COVER STORY

A Challenging Market

by Nancy Wojcik

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As an assessor, the 2008 assessment looks to be my toughest assessment ever, both in setting values and in defending them. The real estate market during the past year caught many people by surprise. We had moved assessments upward over the past few years in response to what we thought were phenomenal sale price increases. I remember in 2005 when the average sale price in Brooklyn Center was $189,900. The appraisers were commenting that there seemed to be a few too many sales at prices of $230,000. We had a feeling that something just wasn't quite right, but the market transactions appeared valid. Sale prices were moving upward and falling interest rates appeared to be driving those prices up. In Brooklyn Center, which I would consider an "affordable" community, people were beginning to own more than one home, and sometimes as many as three, with "relative" occupants. As an assessor's office, we were ever so cautious about increasing assessment values, but moved them upward each year based on the open market sales.

In the City of Brooklyn Center, the assessment of an average 1,000 square foot rambler increased 37 percent over six years, from $142,700 in 2001 to $195,200 for the January 2, 2007, assessment. Sales data were plentiful in the early years with approximately 400 to 500 sales per year, with only 20 percent of the sales rejected as non-open-market transactions. In 2006 and 2007, the total number of sales began to decline, but investors continued to buy properties, stripping out the equity to finance other properties. Early data in 2007 (January to April) showed the median sale price of residential property at $200,500.

In hindsight, I can now see the issues that came together to create this perfect storm. Soon after the completion of the 2006 Local Board of Appeal and Equalization, the number of non-homestead and rental properties increased. To control the growth in the number of rental properties, the city increased the cost of the rental license and began requiring rental inspections. The number of residential properties penalized for delinquent utility bills and unmowed grass more than doubled. At the same time, the Brooklyn Center Code Enforcement Division was reporting an increase in vacated properties within the city.

For the 2007 assessment, we reduced the estimated market values of 1,200 residential parcels, but overall the assessment of residential property showed a 2.8 percent increase. Our office fielded numerous calls, but we felt the sales data were good. Reduced listing prices appeared to be more of a personal choice to sell a property quickly. Properties that remained on the market longer were able to get close to their asking price.

By the time of the Local Board of Appeal and Equalization on May 1, the market was already turning. When the truth in taxation notices hit mailboxes in November, the citizens of Brooklyn Center had become skeptical. We began to receive phone calls from taxpayers loudly asking us if we "ever watched the news," had we "stepped outside of our office," or "how could we raise values and taxes in the current real estate market?" Educating citizens about the complicated Minnesota tax system, let alone the timing of the property valuation notice as of the assessment date, was a lesson in patience. Trying to explain the date range of sales that are used for the assessment date was more than complicated. We were talking with the owners in May of one year trying to describe how we calculated their estimated market value based on sales from October a year and a half ago through the previous year's September. When explaining the assessment dates to citizens in person, we could watch the glazed-eye look appear, and know we had lost them soon after "hello."

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The City of Brooklyn Center had 11 appearances at the 2007 Local Board of Appeal and Equalization, the largest number ever. One of the appearances at the board was by a local realtor who owned a property for investment purposes. He argued to the board that the forced sales and lower prices were the market. The Local Board of Appeal and Equalization reduced his value slightly, based on the recommendation of our office, but the board had no idea of what was to come. Even though the number of calls we received from the value notice mailing had not increased, the intensity of those calls was wearing all of us out.

We had to explain over and over that only open market sales are used. While we were telling citizens to get a market analysis of open market sales from a local realtor, realtors were telling homeowners that the foreclosures and short sales were the market and that the sale price estimate in their market analysis had to compete with these lower-priced properties. It was the first year that we received calls regarding the estimated market values consistently throughout the entire calendar year. Every story the media released on taxes or value created a swarm of Monday-morning phone calls—a phenomenon that continues to this day.

In addition, Brooklyn Center had many properties that in 2006, were still receiving the benefit of the state's limited market value tax cap program. The 2007 valuation notice was the final phase out year for most of these properties with value increases limited to 15 percent over the previous year's value or 33 percent of the difference between the current market value and the previous year's assessed value, whichever was greater. Owners were already calling on a daily basis wanting to know why we are raising their taxes when property values were plummeting. We knew at this point that the calls from the truth in taxation notices could be even worse.

After the 2007 Local Board of Review, we began to study foreclosure properties. We found that there were 61 properties foreclosed in 2005, and 134 properties foreclosed in 2006. Throughout 2007, there were 248 property foreclosures. That is a more than fourfold increase in annual foreclosures in Brooklyn Center from 2005 to 2007.

Meanwhile, as a city, we were becoming overwhelmed with code enforcement issues, vacant homes, and non-licensed rental properties. During 2005 and 2006, abundantly available sub-prime financing encouraged many citizens to purchase property as an investment to build equity and collect easy rent. Non-homestead properties increased from 586 in 2005 to 824 in 2007. The majority of these properties cannot generate enough rental income to cover the upwardly adjusting mortgage payments, and their owners cannot sell or refinance now that sale prices have dropped lower than the original mortgage amount. These circumstances have caused owners of some of the 443 total foreclosures in the city to just walk away from their property. Adding to the financial stress on investment property owners was the city's decision to crack down on rental properties and double the rental license fee to $450.

In addition to the turbulent market changes, mortgage fraud is surfacing everywhere we turn. During the sub-prime financing era of 2005 to 2007, many people were talked into investment scams. People were willing to put their names on financial documents, contract for deeds, and similar instruments, to purchase property with the understanding that a property manager would handle everything else for them. These people knowingly—and unknowingly—became what is now known as "straw-buyers."

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The original owner may have put money down on the property, but in most cases we are finding 80/20 financing with minimal down. The straw-buyers usually received enough money from the property manager to cover the down payment and were told that the rent received would cover the property manager's fees, the mortgage payment, and the utilities. The straw-buyers were told they would make all their money upon the future sale of the property in two years.

While there may have been a tenant paying rent for the property, no payments were ever made to the mortgage company. Now the property is taken by foreclosure along with the buyer's credit for at least seven years. Meanwhile, the property manager is still collecting the Section 8 rental subsidy. The renter has been evicted and is unable to get his or her deposit back. The mortgage company is sitting on a property for which it has never received a payment and even owes money for all the utilities.

The city has spent much time and resources investigating owners and bad sales. It forwards the information obtained to local police, county authorities, the U.S. Commerce Department, and the Federal Bureau of Investigation to aid in the prosecution of those responsible for fraudulent sales. We are now finding that all the sales we thought were artificially high were, in fact, fraudulent sales.

The City of Brooklyn Center has now finalized the 2008 assessment, and while all the checks and balances are in place, I have never been so unsettled in my 16 years in assessment. We went through the sales with a fine-toothed comb, calling and verifying open market transactions that appeared far too low to be accurate.

The positive item we take forward is that a residential lot sale with an increase to the land value was defendable, and lowering the structure values was accurate. Recent listings for the city's river and lakefront properties have either expired or sold for reduced prices, but did not show as extreme a decline as non-waterfront properties. We watched the total number of foreclosures climb to 446, or 5 percent of the taxable parcels. We've watched the residential sales data decline from 524 open market transactions in 2005 to 182 open market transactions in 2007. Our sales have changed as well. For the 2008 assessment, a startling 54 percent represented open market transactions while 46 percent were rejected sales. Overall, there was a total decline in all sales from the previous year of 48 percent.

After seven years of consistent increases in residential values, we had to make a substantial decrease of approximately 8 percent for the 2008 residential assessment. Just one month after the January 2 assessment date, we found that the 2008 open market sale prices had dropped an additional 6 percent from our 2008 submitted assessment values. As we prepared for the 2008 Local Board of Appeal and Equalization, we found that we couldn't forecast what would happen even four months out.

Because our assessment jurisdiction covers the city, our property information has become a tool for all departments to track, watch, and study the community. What had before been only a tax assessor's office has now become central to the inner-workings of a forecasting tool for the community. I have been placed on census committees, served on rental strategy committees, and become a foreclosed property watchdog.

It has now become my mission to advise city staff on how to maintain existing housing stock. As I research the foreclosures for city staff, I am finding that certain owner names sometimes show up once, twice, and even three times on the sheriff's sale list, and in more than one jurisdiction. We now are receiving calls from renters who need help in finding out when and why they are being evicted, after they have seen the foreclosure notice posted on their door. The city's code enforcement inspectors are deluged with vacant homes where the occupants disappeared in the night leaving garbage and water running at the property. The city policy to *not* shut off the water has now become a nightmare as disgruntled owners and renters kick in the piping or just shut off the heat so the water freezes in the pipes or produces a green mold forest for us to find. We now scan the active listings in the Multiple Listing Service (MLS) for terms such as "as-is," "mold," and "freeze damage" so that housing inspectors can be sent out to tag the property as "unfit." In addition, we have learned to play private detective to try to locate a responsible party for vacant and foreclosed properties. I review the active MLS listings every day only to find increasing numbers of properties falling below $100,000, and check our property characteristics to verify the condition of the property.

In preparation for the 2008 Local Board of Appeal and Equalization, we decided that a digital photograph of every home in the city would assist our handling of valuation appeals. It would give us the ability to visually review every comparable property sale as we talked to citizens on the phone. There were only a few sections that had not been converted to digital, so the staff was directed to go out to those areas to obtain digital images. What they found down almost every street was very sad. Virtually every street had foreclosed or vacated properties. The "for sale" signs lined the streets and citizens told them how adjacent vacant properties were affecting the sale prices of their homes.

As a community, we can only hope for a market correction, but estimates that it may take up to 60 months for all financing to move through the system are heart wrenching. We have homeowners who are unable to escape sub-prime mortgages by refinancing because the appraisal of their property would come in at less than their current mortgage. Homeowners who chose to remodel and improve their homes using home equity loans are also being trapped by rising payments and the inability to refinance.

As I write this, I think about the elderly couple who came into our office in January expressing an interest in selling their property and moving into a townhome. They had a lovely house that had been entirely remodeled and included a large family-room addition. This property is quite a bit larger than our average home in Brooklyn Center. The estimated market value for 2007 had been $205,000. A local realtor they had called about possibly listing their property advised that they should list for $150,000. They were in shock. Needless to say, so was our office. After researching sales, the realtor had underpriced the property to move it quickly. After studying the sales with the assessor's office, the owners decided to get several realtors' opinions of a fair market sale price. Even the realtors are now struggling to get sales, and preying on scared citizens to compete against foreclosure and short-sale pricing. Although time is the best answer we can give to citizens who ask us what will fix this problem, the unfortunate reality is that some of them won't be able to wait long enough for the solution. ■

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Sign of the Times

A note from the managing editor

Recently, I was transporting my son to an appointment (dentist, doctor, soccer, volleyball, or [*insert child's activity here*]). As I drove beneath a railway underpass, I caught a glimpse of a hastily erected roadside sign. with a message that caught my attention. It was one of those signs that crop up overnight, dotting the landscape of backroads and waste areas with urgent messages about earning more income at home, losing weight quickly, or achieving the perfect lawn. As the sign's image flashed in my mind's eye, I felt sure it had read "Tour Foreclosures by Bus." I also thought I saw a Web address.

Intrigued, I made a point of returning that way to get a closer look. Sure enough, www.tourforeclosuresbybus.com is a real site and yes, they do offer foreclosure bus tours.

A realtor in upscale Naperville, Illinois, started these regularly scheduled group excursions to view and tour foreclosure properties throughout the Chicago metropolitan area. For $50, participants get to ride in comfort and view six to eight foreclosure properties per trip accompanied by a running commentary about features, property condition, and other pertinent details. The tour includes a walkthrough of each property and it even includes lunch.

For a slightly higher fee, the realtor will arrange a tour of "luxury" higher-end homes that are in foreclosure. These exclusive properties are offered at a discount for the next 72 hours. After that, they are listed at "market" price. The Web site does not indicate if you get a better lunch on the luxury tour.

The realtor running the tour service also offers to facilitate short sales, negotiate with lenders, and connect potential buyers with other real estate services such as home inspections and contractors.

Challenging markets certainly provide interesting opportunities to creatively sell properties.