

Renters and the Housing Credit Crisis

by Danilo Pelletiere and Keith Wardrip

Traditionally, rental housing in this country is viewed as a residual category embracing only those too young or too insubstantial to be owners (Kruekeberg, 1999): The loss of a rental unit from the habitable stock or the processing of an eviction are events that often go unrecorded (Hartman and Robinson, 2003). Thus, for much of the past two years, as the implosion of credit and housing markets progressed, gaining national attention, the impact on renters and rental housing went largely unrecognized by policymakers and the media. But renters are being hurt by the weakening housing market in at least three significant ways. First and most directly, renters make up a significant share of those facing tenure insecurity and eviction due to the foreclosure of the homes they live in (just as they make up a significant share—32%—of all U.S. households). Second, the current crisis is reshaping the trends and patterns in housing markets, with an increase in rental demand already discernable and uncertainty about where an additional supply of affordable rental units will come from. Compounding this problem is the rapid rate at which banks are taking

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ownership of former rental properties, emptying them and leaving them unoccupied (see below). And finally, housing has once again become a priority on the agenda of local, state and federal government. How renters will fare in this reprioritization of housing policy, however, remains largely to be determined.

Many Renters Caught in Foreclosure

Through emerging data and the pleading of advocates, the great extent to which renters and rental units are caught up in the crisis is now becoming evident. For example, in

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March 2008, RealtyTrac reported that 38% of foreclosures nationwide and roughly half of the recent foreclosures in Nevada, Illinois and New York involved rental properties (cited in CBS Evening News, 2008, March 27). Similarly, the Mortgage Bankers

Association's National Delinquency Survey found that at the end of 2007 almost one in five of all foreclosure starts was a one-to-four-unit rental property (cited in JCHS, 2008).

New York University's Furman Center (2008) found that in New York City, 60% of the 15,000 foreclosure filings in 2007 were properties with two or more units. At least half of the more than 30,000 households in properties in foreclosure were likely renter households. And in Boston, cases of eviction due to foreclosure heard by the Housing Court at least doubled from 2006 to 2007, reaching roughly 20 per week (Appelbaum, 2007). Similarly, in Providence, lenders sought to evict more than 400 tenants from foreclosed homes in the first three months of this year (Arditi, 2008). The National Low Income Housing Coalition estimates that 45% of the units scheduled for auction or owned by banks in New England were rental units (Wardrip and Pelletiere, 2008a). In Hennepin County, Minnesota, 43% of the county's foreclosed properties were not owner-occupied in the first ten months of 2007, potentially affecting between 2,500 and 3,000 tenant households (Hennepin County Task Force, 2007). Furthermore, calls to

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Zelma Henderson

We dedicate this issue of *Poverty & Race* to Zelma Henderson, a beautician, the last named et al. of the 13 *Brown v. Board of Education* plaintiffs, who died in May at age 88. Ms. Henderson grew up in a small Kansas town where she attended an integrated elementary school (Kansas law required racial separation only for elementary schools in towns of 15,000 or more). When she moved to Topeka, her two children were bused to an all-black school across town, which set her teeth on edge: "I knew what integration was and how well it worked, and couldn't understand why we were separated here in Topeka," and so she joined the Supreme Court suit. "None of us knew that this case would be so important and come to the magnitude it has. What little bit I did, I feel I helped the whole nation," she told a *Dallas Morning News* interviewer. Another instance of how important it is for individuals to assert what is right.

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Homeline, a Minnesota tenant hotline, from renters facing eviction as a result of foreclosure increased over 400%, from 78 in 2006 to 424 in 2007 (Heath and Jones, 2008).

Even in a weaker housing market such as Cleveland, rentals make up a significant portion of foreclosure filings. According to recent research (Rothstein, 2008), an estimated 30% of foreclosures in Cuyahoga County were rental properties. The Cleveland Tenants Association, a referral agency associated with the County's "Don't Borrow Trouble Hotline," reported 373 calls from renters in foreclosure between January and March of this year, nearly as many (420) as it received in all of 2007 (Rothstein, 2008). The number of cases with landlords seeking to evict tenants tripled in the Cleveland Housing Court from September 2006 to September 2007 (Harris, 2007).

It should not be surprising that renters are caught up in the current credit crisis. Rental housing, particularly the one-to-four-unit stock (50% of the nation's rental housing), is financed by the same housing finance system as owner-occupied housing; indeed, the largest segment of the rental market (35%) is single-family homes (JCHS, 2006: 23). As the housing market weakens and subprime and predatory loan terms continue to take their toll, this stock is clearly susceptible to the same strains as the owner-occupied stock.

Based on their finding that multi-unit properties in Massachusetts were 30% of foreclosures but only 10% of sales, Foote, Girardi, Goette and Willen (2008) have argued that multi-unit properties actually may be more vulnerable to foreclosure due to higher combined loan-to-value (CLTV) ratios. The thinking, echoed elsewhere (Evans, 2007), is that as prices soared, many smaller rental properties were increasingly held or bought and operated primarily to extract the appreciation in value, not only upon resale but on an ongoing basis through cash-out refinancing. As a result, these

properties were often mortgaged for more than their rental income potential and long-term costs might dictate. It is hypothesized therefore that as values have fallen, owners of these small investment properties go into foreclosure rather than pay for and operate a depreciating asset in which they have negative equity. Along with high CLTV ratios, national statistics suggest non-owner-occupied purchases were more likely to receive higher-priced loans than similar owner-occupied properties (Avery, Brevoort, and Canner, 2007). Essentially, the argument is that if the current crisis was

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brought on by a speculative bubble, as appears to be the case, speculative rental units would be expected to be disproportionately affected by the implosion of that bubble. The renter-occupants who may live in them are simply collateral damage.

A more general and perhaps additional explanation for the high concentrations of rental housing among foreclosures, however, appears to lie in the economic geography of rental housing in the U.S. In short, rental housing in this country is highly concentrated in a relatively few neighborhoods, primarily co-located with economic distress and minority populations. Price declines have likely been steepest in these neighborhoods, thus increasing the likelihood of foreclosure.

It is well known that subprime or predatory loans and high CLTV ratios are concentrated in poor and minority neighborhoods (e.g., Avery, Brevoort, and Canner, 2007). Facing economic distress themselves and/or in their broader community, homeowners and landlords with little accumulated home equity or other accumulated wealth are less likely to find a way to make payments. With prices falling, struggling landlords and homeowners cannot sell their property for enough money to avoid foreclosure (Foote, Girardi,

Goette and Willen, 2008).

Making matters worse in low-income neighborhoods is that, while subprime and predatory loan terms clearly exacerbate the conditions for foreclosure, falling home prices and rising unemployment are emerging as the two best indicators of rising foreclosures. Most low-income neighborhoods experienced anemic or non-existent real income growth for much of this decade, and the recent slowdown has intensified their distress. More recently, there is evidence that after more rapid increases in home prices, many communities with lower-priced homes may now be experiencing more rapid price declines. It is this confluence of poverty, predatory lending and falling home values in low-income neighborhoods that has exposed all mortgaged housing, including the rental stock concentrated in these neighborhoods, to a greater risk of foreclosure. As is often observed, when the broader economy catches a cold, low-income and minority communities come down with pneumonia.

Analysis of New England data from the same source Foote, Girardi, Goette and Willen (2008) used in their analysis of Massachusetts foreclosures supports the conclusion that neighborhood effects are a likely factor in explaining the significant numbers of rental homes in foreclosure (Wardrip and Pelletiere, 2008b). Among neighborhoods with similar shares of rental housing, a greater concentration of poverty within a census tract was found to raise the expected incidence of foreclosure auctions and bank ownership. Conversely, however, greater concentrations of rental housing in a neighborhood indicated no similar pattern among neighborhoods with similar concentrations of poverty. Along with having high foreclosure rates, the high-poverty, high-renter neighborhoods in the study are also home to significantly higher proportions of non-white residents and other measures of economic disadvantage.

High-poverty communities also contain a disproportionate share of the region's multi-unit, non-condominium housing. Therefore, even though

multi-unit structures do not make up a disproportionate share of foreclosures relative to the underlying distribution of the housing stock in these neighborhoods, the disproportionate share of the region's multi-unit and rental housing in these foreclosure-prone communities may explain the unexpectedly large number of these properties that are foreclosed upon overall. As a practical matter, the higher number of multi-unit foreclosures in these neighborhoods also increases the average number of households affected by each foreclosure. Thus, even if concentrations of rental housing do not have an independent effect on an area's foreclosure rate, the fact that many lower-income and minority households rent their homes does create this association.

All Renters Are Challenged by a Changing Market

Beyond the direct injury of an eviction due to foreclosure, low-income renters are feeling the effects of increasing demand for available rental housing. Foreclosed homeowners and renters are entering the market in increasing numbers while the crisis is also diminishing incomes, opportunities for credit and consumers' preference for homeownership, further swelling the number of current and prospective renters. Today, millions more Americans are looking for decent, affordable rental housing.

The U.S. Census estimates that between the first quarter of 2007 and the first quarter of 2008 the number of renter households increased by 980,000. Since 2005, when housing prices were peaking nationally, there has been an increase of nearly 2 million renters. To provide some context for how rapid this increase has become, in the entire first half of the decade, from 2000 to 2005, the number of renters increased by 792,000. More problematic for communities trying to react to the crisis, the number of rent-

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National Commission on Fair Housing and Equal Opportunity

The 40th Anniversary of the Fair Housing Act provides an excellent time to take stock of the status of fair housing and fair lending in the United States and to look forward to the direction enforcement of the Fair Housing Act and other fair housing strategies should take in the future.

The **Leadership Conference on Civil Rights Education Fund, Lawyers' Committee for Civil Rights Under Law, the NAACP Legal Defense Fund, and the National Fair Housing Alliance** have created the National Commission on Fair Housing and Equal Opportunity to conduct regional hearings across the country designed to examine the state of fair housing in America 40 years after the Act's passage.

The Commission will be chaired by former HUD Secretaries Jack Kemp and Henry Cisneros. Other Commissioners include Okianer Christian Dark, Associate Dean, Howard University School of Law; Gordon Quan, former Mayor Pro Tem and Chair of the Housing Committee for the City of Houston; Myron Orfield of the Institute on Race and Poverty at the University of Minnesota; Pat Combs, immediate past President of the National Association of Realtors; and I. King Jordan, President Emeritus, Gallaudet University.

The hearings will explore the persistence of housing discrimination and segregation and its impact on our communities; the nexus between fair housing and other socio-economic factors such as education, access to credit, employment opportunities, environmental injustice, transportation issues, and access to quality health providers; the successes, failures and flaws of the federal fair housing enforcement mechanisms; and strategies to break down residential segregation and provide households isolated in segregated areas the opportunity to find integrative alternatives. The goal is to refocus the nation's attention on fair housing/fair lending and develop a policy agenda to ensure strong enforcement of the Fair Housing Act, a commitment to integrated communities and an increase in the availability of affordable housing.

The hearing schedule is as follows:

July 15th	Chicago
July 31st	Houston – Field Hearing
September 9th	Los Angeles
September 22nd	Boston
October 17th	Atlanta

Each hearing will consist of multiple panels looking at every aspect of enforcement, residential segregation and discrimination in housing. The hearings will culminate with release of a report in December, 2008 detailing the testimony provided at the hearings and outlining future recommendations.

PRRAC is pleased to be providing staff/consulting support to the Commission, along with fair housing consultant Sara Pratt and Julie Fernandes of the Raben Group. For more information, contact Philip Tegeler, ptegeler@prrac.org.

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ers has already increased more than projections were predicting. For example, Harvard's Joint Center for Housing Studies had predicted an increase of just 1.8 million renters for the entire period from 2005 to 2015 (William Apgar, quoted in Swarns, 2008).

This is how one respondent in a recent survey of housing counselors conducted by the National Low Income Housing Coalition (Wardrip and Pelletiere, 2008c) describes the new competition created by foreclosure: "There are both tenants that are displaced by foreclosure as well as potential buyers that can't or don't want to enter into homeownership that are now competing with other tenants for limited rental units." Clearly, foreclosed and evicted homeowners can be added to this list competing for limited affordable rental units.

A foreclosure not only can result in new entrants to the rental market, but it also results in a unit being unoccupied and held off the market at least temporarily during and after the foreclosure process. Particularly in a soft market, it can be a long time before a foreclosed rental property is returned to the market, sold and returned to occupancy. Upon its eventual return, there is no guarantee it will be rented, in good condition, or offered at a similar or lower rent as that before the foreclosure. Moreover, the bias toward homeownership in this country suggests that it will be a lot harder for units to convert, even convert back, from ownership to rental in many locations, certainly more difficult than it was for thousands of units to convert from rental to condominiums and other ownership forms during the height of the boom. Local zoning, neighborhood opposition, condominium and homeowner association rules all generate considerable friction in the conversion from owning to renting. Indeed, the relatively fluid conversion of units from rental to ownership during the boom, often with local government facilitation, is now making it difficult to accommodate

households foreclosed and evicted, often from the very same units, in the rental market. Nearly 300,000 units in large multi-unit properties were converted from rental to condominium ownership in 2005 and 2006 (JCHS, 2008).

It seems likely that in all but the slackest rental markets, increased demand will be met with declining supply in the short run (Rho, Pelletiere, and Baker, 2008). How this situation

Rental housing is highly concentrated in neighborhoods with minority populations.

might be resolved in the long term, whether an excess of units will eventually lead to slacker markets and lower rents as some have predicted (e.g., Timiraos, 2008) for example, remains highly uncertain.

Shifting Policy Priorities Affect Renters

The final channel through which the housing credit crisis is affecting renters is the policy process at the local, state and federal levels. Not only are governments taking steps to directly address the current crisis, but in doing so they are re-ordering their housing policy priorities across the board.

In the majority of states, renters have few rights in a foreclosure, receive little notice and can be evicted shortly after the foreclosure is completed without just cause (such as non-payment of rent). Renters are the last to hear about the impending loss of their home and are evicted through no fault of their own, after having paid rent and losing their security deposit.

Thus, one significant way in which policy has been changing for renters has been to push for greater protections. A number of states have passed new legislation protecting renters in the foreclosure process. Minnesota and Illinois have recently passed laws providing renters with some measure of protection and notice in a foreclosure.

New Jersey and the District of Columbia already had such protections in place. In most instances these are modest proposals that simply provide tenants with more notice and delay the timing of an eviction in the foreclosure process. Some are seeking to provide more protection. In Massachusetts, for example, bills are pending in the legislature that would: prevent lenders and their associates from evicting tenants from foreclosed properties without just cause; impose a one-time six-month moratorium on foreclosures of owner-occupied property with subprime, predatory mortgages; and require a judicial foreclosure system. All of these bills would benefit tenants in pre- and post-foreclosure properties.

It is important to note that while a bias against renters has likely kept them from being recognized in much of the policy discussion, ironically they have also been left out in part because, of all those caught up in this crisis, they are least plausibly to blame for causing their own problems. When the problems of renters are recognized, their blamelessness can be an asset in erecting protections for them.

While some progress has been made in protecting renters in the foreclosure process, it is less clear what states may do to monitor and adjust to the changing dynamics of renting and owning in this country. Still viewing it as a homeownership crisis, few states or localities appear to be focused on accommodating additional renters.

At the federal level, just as at the state level, the majority of proposed policies to assist households in foreclosure, as opposed to builders, banks and realtors, have been targeted at owner-occupied housing. At the same time, however, some proposals would help renters. For example, proposals have been made in both the House and the Senate that would prohibit evictions in a foreclosure until after 90 days or the end of the lease, whichever comes sooner. Also, there has been an effort to provide additional funds to the FEMA Emergency Food and Shelter Program to aid owners and renters facing foreclosure from

homelessness by providing them with temporary financial assistance.

At a more general level, the rush of housing legislation and the focus on housing by policymakers has provided new impetus and a vehicle for the National Housing Trust Fund, which, when fully realized, would use funding from a variety of dedicated sources to build, rehabilitate and preserve 1.5 million units of housing for the lowest-income families within 10 years. Also, neighborhood stabilization funds have been proposed in both houses of Congress that are in part directed at maintaining rental housing for extremely low-income households.

At all levels of government, however, resources are constrained, and resources for a new priority must of-

ten come at the expense of some other budget item. One benefit of a housing trust fund is that its resources are separate from annual appropriation decisions. While the National Housing Trust Fund would not use existing funds from another housing program, Congress still plans to use some of the new dollars to pay for the first years of another new program aimed at preventing owner-occupied foreclosures. This example shows well the constantly shifting balance of gains and losses that are emerging from the new attention on housing. It remains uncertain whether the policy changes afoot will lead to a more balanced housing policy in which low-income people are a greater priority and rental housing is better recognized for pro-

viding millions of Americans with decent housing. There is real concern among advocates that attempts to shore up home prices and stabilize homeowners further will undercut efforts to create and maintain affordable rental housing.

Conclusion

The current credit crisis is not only a crisis for homeownership. Its impacts are not limited to households with subprime loans. Today, it is a crisis that affects the entire U.S. housing market, generating an existential threat to the housing of millions of minority and low-income households, including renters. □

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