

# EMBEDDING “IMMEDIATE” REAL ESTATE CAPACITY IN DETROIT CDOs

## How These Real Estate Capacity Building Recommendations were Developed

These recommendations represent a synthesis of insights from both Real Estate Capacity Providers and CDOs, working in Detroit. Insights were compiled through a) CDO “Kitchen Cabinet” meetings or focus groups, b) the Kresge Foundation CDO Cohort notes, c) individual interviews with 8 CDO Executive Directors representing CDOs from each Council District, and d) individual conversations with multiple CDFI and other Intermediary executives and staff. Notes from these various conversations are available on request. Following these recommendations is background on a) the case for embedding real estate capacity into CDOs, b) general approaches to real estate capacity building, c) gaps in the current capacity building delivery system.

## At-A-Glance “Immediate” Real Estate CDO Capacity Recommendations

In light of the uniqueness of community-based real estate development, the current gaps in the provision of TA for this work, and the specific request for recommendations to embed “immediate” real estate capacity below are some directional recommendations. The assumption is that action can be taken now on these recommendations, even though live real estate projects (especially by smaller, lower capacity CDOs) won’t necessarily materialize before 2020 or beyond.

### GENERAL REAL ESTATE CAPACITY BUILDING

- ✓ **POOLED FUNDING.** Create one single fund, or multiple funds, placed with a neutral intermediary to be used to support CDOs that are more ready to take on real estate projects (with a neighborhood plan and a specific project that fits with that plan):
  - **Pooled Funding targeted for CDO use for real estate projects,** that allows CDOs to access consultative/coaching real estate services
  - **Real Estate “operating support” for CDOs to hire/retain staff;** including an opportunity for multiple CDOs to jointly purchase the time of shared professional real estate staff
  - **Pre-Development capital that is targeted for CDO projects** and easily accessible, ideally in the form of grants or recoverable grants, and with a patient timeframe for the use and/or repayment of these funds. These funds would be used for feasibility and market analysis, site control, environmental review and other necessary pre-development work.
  - **Competitive Capital Stream for CDOs to finance single family home rehab projects,** where appropriate
- ✓ **CDO REAL ESTATE CAPACITY BUILDING SERVICES CONSORTIUM.** To support CDOs whose capacity is dormant or new, create and incentivize a small group of a few *select and willing* CDFIs and CDOs and city officials, to build off their experience and current offerings to quickly generate a few necessary new products and services over the next few months. These services could be placed/offered through Co.act:
  - **Cadre of Real Estate Coaches and Real Estate Technical Professionals.** Support one CDFI to quickly recruit and qualify a) a cadre of local real estate coaches that can help CDOs through an entire project; and b) a cadre of real estate technicians who can handle appraisals, environmental reviews, legal support and other technical functions. This CDFI could work with Co.act to refer CDOs to these services. These coaches should include professionals with experience in CDO-sponsored real estate, and experienced CDOs willing to teach other CDOs. An efficient vetting process should be used to assure these individuals will provide high-quality services to CDOs.
  - **Intake/Referral and Marketing.** Support Co.act to create an intake/referral service, taking requests from CDOs looking for real estate TA/coaching and refer CDOs to the cadre of real estate professionals referred to above.
  - **Basic Real Estate Education.** Support a few CDFIs and CDOs to create:

- a. An online seminar: What is community-based real estate development in its various forms, what do the housing and commercial real estate processes look like, and what are the various roles that CDOs can play in it? What city processes are required?
  - b. A second online seminar: What are some alternative real estate models and where are the examples of where they work?
  - c. A clearinghouse/data base of available TA services for real estate, including CDOs with real estate experience willing to coach on various community-based development techniques and models
  - d. A clearinghouse/data base of various current financing tools for real estate development
  - **Cohort “Boot Camp” Training**
    - e. Support Capital Impact Partners to create a targeted CDO-focused real estate course, using CDO input. Depending on resources and time there could be separate cohorts focused on different types of real estate work: i.e. a SF Rehab cohort, a LIHTC Multi-Unit cohort, a commercial development cohort
- ✓ **COMMUNITY-BASED REAL ESTATE DISCUSSION SERIES:** Support the Consortium to sponsor a regular discussion series among CDFIs, CDOs and grass roots organizations; the discussion series could include a) story-telling on various Detroit real estate projects, b) discussion on strategies for the lowest-income residents with information on various affordability and alternative real estate strategies, c) brainstorming on ways to expedite property acquisition, city permitting and zoning processes

#### **SINGLE FAMILY REHAB STRATEGIES CAPACITY BUILDING**

- ✓ **DISTRICT-BY-DISTRICT SINGLE FAMILY REHAB/OWNERSHIP PILOT.** Detroit Home Mortgage (an affiliate of the national Community Reinvestment Fund) is prepared to mobilize to work on a “pilot” with one CDO-per-Council-District, in the more fragile markets in each District. In this concept, DHM Project Managers would support/coach a CDO in each District to facilitate a home-buyer qualification process, and a housing rehab, for 1-5 rehab-buy projects. The goal would be to eventually engage many CDOs all over Detroit, to facilitate home-buying and single-family rehab processes. This pilot would test a **concept whereby homebuyers are pre-qualified and counseled and bring necessary rehab financing through DHM.**
- ✓ **DLBA PARTNERSHIP FOR PROPERTY DISPOSITION.** Support the Consortium engaging with the DLBA “Strategic Initiatives Unit” to develop and test some targeted and user-friendly DLBA property acquisition strategies for CDO projects. The DLBA indicates a readiness to work on this. The goal would be to develop a concept whereby **DLBA homes would be matched with CDOs, which would finance the rehab work, then work with partners to identify and qualify homebuyers and sell the homes through equitable land contracts.** This strategy would necessarily have to be match with a competitive capital stream for CDOs to oversee completion of the rehab work, and pay for the rehab work.

The BECDD process has already produced a partnership concept (CDO rehab of SF DLBA homes), and is preparing to work with the Detroit Housing Compact on this idea. This design process could be linked to the larger discussion described above.

**See the next few pages for background on these recommendations.**

## **Background:**

### **Community Development Real Estate Capacity: A General Overview**

#### **Why is CDO-sponsored real estate work important?**

In the cities that BECDD studied we learned some important insights from CDOs in other cities:

- ✓ CDOs, because of their mission, begin with a different motivation for sponsoring real estate work: they generally want to a) put their residents to work to alleviate poverty, b) ensure affordability for low income people, c) clean up blight, and d) spur market activity where none exists. Whereas conventional real estate developers will place their projects in areas with strong market conditions, CDOs will work to make real estate work happen in the neighborhood they serve, regardless of market conditions. In a city like Detroit, with its vast swaths of fragile-market neighborhoods, this is critical. Detroit's 200-plus neighborhoods are too fragile for CDOs to NOT be part of the solution.
- ✓ CDOs have the inherent capacity to attract and absorb necessary subsidy, especially charitable subsidy, because of their mission. That subsidy makes the difference in a fragile-market neighborhood.
- ✓ CDOs that do real estate work can achieve a level of organizational sustainability (unlike other nonprofits) because in the right conditions, they can leverage their real estate portfolios to subsidize their operations or their resident engagement activities.
- ✓ CDOs' dedicated, place-based real estate work results in the development of dedicated constituencies – whether they are renters, buyers, local business tenants, shoppers or service clients – which creates power and a strong voice for a neighborhood at government tables.
- ✓ CDO real estate interventions in fragile neighborhoods can result, over time, in market forces normalizing – a condition that would not happen without the CDO intervention.

#### **How is CDO-sponsored real estate development different from conventional real estate development?**

- ✓ CDO-sponsored real estate work will often flow from a neighborhood-driven planning process, where residents have generated and approved the plans. A CDO real estate project will typically be created from the bottom up, through a representative CDO, with significant resident engagement in creating the project.
- ✓ CDO-sponsored real estate will typically focus on affordability, and will be motivated primarily by the need to create jobs, provide affordability especially in the face of gentrification, or eliminate blight.
- ✓ CDO real estate work will typically be done in neighborhoods that conventional development won't favor, resulting often in a project requiring even more subsidy than normal for a period of time.
- ✓ CDO real estate work will often strive for some form of community ownership or community investment, whether it be through ownership of land by the representative CDO, a community land trust, a community investment model, a co-op model.
- ✓ A CDO real estate project will often include quality-of-life amenities that reduce profitability (green space, community space, recreation space, or building space for human service institution to lease), thereby requiring more subsidy.
- ✓ Because a CDO at its best thoroughly knows and understands its target neighborhood, a CDO will be more likely to plan for appropriate real estate work that will be accepted and embraced by residents (i.e. SF Rehab strategies vs. multi-unit rental strategies).
- ✓ A CDO-sponsored real estate project will typically be concerned with the larger neighborhood context, well-being and long-term sustainability of a project, and not just the near-term financial return.

#### **Mindset/New Assumption: CDOs are key players in neighborhood real estate development**

For CDO-sponsored real estate work to proliferate in all of Detroit's neighborhoods, assumptions about the importance of a CDOs role, and its current or potential capacity, will have to shift as part of any effort to build CDO real estate capacity. We will need to believe that if we are going to make a citywide difference in how our neighborhoods develop physically, CDOs will have to play a key role.

### **Necessary Internal and External Conditions as a Starting Point**

Since CDOs at their best reflect the priorities of a neighborhood and its board of directors, there are certain basic “*necessary conditions*” that should be present within a CDO and its target neighborhood, to engage in real estate capacity building work:

- The CDO and its Board of Directors should have a desire to do real estate work and therefore to build the capacity to do so;
- There should be at least one “live” potential real estate project in play to facilitate the best learning;
- The project should make sense for the neighborhood – either because it has already been justified by a market analysis, a needs analysis or a well-researched neighborhood plan

Furthermore, all the learning/training/coaching available won’t result in more real estate work, without *two external conditions being met*:

- Available financing for a variety of real estate projects **IE:** LIHTC allocations, HOME dollars, pre-development capital, and other debt/equity tools to fund financing gaps).
- A clear strategy and/or pathway, including financing, for initial site control of the project site

### **Optimal approaches to real estate capacity building strategies for Detroit**

Conversations with both Detroit CDOs and Capacity Providers resulted in general consensus on the best way to help a CDO develop real estate capacity:

✓ *First, there should be a range of options (“a continuum”) for a) the various kinds of real estate work that a CDO undertakes and b) the various roles that a CDO plays in real estate and c) the various kinds of capacity that a CDO believes is best for itself.* Several CDOs mentioned their desire to begin with coaching/mentoring to get an initial project started and to build capacity, leading to longer-term capacity to hire and keep full time real estate staff. Other CDOs felt that being equipped with real estate knowledge, and being able to transmit that knowledge to residents, so as to play a strong negotiating role, would be sufficient. Some CDOs have the knowledge and skill and simply need more professional staff support to complete more projects. Some CDOs want to focus on Single Family Rehab strategies. Others want to focus on commercial corridor strategies and commercial real estate. Given that each neighborhood and each market is different, it makes sense for options to be available.

✓ *Second, market/site feasibility is critical* for a CDO to determine a) the kind of real estate strategies that will work in a neighborhood and b) the role the CDO can play. Technical assistance should be matched to these assessments.

✓ *Third, classroom training can be valuable as a starting point, especially “boot camp” style:* intensive training to provide basic knowledge and to offer value-add peer support through a cohort model in a short period of time. In the context of classroom training, learning from peers is invaluable.

✓ *Fourth, high-touch coaching/consulting makes the ultimate difference;* classroom training is useful but bears fruit when it is accompanied or followed closely by this form of support.

✓ *Next, “learning by doing” is the best form of learning how to do real estate.* Working on an actual real estate project, with a coach/consultant, results in more long-lasting learning.

✓ *In Detroit, a “hybrid” model of capacity building is in play.* The proliferation of CDFIs in the Detroit market in the past several years has been phenomenal, compared to the days when LISC was the only CDFI player. Equally important, the CDFIs are vertically integrated to *provide both capital and technical assistance* in the development of real estate projects. In this model, a CDFI/ TA provider might be a co-developer, a hired consultant, a trainer, or a capital provider, or some combination. In Detroit there are current examples of these kinds of partnerships now in play.

- Depending on the CDOs experience and capacity, a CDO might play a role in some aspects of the development, but not every role; and might take a portion of the developer’s fee;
- A separate, trusted partner organization might play a key technical role while also coaching the CDO, and might be paid through a separate consulting agreement;

- Partner organizations could be CDFIs, small for-profit developers, other non-financial intermediaries, or a more experienced CDO.
- ✓ *Finally, the delivery of these services should be coordinated and focused for CDOs so that a) the technical assistance is user-friendly for the CDO client organization, b) the support is geared toward the unique CDO approach to real estate work and b) the various players - including the CDOs - can learn together and make all of our neighborhoods more viable together. During 2018 the BECDD Intermediary System Task Force developed a “Community Development Capacity Building Function” project concept that accounts for these components: Intake/Assessment, Referral, Service Delivery, Monitoring/Evaluation, Payment.*

## **Current Gaps in the Delivery of Real Estate Capacity to CDOs in Detroit**

Within this context, below is a brief summary of the current gaps in the delivery of real estate capacity for CDOs in Detroit.

1. **Mindset Problem.** In the past 15 years (as Detroit’s population loss escalated, the Great Recession ravaged the densest neighborhoods, and the bankruptcy depleted our resources) CDO funding shrunk and, in many cases, CDO real estate capacity was depleted, went dormant or disappeared. Unfortunately, these conditions led to an erroneous assumption in the public and private sector that CDOs “don’t know how to do real estate.” As Detroit emerged from bankruptcy and the thirst for real estate investment escalated and real estate capital proliferated the mainstream mindset assumed that only for-profit developers should be engaged to build our neighborhoods. The idea of supporting CDOs to do real estate has not entered the mainstream conversation until recently.

Even worse, in some corners of the City there has been a perception (although it is changing) that CDOs aren’t “objective” enough to be able to do the kind of planning and real estate work that is important for neighborhoods. And by far worst, current mainstream thinking still doesn’t fully account for the fact that Detroit’s poverty rates are arguably the highest in the nation. So, requiring 20% affordability at 80% AMI in our multi-unit projects, for example, doesn’t come close to resolving the real dearth of quality, truly-affordable housing in Detroit.

2. **Lack of Understanding of CDO Real Estate: What is it? What Role(s) Can CDOs Play?** There are CDOs and CDO Executives in Detroit that want to consider developing real estate capacity but need a basic understanding of what the options are. What are the various forms of housing real estate and what does a housing real estate process look like? What are the various forms of commercial real estate and how does a commercial real estate process work? How is a CDO-sponsored real estate strategy different from a conventional for-profit real estate strategy? What are the various roles that a CDO can play in real estate – from acting as advocate/resident voice to serving as a sole developer? What are some alternative real estate ownership models?
3. **Insufficient, Dormant or Non-Existent CDO Real Estate Capacity.** We suggest that three factors have contributed to the demise of CDO real estate capacity: the “mindset” problem, the Great Recession and the Detroit bankruptcy. As a result, some CDOs have lost their real estate capacity (but not their institutional memory); some CDOs have opted not to try to develop it at all; and some CDO Executives are doing the real estate work while also running the whole organization.
4. **CDO Real Estate Capital Gap.** The availability of debt capital for Detroit real estate projects is acknowledged as an opportunity and indeed there are multiple CDFIs offering that capital. There is concern expressed about the lack of focused and strategic capital for Single Family Rehab projects. More importantly, for CDOs the real estate capital gap lies in three major areas.

First, there is a lack of funding to hire real estate staff who can shepherd projects for the CDOs pipeline, and who can coordinate and execute real estate projects; initially, coaches can be engaged to help build CDO capacity, but many CDOs want to have the option, eventually, of hiring dedicated real estate staff. Second,

there is a lack of easily-accessible and no-cost pre-development funding to pay for site control costs, legal costs, environmental review costs and other pre-development work. Third, CDO balance sheets can be too weak to survive underwriting criteria. So a “backstop” function needs to be developed to mitigate this problem, until CDOs generally develop stronger balance sheets. Finally, very low cost/patient capital streams (through impact investing/PRI) need to be available to equip CDOs to take on Single Family Rehab/Resale work.

5. **Lack of Coordination and Focus on CDO Real Estate Capacity Building Services.** There is apparently *no coherent or focused or centralized mechanism* by which a CDO can easily identify all the TA support is available for real estate, and then access it easily. Certainly, there is information available as to what some TA offerings are, and some CDOs are working to take advantage of those resources; and CDFIs (the main providers of real estate TA in Detroit) are marketing their services and seeking projects. Equally important, there appears to be no program or strategy for the *focused* provision of technical assistance and support to CDOs or for CDO-sponsored projects. Training and TA comes in many forms from CDFIs, but there is no targeted strategy for CDOs.
6. **Lack of Understanding of Real Estate Options.** There is a general appreciation for the City of Detroit’s increased capacity for planning and development, but there is equal concern for what is perceived to be cookie cutter thinking about a) the kinds of real estate solutions that the city will support, or b) which neighborhoods the city is willing to invest in. The Mayor’s SNF strategy is focused primarily (although not exclusively) on LIHTC projects and on certain neighborhoods and not others. Yet most of Detroit’s neighborhoods are occupied by single-family or two-family structures badly in need of rehab and repair. CDOs and residents have been clamoring for a number of years for resources for minor and major home repair and rehab. While no one disputes the challenges inherent in creating a citywide single-family home strategy in Detroit’s fragile neighborhood markets, there is concern about the perceived lack of priority to create such a strategy, along with commensurate resources. So, a capacity building strategy should account for this gap. To the extent that Detroit’s inventory of vacant land represents a unique problem and real estate opportunity for Detroit’s comeback, there is equal concern about the apparent lack of an open-space strategy, with commensurate resources.
7. **CDFIs Services are Key, But Incomplete and Not Strategically Focused.** Other than MCRs pro-bono legal brokering service, there are apparently no *non-financial* intermediaries in Detroit with a specialty in delivering coordinated CDO real estate capacity services. Rather, these services are being provided through a number of CDFIs that are also capitalizing real estate projects, including Enterprise, IFF, Cinnaire, Capital Impact Partners. Furthermore, the capacity support that is being provided isn’t specifically attuned to the unique perspective that CDOs bring to real estate development; and alternative real estate models are not part of the CDFIs’ range of services. Many CDOs are aware of and appreciate the CDFI services; but there is concern that the provision of capital for real estate, and the provision of technical assistance for real estate, should ideally be:
  - ✓ provided by an organization(s) specializing in community development real estate capacity building, not necessarily by organizations looking to close real estate deals;
  - ✓ provided in a more coordinated and strategic (versus competitive) way;
  - ✓ delivered with more of a strategic overlay that accounts for the range of real estate options, CDO capacity and differing real estate markets in Detroit’s multiple neighborhoods;
  - ✓ competitive (very low cost/patient) capital streams for single family rehab; and
  - ✓ offering support for alternative real estate models including co-operatives, community land trusts or other forms of community-based ownership.

Among some CDFIs, there is alignment on some of these CDO concerns. Even some CDFIs acknowledge they have not yet developed a cohesive or coordinated strategy for CDO real estate capacity building, although many of them are interested in creating such a strategy.

