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## AN URBAN SLICE OF APPLE PIE: RETHINKING HOMEOWNERSHIP IN U.S. CITIES

GEORGETTE CHAPMAN PHILLIPS\*

"For *some* families *some* houses represent wise buys, but a culture and real estate industry that give blanket endorsement to ownership fail to indicate *which* families and *which* houses."

—John P. Dean (1945)<sup>1</sup>

The romantic notion of homeownership is deeply rooted in the American psyche. Homeownership as the "American Dream" borders on cliché. We proclaim that June is "National Home Ownership Month."<sup>2</sup> However, it is worth asking whether this aspiration to own a home can or should be spatially differentiated. Beginning with the first Home Owners' Loan Corporation (HOLC) maps that infamously redlined inner-city neighborhoods, the push toward homeownership favored suburban locations.<sup>3</sup> As GIs returned from World War II, suburban Levittown-type developments beckoned with the promise of a safe and tranquil escape from the tensions of the city. Homeownership rates in the suburbs typically far outstripped homeownership rates in the metropolitan cities of the United States.<sup>4</sup> Other government policies built upon this suburban favoritism leaving city dwellers to wonder if they were, in fact, permitted to share in the same dream.

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1. JOHN P. DEAN, *HOMEOWNERSHIP: IS IT SOUND?* (1945) (*quoted in* Lawrence Vale, *The Ideological Origins of Affordable Home Ownership*, in *CHASING THE AMERICAN DREAM: NEW PERSPECTIVES ON AFFORDABLE HOMEOWNERSHIP* 37 (William M. Rohe & Harry L. Watson eds., 2007)).

2. A. Mechele Dickerson, *The Myth of Home Ownership and Why Home Ownership Is Not Always a Good Thing*, 84 IND. L.J. 189, 190 (2009).

3. See *infra* note 144 and accompanying text.

4. In 1950, the city owner occupied percentage was 50% and the suburban owner-occupied percentage was 56%. 1 BUREAU OF THE CENSUS, U.S. DEP'T OF COMMERCE, CENSUS OF HOUSING: 1950, PT. 1, AT 2 TBL. 2 (1953) [hereinafter 1950 CENSUS OF HOUSING]. By 1960, the city owner-occupied percentage was 47%, and the suburban owner occupied was 67%. 4 BUREAU OF THE CENSUS, U.S. DEP'T OF COMMERCE, CENSUS OF HOUSING: 1960, pt. 1B, at 23 tbl. 1 (1962) [hereinafter 1960 CENSUS OF HOUSING].

Urban economists, sociologists and policy makers, however, extolled both the individual benefits of homeownership (wealth creation, forced savings) and the positive externalities (stability, crime reduction, etc.), and pushed for an increase in homeownership rates in urban neighborhoods.<sup>5</sup> Citing the long history of racial discrimination in mortgage lending, advocates of homeownership pushed for regulation barring this type of discrimination and opening the mortgage markets to previously underserved populations. In the most recent past, the Community Reinvestment Act of 1977 (CRA) and policy changes at the mortgage giants Fannie Mae and Freddie Mac had the explicit goal of increasing homeownership in historically underserved city neighborhoods.<sup>6</sup>

City homeownership did have a substantial increase in the 2000 census when the rate of urban homeownership hit 53.4%.<sup>7</sup> However, the soft underbelly of this increase was the creeping reliance on subprime loans to finance this ownership. Even before the current crisis, there was a heavier use of non-prime loans in minority and inner-city neighborhoods.<sup>8</sup> The advent of the subprime adjustable rate mortgage (ARM) may have contributed to a noted increase in urban homeownership. However, as that bubble began to burst, not only did the dreams of the individual homeowners evaporate into foreclosure, the visions of city leaders built upon the same dreams morphed into fiscal nightmares.

That leaves us with the salient question: Does (or should) the distinctly suburban mindset of homeownership have a place in urban policy? The fact that many households hold their wealth through homeownership does not mean that this should be true of all.<sup>9</sup> Indeed, to answer the question we must first historically contextualize patterns of urban housing tenure and contrast it with the growing push toward suburban homeownership. The next step will entail discussing the recent federal policy initiatives directed specifically at *urban* homeownership and their effect on housing tenure. The recent boom and bust of the residential housing market had grave implications for urban communities

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5. See Joseph M. Harkness and Sandra J. Newman, *Effects of Homeownership on Children: The Role of Neighborhood Characteristics and Family Income*, FED. RES. BANK N. Y. ECON. POL'Y REV., June 2003, at 87; Melissa B. Jacoby, *Home Ownership Risk Beyond a Subprime Crisis: The Role of Delinquency Management*, 76 FORDHAM L. REV. 2261, 2261-62 (2008).

6. Pub. L. No. 95-218, tit. VIII (Community Reinvestment), §§ 801-806, 91 Stat. 1111, 1147-48 (codified as amended at 12 U.S.C. §§ 2901-2908 (2000)).

7. U.S. DEP'T HOUS. & URBAN DEV. & U.S. DEP'T COMMERCE, AMERICAN HOUSING SURVEY FOR THE UNITED STATES: 2007, 12 tbl. 1B-1 (2007), available at <http://www.census.gov/prod/2008pubs/h150-07.pdf>.

8. U.S. DEP'T HOUS. & URBAN DEV., SUBPRIME LENDING REPORT, UNEQUAL BURDEN: INCOME & RACIAL DISPARITIES IN SUBPRIME LENDING (2000).

9. See Jacoby, *supra* note 5, at 2278. But see J. Peter Byrne & Michael Diamond, *Affordable Housing, Land Tenure, and Urban Policy: The Matrix Revealed*, 34 FORDHAM URB. L.J. 527, 544 (2007) (advocating for homeownership for low-income families).

due, in large part, to the intersection of racial concentration in residential living patterns coupled with extraordinary penetration of subprime mortgages into the minority housing markets. The foreclosure crisis occupies a focal point of this discussion. The conclusion advocates a rethinking of urban housing policy to incorporate not just the goal of individual homeownership, but also the stability and economic well being of the city's neighborhoods—including those who are not able to join the ranks of homeowners.

## I. HISTORICAL NOTIONS OF URBAN HOMEOWNERSHIP

From its agrarian roots, the United States has shifted into a nation that is increasingly urbanized. In the 1920 census the split between rural and urban residents was almost even.<sup>10</sup> The gap began to widen as early as the 1930s, when the rural population dropped from 48.8% to 43.9%, and the urban population increased from 51.2% to 56.1%.<sup>11</sup> The difference became even more pronounced in the 1950s with 36% of the population living in rural areas and 64% in urban areas.<sup>12</sup>

Mass urbanization began with a shift from an agriculturally focused nation to a more industrially driven nation. As workers streamed into the city, they swelled the unsanitary and unsafe tenement houses and rental apartments.<sup>13</sup> Teeming masses in squalid living conditions stand in stark contrast to the traditional Jeffersonian ideal of private landownership that has permeated American culture since the inception of the country.<sup>14</sup> Thus the seeds of tension of urban living and homeownership were sown.

In point of fact, however, the idealized notion of homeownership was not prevalent in urban centers of the United States for the first several centuries.<sup>15</sup> The idea of owning a single-family home gained a foot-

10. Fifty-one percent of the total population was urban and 49% was rural. 2 BUREAU OF THE CENSUS, U.S. DEP'T OF COMMERCE, CENSUS OF POPULATION: 1920, ch. 15, at 1302 tbl. 9 (1922).

11. 1 BUREAU OF THE CENSUS, U.S. DEP'T OF COMMERCE, CENSUS OF POPULATION: 1930, at 8 tbl. 3 (1931).

12. 1 1950 CENSUS OF HOUSING, *supra* note 4, pt. 1, at xxv tbl. F.

13. Charles C. Bohl, *Affordable Housing Design for Place Making and Community Building*, in CHASING THE AMERICAN DREAM, *supra* note 1 at 114.

14. See Georgette C. Poindexter, *Collective Individualism: Deconstructing the Legal City*, 145 PA. L. REV. 607, 625 (1997) [hereinafter Poindexter, *Collective Individualism*]. See also Byrne & Diamond, *supra* note 9. It is interesting to note that this Jeffersonian ideal tied civic participation to land ownership. Tenants were not permitted to vote in federal elections until 1860. See William M. Rohe and Leslie S. Stewart, *Homeownership and Neighborhood Stability*, 7 HOUSING POL'Y DEBATE 37, 37 (1996).

15. In fact, homeownership rates dropped from 1890 to 1920. William H. Rohe & Harry L. Watson, *Introduction: Homeownership in American Culture and Public Policy*, in CHASING THE AMERICAN DREAM, *supra* note 1 at 1, 9; see also Ira Rheingold, Michael Fitzpatrick & Al Holfield, Jr., *From Redlining to Reverse Redlining: A History of Obstacles for Minority Homeownership in America*, 34 CLEARINGHOUSE REV. 642, 642 (2001).

hold during the 1920s, and urban homeownership rose. Homeownership rates jumped from 45.6% in 1920 to 47.8% in 1930.<sup>16</sup> Even then it was far from a foregone conclusion that a family (even one of financial means) would choose to buy a home rather than rent.<sup>17</sup> However, the bottom of the housing market fell out almost completely during the Great Depression, and ownership rates dipped once more.<sup>18</sup> In an attempt to shore up the failing real estate industry, the federal government intervened into the private mortgage market with the creation of the Federal Housing Administration (FHA).<sup>19</sup> Interestingly, the market drop cut across economic statuses. Homeownership rates after the Depression were not markedly different across class lines. In 1940, the homeownership rates for skilled and unskilled manual workers were not far below that for professionals (slightly less than 44%).<sup>20</sup> Prior to World War II, it was common for people (especially those in the working class) to buy their first home in their forties when the eldest children had entered the work force and could contribute to the family income.<sup>21</sup>

After World War II, homeownership rates skyrocketed in the suburbs, often at the expense of the city. At the beginning of the twentieth century, most Americans did not own their own homes.<sup>22</sup> By 1960, about 61.9% of Americans owned their own homes.<sup>23</sup> But this growth was uneven. In 1960, 47% of city units were owner-occupied, whereas 67% of suburban units were owner-occupied.<sup>24</sup> The suburbs became cheap and easy. First of all, land was cheaper away from the city core, which made homeownership more available.<sup>25</sup> Furthermore, the federal income tax code included deductibility of mortgage interest and real estate taxes, which made owning a suburban bungalow even cheaper.<sup>26</sup> Federal highway dollars built concrete connectors from bedroom to office

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16. Vale, *supra* note 1, at 16.

17. MARGARET GARB, *CITY OF AMERICAN DREAMS: A HISTORY OF HOME OWNERSHIP AND HOUSING REFORM IN CHICAGO 1871–1919* 119–120 (2005) (discussing the ambivalence of upper middle-class families in Chicago in choosing to rent or to buy a home).

18. Rheingold et al., *supra* note 15, at 642–643.

19. See U.S. Dep't Hous. & Urban Dev., The Federal Housing Authority (FHA), <http://www.hud.gov/offices/hsg/fhahistory.cfm> (last visited June 21, 2010).

20. Richard Harris, *The Suburban Worker in the History of Labor*, 64 INT'L LAB. AND WORKING CLASS HIST. 8, 8–24 (2003); Rohe & Watson, *supra* note 15, at 9; Richard Harris, *Working-Class Home Ownership in the American Metropolis*, 17 J. URB. HIST. 46, 50 (1990).

21. Harris, *supra* note 20, at 49.

22. U. S. BUREAU OF THE CENSUS, U.S. DEP'T OF COMMERCE, *HISTORICAL CENSUS OF HOUSING: HOMEOWNERSHIP*, <http://www.census.gov/hhes/www/housing/census/historic/owner.html> (last visited June 21, 2010).

23. *Id.*

24. 1960 Census of Housing, *supra* note 4, pt. 1B, at 23 tbl. 1.

25. Harris, *supra* note 20, at 59.

26. I.R.C. § 163(h)(3) (2006). See also Byrne & Diamond, *supra* note 9, at 542.

that facilitated commuting from the suburbs.<sup>27</sup> Federal mortgage guarantees through the FHA enticed buyers to the suburbs. The GI Bill (along with Veterans Affairs-insured mortgages) opened up capital to returning soldiers who found they could afford a single-family detached house in the suburbs.

The propaganda extolling the virtues of homeownership dates back to Herbert Hoover's "Own-Your-Own-Home" campaign when he was Secretary of Commerce under Presidents Harding and Coolidge.<sup>28</sup> However, in post-War America, the push toward homeownership was embraced with new fervor. Whether for economic (promoting self sufficiency and wealth building), psychological (promoting positive well-being) or social (promoting stable neighborhoods and communities) reasons,<sup>29</sup> almost no one dared to question the seemingly foregone conclusion that all Americans should strive to own their own home.<sup>30</sup> This thread of tying homeownership to "the American Way" continues strong through today.<sup>31</sup>

Two separate but powerful changes drastically bent the curve in homeownership growth: the FHA and zoning. In an effort to jump-start the moribund construction industry, the FHA was created to insure home mortgages.<sup>32</sup> This alone has no urban/suburban dichotomy. Where the division arises lies in the geographically prescribed limits in which these mortgages can secure a home loan. The invidious HOLC

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27. See Georgette C. Poindexter, *Towards a Legal Framework for Redistribution of Poverty-Related Expenses*, 47 WASH. U. J. URB. & CONTEM. L. 3, 8 (1995); Byrne & Diamond, *supra* note 9, at 564; William A. Fischel, *An Economic History of Zoning and a Cure for Its Exclusionary Effects*, 41 URB. STUD. 317, 327 (2004).

28. Vale, *supra* note 1, at 19. As an ironic aside, when Hoover was President during the Great Depression, encampments of homeless Americans were dubbed "Hoovervilles."

29. Jacoby, *supra* note 5, at 2262.

30. Notable critics at the time were Carol Aronovici (who complained that renters were "not given a proper place on the roster of solid citizenry") and John P. Dean. Vale, *supra* note 1, at 37 (quoting CAROL ARONOVICI, *HOUSING THE MASSES* (1939)). In fact, the Atlantic Monthly chastised another periodical's criticism of homeownership stating, "criticism of homeownership is almost as reprehensible as an attack upon the Deity or a denial of the sincerity of mother's love." *Id.* (quoting C.B. Reeves, *Gamble of Homeownership*, ATLANTIC MONTHLY, April 1937, at 450, 450).

31. In August 1986, *Newsweek* magazine announced that, "Homeownership has finally joined motherhood and apple pie on the list of unassailable American Institutions." Eric Gelman et al., *How Tax Reform Affects You*, NEWSWEEK, August 25, 1986 at 19. The same exaltations of homeownership can also be heard in Canada, where scholars have noted that, "Americans have commonly referred to home ownership as the 'American dream,' but it can with equal justice be described as the dream of Canadians." See Richard Harris, *More American Than The United States*, 26 J. URB. HIST. 456, 462 (2000). Contrast this with Switzerland, which has the lowest homeownership rate in Europe (30%) and is the only developed nation to tax imputed rent. See Fischel, *supra* note 27, at 334.

32. Rheingold et al., *supra* note 15, at 644.

maps that literally redlined massive swaths of urban neighborhoods (thus preventing lending on houses in these neighborhoods) serve as the subject of countless books, articles and scholarly treatises.<sup>33</sup> The story is well-told, but it bears a distinct reference here because this was a crucial step in creating a schism in the rates of homeownership between the city and the suburbs. Requirements for minimum lot sizes and setbacks, plus a preference for new construction, all combined to push homeowners to the suburbs.<sup>34</sup> The crowning fact that the maps were explicitly race-based left its legacy on countless city neighborhoods where access to capital was nigh impossible.<sup>35</sup>

Furthermore, changes in local government law that affirmed the constitutionality of zoning catapulted the single-family house into exalted status. The primacy of single-family dwellings had its roots in previous land use law initiatives—most notably the publication of *A Model Tenement House Law in New York* in 1910.<sup>36</sup> This model legislation categorized dwellings into three classes (single-family, two-family, and multiple-family) with the goal of eventually eliminating multiple-family dwellings altogether.<sup>37</sup> In 1926, the United States Supreme Court upheld a zoning law whereby the municipality could restrict a landowner from using the property except in accordance with the zoning code. The Court held that it is permissible to segregate land uses for the “health, safety, and welfare” of the populace.<sup>38</sup> Among the reasons the Court stated to justify the separation was that the proximity of “apartment houses” to single-family homes ruined the latter.<sup>39</sup>

If one imagines a zoning code as a triangle with the most intensive land uses on the bottom, the single-family home designation rests at the pinnacle. In development, a property can be “up-zoned,” meaning that, in most instances, it can legally be used for less-intensive uses than what the code allows (e.g., you can build a single house in an area zoned for multi-family houses). However, it cannot be “down-zoned” (e.g., you cannot build a multi-family structure in an area zoned for single houses) without a variance, which will be based on a showing of hardship and/or necessity. As one commentator has noted, there is no theoretical reason

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33. See generally KENNETH T. JACKSON, *CRABGRASS FRONTIER: THE SUBURBANIZATION OF THE UNITED STATES* (1985).

34. See Charles L. Nier, III, *Perpetuation of Segregation: Toward a New Historical and Legal Interpretation of Redlining Under the Fair Housing Act*, 32 J. MARSHALL L. REV. 617, 625 (1999).

35. See *infra* notes 144–45 and accompanying text.

36. LAWRENCE VEILLER, *A MODEL TENEMENT HOUSE LAW* (1910). This book, published in 1910, detailed a model law aimed at improving multi-family housing in cities across the country. It was based on the Tenement House Law of 1901.

37. Vale, *supra* note 1, at 18.

38. *Village of Euclid v. Ambler Realty Co.*, 272 U.S. 365, 394 (1926).

39. *Id.*; see also Tim Iglesias, *Our Pluralist Housing Ethics and the Struggle for Affordability*, 42 WAKE FOREST L. REV. 511, 576 (2007).

that other land uses should be regarded as less important—but they are.<sup>40</sup> Zoning a piece of land as single-family endows it with the value that all surrounding land will be used comparably, preserving the economic value of the land and incentivizing consumption. This works well for undeveloped land in the suburbs. However, in urban centers already built up with attached housing and mixed uses, the endowment value is unattainable.

A by-product of these policies and laws was the increasing economic and racial stratification in metropolitan areas. The suburbs grew wealthier and whiter. The central core grew poorer and more dominated by minority populations. Historically, the gap between Black and White homeownership was narrowing before 1940.<sup>41</sup> However, as an increasing number of Blacks left the rural South for the urban North, the gap widened because homeownership rates for residents of central cities remained low.<sup>42</sup> There is no dispute that although racial segregation might have predated federal housing and transportation initiatives, these programs reinforced mobility barriers that kept minorities out of the suburbs and put homeownership beyond their grasp.<sup>43</sup>

Civil unrest left many of America's cities bursting into rioting flames in the late 1960s. One response of the federal government was an attempt to create housing and homeownership opportunities for low-income families. Title VIII of the Civil Rights Act of 1968,<sup>44</sup> also known as the Fair Housing Act, sought to eliminate housing discrimination and level the playing field across racial lines in access to housing. It had two major goals: expand minority housing opportunities, and foster residential integration.<sup>45</sup> Its centerpiece program, Section 235, however, rests in the history books as a failure. Middle-income white families used the program to purchase new suburban housing, while Black families were forced into over-priced, old, inner-city homes of questionable structural integrity.<sup>46</sup> Notwithstanding the failure of the Section 235 program,

40. Fischel, *supra* note 27, at 327.

41. See GEORGE S. MASNICK, HOME OWNERSHIP TRENDS AND RACIAL INEQUALITY IN THE UNITED STATES IN THE 20TH CENTURY 9 (2001).

42. See William J. Collins and Robert A. Margo, *Race and Home Ownership: A Century-Long View*, 38 EXPLORATIONS IN ECON. HIST. 68, 89 (2001).

43. The racial impact of federal programs is so well-accepted as to constitute a stylized fact. See JACKSON, *supra* note 33, at 362; see also Collins & Margo, *supra* note 42, at 84–85; Nier *supra* note 34, at 618; Byrne & Diamond, *supra* note 9, at 564; John A. Powell, *Reflections on the Past, Looking to the Future: The Fair Housing Act at 40*, 41 IND. L. REV. 605, 612 (2008); Rheingold et al., *supra* note 15, at 644–645.

44. Pub. L. No. 90-284, tit. VIII (Fair Housing), §§ 801–819, 82 Stat. 73, 81–89 (codified as amended at 42 U.S.C. §§ 3601–3631 (2006)).

45. Nier, *supra* note 34, at 617.

46. For an in-depth analysis, see Kevin Fox Gotham, *Separate and Unequal: The Housing Act of 1968 and the Section 235 Program*, 15 SOC. F. 13, 13 (2000); see also Rheingold et al., *supra* note 15, at 645.



there were indeed gains made in homeownership rates among people of color. In 1950, the non-white homeownership rate was 34.9%; by 1960 it had grown to 38.4%; and by 2000 almost half (47.5%) of non-whites owned their homes.<sup>47</sup> These statistics should have been analyzed as compared to white ownership rates of 57%, 64.4% and 73% during the same period.<sup>48</sup>

In the wake of the Fair Housing Act, several government programs shifted away from homeownership and focused instead on ensuring affordability in the central city and toward affordability in the rental market. Notably, the Voucher Program under Section 8 introduced tenant portability to low-income rental housing subsidies.<sup>49</sup> The Low Income Housing Tax Credit, begun in 1987, incentivizes developers to build low-income housing by subsidizing the cost of capital.<sup>50</sup> Urban homeowners, though, no longer occupied center stage in the policy arena.

## II. MORE RECENT GOVERNMENT POLICIES AFFECTING URBAN HOMEOWNERSHIP

Despite the turn towards rental housing, seeds of homeowner policy remained. Recognizing the disparity between suburban and urban homeownership rates (and acknowledging that federal policies had a large hand in creating these disparities), the federal government did embark on several programs aimed at increasing urban homeownership—specifically ownership among the low-to-moderate-income (LMI) groups—whose effect is still felt today.<sup>51</sup> These housing programs carried the same tune of previous federal policies, emphasizing homeownership as an asset-building, socially beneficial, and economically positive goal (bordering

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47. 1 1950 CENSUS OF HOUSING, *supra* note 4, pt. 1, 2 tbl. 3; 1960 CENSUS OF HOUSING, *supra* note 4, pt. 1, at xxvii tbl.; BUREAU OF THE CENSUS, HISTORICAL CENSUS OF HOUSING TABLES HOMEOWNERSHIP BY RACE AND HISPANIC ORIGIN: 2000, <http://www.census.gov/hhes/www/housing/census/historic/ownershipbyrace.html> (last visited June 21, 2010). See also Robert A. Margo, HISTORICAL PERSPECTIVES ON RACIAL ECONOMIC DIFFERENCES: A SUMMARY OF RECENT RESEARCH, NBER Reporter, Winter 2005, available at <http://www.nber.org/reporter/winter05/margo.html>.

48. See MASNICK, *supra* note 41, at 21; see also Powell, *supra* note 43, at 608 (reflecting on the positive gains of the civil rights movement in minority homeownership).

49. See U.S. Dep't Hous. & Urban Dev., Section 8 Assistance for Public Housing Relocation/Replacement, <http://portal.hud.gov/portal/page/portal/HUD/programdescription/phrr> (last visited June 21, 2010).

50. I.R.C. § 42 (2006). See also U.S. Dep't Hous. & Urban Dev., Low-Income Housing Tax Credits, <http://www.huduser.org/portal/datasets/lihtc.html> (last visited June 21, 2010).

51. Since previous federal policies had either the explicit or implicit goal of moving the white middle class to the suburbs, the literature and policy analysis of urban homeowners is inextricably intertwined with both class (lower income) and race (minority). To tease out the differences here would not serve the underlying goal of this article, as the effect of the difference would be minimal.

on virtue).<sup>52</sup> In particular, two recent developments are generally acknowledged as the major policy initiatives increasing urban homeownership—the CRA, and the changes at Fannie Mae and Freddie Mac.

### A. *Community Reinvestment Act*

Congress enacted the CRA in 1977 as an attempt to increase access to credit for lower- and moderate-income borrowers, who were limited by policies, such as redlining, that systematically excluded certain neighborhoods (based on, among other indicia, racial composition) from access to mortgage capital.<sup>53</sup> It emerged during a time when bank competition was legally limited, and lenders had little incentive to develop business in low-income neighborhoods.<sup>54</sup> This underinvestment in certain communities was held out as the cause of the continued depressed circumstances in these neighborhoods.<sup>55</sup> The premise underlying the passage of the CRA was that since banks receive certain benefits, such as low-interest rates, federal charters, and federal deposits from the government, banks should reinvest money into lower income communities, especially communities where they operate.<sup>56</sup> The mission of the CRA is “intended to encourage depository institutions to help meet the credit needs of the communities in which they operate, including low- and moderate-income neighborhoods, consistent with safe and sound banking operations.”<sup>57</sup>

The CRA, however, does not force banks to loan money to lower- and moderate-income communities or set specific quotas for lending, as Congress did not want to dictate an individual bank’s lending practices.<sup>58</sup> Instead, banks are periodically evaluated for their ability to meet the credit needs of the communities in which they operate through an examination by the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation, the Office of the Comptrol-

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52. See Byrne & Diamond, *supra* note 9, at 543.

53. Nier, *supra* note 34, at 633; Rheingold et al., *supra* note 15, at 648; see also Ben S. Bernanke, Chairman, Fed. Reserve, The Community Reinvestment Act: Its Evolution and New Challenges, Address at The Community Affairs Research Conference (March 30, 2007), available at <http://www.federalreserve.gov/newsevents/speech/bernanke20070330a.htm>.

54. Howard Husock, Op-Ed., *Housing Goals We Can't Afford*, N.Y. TIMES, Dec. 10, 2008, at A49.

55. Kathleen C. Engel & Patricia A. McCoy, *The CRA Implications of Predatory Lending*, 29 FORDHAM URB. L.J. 1571, 1571 (2002).

56. Raymond H. Brescia, *Part of the Disease or Part of the Cure: The Financial Crisis and the Community Reinvestment Act*, 60 S.C. L. REV. 618, 631 (2009).

57. Federal Financial Institutions Examination Council, Community Reinvestment Act, Background & Purpose, <http://www.ffiec.gov/CRA/history.htm>.

58. Brescia, *supra* note 56, at 631.

ler of the Currency, or the Office of Thrift Supervision.<sup>59</sup> The governmental institutions that oversee banks give them one of four ratings—outstanding, satisfactory, needs to improve, or substantial non-compliance.<sup>60</sup> In 1995, the Clinton Administration made lending in LMI neighborhoods a requisite for an “outstanding” rating.<sup>61</sup> However, a fundamental issue that would later play a key role in the recent financial crisis was that banks were not judged on how their loans performed but rather on the volume of loans originated.<sup>62</sup>

Banks are expected to originate loans in areas where they take deposits. This is determined by where the bank has its main office, a branch, or deposit-taking ATMs.<sup>63</sup> Non-deposit mortgage lenders are not subject to the CRA, and commercial banks have the choice whether or not to count affiliates in their CRA examinations.<sup>64</sup> One of the reasons that there may be doubt about whether the CRA leads to more mortgages for LMI families in urban areas is that so few of the mortgages issued to these families have been originated by institutions covered by the CRA. In fact, only 6% of higher-priced mortgage loans in 2005 and 2006 were covered by the CRA.<sup>65</sup>

One concern with the CRA is that the statute is loosely written; accordingly, it is difficult for the regulatory agencies to interpret what constitutes compliance.<sup>66</sup> Another issue is that it is very difficult for courts to overrule regulatory decisions related to the CRA.<sup>67</sup> Additionally, the CRA has rarely been enforced—less than .06% of bank applications from 1988 through May 2007 were denied for failing to meet CRA criteria.<sup>68</sup> In light of these deficiencies, efforts were made during the

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59. Federal Financial Institutions Examination Council, Community Reinvestment Act, <http://www.ffiec.gov/CRA/history.htm>.

60. 25 C.F.R. § 25.21 (2010).

61. See *Hearing on Perspectives and Proposals on the Community Reinvestment Act Before the H. Subcomm. on Financial Institutions and Consumer Credit*, 111th Cong. (2010) (written statement of Eugene A. Ludwig, Chief Executive Officer, Promontory Financial Group). See also Bd. of Governors of Fed. Reserve Sys., *The Performance and Profitability of CRA-Related Lending* (July 17, 2000), available at <http://www.federalreserve.gov/boarddocs/surveys/craloansurvey/cratext.pdf>. For current CRA regulations see 12 C.F.R. § 228.21–29 (2010).

62. Husock, *supra* note 54.

63. Brescia, *supra* note 56, at 633.

64. *Id.* at 632.

65. Brescia, *supra* note 56, at 643–44.

66. Glenn B. Canner et al., *Does the Community Reinvestment Act (CRA) Cause Banks to Provide a Subsidy to Some Mortgage Borrowers?*, 2002 BD. OF GOVERNORS OF THE FED. RES. FIN. & ECON. DISCUSSION SERIES 1, 7–8.

67. Brescia, *supra* note 56, at 654.

68. *Id.* at 653.

1990s to increase enforcement of CRA requirements.<sup>69</sup> However, these efforts were insufficient. Accordingly, because of these and other issues, in 1995, U.S. President Bill Clinton pushed for changes in the CRA that made the criteria easier to understand, made the forms easier for banks to file, and placed an increased focus on the actual lending.<sup>70</sup>

The efficacy of CRA requirements is decidedly mixed when analyzing the goal of increased access to mortgage financing for LMI families. On the one hand, as Ben Bernanke has stated, “[r]esearch on the CRA has tended to find positive net effects, but the results are not uniform.”<sup>71</sup> Literature reviews, along with studies based on CRA discussion groups, have reached similar findings.<sup>72</sup> Moreover, there are several studies whose findings imply no effect of the CRA on lending to LMI communities. Christopher Berry and Sarah Lee found no CRA effect on lending when comparing “matched pairs” of houses where one is just above the CRA threshold and one is just below.<sup>73</sup> Jeffery Gunther found that, between 1993 and 1997, CRA-covered lenders increased their mortgage originations to non-LMI borrowers more than to LMI borrowers while non-CRA-covered lenders exhibited the opposite results.<sup>74</sup> As Bernanke has also noted, “some critical studies have argued that the CRA has been ineffective in addressing discrimination and market failures and that its social costs outweigh its benefits.”<sup>75</sup>

Few studies on the CRA were available before 1993 due to a lack of publicly available information on independent mortgage companies.<sup>76</sup> In fact, one reason there may have been an increase in lending under the CRA was the release of public CRA data in 1990, which not only placed

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69. Rheingold et al., *supra* note 15, at 649. Along with the increased enforcement, there were also several new initiatives to promote LMI homeownership, most notably Homeownership and Opportunity for People Everywhere (HOPE). *Id.*

70. Liz Laderman, *Has the CRA Increased Lending for Low-Income Home Purchases?*, 2004-16 FED. RES. BANK OF SAN FRANCISCO ECON. LETTER 1, 2-3 (2004), available at <http://www.frbsf.org/publications/economics/letter/2004/el2004-16.html>. The Clinton Administration also initiated a National Home Ownership Strategy focusing on increasing access to credit. See Rheingold et al., *supra* note 15, at 649.

71. Bernanke, *supra* note 53.

72. See Eric S. Belsky et al., *Insights into the Practice of Community Reinvestment Act Lending: A Synthesis of CRA Discussion Groups* 4 (Joint Ctr. for Hous. Studies, Working Paper No. CRA00-1, 2000); Brescia, *supra* note 56, at 638.

73. Neil Bhutta, *Giving Credit where Credit is Due? The Community Reinvestment Act and Mortgage Lending in Lower-Income Neighborhoods* 5 (Fed. Reserve Bd. Fin. and Econ. Discussion Series, Working Paper No. 2008-61, 2008) (citing Christopher R. Berry & Sarah L. Lee, *The Community Reinvestment Act: A Regression Discontinuity Analysis* (Univ. of Chicago, Harris Sch., Working Paper No. 07.04, 2007)).

74. Laderman, *supra* note 70, at 2 (citing Jeffery W. Gunther, *Should CRA Stand for 'Community Redundancy Act'?*, 23 REGULATION 56, 58 (2000)).

75. Bernanke, *supra* note 53. See also Michael S. Barr, *Banking the Poor*, 21 YALE J. ON REG. 121, 233 (2004); Keith N. Hylton, *Development Lending and the Community Reinvestment Act*, 29 W. NEW ENG. L. REV. 59, 62-64 (2006).

76. Laderman, *supra* note 70, at 1.

pressure on banks to lend to LMI borrowers to avoid potentially negative publicity, but also served to strengthen community organizations' push for increased lending.<sup>77</sup> CRA discussion-based groups reveal that regulatory factors leading to increased CRA lending included the Federal Reserve's Board of Governors' 1989 denial of a merger request by Continental Illinois National Bank and Trust Company of Chicago "on the ground that the bank had not met its obligations under the CRA"; increased Congressional pressure to enforce the CRA in the early 1990s; and the changes to the CRA instituted under President Clinton in 1995.<sup>78</sup>

More recent studies, however, do find a significant effect of the CRA on LMI mortgage lending.<sup>79</sup> Along with this finding, researchers note that lenders subject to the CRA originate a higher portion of loans to LMI borrowers and neighborhoods where there is active community organization focused on promoting the expansion of credit than to areas lacking community involvement.<sup>80</sup> This could explain some increases in LMI lending, as CRA agreements increased significantly after President Clinton's reform—from \$150 billion in 1995 to \$397 billion in 1997.<sup>81</sup> Also, researchers find that CRA lenders make a higher portion of loans in metropolitan statistical areas (MSAs) where a higher percentage of the areas within those MSAs are CRA assessment areas.<sup>82</sup> Ellen Seidman, director of the federal Office of Thrift Supervision, said in a speech before the Greenlining Institute in 2001, "Our record home ownership rate [increasing from 64.2% in 1994 to 68% in 2001], I'm convinced,

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77. Eric S. Belsky et al., *The Effect of the Community Reinvestment Act on Bank and Thrift Home Purchase Mortgage Lending* 10 (Joint Ctr. for Hous. Studies, Working Paper No. CRA01-1, 2001) [hereinafter Belsky et al., *Effect of the CRA*].

78. *Id.* at 11, 13, 14. The CRA regulations adopted in 1995 established for large institutions a three-pronged test based on performance in the areas of lending, investments, and services. See Bernanke, *supra* note 5. While the regulations placed the greatest emphasis on lending, they encouraged innovative approaches to addressing community development credit needs. *Id.* Several provisions were included to reduce compliance costs, among them a new rule that allowed small banks to meet their requirements by means of a streamlined examination focused on lending activities. *Id.*; see also Press Briefing by Lloyd Bentsen, Secretary of the Treasury, Robert Rubin, Assistant to the President for Economic Policy, & Eugene Ludwig, Comptroller of the Currency (Dec. 8, 1993), available at <http://clinton6.nara.gov/1993/12/1993-12-08-briefing-by-bentsen-and-rubin.text.html>.

79. Belsky et al., *Effect of the CRA*, *supra* note 77, at 1; Stuart A. Gabriel & Stuart S. Rosenthal, *Government-Sponsored Enterprises, the Community Reinvestment Act, and Home Ownership in Targeted Underserved Neighborhoods*, HOUSING MARKETS AND THE ECONOMY: RISK, REGULATION, AND POLICY 202, 210 (Edward L. Glaeser & John M. Quigley eds., 2009) (citing Raphael Bostick & Breck L. Robinson, *Do CRA Agreements Increase Lending?*, 31 REAL EST. ECON. 23 (2003)).

80. Belsky et al., *Effect of the CRA*, *supra* note 77, at 2.

81. *Banks Pledge More Loans in Minority Communities*, WALL ST. J., March 20, 1998.

82. Belsky et al., *Effect of the CRA*, *supra* note 77, at 1–2.

would not have been reached without CRA and its close relative, the Fannie/Freddie requirements.”<sup>83</sup>

Possible explanations for the increase in CRA activity are the emergence of larger, more experienced firms who were able to more efficiently handle CRA loans, and a booming economy that made the risk of lower- and moderate- income applicants appear lower to banks.<sup>84</sup> Another reason cited as leading to increased LMI mortgages is a wave of consolidation in the financial industry, which increased banks’ incentives to avoid potential merger application denials.<sup>85</sup> However, banks walked a fine line when the loans purporting to comply with CRA requirements could also be viewed as predatory or abusive. An illustrative case is the Citigroup/EAB merger. Although the merger was approved, the Fed stated that “[b]orrowers do not benefit from expanded access to credit if the credit involves abusive lending practices.”<sup>86</sup>

One concern with these studies is that they do not address whether CRA mortgage originations crowd out mortgage originations from non-CRA lenders.<sup>87</sup> The evidence is mixed on this “crowding out” argument. Although one could argue that CRA mortgage lending crowds out mortgage origination to LMI borrowers by firms that are not subject to the CRA, one researcher finds no crowd-out effect in the data and instead finds a slight “crowd-in effect” in areas with previously low home sale rates.<sup>88</sup>

However, despite these findings, one continuing theme with the CRA is the interaction between an increasing portion of LMI mortgage loans made to borrowers not covered by the CRA, and the galloping growth of the subprime market. As discussed below, the biggest market in these neighborhoods is subprime lending.<sup>89</sup> Interestingly, most CRA banks are not subprime lenders, since an overwhelming majority of subprime lenders are non-bank lenders or mortgage companies.<sup>90</sup> In fact, CRA does not typically scrutinize the subprime lending activities of non-bank finance companies, and independent mortgage companies are

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83. Edward Pinto, Op-Ed., *Acorn and the Housing Bubble: The Liberal Pressure Group Helped Congress Write the Affordable Housing Rules That Got Us into Trouble*, WALL ST. J., Nov. 12, 2009, at A23. Mr. Pinto was the chief credit officer at Fannie Mae from 1987 to 1989.

84. Belsky et al., *Effect of the CRA*, *supra* note 77, at 14–16.

85. It should be noted though, that the CRA led to larger increases in LMI lending in areas with banks that were seeking to merge and in more competitive markets where positive publicity was granted additional importance. *Id.* at 12, 25.

86. Board of Governors, Order Issued Under Bank Holding Company Act , Citigroup Inc., New York, N.Y., 87 Fed. Res. Bull. 600 (Sept. 2001).

87. Belsky et al., *Effect of the CRA*, *supra* note 77, at 3.

88. Bhutta, *supra* note 73, at 22.

89. See *infra* note 120 and accompanying text.

90. Engel & McCoy, *supra* note 55, at 1585.

exempt from CRA.<sup>91</sup> A review of the research has shown that the “explosion of new forms of lending, the growing importance of mortgage brokers and mortgage banking operations, and the expansion of secondary mortgage markets” have reduced the CRA’s impact.<sup>92</sup> The New York Federal Reserve Bank estimates the CRA effect to have decreased from 3.7% in 1993 to 1.6% in 2000.<sup>93</sup> This is not to say that CRA banks are free from subprime lending, for some estimate that 50% of the high-risk loans bought by Fannie and Freddie were CRA loans.<sup>94</sup> Furthermore, CRA fails to penalize lenders that engage in predatory lending (either directly or through subsidiaries). Some argue that CRA lenders that do engage in subprime or predatory lending are not meeting the needs of the community and, at the very least, should not get credit for these types of loans.<sup>95</sup> This landscape may shift further as some community groups are pressuring Congress to expand CRA to cover all mortgage lenders, credit unions, insurance companies, and others in the financial industry.<sup>96</sup>

It is difficult to arrive at any definitive conclusion regarding whether changes in government policy in CRA have led to increases in mortgage originations to urban LMI borrowers. However, the research does seem to point to the CRA having a slight positive effect on mortgage originations, though this effect has been confounded in the recent spate of lending by mortgagees not subject to CRA. Because the CRA only covers a small percentage of mortgages now originated to LMI borrowers, it would be interesting to see if the CRA would still have an effect if all mortgage originators were subject to the CRA. It would also be interesting to see if one could show whether President Clinton’s changes in 1995 directly led to increased mortgage lending for LMI borrowers or whether increases were due to subprime lending which escaped the purview of the CRA. It is possible that larger metropolitan areas have received most of the benefits of the CRA for varied reasons that could include more regulatory oversight, more established community groups ready to protest transactions and push for CRA agreements, and/or increased value of goodwill in a competitive market. Although much of the data has been done on a national scale, more research needs to be done on the effects of the CRA within individual metropolitan areas.

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91. *Id.* at 1588.

92. JOINT CTR. FOR HOUS. STUDIES, HARVARD UNIV., *THE 25TH ANNIVERSARY OF THE COMMUNITY REINVESTMENT ACT: ACCESS TO CAPITAL IN AN EVOLVING FINANCIAL SERVICES SYSTEM* 8 (2002).

93. William C. Apgar & Mark Duda, *The Twenty-Fifth Anniversary of the Community Reinvestment Act: Past Accomplishments and Future Regulatory Challenges*, FED. RESERVE BANK OF N.Y. ECON. POL. REV., 169, 177 (June 2003).

94. Pinto, *supra* note 83.

95. Engel & McCoy, *supra* note 55, at 1571, 1585, 1592.

96. Pinto, *supra* note 83.

### B. *Fannie Mae and Freddie Mac*

Congress established the housing government-sponsored entities (GSEs), Fannie Mae and Freddie Mac, to increase the flow of funds to mortgage borrowers.<sup>97</sup> Fannie Mae states that its mission is “to provide liquidity, stability and affordability to the U.S. housing and mortgage markets.”<sup>98</sup> The mission of Freddie Mac (created to spur market competition with Fannie Mae) is analogous.<sup>99</sup> In 1992, the Federal Housing Enterprises Financial Safety and Soundness Act<sup>100</sup> (also known as the GSE Act) was signed, increasing the requirements for Fannie’s and Freddie’s purchases of low-income mortgages, and allowing the U.S. Department of Housing and Urban Development (HUD) to establish “affordable housing goals” for the GSEs.<sup>101</sup>

This set the stage for Fannie and Freddie to acquire more than \$6 trillion of single-family housing loans over the next sixteen years.<sup>102</sup> Consistent with increases in goals for lower-income housing, the GSEs, especially after the 1992 regulations, increased their purchases of LMI mortgages. From 1992 to 1995, Fannie Mae increased its share of lower-income mortgages by 100%, while Freddie Mac increased its share by 50%.<sup>103</sup> In a foreboding cloud, there is evidence to support the charge that Fannie and Freddie were buying risky loans in 1993, and routinely misrepresenting the loan quality as “prime,” when in fact the loans were subprime (or Alt-A).<sup>104</sup>

In 1999, Fannie was pushed to start a pilot program to increase access to credit for LMI homebuyers.<sup>105</sup> Fannie prided itself on a sophisticated computer program that would give credit comfort by accurately assessing credit risk. Armed with this technological capability, Fannie announced in 2000 that it would buy \$2 trillion worth of loans from

97. Federal Subsidies for the Housing GSEs: Hearing before the Subcommittee on Capital Markets, Insurance, and Government Sponsored Enterprises, U.S. House of Representatives, 107th Cong. 1 (May 23, 2001) (statement of Dan L. Crippen, Director, Congressional Budget Office), *available at* <http://www.cbo.gov/doc.cfm?index=2839&type=0>.

98. Fannie Mae, About Us, <http://www.fanniemae.com/kb/index?page=home&c=aboutus> (last visited May 23, 2010).

99. Freddie Mac, Our Mission, [http://www.freddie.mac.com/corporate/company\\_profile/our\\_mission](http://www.freddie.mac.com/corporate/company_profile/our_mission) (last visited May 23, 2010).

100. Pub. L. No. 102-550, tit. XIII (Government Sponsored Entities), §§ 1301–95, 106 Stat. 3672, 3941–4012 (codified as amended at 12 U.S.C. §§ 4501 et seq. (2006)).

101. Gabriel & Rosenthal, *supra* note 79, at 207.

102. Pinto, *supra* note 83.

103. Gabriel & Rosenthal, *supra* note 79, at 211.

104. Peter J. Wallison, Op-Ed., *The Price for Fannie and Freddie Keeps Going Up*, WALL ST. J., Dec. 30, 2009, at A17.

105. Steven A. Holmes, *Fannie Mae Eases Credit to Aid Mortgage Lending*, N.Y. TIMES, Sept. 30, 1999, at A28.



low-income, minority, and risky borrowers by 2010.<sup>106</sup> This shift in GSE policy toward LMI loans was further encouraged under President George W. Bush. In 2002, the Bush administration challenged the GSEs to increase their minority commitment goals by more than \$440 billion.<sup>107</sup> The administration also encouraged the financial sector to create innovative products to promote homeownership and supported efforts for a zero-down payment FHA loan program.<sup>108</sup>

These increases in loan purchases did not necessarily translate into increases in home mortgages to LMI families. In a 2000 study, Stuart Gabriel and Stuart Rosenthal ran a model that isolated the effects of the CRA and GSEs on LMI homeownership. Their model found “a small positive CRA effect” on local homeownership rates.<sup>109</sup> However, their model found “essentially no evidence” of an effect of GSEs’ home loan purchasing on homeownership in LMI communities.<sup>110</sup>

Other studies of loans during the late 1990s have also had difficulties finding evidence of GSEs’ effects on LMI home mortgage originations. In a study analyzing the mortgage markets in the largest 308 MSAs between 1995 and 1999, Brent Ambrose and Thomas Thibodeau were only able to find that GSEs led to expansions in the credit market for LMI borrowers in 1998.<sup>111</sup> Another study by Raphael Bostic and Stuart Gabriel specifically looked at housing outcomes in California and found “little efficacy of the GSE home loan purchase goals in elevating the homeownership and housing conditions of targeted and underserved neighborhoods.”<sup>112</sup> A study that evaluated the effects of GSEs in Cleveland also found no evidence of their efficacy.<sup>113</sup>

However, this picture changed after 2004 when Fannie and Freddie (after a big push by neighborhood groups and HUD) added a great deal of flexibility to their underwriting guidelines and expanded the scope of

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106. Charles Duhigg, *Pressured to Take More Risk, Fannie Reached Tipping Point*, N.Y. TIMES, Oct. 5, 2008, at A1 [hereinafter Duhigg, *Pressured*].

107. *Bush Aims to Boost Minority Home Ownership*, CNN.COM, June 17, 2002, available at <http://archives.cnn.com/2002/ALLPOLITICS/06/17/bush.minority.homes/index.html>.

108. Dickerson, *supra* note 2, at 193.

109. Gabriel & Rosenthal, *supra* note 79, at 205.

110. *Id.*

111. Brent W. Ambrose & Thomas G. Thibodeau, *Have the GSE Affordable Housing Goals Increased the Supply of Mortgage Credit?*, 34 REGIONAL SCI. & URB. ECON. 263, 271 (2004).

112. Raphael W. Bostic & Stuart A. Gabriel, *Do the GSEs Matter to Low-Income Housing Markets? An Assessment of the Effects of the GSE Loan Purchase Goals on California Housing Outcomes*, 59 J. URB. ECON. 458, 458 (2006).

113. Xudong An & Raphael W. Bostic, *GSE Activity, FHA Feedback, and Implications for the Efficacy of the Affordable Housing Goals*, 36 J. REAL EST. FIN. & ECON. 207, 209–10 (2008) (citing Lance Freeman, George Galster & Ron Malega, *The Impact of Secondary Mortgage Market and GSE Purchases on Underserved Neighborhood Markets: A Cleveland Case Study*, 42 URB. AFF. REV. 193 (2006)).

loans eligible for securitization. Under the “American Dream Commitment,” Fannie pledged to finance six million new homeowners, including 1.8 million new minority homeowners by 2014.<sup>114</sup> To achieve that goal, Fannie announced that it would increase the average annual number of minority first-time homebuyers it financed by 93,000 households (more than double the previous four years’ averages).<sup>115</sup> President Bush boosted the affordable housing goal from 50% to 56%, and challenged Fannie and Freddie, saying they “must do more.”<sup>116</sup> To address directly the dearth of lending to those on the bottom of the economic spectrum, HUD imposed further requirements on Fannie and Freddie in 2005. It mandated that 32% of their loan portfolios must be to borrowers in central cities (or other underserved areas), and that 22% of the loans must be to very-low-income families or to borrowers living in very low-income neighborhoods.<sup>117</sup> By 2008, 47% of the GSEs’ purchases of mortgages were LMI loans, compared to 45% in 2005.<sup>118</sup>

Alongside these changes, however, the seeds for disaster were sown. The disconnect between policy imperatives to increase homeownership and the economic reality of the borrowers in the pool exploded the subprime market. The first pull into the waters of less-than-prime lending occurred in 1995, when HUD agreed to allow Fannie and Freddie to get affordable housing credit for buying subprime securities.<sup>119</sup> The expansion in lending went hand-in-hand with the increase in exposure to risk. By 2004, Fannie and Freddie’s purchases of subprime loans had risen tenfold.<sup>120</sup> Between 2005 and 2008, Fannie purchased or guaranteed more than \$270 billion in risky loans—more than three times as much as in all earlier years *combined*.<sup>121</sup> This increase in subprime loans was by design—not by happenstance. Internal Fannie documents from 2006 state the objective of increasing “our penetration into the subprime market.”<sup>122</sup> Some former Fannie employees express regret in moving so

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114. Robert J. Levin, *Forward* to Demetrios Papademetriou & Brian Ray, *From Homeland to a Home: Immigrants and Homeownership in Urban America*, 2004 FANNIE MAE PAPERS 1, available at <http://www.ilw.com/articles/2004,0804-Papademetriou.pdf>.

115. *Id.*

116. Carol D. Leonnig, *How HUD Mortgage Policy Fed The Crisis: Subprime Loans Labeled ‘Affordable’*, WASH. POST, June 10, 2008, at A1. Likewise, Capitol Hill (especially Democratic lawmakers) prompted Fannie to increase its lending to LMI borrowers. See Charles Duhigg, *The Reckoning Pressured to Take More Risk, Fannie Reached Tipping Point*, N.Y. TIMES, Oct. 5, 2008, at A1.

117. Husock, *supra* note 54.

118. U.S. DEP’T HOUS. & URBAN DEV., OVERVIEW OF THE GSEs’ HOUSING GOAL PERFORMANCE, 2000–2007 6 (2009).

119. Leonnig, *supra* note 116.

120. *Id.*

121. Duhigg, *Pressured*, *supra* note 106.

122. David S. Hilzenrath, *Fannie’s Perilous Pursuit of Subprime Loans: In an Attempt to Increase Its Business, Company Gave the Risks Short Shrift*, WASH. POST, Aug. 19, 2008, at D1.

deeply into the subprime market,<sup>123</sup> and ask whether by enticing borrowers into dangerous subprime loans Fannie was “setting them up for failure.”<sup>124</sup> Others stand by the decision, disputing allegations of abusive lending and sloppy underwriting by claiming that they could not have predicted that subprime lending would dominate the market so quickly.<sup>125</sup>

Fannie and Freddie lost their quasi-independent status in 2008, when the federal government took over both agencies. Most studies on the GSEs are based on data before the 1999 relaxation of credit standards and the 2004 expansion in LMI lending goals. It may be worthwhile to recreate studies based on data after both of these events. One might doubt that the legacy of the softening of credit is increased homeownership. In fact, recent data confirmed that a significant proportion of the subprime loans were not used to push people from the rental market into homeownership. These loans were used by existing homeowners to re-finance their homes or as a home equity loan. Nationwide, between 1998 and 2006, only 1.4 million of 15.1 million subprime loans were made to first-time homebuyers.<sup>126</sup> Furthermore, as to city homeowners, any gains that were achieved through this effort (and, perhaps even more troubling, the significant gains made before 2000) were washed away completely in a foreclosure tsunami.<sup>127</sup>

### III. SUBPRIME MORTGAGE PENETRATION IN CITY HOMEOWNERSHIP

As alluded to above, the mortgage loans made in many city neighborhoods escaped CRA compliance, as they were not made by banks subject to the CRA.<sup>128</sup> Financial service firms and mortgage companies dominated the market.<sup>129</sup> When programs such as the CRA were created, it might have been inconceivable that these same neighborhoods could, in fact, have too much credit.<sup>130</sup> However, while facially serving the needs of the community with access to capital, this access came at the very high price of so-called “subprime” lending. No discussion of city homeownership can be complete without integrating the effect of the penetration of subprime mortgages. Numerous studies have confirmed that for decades, minority neighborhoods experienced a significant con-

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123. William C. Apgar Jr., who was an assistant HUD secretary under Clinton, said he regrets allowing the companies to count subprime securities as affordable. See Leonnig, *supra* note 116.

124. Hilzenrath, *supra* note 122 (quoting Fannie Mae Executive Vice President Thomas A. Lund).

125. Leonnig, *supra* note 116 (quoting HUD Spokesman Brian Sullivan).

126. Dickerson, *supra* note 2, at 209.

127. See *infra* notes 147–53 and accompanying text.

128. See *supra* Part II.A.

129. Dickerson, *supra* note 2, at 203–06.

130. Engel & McCoy, *supra* note 55, at 1571.

centration of subprime loans.<sup>131</sup> In fact, HUD recognized the problem more than ten years ago. In 1998, it determined that subprime loans were over five times more likely to occur in a Black neighborhood than in a White neighborhood.<sup>132</sup>

Of course, a borrower may be unable to obtain a loan on traditional terms (e.g., thirty-year, fixed-market-rate) due to many factors, not the least of which is creditworthiness of the borrower. One possible explanation for such concentration is the possibility of greater incidences of low credit scores within particular subpopulations. However, even taking into consideration the possibility that minority borrowers might have a lower average credit score still does not fully account for the disproportionate percentage of subprime loans in minority neighborhoods. Studies have shown that even after taking into consideration the creditworthiness of the borrower, the percentage of minority homeowners in the neighborhood (in that particular study, specifically African American neighborhoods) is positively correlated with the subprime share of loans.<sup>133</sup>

In another study, different authors came to the same conclusion: racial disparities affect whether a borrower obtains a subprime loan.<sup>134</sup> Their study led the researchers to conclude that "[r]egardless of whether we call it efficient risk-based pricing or invitation to predatory abuse, subprime mortgage lending is tightly bound up with the enduring racial-geographic inequalities of American housing."<sup>135</sup> What differentiates the previous era of subprime lending from the present environment is not so much the economic disparity in the loan terms but rather the higher incidence of foreclosure.<sup>136</sup> In other words, while past lending patterns may have resulted in minority homeowners paying higher costs for home financing, subprime loans of a more recent vintage have wreaked their havoc when homeowners have been unable to pay, resulting in loss of the home by the borrower and loss to the neighborhood with a now-abandoned home.

The effect of the recent meltdown in the subprime market was acutely felt in minority neighborhoods. In 2004, 2005, and 2006 (the height of the subprime lending era) white borrowers certainly participated fully in the market. They accounted for slightly more than half of

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131. For a complete discussion, see Paul S. Calem et. al., *The Neighborhood Distribution of Subprime Mortgage Lending*, 29 J. REAL EST. FIN. & ECON. 393, 394 (2004).

132. HUD documented that in 1998, subprime lending accounted for 51% of loans in Black neighborhoods. and only 9% of loans in predominately White neighborhoods. U.S. DEP'T OF HOUS. & URBAN DEV., *UNEQUAL BURDEN: INCOME & RACIAL DISPARITIES IN SUBPRIME LENDING IN AMERICA 2* (2000).

133. Calem et. al. *supra* note 131, at 401.

134. ELVIN K. WYLY ET. AL., *UNIV. OF BRITISH COLUMBIA, SUBPRIME MORTGAGE SEGMENTATION IN THE AMERICAN URBAN SYSTEM*, 21-22 (2007).

135. *Id.* at 26.

136. Kristopher Gerardi & Paul Willen, *Subprime Mortgages, Foreclosures, and Urban Neighborhoods*, 9 B.E.J. ECON. ANALYSIS & POL'Y Article 12, 10 (2009).

the subprime loans originated in 2004-2006.<sup>137</sup> However, a clearer picture of the impact of subprime lending emerges when a different question is posed: what percentage of borrowers (according to racial demographics) were subprime borrowers?

TABLE 1: PERCENTAGE OF SUBPRIME BORROWERS  
BY SELECTED RACIAL DEMOGRAPHICS<sup>138</sup>

|                 | 2004 | 2005 | 2006 |
|-----------------|------|------|------|
| <b>Black</b>    | 31%  | 51%  | 53%  |
| <b>Hispanic</b> | 18%  | 38%  | 41%  |
| <b>White</b>    | 8%   | 19%  | 22%  |

If we focus the analysis on *urban* homeownership, the analysis becomes even starker. There is a far wider geographic dispersion of white borrowers across city, suburban and even rural areas. In contrast, Black and Latino borrowers concentrate in the urban core.<sup>139</sup> Racially segregated and concentrated living patterns exacerbate the effect of the subprime crisis in minority neighborhoods. There is a steady increase in the percentage of subprime loans as the neighborhood composition becomes more concentrated by minorities. Building on trends identified in several studies from the early 1990s through 2004, minority neighborhoods experienced a strong geographic concentration of subprime mortgages.<sup>140</sup> Moreover, several studies have shown that even when controlling for the income and credit scores of these neighborhoods, subprime mortgages are concentrated in locations with high proportions of Black and Hispanic residents.<sup>141</sup> In 2006, if a neighborhood was less than 10% minority, 22% of the residential loans were classified as subprime. By contrast, if the neighborhood was 90–100% minority, 48% of borrowers were subprime borrowers.<sup>142</sup> The ironic twist to this scenario is that, according to some estimates, 30% of subprime borrowers could have qualified

137. Maurice Jourdain-Earl, *The Demographic Impact of the Subprime Mortgage Meltdown 13*(2008), available at <http://www.mortgagebankers.org/files/Conferences/2008/RegulatoryComplianceConference08/RC08SEPT25DEMOMauriceJourdain.pdf>.

138. *Id.* at 8.

139. *Id.* at 26.

140. Calem et al., *supra* note 131, at 401.

141. Chris Mayer & Karen Pence, *Subprime Mortgages: What, Where, and to Whom?* 3, 14, 29 (Fed. Reserve Bd. Fin. and Econ. Discussion Series, Working Paper No. 2008-29, 2008). “Even controlling for credit scores and other Zip code characteristics, race and ethnicity appear to be strongly and statistically significantly related to the proportion of subprime loans.” *Id.* at 14. For a discussion of earlier subprime lending, where the same pattern holds true, see also Calem et al., *supra* note 131, at 401.

142. Jourdain-Earl, *supra* note 137, at 11.

for safer, lower-cost prime loans but instead were steered to the subprime market.<sup>143</sup>

HOLC maps geographically represent race-based lending. For example, the HOLC map for Philadelphia paints minority neighborhoods red.<sup>144</sup> Remaining in Philadelphia, these same neighborhoods tend to exhibit a higher incidence of subprime mortgages.<sup>145</sup>

While it is true that subprime lending can help make homeownership a reality for many who would not otherwise qualify for mortgage financing, subprime lending can also lead to homeownership loss. Generally, subprime borrowers exceed the 30% maximum federal housing affordability guidelines for housing costs. In 2007, subprime borrowers spent approximately 37% of their after-tax income on mortgage payments, insurance and property taxes.<sup>146</sup> Devoting such a large portion of income to housing costs put borrowers, who were already stretching their resources thin to achieve homeowner status, into a precarious financial position. The more recent wave of subprime lending contained an even bigger threat to borrower stability: the emergence of teaser-rate adjustable mortgages. While the subprime loans of previous vintage may have carried high interest rates (and hence were still subject to charges that they were predatory), subprime loans of more recent origination were designed to require the borrower to refinance within twelve to twenty-four months, or the rate would reset to one that generally outstripped the payment ability of the borrowers. Hence, mortgage foreclosures spiked when the market softened and interest rates rose.

Losses to individual homeowners have been staggering. A paper by the Center for Responsible Lending notes homeownership gains to 50,925 for first-time African American homebuyers and 72,981 for first-time Latino homebuyers, but projects a homeownership loss of 98,025 for African Americans and 110,674 for Latinos based on a total of 1,075,770 subprime loans issued to minorities in 2005.<sup>147</sup> According to a study of neighborhoods in Boston in 2007, almost half of the changes in ownership in Black-owned housing were a result of foreclosure.<sup>148</sup> Although there is debate as to whether subprime lending actually increased the absolute number of minority homeowners, the impact of

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143. Leonnig, *supra* note 116.

144. HOLC map on file with author.

145. See Paul Milstein Ctr. For Real Estate, Columbia Business School, Subprime Google Earth Maps, <http://www4.gsb.columbia.edu/realestate/research/housingcrisis/subprimemaps> (last visited June 21, 2010).

146. Dickerson, *supra* note 2, at 207.

147. CTR. FOR RESPONSIBLE LENDING, CRL ISSUE PAPER NO. 14, SUBPRIME LENDING: A NET DRAIN ON HOMEOWNERSHIP 4 (2007), *available at* <http://www.responsiblelending.org/mortgage-lending/research-analysis/Net-Drain-in-Home-Ownership.pdf>.

148. Gerardi & Willen, *supra* note 136, at 18.

foreclosure is beyond debate. The loss of equity to subprime borrowers of color is estimated to be nearly a quarter of a trillion dollars.<sup>149</sup>

The effect on other minority neighborhoods has been equally devastating. In Chicago, "neighborhoods where the population is more than 80 percent non-white account for 65 percent of all [foreclosure] cases, up from 61 percent in 1993."<sup>150</sup> This trend is not unique to Illinois; it has appeared in many major metropolitan areas across the country. One study in Cleveland and surrounding Cuyahoga County found that census tracts with a high proportion of African American borrowers correlate to the highest incidence of foreclosure of subprime loans.<sup>151</sup> Similar tales can be told in cities such as Atlanta and Philadelphia.<sup>152</sup> Cities with large minority populations also suffered from the effects of high foreclosure rates experienced by minority communities. Losses to these cities include decreased tax bases, increased police and fire commitments, and other social pathologies (including community displacement) that follow clusters of properties left vacant and neglected as a result of foreclosure.<sup>153</sup>

In response to the wave of foreclosures, citizens and cities have brought suits against lenders.<sup>154</sup> The allegations go to the heart of the lending crisis. Individual homeowners have challenged subprime lenders, alleging that they were "sold an exotic high cost adjustable rate mortgage (ARM) . . . without consideration of [their] ability to pay the loan's hidden maximum interest rate, which far exceeded the initial teaser rate and made the loan unaffordable"; that lenders targeted "financially distressed consumers with the intent of artificially inflating their earnings and without regard to whether borrowers could repay the loans"; and that lenders "knowingly and affirmatively *misrepresented* the most important measurement of the affordability of a mortgage product: *the total amount of each monthly installment on the loan relative to the borrowers existing debt to income ratio*."<sup>155</sup> Another case charged that the borrowers were qualified for a loan with better terms but that the lender paid a

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149. Powell, *supra* note 43, at 624.

150. Vikas Bijaj & Ron Nixon, *For Minorities, Signs of Trouble in Foreclosures*, N.Y. TIMES, Feb. 22, 2006, at A1.

151. CLAUDIA COULTON ET AL., CASE WESTERN RESERVE UNIV., PATHWAYS TO FORECLOSURE: A LONGITUDINAL STUDY OF MORTGAGE LOANS, CLEVELAND AND CUYAHOGA COUNTY, 2005–2008, at 14 (2008).

152. Bijaj & Nixon, *supra* note 150.

153. See Richard E. Gottlieb & Andrew J. McGuinness, *Subprime Lending As a Public Nuisance: Casting Blame on Mortgage Lenders and Wall Street for Inner City Blight*, 62 CONSUMER FIN. L.Q. REP. 4, 6 (2008).

154. State attorneys general have also filed suit against unscrupulous lenders. See Justin Collins, *Without Other Options: The Limited Effectiveness, Unique Availability, and Overall Impact of State-Directed Lawsuits Against Predatory Lenders*, 17 J.L. & POL'Y 231, 233 (2008).

155. See *Biggins v. Wells Fargo & Co.*, No. 09-01272, 2009 WL 2246199, at \*30–31 (N.D. Cal. July 27, 2009) (citing Second Amended Complaint) (emphasis in original).

mortgage broker to arrange a loan with less favorable terms.<sup>156</sup> However, these individual lawsuits, and even class action suits, have failed to gain traction in the judicial system, where they have floundered on procedural grounds.<sup>157</sup>

Some cities have taken a proactive stance. Both Baltimore and Cleveland have filed suits challenging lending practices of major banks in predominately minority neighborhoods.<sup>158</sup> They allege damages to the cities stemming from vacancies, decreased property tax revenue, and increased fire and police costs, and public nuisance. Neither case has had its final disposition. However, the arguments raised by Baltimore and Cleveland against banks such as Wells Fargo and Deutsche Bank are interesting because the underlying premise is that lending was not an economic decision but rather a political/racial decision. As noted above, several studies have shown that subprime mortgages are concentrated in locations with high proportions of Black and Latino residents, even controlling for the income and credit scores of these neighborhoods. This lends considerable credibility to the position of the cities that lenders have, once more, engaged in discriminatory lending practices.

Although some commentators have highlighted the paradoxical<sup>159</sup> and tautological<sup>160</sup> aspects of the cities' cases,<sup>161</sup> these accusations only have merit if the underwriting of the loans was based solely on financial criteria. Study after study has shown that there is more than economics at play here. Yes, the cities are "walking a fine line,"<sup>162</sup> but individual owners bringing suit lack efficiency to tackle large-scale problems. Interven-

156. *Weller v. Accredited Home Lenders, Inc.* No. 08-2798, 2009 WL 928522, at \*3 (D. Minn. Mar. 31, 2009).

157. For example, the *Biggins* complaint suffered from a lack of specificity, and plaintiffs survived a motion to dismiss by the granting of leave to amend complaint. *Biggins*, 2009 WL 2246199, at \*65. The Plaintiffs in the *Weller* complaint likewise were granted leave to re-file their complaint with more information and specificity. *Weller*, 2009 WL 928522, at \*21–22.

158. *City of Cleveland v. Deutsche Bank Trust Co.*, 571 F. Supp. 2d 807, 810 (N.D. Ohio 2008); *Mayor and City Council of Baltimore v. Wells Fargo Bank*, No. JFM 1:08 CV-00062, 2010 WL 46401, \*1–2 (D. Md. Jan. 6, 2010). Also, the city of Philadelphia took an interesting (though likely illegal) approach: the sheriff of Philadelphia refused to conduct court-ordered foreclosure auctions on homeowners even though his office is charged with the sole responsibility of conducting these auctions. See Raymond H. Brescia, *On Public Plaintiffs and Private Harms: The Standing of Municipalities in Climate Change, Firearms, and Financial Crisis Litigation*, 24 Notre Dame J.L. Ethics & Pub. Pol'y 7, 21–28 (2010); Michael M. Phillips, *He's Taking Law Into His Own Hands To Help Broke Homeowners: Trouble Is, He is the Law; Philly's Sheriff Green Doesn't Do Foreclosures, to Lenders' Dismay*, WALL ST. J., June 6, 2008, at A1.

159. Subprime borrowers are thought to be a more risky investment, so there should be no surprise when the loans go into default.

160. Loan underwriting is irresponsible when a subprime borrower defaults because they cannot afford the loan.

161. *Gottlieb & McGuinness*, *supra* note 153, at 8–9.

162. *Id.* at 6.



tion by the cities allows the courts to address the wider societal ramifications of subprime mortgage penetration in urban minority neighborhoods. The foreclosures are a symptom; continued racial and ethnic profiling is the underlying problem.<sup>163</sup>

#### IV. RETHINKING THE PATH OF URBAN HOMEOWNERSHIP

This section begins with an assumption: as it pertains to metropolitan residential patterns, there is a conflation of race/ethnicity and socioeconomic status that permits the discussion to be as much about race/ethnicity as it is about class. There is ample evidence of some minority penetration into suburban neighborhoods.<sup>164</sup> There are some cities where the people of color do not constitute the majority of the urban poor.<sup>165</sup> However, by and large, when we discuss the topic of homeownership in American cities, we are talking about the plight of LMI people of color. This conflation is especially apt since the root patterns of housing segregation were explicitly based on race/ethnicity. There may come a time when race is not a satisfying proxy for socio-economic status (and vice versa) in the urban core, but that time is not today.

With that caveat in mind, a rethinking of the goal of urban homeownership acknowledges that the laudable goals of individual wealth creation and neighborhood social stability have all but evaporated in light of the massive foreclosures that have swept across American cities. As one commentator noted, "[t]he oft-stated benefits of homeownership are largely inconsistent with recent trends that indicate that, for many, attempting to become a homeowner is a painfully short and ultimately unwise investment."<sup>166</sup> The similarities shown above between the HOLC map and the foreclosure map indicate that minority neighborhoods are once more being shut out of the homeownership market. After this sobering acknowledgement, the dichotomy between place-based strategies and people-based strategies becomes relevant.<sup>167</sup>

163. Dickerson sees the problem slightly differently. To her, the problem is "an irrational obsession with attaining the status of homeownership." Dickerson, *supra* note 2, at 232. While I do not disagree with her premise, I submit that the foreclosure rate that disproportionately plagues city minority neighborhoods could have been diminished with non-racially based lending criteria.

164. Sheryll D. Cashin, *Middle-Class Black Suburbs and the State of Integration: A Post-Integrationist Vision for Metropolitan America* 9 (Georgetown Univ. Law Ctr., Working Paper No. 241245, 2000), available at [http://papers.ssrn.com/papers.taf?abstract\\_id=241245](http://papers.ssrn.com/papers.taf?abstract_id=241245) [hereinafter Cashin, *Middle-Class Black Suburbs*]. See also Sheryll D. Cashin, *Localism, Self-Interest, and the Tyranny of the Favored Quarter: Addressing the Barriers to New Regionalism*, 88 GEO. L.J. 1985, 2048 (2000).

165. For example, Portland, Salt Lake City, and Seattle. See Cashin, *Middle-Class Black Suburbs*, *supra* note 164, at 16.

166. Dickerson, *supra* note 2, at 207.

167. There is one mixed strategy that combined place- and people-based focuses. Farmers Home was a mortgage guarantee program providing low-cost loans to people in

Place-based homeownership strategies focus on empowering neighborhoods. Examples from previous programs include the Home Mortgage Disclosure Act,<sup>168</sup> the CRA, Public Housing Demonstration (a Reagan-era program providing for the sale of public housing units to tenants), Nehemiah,<sup>169</sup> and HOME.<sup>170</sup> People-based strategies focus on empowering the individual.<sup>171</sup> Examples from previous programs include the FHA, VA, Fannie and Freddie Mac, Section 235, ECOA, the National Homeowner Strategy, and the Blueprint for the American Dream.<sup>172</sup>

As it relates to urban homeownership, none of these programs can be deemed a resounding success. What little impact some programs might have had was lost in the foreclosure crisis.<sup>173</sup> The stubborn truth about place-based initiatives is that they do not allow for wealth creation due to neighborhood limitations. The stubborn truth about people-based initiatives is that those who can afford to leave the distressed area leave; those who cannot afford to leave are forced to remain in marginal neighborhoods with financial instability. Such parallelism crystallizes the choice of goals in urban homeownership programs: to help people or to help neighborhoods. While it is difficult to do both simultaneously, we have suffered through choosing one over the other with less-than-

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rural areas. However, its rural focus makes it inapplicable to the current discussion. See U.S. DEP'T OF AGRICULTURE, A BRIEF HISTORY OF FARMERS HOME ADMINISTRATION (1989), available at <http://www.rurdev.usda.gov/rd/70th/history%20of%20farmers%20home.pdf>. The Farmers Home Administration was restructured as the USDA Rural Development Program in 1995.

168. Home Mortgage Disclosure Act of 1975, Pub. L. No. 94-200, tit. III, 89 Stat. 1125 (codified as amended at 12 U.S.C. §§ 2801-10 (2006)).

169. Nehemiah is a down payment assistance program. See 24 C.F.R. pt. 280 (2010) (setting forth program regulations).

170. See 24 C.F.R. pt. 92 (2010) (setting forth program regulations).

171. There is a very strong argument to include the tax advantages of home ownership as a people-based program. See Joseph Gyourko & Todd Sinai, *The Spatial Distribution of Housing-Related Ordinary Income Tax Benefits*, 31 REAL EST. ECON. 527 (2003). However, since the deductibility of mortgage interest and local taxes depends on the taxpayer itemizing deductions, this benefit is all but lost for LMI homeowners. Even those taxpayers itemize the value because the marginal tax rate is lower. See Powell, *supra* note 43, at 624.

172. The FHA allows for the purchase of homes with low down payments. The U.S. Department of Veterans Affairs provides a loan guaranty program for veterans. See U.S. Dep't of Veterans Affairs, Loan Guaranty Home Loan Program, <http://www.home.loans.va.gov> (last visited June 21, 2010). The ECOA ("Equal Credit Opportunity Act") prohibits discrimination in the granting of credit. Pub. L. No. 93-495, tit. V, 88 Stat. 1500 (codified at 15 U.S.C. § 1691 (2006)). The National Homeowner Strategy was a 1994 strategy introduced by Pres. Clinton to overhaul Fannie Mae practices. Blueprint for the American Dream was an HUD effort to increase minority homeownership by 5.5 million by 2010. See U.S. DEP'T HOUS. & URBAN DEV., BLUEPRINT FOR THE AMERICAN DREAM (2003), available at <http://archives.hud.gov/initiatives/blueprint/blueprint.pdf>.

173. Powell, *supra* note 43, at 616.

resounding results. One avenue of inquiry might be to split the middle with ideas such as shared ownership, subsidized co-ops with limited transferability, and shared appreciation financing.<sup>174</sup> However, these ideas tend to be impractical on a wide-scale basis.

If the choice is to promote place-based policies, the first order at hand would be to eliminate differences between cities and suburbs. Previous attempts at place-based strategies have left intact the legacy advantages enjoyed by the suburbs and have instead focused on subsidizing the urban core.<sup>175</sup> One solution might be to go the other way and strip the suburbs of the value of past policies in order to level the playing field. Gone are the disparities between federal highway dollars and subsidies for mass transit. Zoning and land use laws would be regionalized. In this way, cities can compete for more of the share of metropolitan homeowners. On the other hand, some commentators have advocated abandoning people-based homeownership programs all together. Instead of incentivizing homeownership for urban residents, they argue, housing policy should focus on providing quality affordable rental housing.<sup>176</sup> This approach accepts that some people should not be homeowners but still have the right to decent, affordable housing. Since suburbs can successfully zone out low-income rental housing,<sup>177</sup> this makes the city the repository of the metropolitan poor renters. Both extremes are not only politically unfeasible, but also unsatisfying from a social welfare perspective.

It might be instructive to turn attention away from the housing purchase market and look at the rental housing market. Here the same people/place decisions are made. To address the multitude of social, economic and legal woes of mass-produced public housing, several policies regarding the housing of the nation's poor have arisen. For example, policies such as the Gautreaux Assisted Housing Program<sup>178</sup> and Moving to Opportunity (MTO)<sup>179</sup> are both people-based programs. Both programs

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174. For more ideas in this vein, see Byrne & Diamond, *supra* note 9, at 547.

175. See *supra* note 168–72 and accompanying text.

176. Dickerson, *supra* note 2, at 233–34.

177. This is subject to any limitations that might be in place, such as Mount Laurel-type fair share regulations, which prohibit states and municipalities from discriminating against lower-income residents in their land use planning.

178. A metropolitan-wide remedy to “white flight” by dispersing lower income tenants in Chicago was upheld in *Hills v. Gautreaux*, 425 U.S. 284, 286 (1976). For discussion, see Poindexter, *Collective Individualism*, *supra* note 14, at 628.

179. Five cities (Baltimore, Boston, Chicago, Los Angeles, and New York) were chosen to participate in this program under Section 152 of the Housing and Community Development Act of 1992. Pub. L. No. 102-550 §152, 106 Stat. 3672 (1992). See also U.S. Dep’t Hous. & Urban Dev., Moving to Opportunity for Fair Housing, <http://portal.hud.gov/portal/page/portal/HUD/programdescription/mto> (“Moving to Opportunity for Fair Housing (MTO) is a 10-year research demonstration that combines tenant-based rental assistance with housing counseling to help very low-income families move from poverty-stricken urban areas to low-poverty neighborhoods.”)

build upon the Section 8 voucher program that empowers tenants to find housing outside of traditional public housing projects. The important step that Gautreaux and MTO take is that both explicitly push residents outside their urban neighborhoods and into more economically diverse neighborhoods—even into the suburbs. In contrast, HOPE VI is a place-based strategy that targets the nation's worst public housing projects. The projects are demolished (or substantially renovated), and the resulting development has both low-income and market-rate units for rent.<sup>180</sup> Existing tenants are given the opportunity to return.<sup>181</sup>

#### A. Homeownership Zone Program

One ownership program that began to tie together both people- and place-based strategies is the Homeownership Zone demonstration project. Utilizing New Urbanist concepts, in 1996 HUD, under Secretary Henry Cisneros, launched the Homeownership Zone (HOZ) demonstration program as part of a national strategy to expand homeownership. Its goal is to subsidize homeownership while building economic and social capital in the neighborhood by facilitating new housing construction or substantial rehabilitation. According to the HUD website,

[t]he goal of the HOZ initiative is to test the idea that cities can transform their blighted areas into vibrant communities by creating entire new neighborhoods of mixed-income single-family homes, called Homeownership Zones. Homeownership Zones usually consist of several hundred new homes in a concentrated target area near major employment centers.<sup>182</sup>

HUD issued an interim report on the initiative in 2007 indicating that, on the whole, the program achieved its goal of providing opportunities to LMI families and market rate buyers in the purchase of their first home.<sup>183</sup>

HOZ is a demonstration project with funding of \$50 million. HUD money was leveraged with private capital and public capital from other sources. Eleven cities were granted funding for their projects,<sup>184</sup>

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180. For a complete description, see Jerry J. Salama, *The Redevelopment of Distressed Public Housing: Early Results from HOPE VI Projects in Atlanta, Chicago, and San Antonio*, 10 HOUS. POL'Y DEBATE 95 (1999).

181. See SUSAN J. POPKIN, URBAN INST., *THE HOPE VI PROGRAM, WHAT ABOUT THE RESIDENTS?* (2002). See also Georgette C. Poindexter, *Who Gets the Final No? Tenant Participation in Public Housing Redevelopment*, 9 CORNELL J.L. & PUB. POL'Y. 659, 662–63 (2000).

182. U.S. Dep't of Hous. & Urban Dev., Homeownership Zones (HOZ), <http://www.disasterhousing.gov/offices/cpd/affordablehousing/programs/hoz/index.cfm>.

183. JOE KIRCHNER ET. AL., U.S. DEP'T OF HOUS. & URBAN DEV., *INTERIM EVALUATION OF HUD'S HOMEOWNERSHIP ZONE INITIATIVE* 12 (2007).

184. *Id.* These cities were Baltimore, Buffalo, Cleveland, Flint, Indianapolis, Louisville, New York, Philadelphia, Sacramento, San Juan, and Trenton.

which ranged in size from 121 units (New York) to 465 units (Cleveland).<sup>185</sup> Participating cities utilized various capital structures, including CDBG grants, Section 108 loans, and low-income tax credits (when rental units were part of development).<sup>186</sup> Affordability was addressed through construction subsidies, down payment assistance, subsidized mortgages and “soft second” mortgage.<sup>187</sup> Specifically, the goals included:

- Provide for significant new single-family (1-to-4 unit) homeownership opportunities (an application that includes at least 300 new single family homes will be presumed to meet this standard; others may demonstrate how a smaller number of units will suffice to create visible change and revitalize the neighborhood).
- Result in measurable, visible improvement in the neighborhood.
- Provide for a mix of income levels.
- Leverage significant public and private resources.
- Establish extensive partnerships with business, lending institutions, real estate professionals, builders, educational institutions, religious entities, and/or other private or nonprofit organizations.
- Provide opportunities for participation by community residents, including opportunities for homeownership.
- Include the development of housing opportunities as part of a comprehensive, coordinated approach to the overall revitalization of the neighborhood.
- Show streamlined local processes to ensure rapid construction and program implementation.
- Begin development within 60 days of grant approval.
- Establish clear benchmarks for measuring performance.
- Use innovative construction techniques and land use planning to reduce the cost of housing construction and minimize regulatory barriers.
- Take advantage of the most recent advances in urban housing design to create a sense of neighborhood and community throughout the overall plan for the area.<sup>188</sup>

Although significant issues were encountered (including but not limited to delays in construction, difficulty in site acquisition, and reloca-

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185. *Id.* at 14.

186. U.S. DEP’T OF HOUS. & URBAN DEV., HOMEOWNERSHIP ZONES (HOZ), <http://www.disasterhousing.gov/offices/cpd/affordablehousing/programs/hoz/index.cfm> (last visited June 21, 2010).

187. For example, a “soft second” mortgage of up to \$25,000 was given to homeowners in Louisville with the requirement that the homeowner remain in the house for ten years, with a percentage of the loan forgiven each year. Telephone Interview with Tim Barry, Director of Louisville Metro Housing Authority (Feb. 2010).

188. KIRCHNER ET. AL., *supra* note 183, at 5–6.

tion of existing residents during the construction), most projects achieved the stated goals.<sup>189</sup> In interviews with local Housing Authority officials, there was unanimous agreement that they would participate in the program again if offered the opportunity.<sup>190</sup> Foreclosures have been virtually non-existent. Crime decreased. Neighborhoods were revitalized with parks.<sup>191</sup> Neighborhoods that once had residents by default now had residents by choice. In the words of one Housing official: “[y]ou must give incentive to people who have choice to come back.”<sup>192</sup>

Perhaps the most exciting use of this program was when Louisville tied HOZ development with HOPE VI development. Likewise, in Baltimore a Hope VI project sits adjacent to the homeownership zone but was developed separately. In their assessment of the project, HUD reviewers stated in their interim evaluation in 2005 that “the HOZ approach has resulted in significant, positive changes in most of the target areas.”<sup>193</sup> The report praised “how the HOZ approach can be combined with HOPE VI development to integrate public housing rental units with middle-income homeownership housing in a totally rebuilt neighborhood.”<sup>194</sup>

According to HUD, HOZ was a demonstration project and no additional funding was proposed. The Obama Administration has, instead, enlarged the Neighborhood Stabilization Program (NSP2) (ownership) and the Choice Neighborhood Initiative (rental), and incorporated some HOZ-type elements.<sup>195</sup> In 2009, NSP2 was established through the American Recovery and Reinvestment Act.<sup>196</sup> On January 14, 2010, HUD awarded \$1.93 billion in grants to fifty-six nationwide grantees.<sup>197</sup> NSP2 funds were also distributed to consortiums, not only state and local governments.<sup>198</sup> NSP2 funds are intended to be used over

189. See Salama, *supra* note 180.

190. Telephone interviews with Henrietta Owusu, Dir., Div. of Hous. Prod., City of Trenton (Feb. 2010); Clint Tearnan, Econ. Dev. Officer, Office Project Fin., City of Baltimore (Feb. 2010); Robert Stitt, Mgmt. Analyst/Homeownership Zone Coordinator, Sacramento Hous. & Redev. Agency, City of Sacramento (Feb. 2010).

191. Some of the developments (notably Baltimore and Sacramento) initially hoped to attract commercial activity but have, as yet, been unable to clear this hurdle.

192. Telephone interview with Tim Barry, Dir., Louisville Metro Housing Authority (Feb. 2010).

193. KIRCHNER ET. AL., *supra* note 183, at 13.

194. *Id.*

195. Interview with Ginger Macomber, HOZ Coordinator, HUD (Feb. 2010).

196. Pub. L. No. 111-5, tit. XII (Transportation and Housing and Urban Development, and Related Agencies), 123 Stat. 203 (2009). See also U.S. Dep’t Hous. & Urban Dev., Neighborhood Stabilization Program 2, <http://www.hud.gov/offices/cpd/communitydevelopment/programs/neighborhoodspg/arrafactsheet.cfm>.

197. Neighborhood Stabilization Program 2, *supra* note 196.

198. U.S. Dep’t Hous. & Urban Dev., Neighborhood Stabilization Program 2, FAQs on NSP2, [http://www.hud.gov/offices/cpd/communitydevelopment/programs/neighborhoodspg/nsp2\\_quest\\_answers.pdf](http://www.hud.gov/offices/cpd/communitydevelopment/programs/neighborhoodspg/nsp2_quest_answers.pdf).

a three-year period, with over 50% of the grant needing to be spent within the first two years.<sup>199</sup>

While NSP2 targets vacant, abandoned and dilapidated housing (i.e., it is a place-based strategy), it also incorporates people-based strategies by including consortiums of local leaders in the development process. Expansion of the demonstration program provides an exciting opportunity to rethink our approach to urban homeownership. First, the program addresses one of the major problems of current urban homeownership—the dilapidated state of available housing stock. One of the big attractions of the push to suburban living was a new house, and this program offers the same attraction to urban residents. Second, it addresses the proper use of federal financial intervention. Indirect market intervention (through Fannie and Freddie) proved disastrous, and regulatory intervention (through CRA) was spotty. HOZ program uses the federal money as leverage. Different communities utilized a range of funding sources but all relied on a mix of some sort.

The final, and perhaps most important, component of HOZ is that it is easily bundled with other rental-based programs such as HOPE VI and the Choice Neighborhood Initiative. The Choice Neighborhood Initiative was passed to “expand on the legacy of HOPE VI by expanding the range of activities eligible for funding and capitalize on the full range of stakeholders we know are needed and want to be involved—from local governments and non-profits to private firms and public housing agencies.”<sup>200</sup> The Choice Neighborhood Initiative is essentially HOPE VI funding with available funds being able to be used for early childhood education programs and criteria that also take into account “green development and energy efficiency strategies.”<sup>201</sup> HUD’s proposed fiscal 2010 budget has funding for the Choice Neighborhood Initiative and HOPE VI set at \$250 million, compared to the \$120 million used for HOPE VI funding in fiscal 2009.<sup>202</sup>

Homeownership anchors neighborhoods and can, given the right set of circumstances, permit owners to build capital. But homeownership is not for everyone. At the same time, decent affordable neighborhoods

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199. *Id.*

200. Shaun Donovan, Secretary, U.S. Dep’t of Hous. & Urban Dev., Prepared Remarks at the Brookings Institution Metropolitan Policy Program’s Discussion: From Despair to Hope: Two HUD Secretaries on Urban Revitalization and Opportunity (Jul. 14, 2009), *available at* <http://www.hud.gov/news/speeches/2009-07-14.cfm>.

201. Press Release, U.S. Dep’t of Hous. & Urban Dev., HUD Announces \$113 Million Available for Public Housing Transformation, Community Revitalization; Obama Administration Stresses Early Childhood Education in 2009 Hope VI Program, *available at* <http://www.hud.gov/news/release.cfm?content=PR09-119.cfm>.

202. Press Release, U.S. Dep’t Hous. & Urban Dev., HUD Announces \$113 Million Available for Public Housing Transformation, Community Revitalization (July 14, 2009), *available at* [http://portal.hud.gov/portal/page/portal/HUD/press/press\\_releases\\_media\\_advisories/2009/HUDNo.09-119](http://portal.hud.gov/portal/page/portal/HUD/press/press_releases_media_advisories/2009/HUDNo.09-119).

are the right of all citizens—not just those able to buy a home. A sound approach to urban policy ties together both owner and rental programs. Such a holistic approach would not only build city neighborhoods, but also empower city residents. HOZ demonstrated that such an approach can have profound positive effects in cities as disparate as Trenton and Sacramento. Such opportunities should be replicated nationwide.



