in late 2007 have also extended the time to complete foreclosures in both judicial and non-judicial states. The estimated average foreclosure timeline for borrowers in judicial states has increased 72 percent since the start of the mortgage crisis in early 2007.¹⁰

Recent Changes to the Process

In New York State, a number of changes were made to the foreclosure process in the wake of the mortgage crisis. Many of the changes were designed to encourage negotiations with lenders and servicers that would enable borrowers to avoid foreclosure. However, some of these measures appear to have drawn out the time needed to complete the foreclosure process and even prevented some cases from completing the process.¹¹

Mandatory Settlement Conferences

In 2008, mandatory settlement conferences were instituted in New York's judicial residential foreclosure process. The court is required to hold a conference where the plaintiffs (typically lenders or loan servicers) and borrowers meet to determine whether the parties can reach a mutually agreeable solution other than foreclosure (for example, a loan modification). Initially, the mandatory settlement requirement applied only to certain high-cost residential mortgages; however, mandatory settlement conferences were subsequently extended to nearly all owner-occupied residential cases.

A survey of mortgage servicers conducted by the State Department of Financial Services (DFS) indicates that, on average, the settlement conferences add 110 calendar days to the foreclosure process downstate and 80 calendar days in upstate courts. (See Figure 1.) A single foreclosure case can be subject to multiple foreclosure conference appearances (including adjournments in cases where the parties are not adequately prepared to proceed with the conference). The courts have tried to shorten the process (and manage the workload) by reducing the number of settlement conference appearances per case. As of early 2015, the average number of settlement conference appearances for an active case was four—down from seven two years earlier.¹² The reasons for multiple conference appearances are many and varied: sometimes borrowers lack necessary paperwork, or the plaintiff (typically a loan servicer) sends a representative without authority to settle the case, or required documents prepared months earlier have become outdated and need to be redone or cannot be located.

Figure 1

Average Time for Phases of the Foreclosure Process in New York State

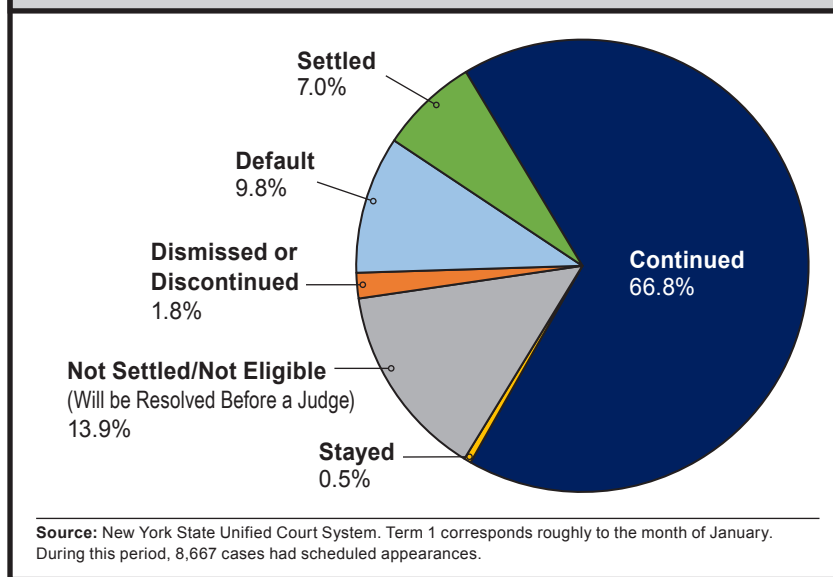
| Phase of Foreclosure | Average Number of Calendar Days | |
|--|---------------------------------|---------|
| | Downstate | Upstate |
| Filing of Foreclosure Action to Filing of Service of Process | 33 | 30 |
| Filing of Service of Process to Filing of Request for Judicial Intervention | 168 | 162 |
| Filing of Request for Judicial Intervention to First Mandatory Settlement Conference | 161 | 39 |
| First Mandatory Settlement Conference to Last Mandatory Settlement Conference | 110 | 80 |
| Last Mandatory Settlement Conference to Entry of Judgement of Foreclosure and Sale | 430 | 343 |
| Entry of Judgment of Foreclosure and Sale to Auction of Foreclosed Property | 172 | 148 |

Source: Department of Financial Services (DFS). Reproduced from DFS, *Report on New York's Foreclosure Process* (May 2015), p. 7. The data are based on a survey of mortgage servicers. The survey asked about foreclosure cases for owner-occupied one-to-four family residential mortgages from January 1, 2010 through September 30, 2013. Downstate is defined as the five boroughs of New York City plus Nassau, Suffolk, Rockland and Westchester counties.

Not surprisingly, then, a common result for any given settlement conference appearance is a continuance. As shown in Figure 2, two-thirds of appearances scheduled during the beginning of 2015 resulted in a continuance. Of the remainder, nearly 14 percent were referred to be resolved before a judge, 10 percent were found to be in default (i.e., no settlement was reached, the court agreed with the plaintiff, and the foreclosure would move forward), 7 percent were settled, 2 percent were dismissed or discontinued (which could happen, for example, if the lender/servicer decides not to pursue the case or if the borrower pays off the loan and any penalties), and the remainder were stayed (temporarily halted), which can happen, for example, in cases where the borrower has filed for bankruptcy.

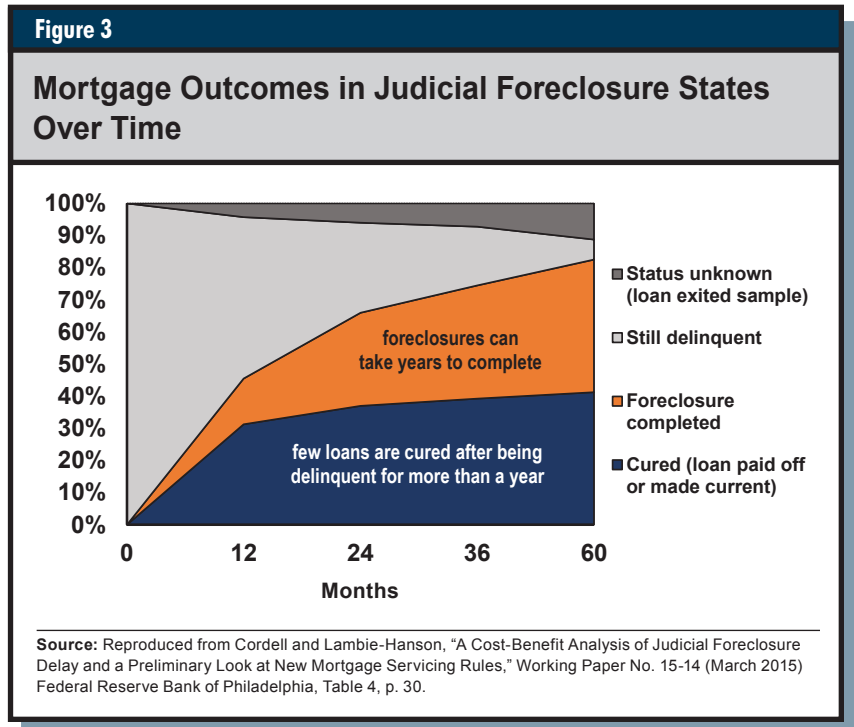
Figure 2

Foreclosure Settlement Conference Appearance Results: Two-Thirds of Cases are Continued (During Term 1 of the 2015 Court Calendar)



The relatively low settlement rate at these conferences may be exacerbated by the time that the conference process itself takes. A Federal Reserve Bank study using national data found that if cases are not “cured” (i.e., loans paid off, or made current) within the first year or so, they are unlikely to ever be cured.¹³ (See Figure 3.) While the case remains in the foreclosure process, the costs for the borrower escalate over time. So what could have been an affordable settlement for the borrower in a short process, becomes increasingly unaffordable as time goes on: “Each month of delinquency adds interest (often at a higher

default rate), penalties, and fees to a borrower’s outstanding balance. To obtain a modification, those accruals are ordinarily capitalized into the unpaid principal balance of the loan.”¹⁴ Foreclosure delays—and their attendant costs—can also reduce servicers’ willingness to negotiate “graceful exits” for borrowers such as a “deed in lieu of foreclosure” (where the borrower deeds the property to the lender in exchange for a release of all obligations under the mortgage before the completion of the foreclosure process) or a short sale (in general, where the property is sold at fair market value, typically a lesser amount than what is owed on the loan).¹⁵

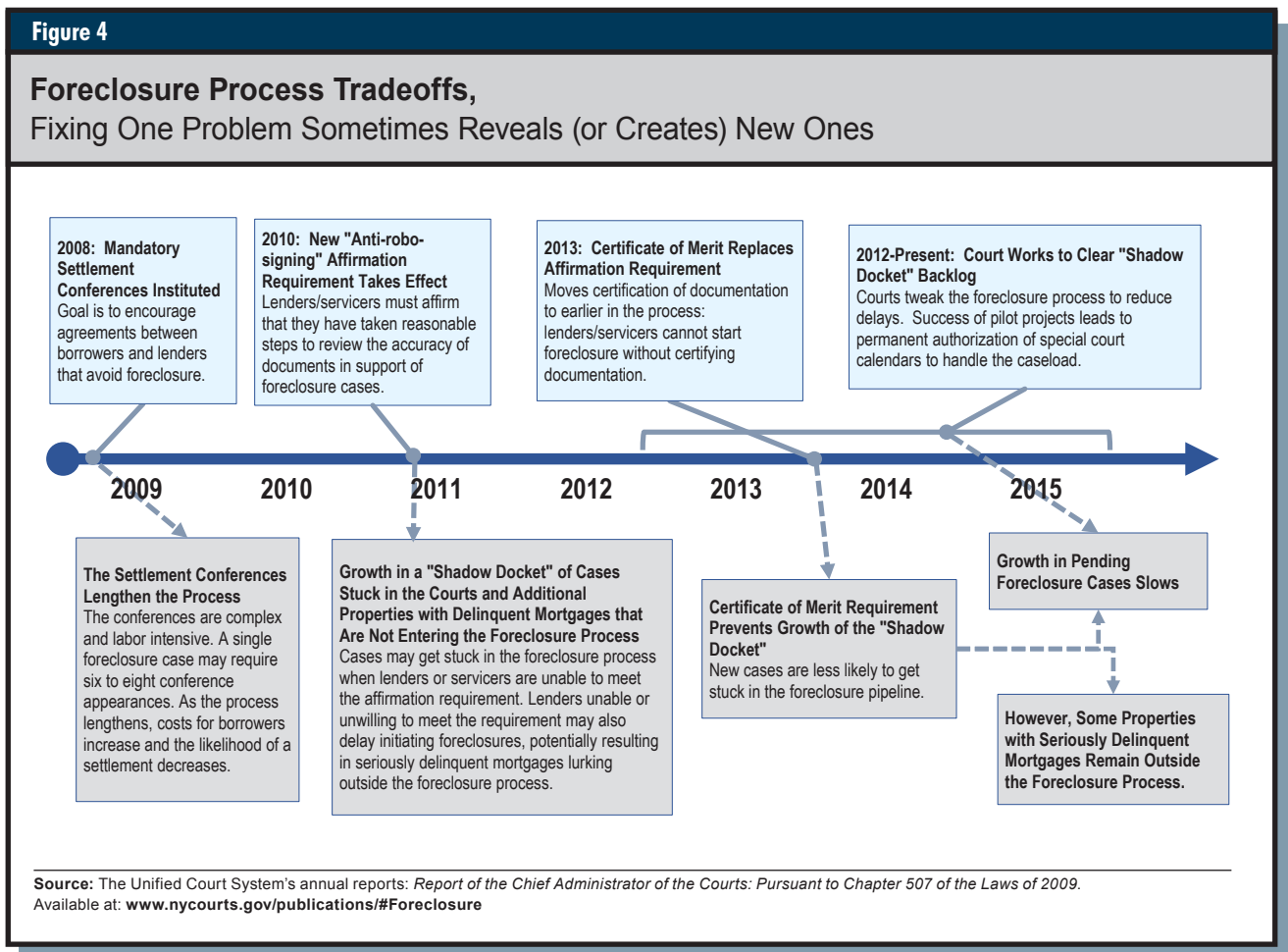


Anti-Robo-Signing Policies Cause Some Cases to Get Stuck in the Foreclosure Process

Another change to the foreclosure process that also had unintended negative consequences was the institution of additional filing requirements for residential foreclosures. At the height of the housing crisis, reports of “robo-signing” (where representatives of financial institutions, “claimed to have personally examined thousands of foreclosure-related documents in impossibly short periods of time”) began to emerge in the media.¹⁶ To prevent such abuses, starting in October 2010, New York courts began to require that attorneys for plaintiffs (banks, other lenders and servicers) submit an affirmation that they had taken reasonable steps to verify the accuracy of court documents in support of residential foreclosure cases and certify that crucial documents were thoroughly reviewed and that the documents were not “robo-signed.”¹⁷

Between 2010 and 2011, the number of foreclosure filings in New York dropped from 46,572 to 16,655, likely in response to the affirmation requirement, reducing the number of new cases entering the system.¹⁸ However, the affirmation requirement created a new obstacle for properties already in the foreclosure process when the requirement went into effect. If plaintiffs were unable to file an affirmation, they could not file a “request for judicial intervention,” which was necessary to move forward with the foreclosure, and so the property remained in legal limbo.

Foreclosure cases may also get stuck in the process when lenders abandon their cases. This can happen if they determine, subsequent to filing, that the amount recoverable upon the eventual sale of the property will not offset the costs of going through the lengthy foreclosure process. A 2010 report by the U.S. Government Accountability Office found that abandoned foreclosures occur infrequently, but that, “they most frequently involved loans to borrowers with lower quality credit—nonprime loans—and low-value properties in economically distressed areas.”¹⁹



The cases delayed in the foreclosure process are often referred to as the “shadow docket.” The courts are taking steps to speed up the process and clear the cases in the shadow docket, including pilot projects in some of the areas with the largest backlogs.²⁰ To prevent new cases from entering the shadow docket, in 2013, the State enacted legislation replacing the affirmation requirement with a “certificate of merit” requirement and moving it up to the beginning of the foreclosure process so that only cases with proper documentation could be filed.²¹

Beyond the “Shadow Docket”

Clearing the shadow docket could help borrowers move on with their lives and help get foreclosed properties into the hands of new owners who are willing and able to maintain and/or develop them. However, clearing the shadow docket alone will not eliminate the inventory of properties subject to foreclosure. A second group of properties in limbo exists outside of the court system’s foreclosure process. Some potential plaintiffs decide not to file for foreclosure. Lenders or servicers may decide not to file a foreclosure action because they cannot obtain the proper documentation in order to meet the filing requirements to begin the foreclosure action. In other instances, lenders or servicers may decide that it is in their interest to delay initiating foreclosure proceedings or to forgo foreclosure altogether.

A DFS survey of mortgage servicers in New York found that:

“Servicers . . . reported that they have not initiated a foreclosure action in the first instance on approximately 47% of already-vacant Upstate properties and approximately 34% of already-vacant Downstate properties. Some servicers explained that they decline to initiate a foreclosure based on an analysis of the potential recovery measured against the cost of foreclosing. The longer a vacant and abandoned property remains in foreclosure, the greater the deterioration of the property, which results in a lower expected recovery upon foreclosure sale. The lower the expected recovery, the less likely such recovery will sufficiently offset the legal costs required to complete the lengthy foreclosure process. Similarly, some servicers reported voluntarily discontinuing foreclosures where the underlying property was vacant at the time of the discontinuance.”²²

Since forgone foreclosures mostly involve low-value properties, this particular problem is most acute in poor neighborhoods.

As time passes, assessing the size of this pool of properties outside the court system with delinquent mortgages and uncertain ownership has become a priority for regulators and other stakeholders. DFS collects data on pre-foreclosure filings. This enables DFS to determine how many properties with seriously delinquent mortgages remain outside of the judicial foreclosure process. This could serve as a leading indicator of foreclosure activity that could help the courts, local governments and State policy makers anticipate foreclosure trends and target policy interventions where the need is greatest.

Foreclosures, Limbo and “Zombie Properties”

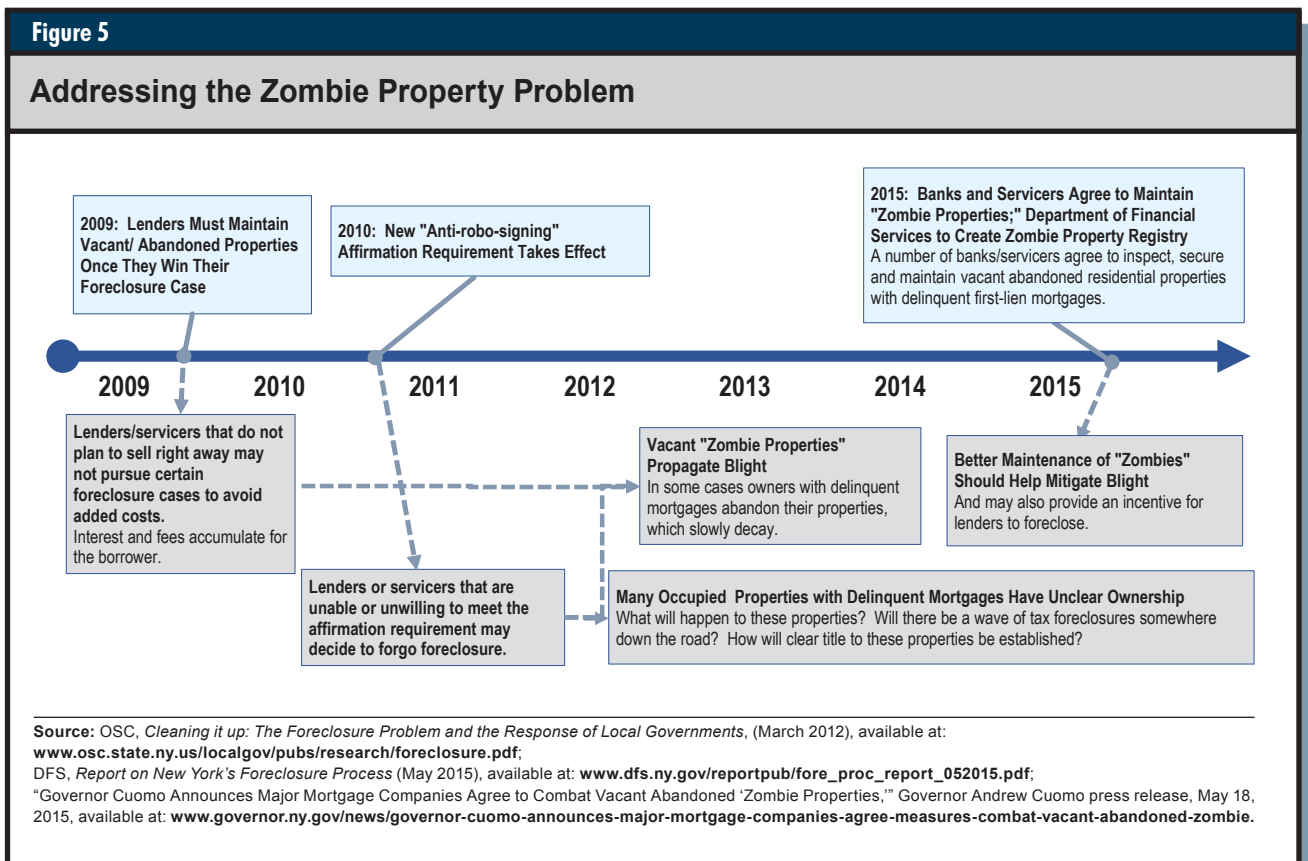
Vacant abandoned properties are at the heart of the foreclosure-related concerns for local governments. The DFS survey of mortgage servicers in New York State found that, “Approximately 31% of homes in the foreclosure process upstate started out vacant or became vacant at some point during foreclosure.”²³ Delinquent borrowers may abandon their homes, not realizing that they can stay in them while the foreclosure process plays out (and also in some cases not realizing that interest and penalties continue to accrue, even after the borrowers have abandoned the property). A property could be abandoned for other reasons—for example a divorce, a health crisis or death.²⁴ Vacant abandoned homes that are not yet the property of the financial institution or a new owner are popularly known as “zombie properties.” Zombie properties are likely to decay, bringing down surrounding property values and attracting crime.

In response in part to concerns about zombie properties, legislation was enacted in 2009 requiring lenders and servicers to maintain vacant or abandoned residential properties once they obtain a judgment of foreclosure and sale, until ownership of the property is transferred. This legislation also grants municipalities the right to enforce the requirement and to recover costs they incur to maintain vacant or abandoned properties. This helps ensure that vacant or abandoned properties are maintained after the property is foreclosed, but it does not help in the case of “shadow docket” zombie properties stalled in the courts or those where lenders or servicers decided not to initiate foreclosure.

To address problems associated with vacant and abandoned residential properties, the New York State Attorney General has proposed legislation (the Abandoned Property Neighborhood Relief Act) to, among other things, require lenders or servicers and their agents to maintain vacant abandoned properties even before the foreclosure process is complete.²⁵ The legislation did not pass in 2015; however, some of the proposed legislation’s objectives were achieved when a number of major banks and mortgage servicers agreed to follow a set of “best practices” including inspecting, securing and maintaining vacant abandoned residential properties with delinquent first-lien mortgages.²⁶ First-lien mortgages have priority over all other claims (for example, second mortgages) on the property in case of default. The banks and mortgage companies and credit unions are supposed to report vacant and abandoned properties to a State registry developed by DFS to share that information with local governments. The registry should help local governments identify lien holders and hold them accountable for maintaining abandoned properties. Thirteen mortgage companies, representing about 70 percent of the New York mortgage market have agreed to follow the best practices.²⁷

The adoption of these best practices should theoretically encourage lenders and servicers to work to resolve foreclosure cases involving vacant abandoned properties more quickly, in order to avoid having to spend money maintaining zombie properties. However, participation is voluntary and not all lenders or servicers have signed on. Also, these best practices make allowances for restrictions lenders or servicers may have in accessing properties. Lenders or servicers generally have limited rights to access properties before and even during the foreclosure process. So, while it may be relatively easy for them to board up a vacant abandoned property, mow the lawn and prune overgrown shrubbery, it might be more difficult to gain access to the interior of homes to assess the condition and repair damage from leaky roofs or frozen pipes. The best practices also exempt servicers from maintaining properties on which they have released the lien (their claim of ownership of the property).

The Attorney General has stated that he will continue to work to promote passage of the Abandoned Property Neighborhood Relief Act to codify the best practices, make sure they apply to all lenders and servicers, and increase information transparency.



Impact of Foreclosures on Municipalities and Communities

Increased Costs and Higher Crime Rates

Local governments may incur, and may not be able to fully recover, a wide variety of costs associated with foreclosures—particularly foreclosures of vacant abandoned properties. These include costs for code enforcement, delinquent taxes, unpaid water/sewer bills, and, in the case of abandoned buildings that burn down or otherwise become a safety hazard, demolition costs.

High foreclosure activity also imposes a number of indirect costs. Communities may experience more crime, which can increase municipal costs for policing and fire prevention. Studies have found that zombie properties provide venues for a wide range of nuisance and criminal activity. One study found that neighborhoods with high foreclosure rates tend to have higher rates of violent and property crime than similar neighborhoods with lower levels of foreclosure activity.²⁸ Another study estimated that an increase in the foreclosure rate of about 2.8 foreclosures for every 100 owner-occupied properties in one year corresponded to an increase of approximately 6.7 percent in neighborhood violent crime.²⁹ Government Accountability Office interviews with local government officials across the country found that, “vacant and abandoned properties were subject to break-ins, drug activity, prostitution, arson, and squatting, among other things.”³⁰

Shrinking Municipal and School District Tax Bases

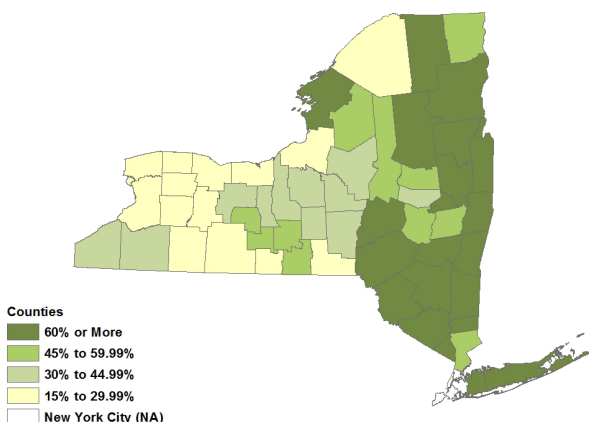
Some local governments may see a reduction or delay in tax collections attributable to foreclosed properties.³¹ In addition, a growing body of research confirms that foreclosures can contribute to lower property values, which in turn can affect local governments’ tax bases. A number of studies have shown that foreclosures depress home sale prices by an average of one percent for each nearby foreclosed property.³² Researchers hypothesize that this may have to do with the fact that most homes in foreclosure are not as well maintained, depressing property values in the surrounding neighborhood.³³

Lower home sale prices are likely to lead to lower assessed values and shrinking property tax bases. Figure 6 shows where the property tax base expanded during the housing boom, and where it has contracted since the recession. Eastern New York counties experienced rapid growth in their property tax bases in the years preceding the recession (from 2003 to 2008). Following the recession, growth slowed for most counties, while for counties in the Mid-Hudson region and Long Island, from 2008 to 2013, the property tax base actually began to shrink. These are counties with high foreclosure rates (measured as the number of pending foreclosure cases as a percentage of housing units) and growing pending foreclosure caseloads.³⁴ The foreclosure crisis did not cause this widespread and dramatic decline in property values—it was just one part of a cycle of devaluation. Credit tightened, demand shrank, prices fell, and many borrowers owed more than their houses were worth. This made it difficult for borrowers to refinance or sell their properties if they got behind on their mortgages, and so foreclosures increased. In neighborhoods with large numbers of foreclosures, any eventual recovery in real property values could be slowed by the effect of foreclosures in depressing home prices.

Figure 6

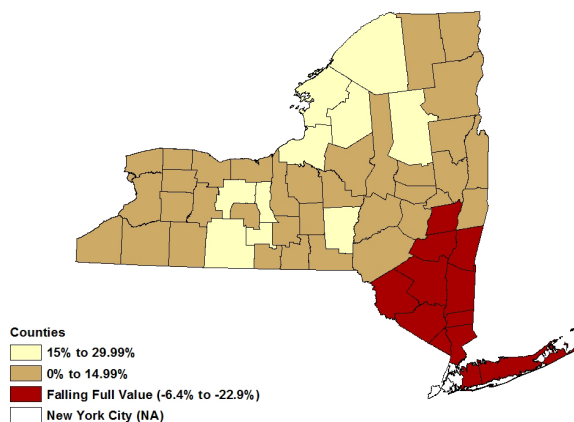
From 2003 to 2008, the Tax Base Grew Substantially in Eastern New York Counties

Percentage Change in Taxable Full Value, 2003 to 2008



Then from 2008 to 2013, the Tax Base Shrank in Downstate Counties

Percentage Change in Taxable Full Value, 2008 to 2013



Source: OSC calculations using data from OSC and the Department of Taxation and Finance.

Foreclosures Could Depress Homeownership Rates

Lenders or servicers have trouble making money on low-value loans on properties caught up in lengthy foreclosure cases. Servicers incur greater costs in property taxes, hazard insurance, and maintenance/repairs as the time to foreclose lengthens.³⁵ The costs of servicing delinquent loans are much higher than the costs of servicing performing loans. Analysis of national data found that, “In 2013, the annual cost of servicing a nonperforming loan was on average 15 times that of servicing a performing loan—\$2,357 versus \$156.”³⁶ The same study found that the cost to service delinquent loans is rising much faster than the cost to service performing loans.

To prevent such losses, lenders have tightened access to credit for high-risk borrowers. This means that “risky” borrowers willing to pay a higher price in the form of a higher interest rate may nevertheless experience difficulties obtaining loans, because lenders are unable or unwilling to estimate the price that would compensate for the risks of servicing nonperforming loans through very lengthy foreclosure processes. Instead, they manage the risk by raising lending standards in order to avoid making risky loans at all.³⁷ This serves to depress the lower end of the housing market and reduce home ownership rates among families with lower incomes and/or credit scores.

Potential Beneficiaries: Occupants of Properties with Delinquent Mortgages

New York’s lengthy foreclosure process offers some benefits to borrowers or other people who occupy homes while the loans are delinquent. Borrowers have a right to occupy their properties until the foreclosure process is complete. Doing so enables them to avoid the costs of mortgage, tax and home insurance payments. Researchers estimate the average savings in the form of unpaid principal and interest for “post-crisis” borrowers in judicial foreclosure states at \$38,400, assuming a foreclosure process taking 32 months.³⁸ In New York, the figure could be much higher in many cases, due to both relatively high housing costs and longer foreclosure timelines. And this estimate does not include savings from unpaid property taxes and insurance. Servicers will sometimes offer financial incentives for occupants to vacate once the foreclosure process has run its course.³⁹ In cases where the lender or servicer opts to forgo foreclosure, the benefits to the occupants could be even greater as the time of nonpayment extends. However, borrowers in these situations suffer a major blow to their credit rating and so have reduced access to and higher cost for credit in the future.

Housing policy in the wake of the housing crisis has mostly focused on keeping borrowers in their homes even through the foreclosure process. To the extent that these policies have been successful, the result is that there is a sizeable pool of occupied homes in foreclosure (or for which the lender or servicer has forgone foreclosure). Many borrowers (or their tenants or others) remain in homes during the foreclosure process—especially downstate. The DFS survey found that only 8 percent of homes in foreclosure downstate became vacant during the foreclosure process.⁴⁰ Therefore, as the foreclosure backlog clears, occupants of many of these homes could be evicted if the borrower is found to have defaulted.

Fighting Zombies: Old and New Tools for Local Governments

Local governments face numerous difficulties in dealing with foreclosures. The judicial foreclosure process involves borrowers and the financial institutions that make or service the loans. Local governments are not parties to the mortgage foreclosure action. However, local governments can take action to address code violations and unpaid property taxes. Holding either borrowers or lenders/servicers accountable for code violations can be difficult, though. Borrowers who have abandoned properties typically do not notify their local government of their departure or leave a forwarding address. And in cases of foreclosures of vacant abandoned properties, figuring out who holds liens on a given property with a delinquent loan can also be difficult.⁴¹ However, the new vacant property registry developed by DFS should improve local governments' ability to get lien-holders to fulfill their obligations. In addition, terms of some State and federal court settlements with large banks over their role in the financial crisis have included provisions requiring banks to provide relief to borrowers (for example by reducing the loan principal amount) in order to enable borrowers to keep their homes.⁴²

Tax Liens and Tax Foreclosures

Generally, when property taxes are levied on behalf of a local government, the taxes become a lien on the properties. If the taxes go unpaid for a certain period of time, the local government responsible for enforcing the taxes may foreclose on the tax liens and acquire title to the properties. Properties acquired in this manner are typically sold at auction. Using auctions to dispose of these properties can promote “unhealthy speculation”—particularly in low-value markets with high concentrations of distressed properties. Unprepared individual investors can end up walking away from their purchases and the local governments end up repeating the process, often with no better result.⁴³ Speculators might also purchase numerous low-value properties, prepared to let them sit vacant for as long as it takes for the real estate market to recover. And officials in at least one New York county found that drug dealers were buying houses at foreclosure auctions with the aim of using the properties to conduct their “business.”⁴⁴

Different classes of local governments may be motivated by different interests and incentives. Most counties enforce delinquent property taxes and, consequently, make their towns and, in at least some cases, their cities whole for uncollected taxes. Counties therefore have more of a financial incentive to recoup back taxes than do the cities and towns where the properties are located. Thus, a county looking to collect unpaid taxes might have less concern about investors planning to leave the properties vacant as they wait to sell once the housing market improves as long as the investor pays the property taxes. On the other hand, a city or town might prefer to encourage buyers who will occupy the homes or developers interested in demolishing groups of dilapidated homes in accordance with a coordinated plan for urban redevelopment. Therefore, intergovernmental collaboration is important in identifying and implementing long-term remedies for dealing with tax delinquent properties.

Land Banks

In response to the persistence of substantial inventories of vacant and abandoned properties in communities across the State, the State Legislature has authorized the creation of up to 20 land banks. Land banks, which are not-for-profit corporations, may be established by certain local governments (or jointly among several local governments) with approval from the New York State Empire State Development Corporation. The main function of land banks is to acquire vacant, abandoned or tax-delinquent properties and then make needed improvements or demolish them if necessary. Land banks offer a means of helping local governments return vacant properties to productive use. Among other things, land banks can convey properties to individuals or entities who will maintain or redevelop them. Having a purchaser for “distressed” properties could create an incentive for lenders or servicers to complete foreclosures on vacant and abandoned properties, if at the end of the process they are able to sell the properties they acquire through foreclosure to a land bank.⁴⁵

In New York State, land banks are a recent addition to the local government landscape, authorized by Article 16 of the New York State Not-for-Profit Corporation Law, where land banks are declared to be “local authorities” for purposes of the Public Authorities Law. The initial authorization for land banks was signed into law in 2011.⁴⁶ New York State currently has 15 land banks. Their missions vary according to community needs. Several involve multiple local governments, which encourages coordination and planning regarding the disposition of foreclosed properties. As part of the U.S. Justice Department’s mortgage settlement with Bank of America, the bank agreed to donate some foreclosed properties in New York State to land banks and community groups and contribute funds towards renovating the properties.⁴⁷ OSC plans to publish a report on New York’s land banks as part of a series of reports on local authorities.

Conclusion

The foreclosure crisis has widespread negative consequences; local governments are among those struggling under this weight. Under certain circumstances, borrowers and lenders or servicers have incentives to walk away from properties. When this happens, local governments and communities have to cope with lengthy delays in returning foreclosed properties to market, or, in the case of zombie properties that have no clear path to responsible ownership, local governments must figure out first, how to identify such properties and second, how to return them to productive use. As policy makers work to address harm caused by persistently high foreclosure activity, they need to ensure that the improvements implemented take into account the interests of all of the key stakeholders—including local governments.

Local governments across New York State have struggled for years with the destabilizing fallout from the mortgage crisis. Reducing the backlog of foreclosure cases and addressing the zombie property issue will help local governments strengthen their housing markets and re-energize their communities. The State should continue to make this a priority. Support for efforts by the courts to work through their pending cases will help move tens of thousands of properties toward clear ownership. The State registry developed by DFS may help local governments monitor zombie properties and ensure that financial institutions adopt and implement the “best practices” in identifying and maintaining zombie properties. But if lien holders prove reluctant to adopt and fully implement these voluntary measures, then a legislative solution may be appropriate.

Notes

- ¹ OSC, *The Foreclosure Predicament Persists*, August 2015. Available at: www.osc.state.ny.us/localgov/pubs/research/snapshot/foreclosure0815.pdf.
- ² 934 days. See RealtyTrac, “1.1 Million U.S. Properties with Foreclosure Filings in 2014, Down 18 Percent from 2013 to Lowest Level since 2006.” Available at: www.realtytrac.com/news/foreclosure-trends/1-1-million-u-s-properties-with-foreclosure-filings-in-2014-down-18-percent-from-2013-to-lowest-level-since-2006/.
- ³ Mortgage Bankers Association, “Mortgage Foreclosures and Delinquencies Continue to Drop,” November 17, 2015 (press release), available at: www.mba.org/2015-press-releases/november/mortgage-foreclosures-and-delinquencies-continue-to-drop. The survey covers first-lien mortgages on one-to-four family residential properties.
- ⁴ New York State Department of Financial Services (DFS), *Report on New York’s Foreclosure Process* (May 2015), p. 12; and U.S. Government Accountability Office (GAO), *Mortgage Foreclosures: Additional Mortgage Servicer Actions Could Help Reduce the Frequency and Impact of Abandoned Foreclosures* (GAO-11-93), November 2010, p. 14.
- ⁵ See Dan Immergluck and Geoff Smith, “The Impact of Single-Family Mortgage Foreclosures on Neighborhood Crime,” *Housing Studies* 21 (6) (November 2006); and Kristopher S. Girardi, Eric Rosenblatt, Paul S. Willen, and Vincent W. Yao, “Foreclosure Externalities: Some New Evidence,” Federal Reserve Bank of Boston, Public Policy Discussion Papers No. 12-5. “Mortgage loan servicers” or “servicers” are persons or entities registered to engage in the business of receiving scheduled periodic payments from a borrower pursuant to the terms of a mortgage loan, including amounts for escrow accounts, and making payments to the owner of the loan or other third parties of principal and interest and certain other payments received from the borrower under the terms of a mortgage service loan document or servicing contract (Banking Law, Section 590[1]).
- ⁶ For a definition of “robo-signer,” see www.investopedia.com/terms/r/robo-signer.asp.
- ⁷ See, for example, Hugh Son and David McLaughlin, “BofA Gave Bonuses to Foreclose on Clients, Lawsuit Claims,” *BloombergBusiness*, June 15, 2013, available at: www.bloomberg.com/news/articles/2013-06-14/bofa-gave-bonuses-to-foreclose-on-clients-lawsuit-claims.
- ⁸ For a detailed example, see, Peter S. Goodman, “Foreclosure Settlement Fails to Force Mortgage Companies to Improve,” *Huffpost Business*, October 25, 2012, available at: www.huffingtonpost.com/2012/08/08/foreclosure-settlement-fails-mortgage_n_1754018.html.
- ⁹ Larry Cordell and Lauren Lambie-Hanson, “A Cost-Benefit Analysis of Judicial Foreclosure Delay and a Preliminary Look at New Mortgage Servicing Rules,” Federal Reserve Bank of Philadelphia, Working Paper No. 15-14 (March 2015), p. 27 (Table 1). Including New York, 22 states primarily use judicial foreclosure (p. 4).
- ¹⁰ *Ibid.*, p. 2.
- ¹¹ For a schematic overview of the foreclosure process in New York State see, New York State Homes and Community Renewal, “Understanding New York State’s Mortgage Foreclosure Process,” available at: www.nyshcr.org/topics/home/owners/foreclosureprevention/factsheets/understanding-foreclosure-process-in-nys-fact-sheet.pdf. See also, the Department of Financial Services’ website: www.dfs.ny.gov/consumer/hetptimeline.htm.
- ¹² Data from the New York State Unified Court System, Office of Court Administration. Since the figures for the average number of settlement conference appearances per case include only cases that were still active and many appearances resulted in a continuance, meaning that they would have additional appearances in the future, the average number of appearances needed to arrive at a disposition must be higher.

Notes

- ¹³ Cordell and Lambie-Hanson, “A Cost-Benefit Analysis of Judicial Foreclosure Delay” (March 2015), *op. cit.*, pp. 5-6.
- ¹⁴ DFS, *Report on New York’s Foreclosure Process*, *op. cit.*, p. 13.
- ¹⁵ *Ibid.*, p. 15.
- ¹⁶ New York State Unified Court System, *2011 Report of the Chief Administrator of the Courts*, p. 1. Available at: www.nycourts.gov/publications/pdfs/ForeclosuresReportNov2011.pdf.
- ¹⁷ *Ibid.*
- ¹⁸ New York State Unified Court System, *2014 Report of the Chief Administrator of the Courts*, p. 3. Available at: www.nycourts.gov/publications/pdfs/2014-Foreclosure-Report-of-the-CAJ.pdf.
- ¹⁹ GAO, *Mortgage Foreclosures* (GAO-11-93), November 2010, *op. cit.*, “Highlights” page; see also p. 14. Nonprime loans include both Alt-A and subprime loans. See p. 8 for definitions of these terms.
- ²⁰ These efforts are described in the annual *Report of the Chief Administrator of the Courts*. Available at: www.nycourts.gov/publications/#Foreclosure.
- ²¹ The legislation (Chapter 306 of the Laws of 2013) added a new Section 3012-b to the Civil Practice Law and Rules.
- ²² DFS, *Report on New York’s Foreclosure Process*, *op. cit.*, p. 12.
- ²³ *Ibid.*, p. 6.
- ²⁴ Properties can be vacant, but not abandoned. For example, an owner may be living elsewhere on a temporary basis, or he or she may be holding the property without renting it with the intention of eventually selling or occupying it.
- ²⁵ The bill (A.6932-A/S.4781-A) was introduced in 2015 by Assemblywoman Helene Weinstein (D-Brooklyn) and Senator Jeffrey D. Klein (D-Bronx/Westchester). It has been referred and reported to appropriate committees. A prior bill was introduced in 2014 (A.9341-A/S.7350-A).
- ²⁶ “Governor Cuomo Announces Major Mortgage Companies Agree to Measures to Combat Vacant Abandoned ‘Zombie Properties,’” Governor Andrew Cuomo press release, May 18, 2015, available at: www.governor.ny.gov/news/governor-cuomo-announces-major-mortgage-companies-agree-measures-combat-vacant-abandoned-zombie.
The industry best practices are available on the DFS website at: www.dfs.ny.gov/banking/best_practices_vac_aban_properties_nys.pdf.
- ²⁷ “Governor Cuomo Announces Two Additional Mortgage Companies Sign on to Combat ‘Zombie Properties,’” Governor Cuomo press release, July 9, 2015, available at: www.governor.ny.gov/news/governor-cuomo-announces-two-additional-mortgage-companies-sign-combat-zombie-properties.
- ²⁸ Michael Bess, “Assessing the Impact of Home Foreclosures in Charlotte Neighborhoods,” *Geography and Public Safety* 1 (3) (October 2008), pp. 2-4; cited in G. Thomas Kingsley, Robin E. Smith, and David Price, *The Impacts of Foreclosures on Families and Communities: A Primer*, The Urban Institute, July 2009, p. 4. Available at: www.urban.org/research/publication/impacts-foreclosures-families-and-communities.
- ²⁹ Dan Immergluck and Geoff Smith, “The Impact of Single-Family Mortgage Foreclosures on Neighborhood Crime,” *op. cit.*, p. 851.
- ³⁰ GAO, *Mortgage Foreclosures* (GAO-11-93), November 2010, *op. cit.*, p. 32.

Notes

- ³¹ Generally, counties insulate school districts and towns from these effects, shifting the liability to county tax rolls.
- ³² Cordell and Lambie-Hanson, “A Cost-Benefit Analysis of Judicial Foreclosure Delay” (March 2015), *op. cit.*, p. 13. The authors cite a number of studies on the negative externalities of foreclosure delays.
- ³³ Kristopher S. Girardi, et. al., “Foreclosure Externalities: Some New Evidence,” *op. cit.*, pp. 30-32.
- ³⁴ OSC, *The Foreclosure Predicament Persists*, *op. cit.*, Appendix.
- ³⁵ Cordell and Lambie-Hanson, “A Cost-Benefit Analysis of Judicial Foreclosure Delay” (March 2015), *op. cit.*, p. 8.
- ³⁶ Laurie Goodman, *Servicing is an Underappreciated Constraint on Credit Access*, The Urban Institute, December 2014, p. 2.
- ³⁷ *Ibid.*, p. 3.
- ³⁸ Cordell and Lambie-Hanson, “A Cost-Benefit Analysis of Judicial Foreclosure Delay” (March 2015), *op. cit.*, p. 30. The estimate is based on loans that became 90 days or more delinquent from February through September 2012.
- ³⁹ Stergios Theologides, “Servicing REO Properties: The Servicer’s Role and Incentives” in *REO and Vacant Properties: Strategies for Neighborhood Stabilization*, Federal Reserve Banks of Boston and Cleveland and the Federal Reserve Board, (September 2010), p. 79. Available at: www.bostonfed.org/commdev/REO-and-vacant-properties/.
- ⁴⁰ DFS, *Report on New York’s Foreclosure Process*, *op. cit.*, p. 6.
- ⁴¹ GAO, *Mortgage Foreclosures* (GAO-11-93), November 2010, *op. cit.*, p. 19 contains a discussion of the difficulties of tracking vacant abandoned foreclosures.
- ⁴² Peter Eavis and Michael Corkery, “Bank of America’s \$16 Billion Mortgage Settlement Less Painful Than It Looks,” *The New York Times*, August 22, 2014. Available at: www.dealbook.nytimes.com/2014/08/21/bank-of-america-reaches-16-65-billion-mortgage-settlement/?_r=0.
- ⁴³ See Thomas Fitzpatrick, “Investors, Speculators, and Data-Driven Decision Making,” panel presentation at the Renters, Homeowners, and Investors conference sponsored by the Board of Governors of the Federal Reserve System, February 26, 2013. Transcript available at: www.federalreserve.gov/mediacenter/files/renters-conference-panel-four-20130226.pdf.
- ⁴⁴ Interview with officials from the Land Reutilization Corporation of the Capital Region, August 19, 2015.
- ⁴⁵ GAO, *Mortgage Foreclosures* (GAO-11-93), November 2010, *op. cit.*, pp. 59-61.
- ⁴⁶ Chapter 257 of the Laws of 2011 as amended.
- ⁴⁷ Peter Eavis and Michael Corkery, “Bank of America’s \$16 Billion Mortgage Settlement” *op. cit.*

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