



**DETROIT  
FUTURE  
CITY**

**ACQUISITION-  
REHAB PILOT  
PROJECT**



# ACQUISITION REHAB PILOT PROJECT

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Detroit Future City for Building the Engine of Community Development in Detroit

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## Overview

Stable, healthy, affordable housing is the critical thread that holds the fabric of a neighborhood together. The unraveling of that thread over time through vacancy and foreclosure impacts not only the market potential but also the human potential of a community. The renovation and occupancy of vacant homes can help reweave that fabric while providing shelter, stability, and wealth-building opportunities for people to reach their greatest potential.

Community Development Organizations (CDOs) have a special role to play in bringing vacant homes back to life. Rather than solely focus on increasing home sales and property values, CDOs focus on people and place. They reconnect the threads of fabric – incorporating resident voice in neighborhood planning, providing pathways to home ownership and uplifting the power of ownership through the assembly of resources and advocacy for rights.

Neighborhood stabilization is also an important goal for Detroit City government and the Detroit Land Bank Authority (DLBA). The Land Bank is the largest owner of vacant houses in the City. Getting more of these homes renovated and occupied by new homeowners has been a top priority of the Duggan Administration.

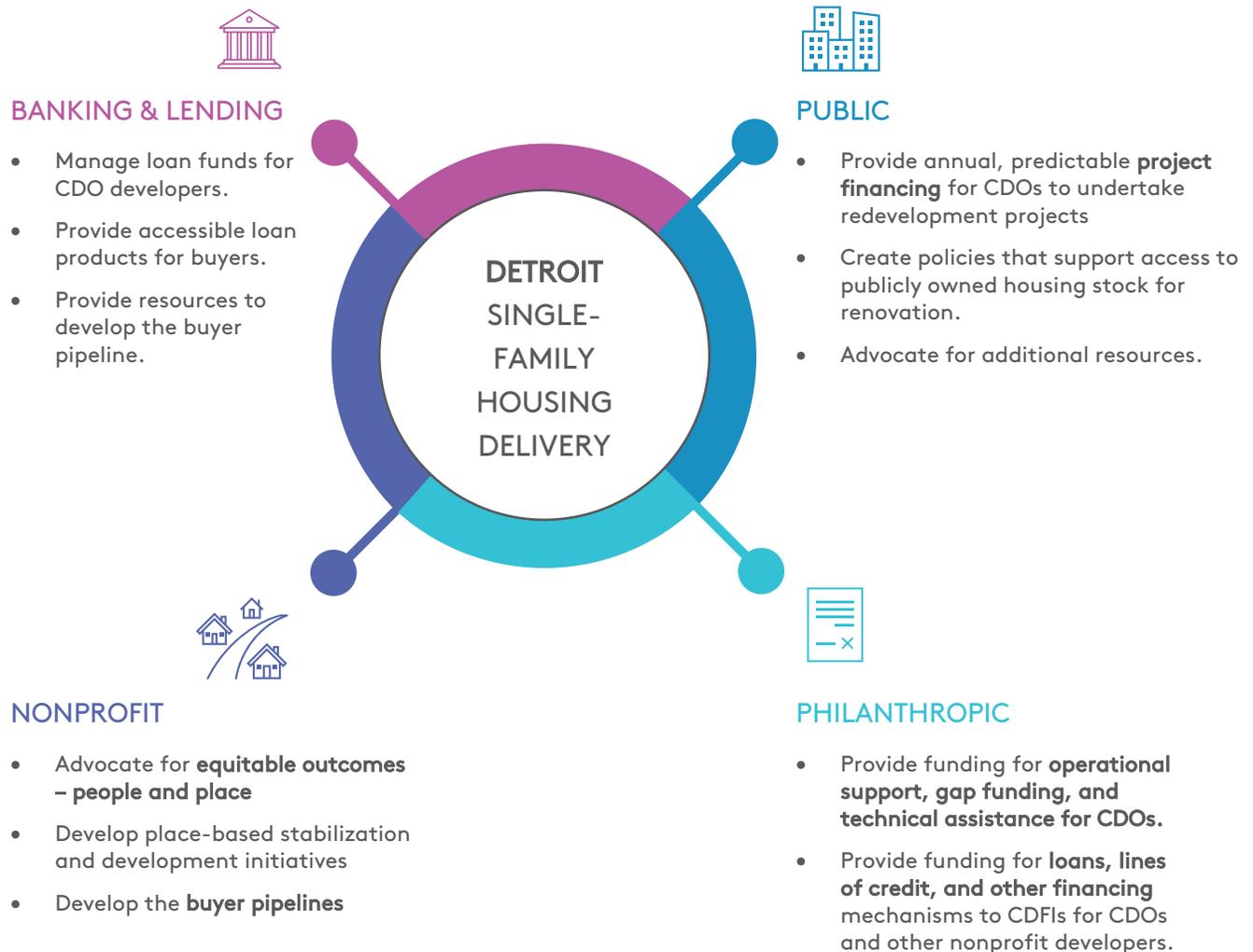
Recognizing this commonality of goals, Detroit Future City, under the auspices of the Detroit Neighborhood Housing Compact and with support from Building the Engine of Community Development in Detroit (BECDD), began convening a group of CDOs, as well as representatives from the City's Housing and Revitalization Department (HRD) and the DLBA. The purpose was to explore the potential to create a new collaborative program for increasing the number of vacant homes renovated and sold to new home buyers each year by Detroit CDOs.

The participating CDOs included Bridging Communities, Central Detroit Christian CDC, Genesis HOPE, Eastside Community Network, Grandmont Rosedale Development Corporation (GRDC), Joy Southfield CDC, Osborn Neighborhood Alliance and USNAPBAC. These organizations have varying levels of experience with and capacity for single-family housing renovation, but all have an interest in expanding this area of work.

What emerged from these discussions was a concept for a comprehensive system to support single-family acquisition, renovation, and resale of vacant homes by CDOs and a proposal for a pilot project involving the eight participating CDOs.

**The purpose of this report is to provide an overview of the systems-level components that are needed for a comprehensive single-family housing delivery system, and to describe the pilot project model recommended by Detroit Future City (DFC).**

DFC is confident that this framework could not only test a new way of engaging the single-family housing delivery system at scale but could prove that doing so brings about more equitable outcomes for residents and neighborhoods. In addition to the renovation of housing, this model is intended to deepen relationships between CDOs and the City, build capacity within the community development and housing rehabilitation sectors, and to provide a baseline assessment of collaboration and impact.



# System Elements

Many CDOs are eager to undertake home renovation and resale projects in their communities but lack the systematic supports needed to develop and sustain renovation programs. There has been no systematic support for the purchase, renovation, and resale of vacant single-family homes by the non-profit sector in the City of Detroit for several years. Some individual CDOs, such as Grandmont Rosedale Development Corporation, Central Detroit Christian CDC and Bridging Communities, have pieced together resources to continue renovation programs on their own, but the number of projects completed has been limited by available resources. The Detroit Land Bank Authority (DLBA) created the Community Partners Program to make vacant property available at discounted costs for renovation by community-based organizations, but participating organizations are on their own to find the resources needed to develop these projects. It is critical to develop and sustain systemic supports and organizational capacities within the ecosystem to specifically sustain CDOs.

The working committee of CDO, HRD, BECDD and DLBA representatives convened by DFC identified several important elements of an effective single-family purchase/rehab/resale program. The chart below identifies these elements and indicates the sectors that are most connected to each. To achieve an effective program, all sectors must work in tandem to have sustained impact and scale.

## Elements of an effective single-family purchase/rehab/resale program

	Public	Philanthropic	Non-profit	Banking & lending
Gap funding	○	○		
Loan capital		○		○
Housing stock for renovation	○			○
Pipeline of buyers			○	
Financing for buyers				○
Down payment assistance	○			○
Homebuyer counseling	○		○	○
Construction contractors				
CDO operating, TA, and capacity building	○	○	○	○

What follows is a brief summary of the system elements identified in the chart above, highlighting the issues raised within the pilot program committee discussions and considerations for how to improve each system element.

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## Gap funding

With the existing condition of Detroit’s housing market and the low housing values in most of Detroit’s neighborhoods, the total development costs for a typical renovation project will exceed market value in most Detroit neighborhoods. Gap funding, usually in the form of grants or forgivable loans, is necessary to make most projects feasible, without reducing rehab standards. The size of the gap will depend on many factors including housing size, housing condition, level of renovation, resale value and funder requirements. A combination of public and philanthropic funding is needed to fill funding gaps. **There should be clear processes and criteria set for multiple CDOs to access gap funding.**

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## Loan capital

Project financing is the fuel that makes the whole system go. The amount of capital available, and on what terms, will influence the number of projects that are feasible and shape other aspects of the delivery system.

For any system to be scalable beyond a small number of housing units, it cannot be reliant on grant funding alone. Some form of revolving credit is needed to maximize the leverage of limited grant dollars. Credit sources should be predictable with clear underwriting standards for both projects and borrowers so that CDOs can develop feasible projects with confidence that financing will be available. **A loan fund should be created that could serve multiple CDOs with a CDFI serving as the fund administrator.**

## Loan capital Financing models

**HOME Program Model:** The federal Home Investment Partnership Program (HOME) has been used to finance the renovation and sale of vacant single-family homes. However, these funds have become less available over time and are not generally available for single-family projects today. Nonetheless, the HOME program could provide a model for non-federal programs.

Under this model, funds are provided as a project loan to be repaid at the time of resale to a new home buyer. However, these loans generally exceed 100% Loan-to-Value (LTV) with the understanding that a portion of the funds will be forgiven at the time of resale to fill any project “gap”.

An advantage of this model is that one intermediary could manage both the loan and grant portions of the project financing within a single transaction. Funds could also be committed on a project-by-project basis to ensure that funds are used only as needed. A disadvantage is that the CDO would not control any pool of funds and may need additional working capital for predevelopment activities.

**Loan + Grant Model:** Under this approach, the loan and grant portions of the financing come from separate pools. An example of this approach would be GRDC’s 2010-2013 rehab program. GRDC had a revolving line of credit from Detroit Development Fund and a pool of philanthropic funds from the Kresge Foundation, Wells Fargo Bank and others. Loans for each rehab project were underwritten separately and capped at 70% LTV. GRDC managed the pool of gap funding separately and could draw on this fund to fill financing gaps as needed, until the pool was exhausted.

An advantage of this model is that the CDO would know how much gap funding it had at its disposal and could manage that pool of funds flexibly to best fit its rehab strategy. A disadvantage would be that if the CDO is not actively developing new projects, the grant funds may sit idle and go unspent.

## Loan capital Financing variations

**Land Contracts:** The two basic models described above assume that rehabbed homes will be sold to new home buyers using mortgage financing to purchase the home. Thus, the buyer's new mortgage would be the source for repayment of the development loan to the project. Some CDOs, such as Bridging Communities, have sold homes to new buyers using land contract financing. This approach allows CDOs to serve home buyers who cannot access traditional mortgage financing due to credit issues or low-value homes and to sell homes with limited rehab. To scale up this approach would require that CDOs have access to longer-term patient capital that is not due upon sale of the rehabbed property.

An advantage of this approach is the greater flexibility provided to CDOs. A disadvantage is that it requires CDOs to take on land contract servicing as an additional responsibility. Long-term funds may also be more difficult to obtain. For the purpose of this collaborative pilot project, it is assumed that homes will receive at least a basic code-compliant level of rehab and not be sold in as-is condition.

**New Markets Tax Credits:** Develop Detroit has recently utilized New Markets Tax Credits (NMTC) to finance single-family renovations in Detroit. This is an unusual and innovative approach to financing this type of project. Develop Detroit has partnered with neighborhood based CDOs to implement this strategy and has expressed the desire to do more in the future. Through this approach, equity is raised through the sale of tax credits and some of that equity can be left in the project at the time of resale to fill the funding gap. The complexity of NMTC financing, however, suggests that while this may be a component of a rehab delivery system in Detroit, other funding strategies will also be needed.

**Detroit Home Mortgage Program (DHM):** DHM was designed to finance the purchase and rehab of single-family homes by individual home buyers. A related program was developed to use the DHM tool to support purchase/renovation/resale by private developers but drew limited interest from developers and has been discontinued. A similar off-shoot of the DHM has been considered for non-profit CDOs. Under this strategy, home buyers would be encouraged to obtain DHM mortgages to pay the entire development costs of each project (in excess of 100% LTV), thereby reducing or eliminating the need for gap subsidies. A grant-funded loss reserve would backstop losses by the CDO in the event that a DHM buyer could not be found. As with NMTC, this approach would work best in neighborhoods with higher price points and quickly appreciating values and does not address the desire for promoting deeper affordability expressed by the participating CDOs.

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## Housing stock for renovation

The DLBA participated in the pilot program working group and showed a strong willingness to support this effort. The DLBA has an existing Community Partnership program that makes vacant properties available to CDOs at a discounted price. The DLBA also has a “hold and maintain” policy by which properties can be held aside for specific community partners in order for the partner CDO to conduct predevelopment activities prior to acquisition. The DLBA has thousands of properties in inventory, although inventories are limited in some of the CDO target areas. DLBA inventory tend to be in poor condition and in need of very substantial rehabilitation. As such, current DLBA inventory should not be the only homes considered by CDOs for renovation. **If non-DLBA property is utilized, acquisition prices will be higher, but there may be some savings on construction costs, depending on the condition of the property acquired,**

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## Pipeline of buyers

The ultimate success of any purchase/rehab/resale program depends on the availability of buyers for renovated homes. This can be a challenge due to low buyer demand in many areas of the city. An additional challenge is the difficulty many buyers have obtaining the financing necessary to purchase a home.

**Developing a pipeline of potential home buyers who are financially capable of purchasing a home should go hand in hand with developing the units for sale.**

This will require support for homebuyer education, flexible financing options and a neighborhood marketing strategy. Any home sales program should be tied to a larger strategy for neighborhood stability and quality of life improvement. For most buyers, the neighborhood environment is as important as the home itself when choosing where to purchase.

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## Financing for buyers

A variety of financial products already exist for qualified home buyers. **Efforts are needed to help more buyers understand and qualify for the mortgage products that exist.** Additional specialty products, such as the Fresh Opportunity Mortgage [which is mortgage product offered by Opportunity Resource Fund that provides flexible credit underwriting and makes small mortgages] should be expanded to provide greater underwriting flexibility and serve a broader range of homebuyers and neighborhoods. Some CDOs have also utilized land contracts as an even more flexible source of purchase financing, but this strategy requires that the CDO have some longer-term sources of capital as discussed above.

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## Down payment assistance

Down payment assistance (DPA) is an important tool for increasing home buyer demand and enabling more people to access home ownership. Lack of cash on hand

is a major obstacle for many would-be home buyers. DPA can also improve affordability by lowering the principal amount financed through a purchase mortgage. DPA is available from a variety of sources including MSHDA and the DHM Program lenders. Bank of America also has a current DPA program and other lenders offer their own programs from time to time.

**Without some form of down payment assistance available for buyers, a scaled-up renovation program will have difficulty selling units.**

The HOME Program described above had DPA integrated into its financing model. In addition to forgiving a portion of the development loan at the time of sale to provide a gap subsidy, a portion of the funds repaid to the City or MSHDA would be returned to the buyer in the form of DPA, generally as a forgivable soft second mortgage that was extinguished over time. Through this mechanism, homes were sold at market value to strengthen the neighborhood housing market, but individual buyers received DPA subsidies to bring their mortgage in line with what they could afford.

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## Homebuyer counseling

Some CDOs have internal capacity to counsel and qualify home buyers. This is not a capacity that each CDO needs in-house, as collaboration among CDOs and with other home buyer counseling agencies can fill this need. However, the cost of providing these services should be factored into the overall program.

The City of Detroit Housing and Revitalization Department is in the process of establishing a network of Housing Resource Centers that can help coordinate the intake of potential homebuyers and direct them to the appropriate services and information. Three of the CDOs involved in the proposed pilot are expected to serve this role. **Homebuyer counseling – both pre- and post-purchase -- has been proven to increase the long-term stability of home purchasers.**

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## Construction contractors

Contractors are an integral part of an overall rehab delivery system. The shortage of construction contractors to carry out renovation work is a commonly expressed concern among CDOs. **Relationships with contractors will need to be cultivated. If a steady flow of projects can be created, this could have the benefit of attracting more contractors to bid on the work.** It will be important to consider strategies for mitigating obstacles faced by small, minority-owned contractors to ensure equitable access to construction contract opportunities. Likewise, loan products should seek to streamline payment processes as much as possible to facilitate contractor cash flow.

CDOs are open to exploring collaborative approaches to recruiting and developing a base of contractors to draw from. One CDO, Central Detroit Christian CDC, has gone so far as to establish their own contracting company to work on their projects.

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## CDO operating support

Operating support will be needed for CDOs to develop and sustain the capacity to carry out purchase, rehab, and resale activities. All CDOs participating in the pilot project are receiving operating support from philanthropy, but it may not be sufficient or dedicated to rehab activities. At least one dedicated project manager would be needed in each organization to achieve the volume of activity projected. Until that volume is reached however, there may be opportunities to share costs between CDOs. **To minimize operating costs and create efficiencies, CDOs are open to exploring collaborative approaches to project delivery, including sharing services between organizations.** For example, multiple organizations could share the services of a specification writer, or one organization may purchase services from another. As noted above, it

would not be necessary for every organization to provide home buyer counseling services when a few organizations with this capacity could meet the needs of the whole system.

The sale of renovated homes would typically generate revenue for the CDO, however as noted above, most projects will need grant subsidies rather than generate net profits. It is good practice for CDOs to include a project management or developer fee in their project budgets to generate income for the organization. This model assumes that these costs could be shared amongst the cohort. The HOME program, for example, would allow budgets to include a 15% developer fee to be included in the budget. In practice, this fee usually becomes part of the development “gap” that needs to be subsidized. While fees such as these are unlikely to cover all the overhead costs of the CDO, they do contribute to CDO sustainability and provide an incentive to increase production. Also, because developer fees are generally not earned until houses are sold, additional operating support is needed to get projects up and running before fees can be earned.

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## CDO technical assistance / capacity building

The CDOs involved in the pilot project development have varying degrees of experience and capacity to undertake single-family rehab and resale activities. Some have been engaged in rehab work for many years and others are just getting started. **At the heart of this proposal is the concept that a cohort of CDOs would be created to collaborate with each other – and with the DLBA and HRD – to develop a system that is mutually beneficial and that will build the capacity of all organizations involved.**

# Pilot Project Recommendations

DFC recommends the creation of a pilot project intended to lay the groundwork for a comprehensive system for single-family acquisition, renovation, and resale projects. This pilot project has the following objectives:

- 1 Create a place-based, locally controlled neighborhood stabilization program.
- 2 Ensure equitable outcomes for people and place – aiming to serve a range of household incomes, including incomes as low as 50% AMI, for accessible homebuying options.
- 3 Leverage the knowledge and skills amongst the partners and within the ecosystem to develop capacity and technical skills at the partner table.
- 4 Demonstrate productive partnerships between City government and the community development sector.

The pilot would use a cohort model to convene a group of CDOs to foster collaboration, capacity building and mutual learning. The eight CDOs that participated in development of this concept could be the initial cohort.

## Project Coordination

DFC proposes to serve as the coordinator of the pilot project. This role would include:

- convening the cohort of CDOs
- designing and hosting learning sessions for CDO capacity building
- identifying one or more CDFIs to structure and manage a revolving loan fund
- identifying potential sources of gap funding
- facilitating collaboration between the public, non-profit, philanthropic, and financial sector stakeholders needed to support the project
- engaging project evaluators
- Coordinating homebuyer pipeline development activities

DFC already convenes the Detroit Neighborhood Housing Compact, a broad cross-sector collaborative focused on improving single-family housing in Detroit neighborhoods. The Compact will provide an excellent forum for incorporating a broad group of stakeholders in the design and execution of the pilot project.

# Pilot Project Budget

The following budget is based on the goal of renovating and selling 80 single-family units over a two-year period at a cost of approximately \$8 million dollars. Budget components include revolving loan capital, gap funding, operating and capacity-building funds for CDOs, project coordination fees for DFC, and funds for marketing and buyer pipeline development.

PILOT PROJECT BUDGET		
<b>Revolving Loan*</b>	<i>Acquisition, rehab, resale</i>	<b>\$4,656,000</b>
<b>Gap Funding</b>	<i>Funding to make acquisition/rehab/resale feasible</i>	<b>\$1,890,000</b>
<b>DFC Project Coordination</b>	<i>Technical assistance, back-office, evaluation</i>	<b>\$445,000</b>
<b>Organizational capacity</b>	<i>Capacity &amp; project admin for 8 CDOs over two years</i>	<b>\$ 1,200,000</b>
<b>Buyer Pipeline</b>	<i>Pre-/post-purchase counseling; other buyer attractions</i>	<b>\$100,000</b>
<b>TOTAL</b>		<b>\$8,291,000</b>

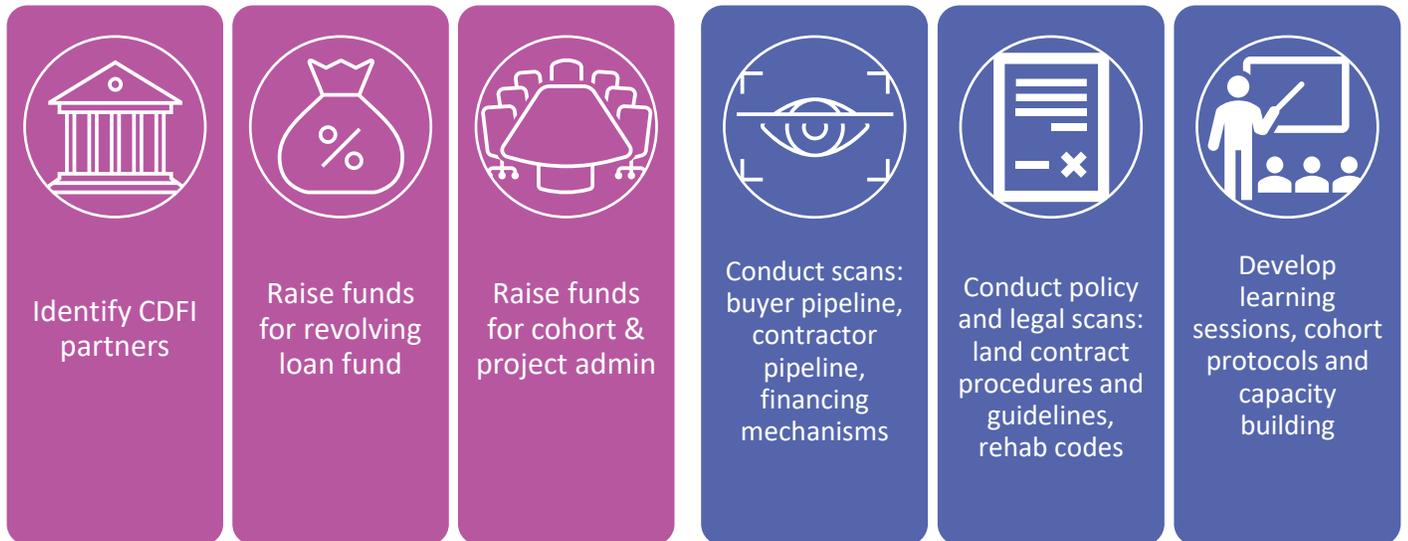
*\* This budget is based on a typical project cost of approximately \$80,000 and a subsidy of \$23,000 per unit. This assumes a small home and a modest level of rehab only. Unit costs could increase significantly based on house size and condition, level of rehab performed, resale value and specific requirements tied to funding sources. It is also assumed that all units will be acquired from the DLBA at nominal cost to the CDOs through its Community Partnership Program to support this program. If other sources of property are used, higher acquisition costs would need to be considered.*

# Next Steps

There is a growing recognition of the fundamental role that CDOs play in the process of neighborhood stabilization and that housing renovation – not just demolition – is needed to strengthen Detroit neighborhoods.

This Pilot Project has already generated significant interest from the City of Detroit and the DLBA. The critical next step is to identify one or more CDFI lending partners and sources of grant funding for filling project gaps and supporting operating, coordination, and capacity-building expenses. This process is already underway. Once funding sources and parameters are identified, DFC is prepared to move forward to convene the CDOs and other partners necessary to implement the systematic program of support and capacity building for single-family acquisition, renovation and resale that our communities need to rebuild and thrive.

## Next steps



Pilot Project | CDO Boundaries | Strategic Neighborhood Fund Overlay

