



# NSP Policy Alert!

## Explanation of Property Types Under Each Eligible Use

**QUESTION:** *What are eligible uses for various property types? What property types are required to satisfy the 25% set-aside requirement?*

**Note:** This guidance contains the original definitions of “foreclosed” and “abandoned” as defined in the original NSP1 and NSP2 Notices. On April 2, 2010, HUD issued a new Notice (5321-N-04) for the NSP2 Program, and on April 9, 2010 (5321-N-03) HUD issued a similar Notice for the NSP1 Program. These Notices changed the definitions of “foreclosed” and “abandoned” for the purposes of identifying eligible properties for NSP1 and NSP2. Guidance on the Impact of New Definitions for NSP-Eligible Properties is available here: <http://hudnshelp.info/index.cfm?do=viewResource&ResourceID=484>.

### Introduction

The Housing and Economic Recovery Act (HERA) uses different terms for each of the five Eligible Uses of funds in the Neighborhood Stabilization Program (NSP). HUD wishes to clarify these terms and explain how this affects what grantees can do with different types of property. Attachment A—NSP Eligible Uses by Property Type, was developed to serve as a visual aid to show the limitations and requirements that apply to NSP funds. The legislative language on Eligible Uses shows the terms that will be discussed in underline. This memorandum also discusses the property types required to satisfy the requirement that 25% of NSP funds are used to house individuals or families whose incomes do not exceed 50% of area median income.

In general, grantees must limit their activities in any Eligible Use only to those property types specifically cited. When combining uses (e.g. Acquisition and Rehabilitation under B with Financing under A), the more restrictive classification applies. All definitions should be understood to apply primarily to areas of greatest need or to constitute an improvement benefiting such areas as part of the overall NSP program. In addition, all activities must meet the national objective of benefiting low-, moderate-, or middle-income persons; NSP grantees may not use slum and blight removal or urgent needs as national objectives. Subsequent guidance will further define the correlated eligible activities from the CDBG entitlement regulations.

### Terms to be Discussed

***Housing and Economic Recovery Act Title III Sec. 2301 (c):***

**(3) ELIGIBLE USES.**—Amounts made available under this section may be used to—

(A) establish financing mechanisms for purchase and redevelopment of foreclosed upon homes and residential properties, including such mechanisms as soft-second, loan loss reserves, and shared-equity loans for low- and moderate- income homebuyers;

(B) purchase and rehabilitate homes and residential properties that have been abandoned or foreclosed upon, in order to sell, rent, or redevelop such homes and properties;(C) establish land banks for homes and residential properties that have been foreclosed upon;

(D) demolish blighted structures; and

(E) redevelop demolished or vacant properties.

***Housing and Economic Recovery Act Title III Sec. 2301 (f) (3) (A):***

(ii) not less than 25 percent of the funds appropriated or otherwise made available under this section shall be used for the purchase and redevelopment of abandoned or foreclosed upon homes or residential properties that will be used to house individuals or families whose incomes do not exceed 50 percent of area median income.

**Discussion**

***A. Financing Mechanisms:***

For “foreclosed-upon homes and residential properties”:

HUD interprets “homes” as any type of permanent residential dwelling unit, such as detached single family structures, townhouses, condominium units, multifamily rental apartments (covering the entire property), and manufactured homes where treated under state law as real estate (not personal property). The NSP Notice defines “foreclosed”; see excerpt below.

“Residential properties” includes all of the above plus vacant land that is currently designated for residential use, e.g. through zoning.

***NSP Notice Definition: Foreclosed.*** A property “has been foreclosed upon” at the point that, under state or local law, the mortgage or tax foreclosure is complete. HUD generally will not consider a foreclosure to be complete until after the title for the property has been transferred from the former homeowner under some type of foreclosure proceeding or transfer in lieu of foreclosure, in accordance with state or local law.

***Appropriate Uses of Financing Mechanisms:*** NSP grantees should be aware that many financial subsidy functions can be accomplished under Eligible Uses B and E. These rely on the highly flexible activity of Direct Homeownership Assistance and on the financing that may be undertaken as part of housing rehabilitation (both single- and multi-family) under 24 CFR 570.202 (b). Homeownership Assistance, for example, not only allows downpayment assistance, but also reduction of principal amounts, in order to make the unit affordable to the LMMI purchaser. See the Policy Guidance on Homeownership Assistance page 9 for more details on Direct Homeownership Assistance.

Despite the flexibility in Eligible Uses B and E with direct homeownership assistance and Rehabilitation, there are some strategies that require Eligible Use A. One such strategy is a large pool of loans for other activities. For example, one grantee used NSP1 funds and local funds to establish a revolving loan fund. This could only be done under Eligible Use A because it would not qualify as a form of direct homeownership assistance.

Similarly, the larger and more purely financial strategies, although rare, would fall under Eligible Use A. These include lump sum drawdowns, loan loss reserve funds and similar mechanisms in which pools of money are utilized.

In terms of Redevelopment, it is true that most redevelopment could be done under E. However, there might be a need to use NSP as a credit enhancement for housing revenue bonds. That part of the transaction would be a financing mechanism.

### **B. Purchase and Rehabilitation:**

For “homes and residential properties that have been abandoned or foreclosed upon”:

As above, HUD interprets “homes” as any type of permanent residential dwelling unit, including detached single family structures, townhouses, condominium units, multifamily rental apartments (covering the entire property), and manufactured homes where treated under state law as real estate (not as personal property). The NSP Notice defines “abandoned” and “foreclosed”; see excerpts below.

“Residential properties” includes all of the above plus vacant land that is currently designated for residential use, e.g. through zoning.

**NSP Notice Definition: Abandoned.** A home is abandoned when mortgage or tax foreclosure proceedings have been initiated for that property, no mortgage or tax payments have been made by the property owner for at least 90 days, AND the property has been vacant for at least 90 days.

**NSP Notice Definition: Foreclosed.** A property “has been foreclosed upon” at the point that, under state or local law, the mortgage or tax foreclosure is complete. HUD generally will not consider a foreclosure to be complete until after the title for the property has been transferred from the former homeowner under some type of foreclosure proceeding or transfer in lieu of foreclosure, in accordance with state or local law.

### **C. Land Banks:**

For “homes and residential properties that have been foreclosed upon”:

The Recovery Act added foreclosed “residential properties” to this category. This additional language is part of the NSP1 Bridge Notice. The Bridge Notice also allows grantees to establish “and operate” land banks. Operations of a land bank include maintenance expenses as project delivery costs eligible under disposition and interim uses that comply with an eligible activity.

Also see the discussion below under Demolition for explanation of meeting a national objective under landbanking.

### **D. Demolition:**

For “blighted structures”:

The NSP Notice defines “blighted structures”, as shown below. HUD has taken the position that any type of structure that is blighted may be demolished with NSP funds. This means that commercial, industrial or other types of structures may be demolished in addition to homes and residential structures in areas of greatest need.

In general, demolition must have an end use that meets a national objective. There are a couple of cases in which the demolition can be an end in itself. First, in a LMMI area, if the property creates an extreme danger to public health or safety (like a meth lab or collapsing structure), then it can be considered an area benefit (LMMA). Second, if the demolition is done in concert with a coordinated program of redevelopment and/or rehab and/or new construction and/or other improvements, including other demolition, in a target area, which together can reasonably be expected to improve the area, then it can also qualify as LMMA.

In all other cases, as with property in a land bank, it should lead to an end use that is eligible and meets a national objective in NSP. In this respect, land banked property and demolished property are just interim uses for which end uses must be planned. Such eligible end uses could include housing (redeveloped on the property), sale (or donation) of the property as side lots to LMMI neighbors, donation of the property to a community garden group, or use of the property as a public facility like a park (in NSP1 only). If the property is acquired, it could temporarily be placed in a land bank, but the same requirements will ultimately apply to both types of property.

**NSP Notice Definition: Blighted structure.** A structure is blighted when it exhibits objectively determinable signs of deterioration sufficient to constitute a threat to human health, safety, and public welfare.

#### **E. Redevelopment:**

For “demolished or vacant properties”:

This Eligible Use allows communities to address the broadest range of property types. Because the legislation does not limit this use to homes and/or residential properties, HUD will permit grantees to acquire and redevelop ANY property type. This includes commercial or industrial property in addition to all types of residential property. Note that property acquired under Redevelopment need not be abandoned or foreclosed upon.

However, it MUST be vacant. “Vacant properties” includes both vacant land and properties with vacant structures on the land. However, HUD understands redevelopment to imply that properties were once developed or are surrounded by existing development. Therefore undeveloped or “greenfield” sites, at the edge of development, may not be acquired under Eligible Use E. Previously undeveloped in-fill sites are generally eligible.

HUD expects that, unlike land banks, properties acquired and improved under Eligible Use E must proceed expeditiously to construction. Properties that are eligible to be land banked with unknown end uses, or for which the end use is not imminent, should be considered for Land Banks (assuming that they have been foreclosed upon). Some corollary considerations also merit discussion, which follows the next section on housing for low-income persons.

The NSP1 Bridge Notice did not apply the Recovery Act’s limitation on redevelopment to housing activities. Therefore, NSP1 funds may still be used for public facilities and area benefit economic development projects.

#### **Title III Sec. 2301 (f) (3) (A): Housing for individuals or families whose incomes do not exceed 50% of area median income:**

For “purchase and redevelopment of abandoned or foreclosed upon homes and residential properties”:

HERA requires that grantees allocate 25% of their NSP funds for housing that serves lower income persons. Note that this is limited to abandoned or foreclosed upon homes or residential properties. The NSP definitions of “abandoned” and “foreclosed”, listed above, apply here also. HUD takes the position that this section refers to permanent housing; thus, such uses as homeless shelters cannot count toward the 25% requirement.

## **Related Considerations**

The following discussion concerns implications of the preceding clarifications, or instances in which more than one set of requirements apply.

First, new housing construction (benefiting low-, moderate-, or middle-income persons) is permitted under Eligible Use E, and ONLY under Eligible Use E. This supersedes the limitation on new construction of housing in the CDBG program and is described in Sec. II H. 3.c of the NSP Notice (see excerpt below on page 5).

Second, housing rehabilitation has been added by the Recovery Act as a CDBG-correlated eligible activity under Eligible Use E.

Third, grantees may wish to construct new housing for persons at or below 50% of median income, especially affordable rental housing. In this case, the law requires that the property be abandoned or foreclosed upon. The Notice limits new construction to Eligible Use E, which can take place only on vacant or demolished property. Therefore, to meet the 25% requirement, new housing construction can occur only on demolished or vacant land that is either abandoned or foreclosed upon. After publication of the Technical Correction Notice, rehabilitation of vacant residential structures will be permissible, but to meet the 25% requirement the property must also have been abandoned or foreclosed upon.

Fourth, the NSP1 Bridge Notice removes LMMI Jobs as a national objective. Therefore, only economic development activities that qualify under LMMI Area, such as retail stores, now meet a national objective.

Finally, as defined in the CDBG regulations below, shelters for persons with special needs (such as homeless shelters and halfway houses) are public facilities. Renovation or new construction of such structures is eligible as a public facility under Eligible Use E. However, because they are not defined as permanent housing, they cannot count towards the requirement that 25% of the NSP funds “be used to house individuals or families whose incomes do not exceed 50% of area median income”.

On a related topic, the Bridge Notice clarifies that housing counseling, required for all potential homebuyers, is allowed under all Eligible Uses. HUD notes that, while all participants in counseling must be prospective purchasers of NSP homes, payments for housing counseling are eligible even if the trainee does not ultimately purchase a home. This is because a major objective of such counseling is to screen out people who may not be ready to make this substantial commitment.

## Additional References

### ***NSP Notice Dated Oct. 6, 2008***

#### **II. H. Eligibility and Allowable Costs**

**c. New construction of housing** is eligible as part of eligible-use (E) to redevelop demolished or vacant properties.

### ***Housing and Economic Recovery Act Title III Sec. 2301(f)***

#### **(3) LOW AND MODERATE INCOME REQUIREMENT.—**

(A) IN GENERAL.—Notwithstanding the authority of the Secretary under paragraph

(1)—

(i) all of the funds appropriated or otherwise made available under this section shall be used with respect to individuals and families whose income does not exceed 120 percent of area median income; and

(ii) not less than 25 percent of the funds appropriated or otherwise made available under this section shall be used for the purchase and redevelopment of abandoned or foreclosed upon homes or residential properties that will be used to house individuals or families whose incomes do not exceed 50 percent of area median income. (emphasis added)

### ***CDBG regulations 24 CFR 570.201 (c):***

#### **Shelters for persons with special needs.** Excerpt –

“Facilities designed for use in providing shelter for persons having special needs are considered public facilities .... Such facilities include shelters for the homeless; convalescent homes; hospitals, nursing homes; battered spouse shelters; halfway houses for run-away children, drug offenders or parolees; group homes for mentally retarded persons and temporary housing for disaster victims.”

### ***NSP1 Federal Register Bridge Notice dated June 19, 2009 [74 FR 29223]***

Adds rehabilitation and preservation activities to the correlated eligible activities from the CDBG regulations to Eligible use E

### NSP Eligible Uses by Property Type

	Eligible Uses	Foreclosed Homes and Residential Properties	Abandoned Homes and Residential Properties	Blighted Structures	Demolished Properties	Other Vacant Properties
A	Financing Mechanisms	Yes	No	Only if Foreclosed	N/A	Only if Foreclosed
B	Purchase and Rehab	Yes	Yes	If Foreclosed or Abandoned	N/A	No
C	Land banks	Yes (Homes only)	No (Foreclosed only)	Foreclosed home or residential property	No	No
D	Demolition	Only if Blighted	Only if Blighted	Yes	N/A	Only if Blighted
E	Redevelopment	Only if Vacant	Only if Vacant	Only if Vacant	Yes	Yes
	<i>Comments</i>			<i>Locally defined Not limited to residential structures.</i>	<i>Not limited to residential structures.</i>	<i>Land or structures. Not limited to residential property</i>

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**NSP Notice Definition: Foreclosed.** A property “has been foreclosed upon” at the point that, under state or local law, the mortgage or tax foreclosure is complete. HUD generally will not consider a foreclosure to be complete until after the title for the property has been transferred from the former homeowner under some type of foreclosure proceeding or transfer in lieu of foreclosure, in accordance with state or local law.

**Low-income Set-aside** (25% of funds for individuals at or under 50% Area Median Income): The legislation says that these funds “shall be used for the purchase and redevelopment of abandoned or foreclosed upon homes or residential properties”. Vacant land under Eligible Use E, must also be foreclosed upon or abandoned for any housing constructed on it to qualify for the set-aside requirement.

**Homes and Residential Properties:** HUD interprets “homes” as any type of permanent residential dwelling unit, such as detached single family structures, townhouses, condominium units, multifamily rental apartments (covering the entire property), and manufactured homes where treated under state law as real estate (not personal property). “Residential properties” includes all of the above plus vacant land that is currently designated for residential use, e.g. through zoning.