WRAP AROUND MORTGAGES IN A BRONX NEIGHBORHOOD

A Study of the Correlations Between Mortgage Financing and Building Conditions

The City of New York Commission
On Human Rights
Neighborhood Stabilization Program
52 Duane Street
New York, New York 10007

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The City of New York

COMMISSION ON HUMAN RIGHTS

52 DUANE STREET, NEW YORK, N.Y. 10007

Telephones: 566-5050 TTY 566-3913 TTY 673-6974

DR. MARCELLA MAXWELL, *Chairperson*
S. TED ANTHOLES, *Vice Chairperson*
ALBERTA B. FUENTES, *Executive Director*

Fellow New Yorkers:

I am very pleased to forward a copy of Wrap Around Mortgages In A Bronx Neighborhood to your organization. The Commission is making this report available to the public with the hope that it will stimulate awareness and understanding of a recent problem which, we believe, is burdening the housing situation of some of New York City's already beleaguered low and moderate income neighborhoods.

The goal of the Commission's study was to test the hypothesis that, "the financial history of a building (its owner turnover and debt service) can be surmised by assessing its building conditions," and, concomitantly, that those buildings with wrap-around mortgages would show both the highest number and degree of ownership turnovers and debt service, and the worst building conditions. The researcher's theory -- and our concern -- was that if this hypothesis proved to be true in one neighborhood, then similar situations may well prevail in others.

For anyone unfamiliar with building financing, this report provides a succinct, general description of standard mortgage lending practices. For those readers who are already expert, the report offers a step-by-step statistical analysis, detailing the correlations between a building's mortgage category and its number of building code violations, title changes, incidences of housing court litigation, mortgages granted, and its average rent per apartment. Information on virtually all of Stratton Park's multiple-family dwellings is used for the analysis.

The impetus for this report comes from the work of the Commission's Neighborhood Stabilization Program, which is designed to promote viable, stable, integrated communities. NSP helps foster neighborhood development and allay ethnic tensions by organizing structures and creating networks that address issues identified by residents and community groups. These issues are usually both survival and quality of life concerns, such as safety, housing, and economic development. For many communities like Stratton Park, the quality and maintenance of their housing stock is a primary concern that cuts across ethnic and religious lines. Our work with the residents of Stratton Park on these issues led us to conduct this study.

The Commission offers special thanks to Mr. Lou Zaneri, a former organizer with NSP's East Bronx Office. Mr. Zaneri researched and prepared this report.

As citizens concerned about the housing crisis in our city, I know Wrap Around Mortgages In A Bronx Neighborhood will be of interest to you. I hope that it is of both educational and informational value to you in your work.

Sincerely,

Marcella Maxwell

Marcella Maxwell
Chairperson

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INTRODUCTION

Background

During the 1960's and 1970's the number of bank mortgages granted to inner city neighborhoods declined. Savings and loan institutions, the traditional source of low-income interest credit, and commercial banks made it difficult for property owners, especially owners of multiple dwelling apartment buildings, to secure mortgages. Banks denied mortgages both for financing new home purchases as well as for rehabilitation and refurbishment by current owners. When this happened other creditors moved in to fill the void and supply the necessary financing -- private mortgages, purchase money mortgages, and more recently, the wrap-around mortgage.

Difficulty in obtaining bank loans contributed to the steady decline of once flourishing city neighborhoods. This decline usually began with the deterioration of multiple dwellings as maintenance and services were curtailed, which in turn precipitated a high turnover rate among tenants. Homeowners fled the area, fearing that the value of their houses would depreciate.

The decline in housing stock was often followed by a decrease in local commerce. Some businesses failed, others moved to a different area. Many of the remaining businesses hesitated to expand or reinvest.

When staff in the branch offices of the Commission's Neighborhood Stabilization Program (NSP) began developing services for residents and small business owners to stem neighborhood decline, they increasingly encountered the problem of non-bank, wrap-around mortgages. They found that these wrap-around mortgages made it even more difficult for tenants of multiple dwellings to resolve unhealthy, unsafe building conditions because the person controlling the cash flow for the building was not the actual landlord.

The NSP staff found that in many cases the outstanding debts on buildings with wrap-around mortgages were so high that landlords had to turn over virtually their entire rent roll to the wrap-mortgagees, which precluded the use of any surplus money for building maintenance and services. Moreover, there was a high incidence of foreclosures on these buildings because landlords had great difficulty maintaining any surplus capital. After each foreclosure, the wrap-mortgagee could resell the building, inflating the purchase price -- and the debt service -- even more.

To understand the total issue of wrap-around mortgages and the assumptions behind this study, it is necessary to understand how residential real estate financing works. The following discussion is an overview and explanation of current residential real estate practices and how the wrap-around mortgage is creating problems for our city's neighborhoods.

Residential Real Estate Financing

In most cases, land and buildings are not paid for with cash. Instead, part of the purchase is financed through a loan, with the property serving as collateral. That loan is called a mortgage. The person asking for the loan is called the mortgagor; the person or institution granting the loan is called the mortgagee. Banks, which includes both savings and loan and commercial lending institutions, grant the kind of mortgages with which most people are familiar. The terms of lending are strictly regulated by state or federal agencies, depending on whether the institutuion has a state or federal charter. Credit management standards developed since the Depression usually require that the loan amount (the mortgage) not exceed 80% - 85% of the appraised market value or price of the property and building.

Very often, these mortgages contain a provision called a "good repair clause." This provision gives the bank the right to foreclose on the loan if the owner does not keep the building in good repair. If the owner is found to be in violation of any city, state or federal building codes, the bank can foreclose on the mortgage even though all of the payments are up-to-date.

Banks, however, are not the only place purchasers or current owners can go to obtain a mortgage. When banks deny mortgages for buildings in areas they determine to be "risky," buyers and owners sometimes have little choice but to seek other sources of financing. The major source of alternative financing for mortgages is the private mortgage company or "mortgage banker."

These businesses' sole purpose is to buy, sell, and mortgage property.

The type of instrument (mortgage document) used by both banks and mortgage bankers is the same. Banks, however, are required by law to record all the mortgages they grant at the local property registry or county clerk's office. Private mortgagees, mortgage bankers who issue junior mortgages (second or third mortgages), are not subject to this requirement. There is a strong financial incentive not to record. In New York City the recording tax is 1.25% of the total mortgage amount. On a $100,000 mortgage, that's $1,250 saved. Thus, not only does the mortgage banker save money by not recording, he also eludes any careful monitoring of ownership transfers, which may be of concern to tenants.

A mortgage banker can finance the purchase of a building in the same way that a bank does, that is, by extending a loan to a buyer who is purchasing a building from someone else. The building serves as collateral for the bank's or the private mortgage banker's loan. But if the mortgage banker owns the building already (and, like any owner, is responsible for payments on previous mortgages), then he can sell it and provide a "purchase money mortgage" to the buyer.

The purchase money mortgage (PMM) is another type of private mortgage. In this case, the buyer does not seek independent financing to purchase the property. Instead, the seller grants a mortgage to the buyer in lieu of payment of some or all of the purchase price. This differs from conventional methods where the seller receives the full amount of the purchase price at the time of sale and relinquishes all holds on the property. For example, suppose you would like to buy a building that costs $100,000. You have only $10,000 and cannot get a bank loan (bank mortgage) to purchase it. The present owner says, "Ok, give me what money you have, the $10,000, and I'll grant you a $90,000 mortgage payable to me." After the sale, you would hold the title to the property but still owe the seller $90,000. This mortgage would probably have a higher interest rate than a bank mortgage for a number of reasons, but mainly because of the higher credit risk involved in the transaction.

In the cases of both the private and the purchase money mortgage, the new owner would make separate payments to the bank holding the original mortgage and to the private or purchase money mortgagee (the former owner). The new purchase money or private mortgage would be subordinate to the bank mortgage. If the new owner defaults on the loans, the bank will have first claim on the property.

Wrap-Around Mortgages

The last kind of private mortgage is a special kind of purchase money mortgage called "wrap-around mortgage," or "wrap" for short. Here, the owner sells or re-sells a recently acquired building and grants a wrap-around mortgage to the buyer. Wrap-around mortgages are most often used by private mortgage bankers.

This wrap-around or "wrapped" mortgage is like a purchase money mortgage, but has a number of interesting features. First, it gives the wrap-mortgagee, not the landlord (the new owner), first rights to the rent collected through an assignment of rent clause. The landlord still collects the rent, but the "wrapper" has a legal right to claim it if he wishes.

The second interesting feature of the wrap-around mortgage is that all payments due on any already existing mortgages (senior liens, i.e. banks) and the taxes are incorporated into the wrap-around mortgage payments. These previous obligations and the new wrap-around mortgage obligation are "wrapped" together into a large payment which is payable to the wrap-mortgagee, hence the name, wrap-around mortgage.

Using this money, the wrap-mortgagee pays off the bank, the taxes, and/or any other senior liens and takes his cut, too. This eliminates the possibility of foreclosure on any of the liens senior to the wrapper's which would wipe out the wrapper's interest (legal hold) on the property. As discussed above, the primary mortgagee, usually a bank, has first claim to a building if foreclosure on a current owner becomes necessary. If a mortgage banker issued a secondary mortgage on the building, his investment would be lost in the foreclosure action. The wrap-around mortgage, therefore, is a useful method for avoiding the financial risk involved in selling a building that has one or several outstanding senior mortgages.

Private mortgages, particularly wrap-around mortgages, can cause many problems. Since they are not regulated like bank mortgages, some purchasers who would not ordinarily qualify under standard credit review are granted loans. Unscrupulous mortgagees can prey upon unsophisticated people who wish to own a building. These mortgagees sometimes grant loans on a building that may not generate enough operating income (rent) to service the loan (debt service). The loan payment eats up too much of the operating income, leaving too little for services and maintenance. The owner, realizing that he can't make a profit, begins cutting down first on maintenance, then on needed repairs. Finally, services like heat and hot water are reduced.

Eventually the owner may default (fail to make loan payments). But this does not present a problem to the wrapper. Remember, he's paying the bank holding the primary mortgage and the taxes, too. The bank will probably remain uninvolved; it may not even be aware of the situation, since purchase money and wrap-around mortgages are not always recorded (see below). However, even if the bank was apprised of the building's problems, it would not necessarily enforce the "good-repair" clause of the original mortgage because the wrap-mortgagee is ensuring the timely payment of this debt. Furthermore, the wrapper still pays the property taxes, so there is no need for the city to get involved in this messy affair.

This process of foreclosure can actually benefit the wrap-mortgagee. The re-sale of the building will inflate the selling price and therefore the amount of loan necessary for a new purchase. For instance, returning to our earlier example, the owner buys a $100,000 building for $10,000 down and finances $90,000. Suppose the owner defaults in two years and the mortgagee (private, purchase money, or wrapper) forecloses and takes the building. He then resells the building for $120,000 (property appreciation). The new owner puts $10,000 down and finances $110,000. The mortgagee has thus made a profit of $20,000 (the new $10,000 down payment plus the $10,000 added to the new mortgage).

Many private mortgage bankers operate outside of government regulations, using several loopholes. One way is to establish many "dummy" corporations, taking care that each grants less than 20 mortgages per year. Another large loophole is that mortgages on buildings over 6 units (multiple dwellings) are exempt from the 20 mortgage limit. Finally, all purchase money mortgages, including wrap-around mortgages, are also exempt. Using these loopholes, mortgage bankers can issue as many mortgages as they wish. [See N.Y. Banking Law 590, et. seq. (McKinney) and Banking Law Regulations, "3 NYCRR" (Sections 79.1; 79.2; 410.3; 410.4.)]

Mortgage bankers can exert a considerable influence in a neighborhood through their investment in residential buildings, but unlike banks, their business is not covered by the Community Reinvestment Act (CRA). They are therefore not required by law to meet the affirmative credit needs of an area, including the needs of low and moderate income residents.

There is another way mortgage bankers obtain a financial interest in buildings. Once banks decide to divest their interests in an area, they will often pull out of their already existing mortgages. The banks will sell their mortgages on the secondary market, sometimes for a fraction of the outstanding face value. Mortgage bankers scoop up these bargain mortgages.

This is one way that the private mortgage banker can establish his stake in a community and begin his shell game of speculation and owner manipulation.

<u>A Case Study</u>

The following case-study of the tenant organization's enconter with their wrap-mortgaged building illustrates how the problem has surfaced for tenants and organizations working on housing issues in local communities. Our example is based upon the experiences of an N.S.P. staff organizer in the Stratton Park section of the Bronx, the area in which the study was conducted.

A tenant group confered with an N.S.P. staff person with whom they had been working to help them negotiate their problems. When the negotiations failed, the tenants decided to initiate a housing court action against the landlord. The building had typical wrap-mortgage problems: a broken front door, graffitied walls, littered hallways, an inoperative elevator, cracked plaster and peeling paint, sagging ceilings, plumbing leaks, and decrepit windows. Tremendous obstacles faced the tenants in their struggle to correct these conditions. Among these obstacles were:

- Inadequate enforcement and inspection of New York City housing codes due to budgets which are too small to provide enough city-wide inspectors.
- A housing court system unable to cope with the housing crisis in New York City. For instance, in this as in many cases, an ineffective set

of housing laws prevented the court from holding accountable the person actually responsible for the building's conditions -- not the landlord, but the wrap-mortgagee. This is the person, as discussed above, who controls the purse strings of the building and through whom the rent money filters.

- The primary mortgagee, a local savings bank, unwilling to exercise its option under the mortgage's "good repair clause" to foreclose for inadequate upkeep.

The tenant association was seeking the appointment of a 7a administrator, an arrangement used in situations when a court decides that a landlord operates a building without regard to the safety or welfare of the tenants. The same tenant association had been in and out of housing court for the past five years. They had "won" several court cases in which extensive repairs were ordered each time by the court. Nevertheless, these repairs had not been completed. Just two months prior to the current court action the Department of Housing Preservation and Development had sued the landlord for lack of heat and hot water. Significantly, in the past five years the building's ownership had changed hands five times: court orders against previous owners are hard to enforce against a new owner.

Three years before this current 7a case, the group had also petitioned the same court for appointment of a 7a administrator. At that time, their case was shot out from under them through foreclosure on the property by the wrap-around mortgagee. This same wrap-mortgagee, currently holding two of the four outstanding mortgages on the building, again filed for foreclosure against the current landlord in the new 7a case. The same thing was happening all over again.

Only the day before the tenant's case was to begin, another judge, in a different courtroom removed from the scrutiny of the tenants, appointed a receiver to administer the building in place of the landlord who had been forced out by the foreclosure action. The receiver's primary task was to protect the pecuniary interests of the wrap-mortgagee. So while the legal "ownership" changed hands again -- from the previous landlord against whom the tenants had filed their complaint to the new receiver -- the controlling interest in the building, the wrap-mortgagee, did not. Once again, these tenants, like so many others living in wrap-mortgaged buildings, were unable to affect the changes they sought.

The wrap-mortgagee in this case held two mortgages on the building. One was in his own name. The other was held by a corporation he owned. This same "wrapper" is one of several known by Bronx housing groups to hold many mortgages, thereby exerting a strong influence on apartment house financing in the Bronx.

PROJECT OVERVIEW

The curtailment of apartment building financing by banks and the concommitant deterioration of multiple dwelling housing stock is considered by many people who work on housing issues to be one of the primary indicators of redlining in a neighborhood. The assumption behind this study is that wrap-around mortgages are making a significant contribution to the process of neighborhood decline. Specifically, the goal of the study was to test the hypothesis that the financial history of an apartment building (its owner turnover and mortgages) can be surmised by assessing its building conditions. By confining the analysis of the relationship between building financing and building conditions to one neighborhood, we hoped to produce a report that demonstrated enough validity to generate further research in other city-wide areas.

Target Area

The target research area selected for the study was the Stratton Park neighborhood section of the Bronx, which is bounded by the Cross Bronx River Parkway and East Tremont Avenue. Its 25 square blocks contain 72 apartment buildings (of 6 or more units) concentrated in an interior corridor along Beach, Taylor, and Thieriot Avenues. Although almost every block contains an apartment building, the outer blocks mostly consist of private homes. This racially mixed, working class neighborhood is home for older Irish and Italian and newer Black and Hispanic residents. 1980 Census figures show that for Community Board #9 which includes the Stratton Park area, the racial makeup is 43% white, 31% black, 45% Spanish surname, 1% Asian, and 24% other. (The figures do not add up to 100% because many people respond with more than one ethnic category on census surveys.)

1980 mean income was $13,300 for Stratton Park, $14,739 for Community Board #9, $13,342 for the Bronx and $18,218 for New York City. Rents are comparable to other parts of the Bronx and the City. According to 1980 Census figures, multiple dwelling rents are:

Community Board #9	$229
Bronx	$220
New York City	$248

Today they are considerably higher.

METHODOLOGY

Data was gathered on the building conditions of every apartment building of six or more units in Stratton Park. Using computer analysis, we then compared this information against every building's financial history and looked for any relationships. As a measure for building codes, we used N.Y.C. housing code violations cited by the Office of Code Enforcement. The Bronx office of Code Enforcement had just completed an inspection "sweep" of the area during October and November of 1984, making that data very current and more accurate than any other available. Any housing court litigation brought against a landlord was used as a variable for building conditions. This included heat and hot water cases, comprehensive code enforcement suits, 7A administration actions, any emergency repairs instituted by the Department of Housing Preservation and Development, and housing court actions filed by tenants, obtained from H.P.D. and local community associations.

To represent the financial history of these buildings, we researched all mortgage histories and the number of title changes back to 1967 (18 years) through the Bureau of Property Registry. We looked at both the numbers and types of mortgages for each building and also gathered data on any public financial incentives the owner may have been granted. These included: low-cost public rehabilitation loans; including 8A loans, 312 loans, section 8 modification, participation loans; and J51 tax abatements. Finally, we were able to secure the aggregate rent rolls (total rents) for each building from the N.Y.S. Division of Housing and Community Renewal.

For purposes of analysis, the data was broken down as follows:

1. the total number of violation for each building divided by its number of units and violations per unit;

2. incidences of housing court litigation;

3. any building with a low-cost public loan tax abatement;

4. the number of title changes for each building since 1967 (i.e. number of times sold);

5. the average apartment rent in each building;

6. total number of mortgages granted on each building since 1967.

Each building was coded for one of the following six mortgage categories:

a. no mortgages granted;
b. bank mortgages only;
c. bank and public financing;
d. private broker mortgage;
e. purchase money mortgage;
f. wrap-around mortgage.

The mortgages were categorized in this manner for several reasons. Each of the categories (from no mortgages to wrap-around mortgages) represent, in ascending order, a probable increase in building debt service. Each building's outstanding debt would most likely include a bank mortgage. The private, purchase money and wrap-around mortgages would probably be second or even third mortgages (junior liens). Each of the mortgage categories represent, in ascending order, movement away from bank and financial regulatory standards towards unrestricted and poorer financial credit standards. Finally, in keeping with our hypothesis, the ascending mortgage categories would signify decreased landlord financial control and higher building ownership turnover.

All of this data was fed into a computer and reviewed for any significant differences among the six mortgage categories in:

1. violations per apartment;
2. turnover in ownership (title changes);
3. total number of mortgages granted;
4. incidences of housing court litigation;
5. tax arrears;
6. public financial incentives, and
7. apartment rents.

Using statistical procedures, we checked for:

1. statistical patterns;
2. correlations between the above six factors, assessing,
   a. the strength of these relationships, and;
   b. the probabilities associated with the results.

FINDINGS

The results of the statistical testing are displayed in Tables 1 through 8. Table 1 summarizes the crosstabulation results. Tables 2,3,4, and 5 are graphs which highlight the total number of mortgages, the number of title changes, the average number of violations per unit, and housing court litigations per building by the type of mortgage held on the building. Tables 2a, 3a, 4a, and 5a display neighborhood averages and averages of all non-bank and all non-private mortgage categories for the preceding tables. (Non-bank mortgages include private, purchase money, and wrap-around mortgaged buildings. Non-private mortgages include buildings with no mortgages, bank mortgages, and bank mortgages combined with public financing.) Each table displays the frequency of occurance for each variable under the mortgage categories. Table 6 presents the Chi Square and Pearson's results. Table 7 lays out comparison data for those buildings with non-bank mortgages and those without non-bank mortgages. In Table 8, comparisons are made between those buildings with purchase or wrap-mortgages and those without such mortgages.

TABLE 1

STRATTON PARK MORTGAGE STATISTICS

Type of Mortgage	# of Bldgs	% of Bldgs	Title Changes	VPU	Violation Range			Liti-Gation	Pub. Inc.	# of Mtgs.
					Low	Mid	High			
No Mort-gages	7	10.1	1.1	1.3	.57	.29	.14	.14	.29	0.00
Bank Only	13	18.8	1	1.82	.31	.31	.38	.23	.15	1.38
Bank Public	9	13.0	1.1	.9	.67	.33	0	.11	1.00	1.56
Private Mtg.	14	20.3	1.7	1.73	.36	.42	.21	.07	.21	1.86
Purchase Money	16	23.2	2.4	2.77	.13	.44	.44	.25	.06	2.38
Wrapped Mtg.	10	14.5	4.5	2.71	.10	.20	.70	.60	.10	4.5
Neighborhood Average	69	100	2	2	.32	.33	.33	.22	.26	1.96
All Non-Private	29	41.9	1.1	1.40	.48	.31	.21	.17	.45	1.1
All Non-Bank	40	58	2.68	2.39	.20	.38	.43.	.25	.13	2.73

EXPLANATION OF TERMS

Type of Mortgage	One of six mortgage categories previously mentioned
# of Bldgs.	Multiple Dwellings in Stratton Park
Violations VPU	Violations per unit (Total violations/# of units)
Violations Range	Three equal size categories representing ascending order of violations per unit
Lower	Lowest range of violations per unit category (below 1.05)
Middle	Middle range (between 1.05 and 2.39)
High	Highest range (above 2.39)
Litigation	% of buildings where litigation has been brought
Public Inc.	% of buildings granted low cost public rehabilitation loans or tax abatements
Total Mtgs.	Total # of mortgages granted on building since 1967
All Non Private	First three mortgage categories
All Non Bank	Next three mortgage categories

NOTES

All mortgage and title data reflect mortgages granted or title changes occurring since 1967 through 1984, and not the total mortgages outstanding on a building.

Since state law doesn't require junior liens to be recorded, the number of purchase money and wrapped mortgages may be higher.

Inspection data on one wrapped building is missing.

TABLE 2

TOTAL NUMBER OF MORTGAGES SINCE 1967

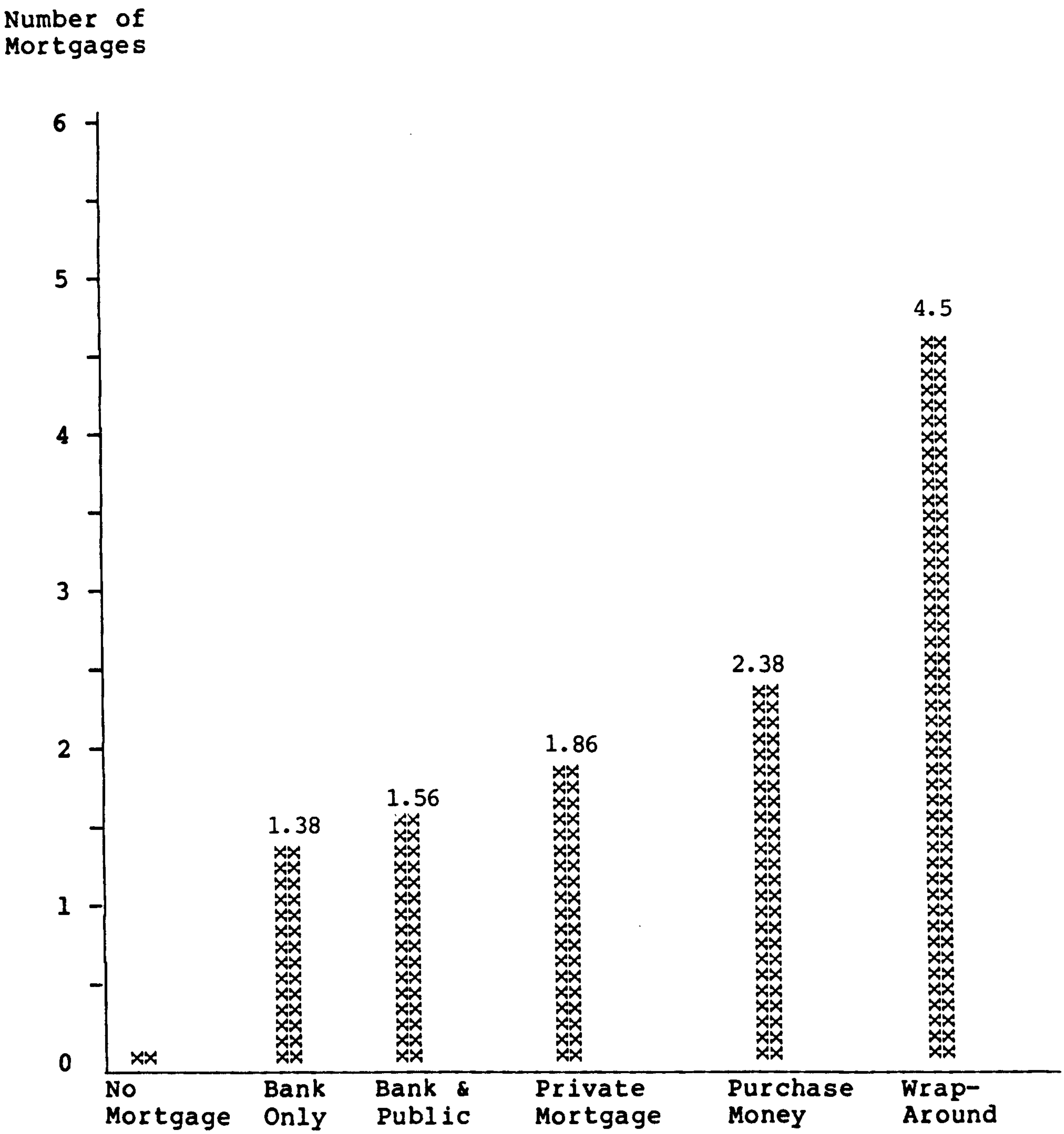


TABLE 2A

TOTAL NUMBER OF MORTGAGES SINCE 1967

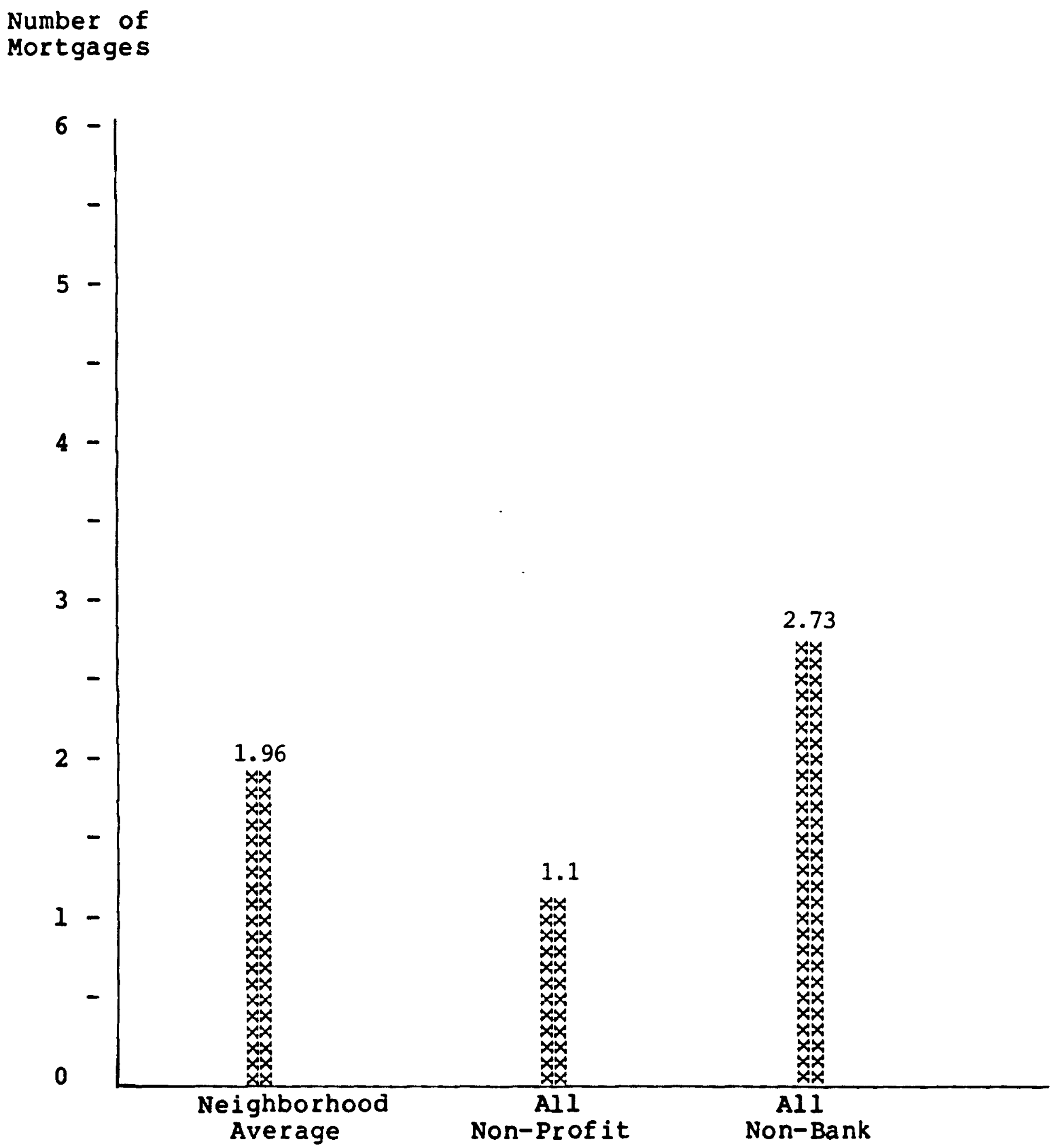


TABLE 3

TITLE CHANGES: OWNERSHIP TURNOVER SINCE 1967

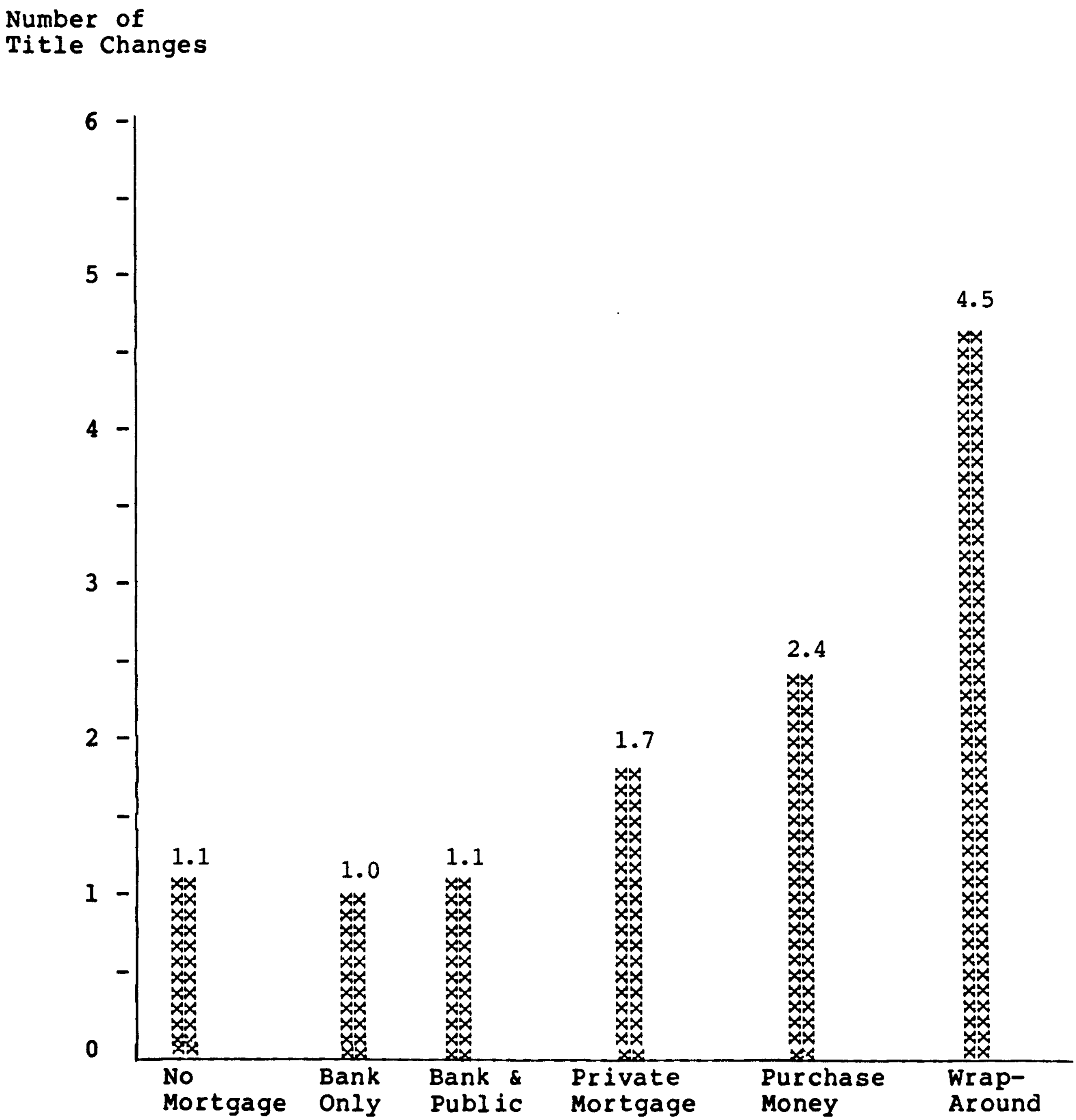


TABLE 3A

TITLE CHANGES: OWNERSHIP TURNOVER SINCE 1967

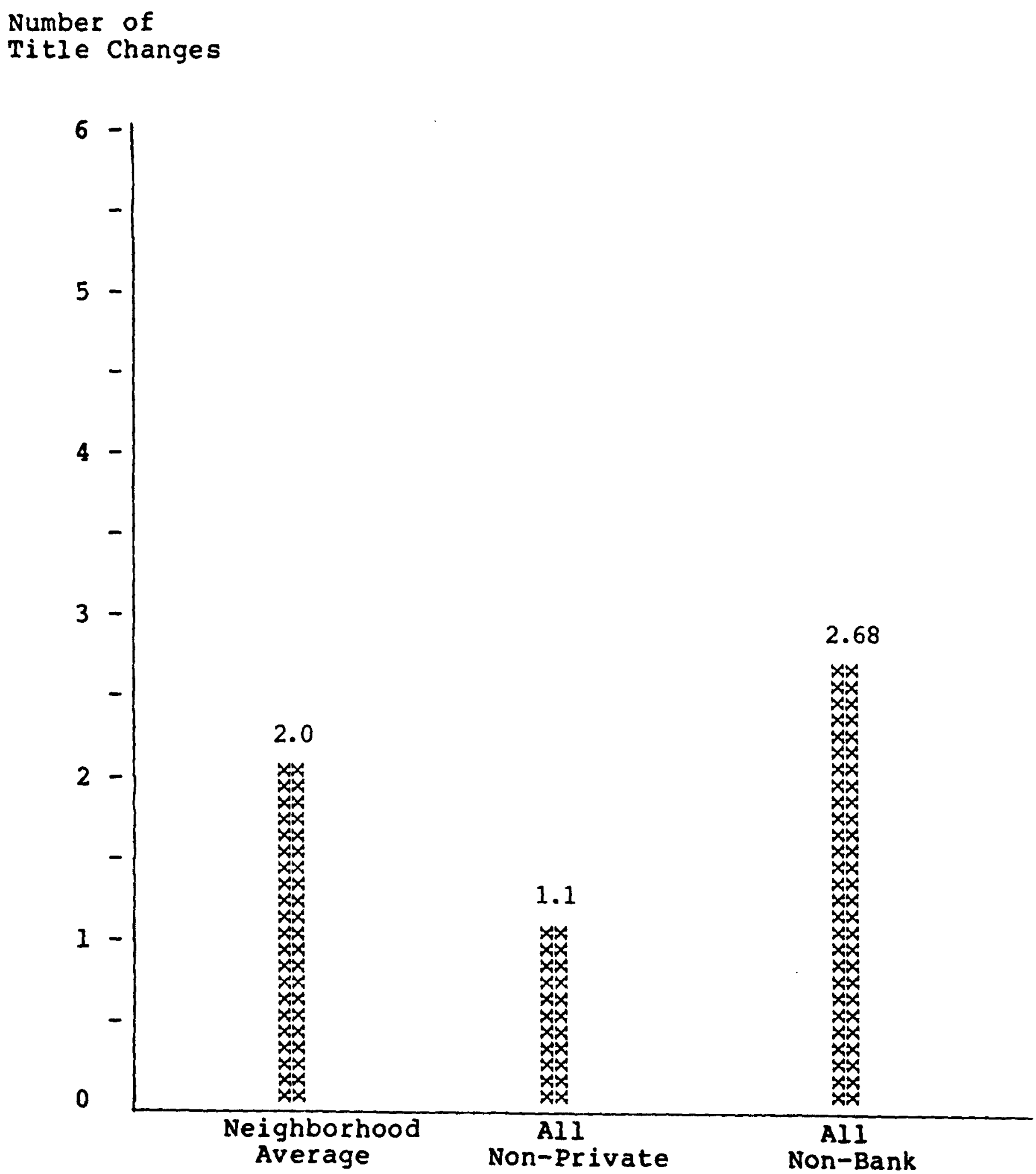


TABLE 4

VIOLATIONS PER UNIT WITHIN A BUILDING

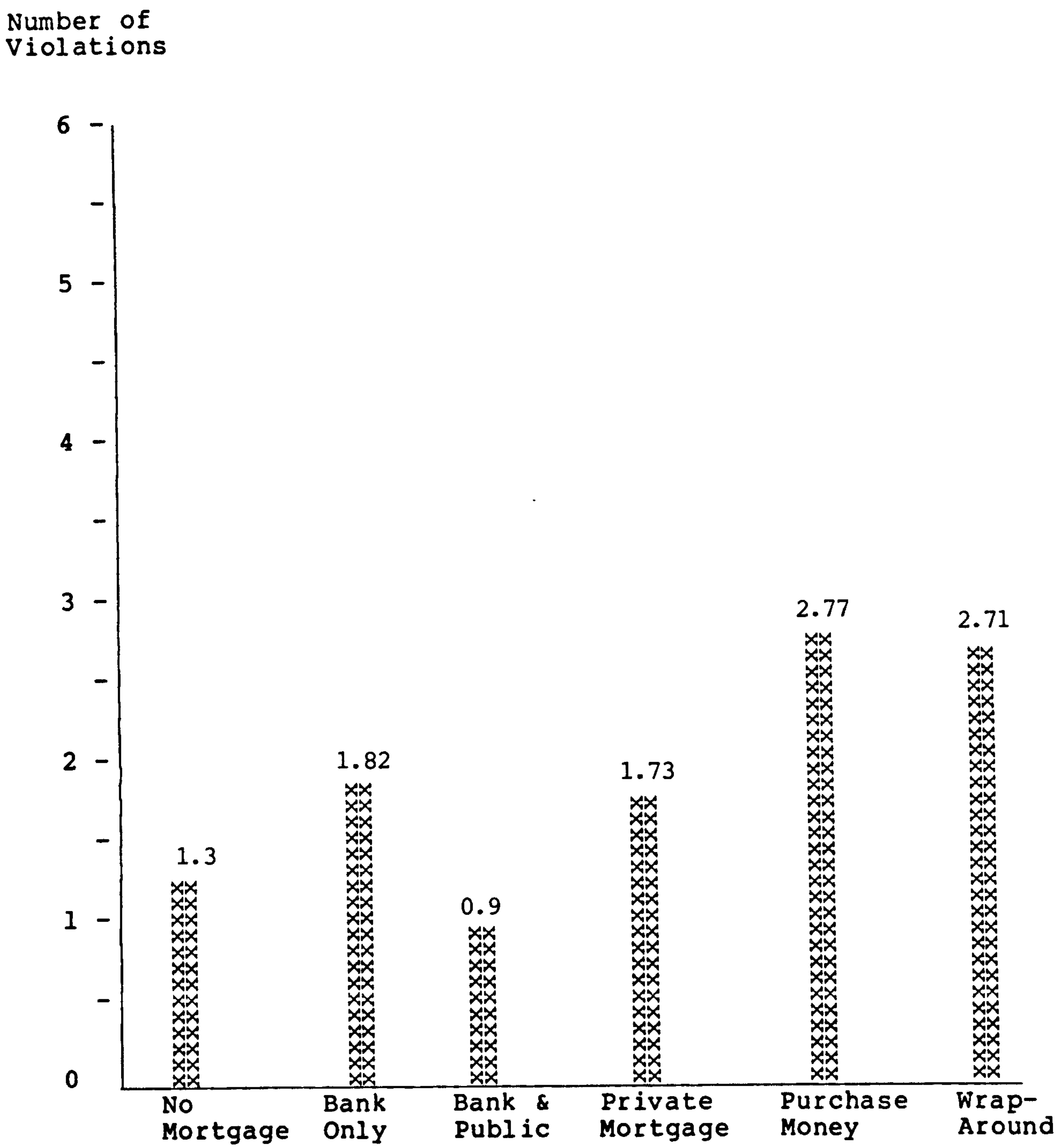


TABLE 4A

VIOLATIONS PER UNIT WITHIN A BUILDING

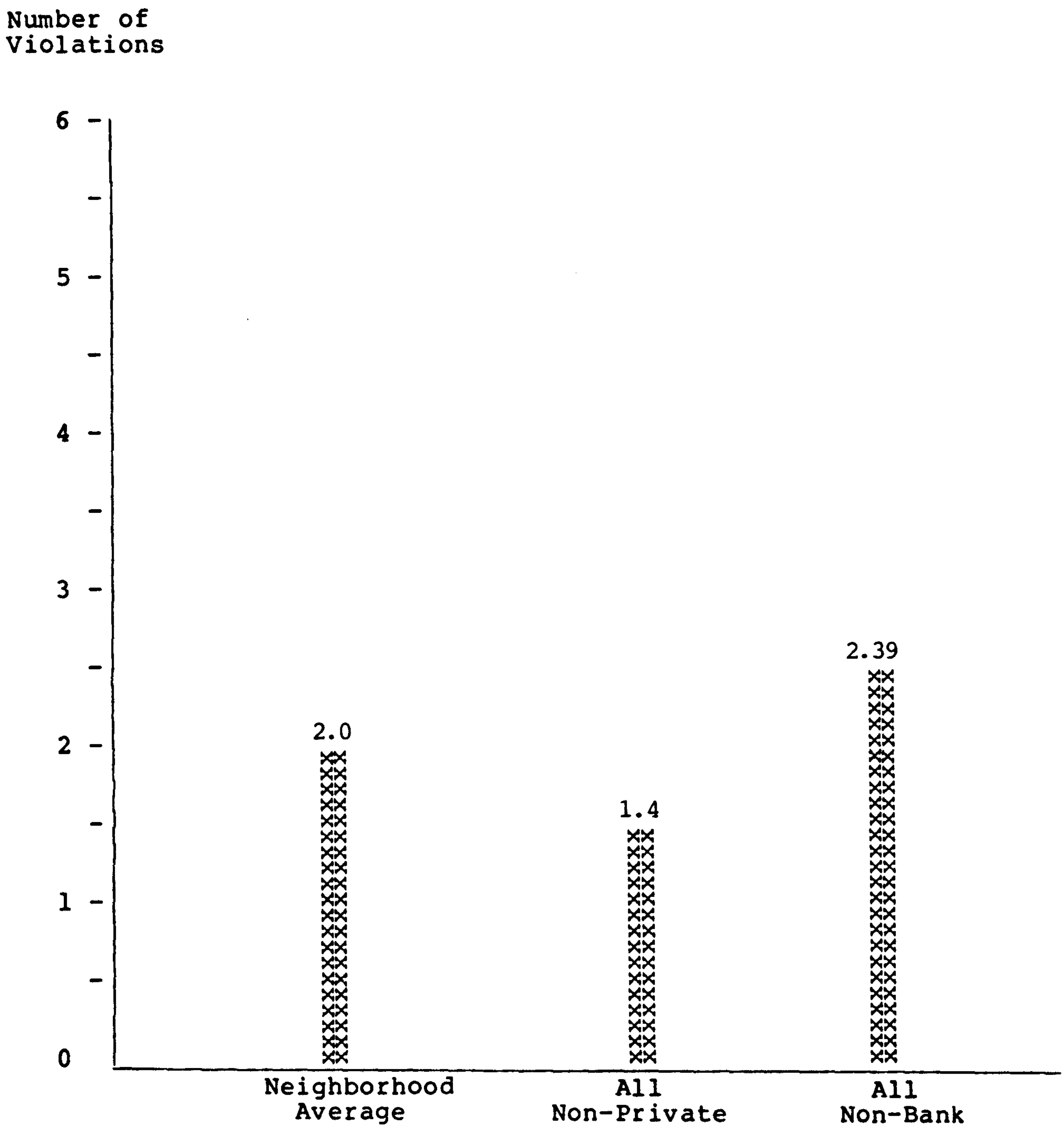


TABLE 5

PERCENT OF BUILDINGS IN HOUSING COURT LITIGATION SINCE 1967

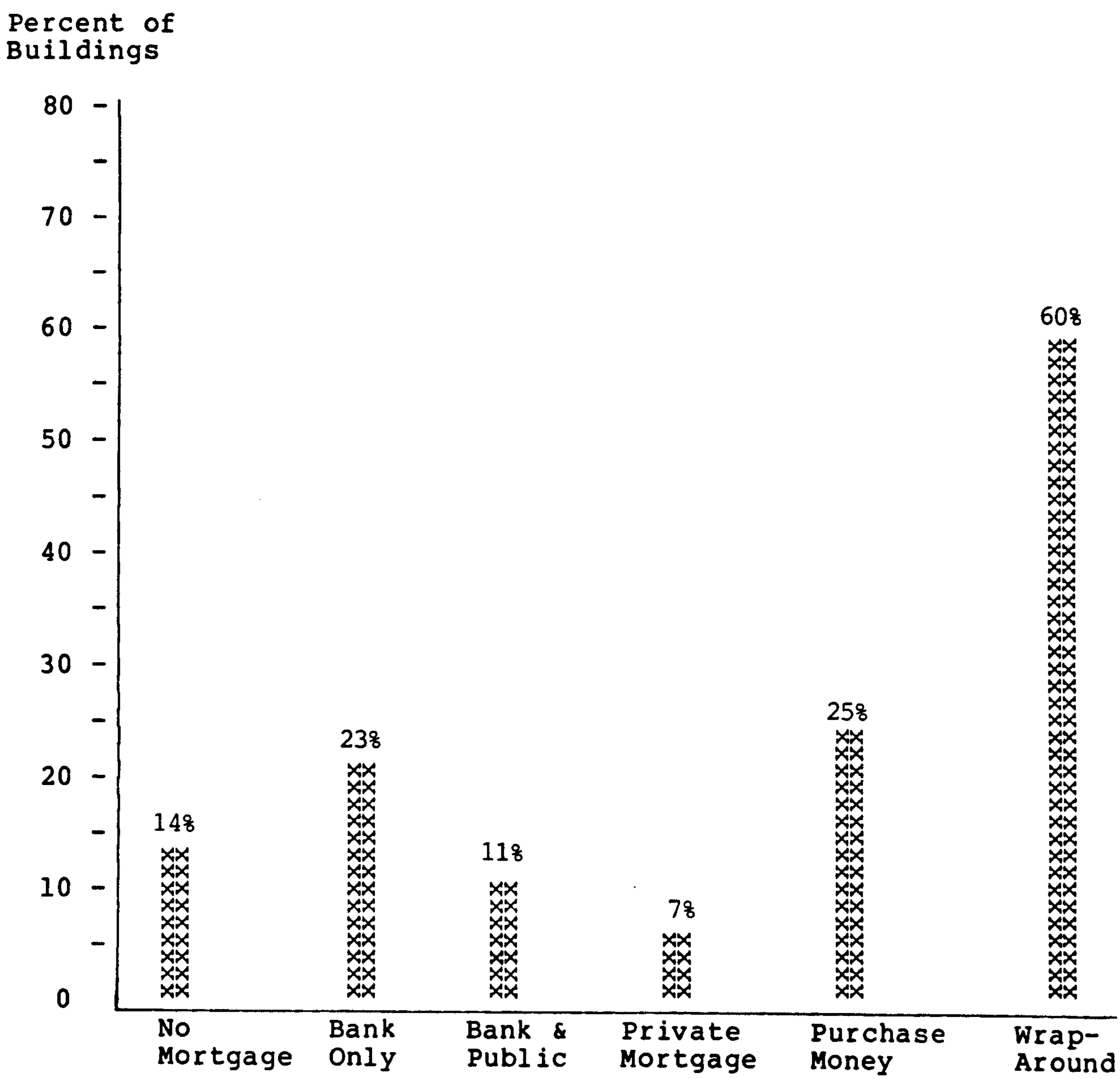
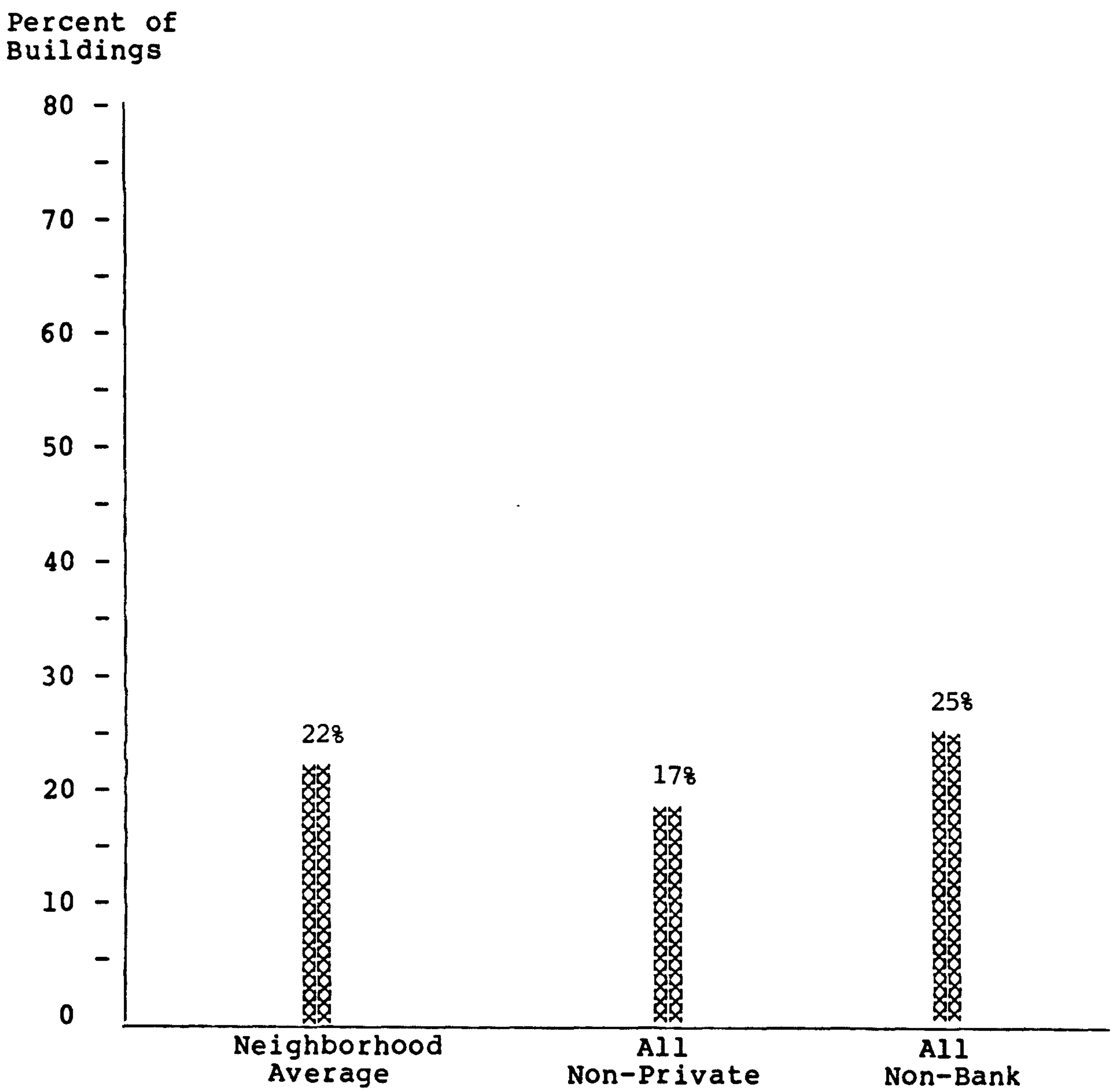


TABLE 5A

PERCENT OF BUILDINGS IN HOUSING COURT LITIGATION SINCE 1967



CROSSTABULATION: FREQUENCIES

MORTGAGES

Table 1 shows that 58% of all the multiple dwellings in Stratton Park had some type of non-bank mortgage, either a private, purchase money, or wrapped mortgage. 10.1% had been granted no mortgage at all. Buildings granted only bank mortgages accounted for only 18.8% of the total. Nine low-cost public rehabilitation loans were granted in these buildings. Out of 133 mortgages granted to all buildings only 38% were bank mortgages. 9% were low-cost publicly financed loans. The rest, 52%, were issued by private mortgage bankers.

As we move down through the mortgage categories in the table from the no mortgage category to the wrapped category, the total number of mortgages granted on the buildings increases dramatically. Starting with zero for the no mortgage category, we then see 1.38 mortgages per building for buildings with only bank mortgages, 1.56 for conventional and public loans, 1.86 for private, 2.38 for purchase money and 4.5 mortgages per building for the wraps. The wrapped buildings had more than 3.5 times as many mortgages as buildings having only bank mortgages. If we combine all the non-bank mortgage buildings (the private, purchase money and wrapped buildings), the total mortgages granted on those buildings is 2.73 compared to 1.1 for the rest. Neighborhood average is 1.96 mortgages per building granted from 1967 to 1984.

OWNERSHIP TURNOVER

The number of times a building changed hands increases as we move down Table 1: 1.1, 1, and 1.1 title changes for no mortgage, bank, and bank and public mortgaged buildings. Looking at the non-bank mortgage categories, we see 1.7 title changes for private, 2.4 for purchase money and 4.5 for the wraps. In other words, there were twice as many title changes for the wraps than other non-bank mortgaged buildings and 4 times the number for the others. This kind of activity inflates the price of the building dramatically. Combining non-bank mortgaged buildings, the average number of titles changes is 2.68 as opposed to 1.1 for the others. Neighborhood average is 2.

VIOLATIONS

In looking at housing code violations, again we see in Table 1 an increase with non-bank mortgages. There are 1.3 violations per unit in no-mortgage buildings, 1.82 per unit in bank only and down to .9 for bank and public mortgaged buildings. This shows good monitoring of building conditions by the Department of Housing Preservation and Development which grants 8A rehabilitation loans used to upgrade those buildings. Moving down the table, the VPU (violations per unit) begin to rise: 1.73 for private, 2.77 for purchase money and 2.71 VPU for the wraps. Combining all non-bank mortgaged buildings, the VPU are 2.39. This is 70% higher than the rest at 1.4 VPU. Neighborhood average is 2 VPU.

When we divided up the buildings into three equal size categories of VPU by ascending order, lowest, middle and highestrange, (below 1.05; from 1.05 to 2.39; above 2.39) the results were more striking. Fifty-seven percent of the non-mortgaged buildings and 67% of the bank and public-mortgaged buildings fall into the lowest VPU range. Compare this against the only 13% of the purchase money and 10% of the wraps. Seventy percent of the wrapped buildings fall in the highest VPU range. No bank and public-mortgaged building surfaced in the highest VPU range.

LITIGATION

The percentage of buildings involved in litigation takes a dip and then increases as we move down Table 1. Surprisingly, the purchase money buildings had the lowest rate at 7%. Later statistical analysis shows no relationship between VPU and litigation (building deterioration and housing court actions). The highest incidence of buildings with litigation are the wraps, at 60%.

TAX ARREARS

The data for tax arrears showed no significant difference among the six categories either by quarter or dollar amount.

PUBLIC FINANCIAL INCENTIVES

Almost all of the public finanical incentives were either J-51 tax abatements or low-interest 8A rehabilitation loans. None of the nine buildings granted 8A loans were in the highest VPU range; 66% fell in the lowest VPU range. Buildings with public incentives showed the second lowest litigation percentage at 11%, the lowest VPU at .9 per unit, and only 1.1 title changes. Eleven buildings were granted J-51 tax abatements. Seven fell in the lowest VPU range, 3 in the middle range, and only one in the highest VPU range. Apparently both programs are working to the benefit of Stratton Park.

RENTS

We could only obtain rent data on 49 of the 69 buildings, i.e. 71% of the total. We decided that too much rent data was missing to include it in Table 1. The rent results are:

Mortgage Category	Average Rent	Total Buildings	Data Available	Data Missing
No Mortgage	$228.70	7	3	57%
Bank Only	$236.70	13	12	8%
Bank & Public	$282.00	9	6	33%
Private Mtge	$249.80	14	12	14%
Purchase Money	$254.00	16	9	44%
Wrap-Around	$257.60	10	7	30%
Neighborhood Average	$251.10	69	49	29%
All-Non Private	$248.80	29	21	28%
All-Non Bank	$253.10	40	28	30%

Except for the bank and public mortgage category, an upward trend of about $4.50 per month in rent is noted. Non-Private mortgaged buildings averaged $4.30 in apartment rents less than non-bank mortgaged buildings. Neighborhood average is $251.10.We divided the buildings into three rent ranges, lowest third, middle third and highest third (rents under $236 per month, from $237 to $254, over $254). For buildings for which the rent information was available:

1. all the no mortgage buildings fell into the lowest range;
2. 50% of the buildings with low-cost rehabilitation loans landed in the highest rent range;
3. 57% of the wrapped buildings had rents in the highest range.

Buildings with low-cost publicly financed rehabilitation loans showed the highest average apartment rents at $282 per month. Because of this rehabilitation, they would qualify for major capital improvement rent increases (MCI's) above the normal rent guidelines. Under MCI regulations, the N.Y.S. Division of Housing and Community Renewal grants landlords rent increases to amortize the cost of rehabilitation and building systems replacement over a five year period. The rent increases, however, are permanent and continue after the cost of the work as been recouped.

CROSSTABULATION: STATISTICAL SIGNIFICANCE

Table 6 shows the joint distribution of two or more variables by dividing the frequency distributions of one variable (times it occurs) by the values of another. We looked at some crosstabulation in the table of results, comparing the type of mortgage, title changes, violations, total mortgages, etc. Of particular statistical significance for our purposes is the Chi square significance levels and Pearson's r significance. Any significance level of .05 or less rules out the possibility that random changes produced these results. A significance value of .05 means there's only a 5 in 100 chance that results will occur randomly. Therefore, we looked for significance values of less than .05 (.05 is the accepted statistical cutoff). Another requirement was that each cell in our crosstabulation must have an expected value of at least 5. The cells are the boxes in the table. The expected value of 5 means that we have enough cases (buildings) so that if our results were distributed randomly throughout all the boxes, we'd expect each to contain at least 5 buildings.

Another way to think of this is to imagine a checkerboard. It has equal size square boxes. We then take 70 grains of sand (the 70 buildings in Stratton Park) and toss them in the air over the board. When the grains finally settle on the board we would expect them to be evenly distributed in all boxes. Any significant deviation from a random distribution of the sand grains prohibits them from settling randomly and evenly. The more unevenly the sand is distributed, the more influential are the factors affecting them. The crosstabulation statistics just mentioned point out which of the factors (VPU, litigation, total mortgages and titles changes) influence the uneven distribution of the crosstabulation results.

Although we collected statistics for every multiple dwelling in Stratton Park (70) there weren't enough buildings to meet the expected value requirement of 5. Therefore, we combined all the non-bank mortgaged buildings into one category to compare against all the rest of the Stratton Park buildings. We compared for:

1. The three violations per-unit ranges
    a. lowest third
    b. middle third
    c. highest third

2. Title change categories
    a. one & under
    b. two through three
    c. over three

3. Total mortgages
    a. one & under
    b. two through three
    c. over three

4. Housing court litigation
    a. yes
    b. no

5. Public Financial Incentives
    a. yes
    b. no

6. Average apartment rent
    a. lowest
    b. middle
    c. highest third

A summary of the results follows in Table 6.

TABLE 6

CROSSTABULATION STATISTICS

First Variable	Second Variable	Chi-Square	Signi-ficance	Pearson's r	Signi-ficance	% Cells 5	Correla-tion
Type of Mortgage	Title Changes	17.9189	.0001	.50345	.0000	16.7	Yes[1]
Type of Mortgage	VPU	6.8169	.0331	.030619	.0052	None	Yes
Type of Mortgage	Liti-gation	.2262	.06344	.09285	.2239	None	No
Liti-gation	VPU	4.3803	.1119	.25163	.0184	16.7	No
Type of Mortgage	Finan. Incen.	7.5113	.0061	-.36340	.0011	None	Yes
Type of Mortgage	Apt. Rent	1.1764	.4155	.17235	.1181	None	No

Mortgage Categories:
1. Non-bank mortgaged buildings
2. All other buildings

Violations Categories:
1. In lowest third VPU range
2. In middle third VPU range
3. In highest third VPU range

Title Change Categories:
1. 1 and under
2. 2 or 3
3. Over 3

Litigation Categories:
1. No litigation
2. Litigation

Rent Categories:
1. Lowest third
2. Middle third
3. Highest third

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[1] Although 16.7% of the cells have an expected value of less than 5, the Pearson's r significance level is very strong.

CROSSTABULATION STATISTICS - INTERPRETATION

The crosstabulation statistics rule out the possibility that random chance would produce these results. In other words, the results showed that for an apartment building there are definite and strong correlations between:

1. the type of mortgage category and the total number of mortgages;
2. the type of mortgage and the number of violations per unit;
3. the type of mortgage and the number of title changes;
4. the type of mortgage and any publicly granted financial incentives.

All of these four items have very strong Chi-square and Pearson's r significance figures. From looking at Table 6 we see that each item easily met the less than .05 significance requirement. Let's take one of the rows in the table to use as an example:

First Var.	Second Var.	Chi-Square	Sign.	Pearson's r	Sign.	% Cells 5	Correlation
Type of Mortgage	Violation per unit	6.81669	.0031	.030619	.0052	None	Yes

On this basis, we can draw the following conclusions. In looking for any correlation between the type of mortgage, (bank versus non-bank -- first variable) and a building's violations per unit (second variable), the Chi-square statistic is 6.81669 and the Pearson's r figure is .030619. The chances of producing this result are the significance levels .0331 and .0052. The odds are 331 out of 10000 for the Chi-square and only 52 out of

10000 for the Pearson's r figure that the type of mortgage and violations per unit are not related.

Similar arguments hold for the other variables:

- title changes;
- violations per unit;
- public financial incentives.

The results show no statistically relevant correlations between:

1. Mortgage category and the probability of housing court litigation;

2. Violations per unit and the probability of housing court litigation.

3. Mortgage category and apartment rents.

The second point explains why, in Table 1, the percentage of litigated buildings doesn't rise as we go down the table through the mortgage categories. There's no correlation between the two items. Apparently, just because a building has substantially higher violations per unit (non-bank mortgaged ones), it doesn't follow that it has a higher probability of being pulled into housing court. Perhaps this reflects the ineffectiveness of housing court to resolve housing code violations.

Item three shows no correlation between mortgage category and apartment rents. No significant difference exists between the average apartment rent in the better maintained, non-private mortgaged buildings and the run down, non-bank mortgaged buildings.Although the rent data showed an average increase of $4.50 per mortgage category, the Chi-square and Pearson's r significance figures discount any correlation between these two items. This raises the question of why people would pay comparable rents for dissimilar building conditions. The probable answer is that there is a lack of viable alternatives. The current 2% New York City vacancy rate prompts people to take any available apartment. The market is skewed upward; rents in New York City only go up, regardless of housing conditions.

To sum up: the crosstabulation statistics show a very strong relationship between an apartment building's type of mortgage and its:

1. violations per unit;
2. ownership turnover;
3. total number of mortgages;
4. public financial incentives.

For non-bank mortgaged buildings, VPU will be higher, title changes higher, total number of mortgages per building higher, and the likelihood of public financial incentives less. These relationships are strongest for the wrap-mortgaged buildings.

T-TEST

For the next step of the statistical analysis, T-Tests were used to check for significant differences between groups of buildings. All the buildings with some type of non-bank mortgage, (Group 2--private, purchase money and wrapped), were compared against those without some type of non-bank mortgage, (Group 1--no mortgage, bank mortgage only, and bank & public financing). The results are summarized in Table 7.

TABLE 7

GROUP 1: WITHOUT NON-BANK MORTGAGES vs. GROUP 2: WITH NON-BANK MORTGAGES

	Group 1 Mean Score	Group 2 Mean Score	.05 Level of Significance
Total No. Mortgages Since 1967	1.10	2.57	.000
Ownership Turnover Since 1967	1.07	2.68	.000
Housing Court Litigation	.21	.35	.322*
Violations per Unit	1.42	2.38	.007
Average Apt. Rent	$248.48	$253.07	.675*

As shown in Table 7, the T-Tests reveal significant differences between the first group of buildings (without non-bank financing) and the second group (with non-bank financing) in the total number of mortgages granted on them since 1967. It shows 1.1 mortgages for Group 1 versus 2.57 mortgages for Group 2, a difference of 134%. Hand-in-hand with mortgages come the title changes (ownership turnover). Group 1 shows significantly less title changes at 1.07 per building when compared against Group 2 at 2.68 title changes.

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* No statistically significant difference.

* No statistically significant difference.

The same holds for violations per unit for each group. The figures are 1.42 VPU for Group 1 and 2.38 violations per unit for Group 2. No significant differences were revealed between both groups in incidents of housing court litigation and average apartment rents.

Since our contention was that the purchase money and wrapped buildings were the worst maintained, we pulled those buildings out and compared them against all the other buildings. Table 8 lists the T-Tests results of the purchase money and wrapped buildings, Group 3 (26) versus those with no mortgage, bank mortgages only, bank and public financing, and private mortgages, Group 4 (43).

TABLE 8

GROUP 3: WITH PURCHASE OR WRAP MORTGAGES vs. GROUP 4: WITHOUT PURCHASE OR WRAP MORTGAGES

	Group 3 Mean Score	Group 4 Mean Score	.05 Level of Significance
Total No. Mortgages since 1967	1.35	2.96	.000
Ownership Turnover since 1967	1.28	3.19	.000
Housing Court Litigation	.14	.54	.026
Violations per Unit	1.52	2.75	.005
Average Apt. Rent	$248.94	$255.50	.001

This time significant differences were found between the groups (purchase money and wrapped buildings versus the rest) in the number of mortgages granted, ownership turnover, housing court litigation and violations per unit, but still not in rent. With private mortgage banker mortgages removed from Group 2, the number of mortgages granted per building rises to 2.96 per building for Group 4. Violations per unit also increase to 2.75 per unit. The biggest increase occurs in the incidence of housing court litigation. The figure for Group 1 decreases from 21% of the buildings to 12% in Group 3. For Group 2, when the private mortgaged buildings are dropped, the figures change from 35% to 54% of the buildings involved in some type of action in Group 4.

In summary, we see that significant differences exist between buildings without any type of non-bank financing and those with non-bank financing (private, purchase money and wrap-around mortgages). For Group 2 (buildings with non-bank mortgages), the number of mortgages granted since 1967, the number of title changes since 1967, and the violations per unit are significantly higher. However, no significant differences exist among these two groups of buildings in average apartment rents or in the percentages involved in housing court litigation.

When the buildings with purchase money or wrap-around mortgages are compared against the rest, the difference between these two groups of buildings extends even further and a significant difference appears in the percentages of buildings in housing court litigation. Again, no significant differences in rents are shown.

CONCLUSION

Apartment building financing for building rehabilitation and refurbishment and property turnovers is in strong demand in the New York City area. In many low and moderate income neighborhoods, banks are not servicing the bulk of this demand. For instance, in Stratton Park, the total number of apartment building mortgages granted since 1967 was 133. Only 38% of these were bank loans. Thus, 62% of all loans granted in this neighborhood over an eighteen year period were obtained from non-traditional financing sources. Many mortgage bankers (non-bank lenders) operate outside of state regulation by using loopholes in current regulations. Mortgage bankers sometimes grant loans on apartment buildings or to owners that banks would not, or should not. These buildings either cannot carry these loans due to too much debt service, or the owner lacks proper management skills. In either case, such loans lead to the deterioration of the non-bank mortgaged buildings, inflicting hardships on the tenants and contributing to neighborhood decline.

Statistical analysis of the data collected for this project shows that a very strong relationship exists between an apartment building's mortgage category and its: 1) debt service (total mortgages on the property; 2) ownership turnover; and 3) violations per apartment.

These relationships are strongest for the purchase money and wrap-around mortgaged buildings. Non-bank mortgaged buildings, especially those with purchase money or wrap-around mortgages, show significantly higher violations per unit, and greater ownership turnover, debt service, and to a lesser extent, housing court litigation.

The higher leverage ratios on the non-bank mortgaged buildings seem to promote higher ownership turnover and mortgage defaults, and lower building maintenance and services. These conditions, however, do not appear to be caused by inadequate rents. On the contrary, only slight differences were noted among the average apartment rents of the six mortgage categories, with the highest rents in the purchase money and wrap-around mortgaged buildings. It is thus reasonable to conclude that the servicing of additional debt on non-bank mortgages, rather than inadequate rents, causes the ownership turnovers, mortgage defaults, and deteriorating building conditions. In a certain sense, the current rent regulation system rewards the landlords (or wrap-around mortgagors) of poorly maintained, run-down buildings through rent increases generated by the turnover of tenants who vacate when conditions in their buildings become intolerable.

Tenants apparently find little relief from these conditions through Housing Court. The data showed no correlation between a building's violations per unit and the likelihood of it being involved in a Housing Court case. Nevertheless, the purchase money and, especially, the wrap-around mortgaged buildings did show a higher frequency of housing court litigation. Unfortunately, Housing Court often proves to be an ineffective remedy for tenants of wrap-around mortgaged buildings. To date, tenants and housing organizations have been unsuccessful in having the controlling interests of these buildings (the "wrappers") held accountable for building conditions.

In Stratton Park the worst maintained and serviced apartment buildings are those with purchase money and wrap-around mortgages. The wrap-around mortgage, in particular, has generated a new and difficult set of problems for the community. If further research indicates that the results of this study can be generalized to other neighborhoods, then the development of appropriate regulatory and/or legislative solutions should be a crucial issue for concerned citizens and public officials.

GLOSSARY

COMMUNITY REINVESTMENT ACT (CRA)

A federal law enacted in 1977 that requires bank regulatory agencies, "to encourage such institutions [commercial banks, savings banks, and savings and loan associations] to help meet the credit needs of the local communities in which they are chartered, consistent with the safe and sound operation of such institutions." CRA further requires regulatory agencies to "assess the institution's record of meeting the needs of the entire community, including low-and moderate-income neighborhoods...."

DEBT SERVICE

Periodic payments of the principal and interest due on a mortgage.

EQUITY

The owner's interest in his/her property. It is calculated by establishing the property's value minus the amount of principal outstanding on any mortgages, and minus the amount of any other liens.

FORECLOSURE

A process by which the mortgagee enforces payment of the debt secured by a mortgage by taking, and usually selling, the mortgaged property.

GOOD REPAIR CLAUSE

A clause in a mortgage contract that requires the mortgagor to keep the mortgaged property in good repair. The clause gives the mortgagee the right of foreclosure if the mortgagor fails to abide by this obligation.

LIEN

A legal right to claim or dispose of property in payment of or as a security for a debt. A senior lien (first mortgage) must be paid first; a junior lien is subordinate to a senior lien.

MORTGAGE

A contract that pledges a piece of property as security for the payment of a debt.

MORTGAGEE

The party or institution that loans the money for purchasing a piece of property (land and/or building). The public record will show this party as having a lien or claim on the property put up as collateral for the loan.

MORTGAGOR

The party who borrows the money to purchase property and uses this property as collateral to secure the loan.

MORTGAGE BANKER

A lender who resells a mortgage to a secondary party, either as a whole loan or as part of a pool of loans. A mortgage banking company or subsidiary is a non-depository institution, sometimes referred to as a "non-bank bank."

PURCHASE MONEY MORTGAGE (PMM)

A mortgage given by the seller to the buyer of property to secure the unpaid balance of the purchase price.

REDLINING

A practice in which banks and insurance companies draw a "red line" (on maps) around neighborhoods where they will refuse to grant loans or issue policies because of the perception that these are "high-risk" areas. In addition to automatically rejecting applications, there are other, more subtle ways of redlining. These include imposing stricter requirements, e.g. higher down payments, shorter loan terms, higher closing costs, and other practices that effectively discourage applicants.

WRAP-AROUND MORTGAGE

A mortgage that combines any pre-existing mortgages with a new purchase money mortgage (pmm). The new pmm "wraps-around" the pre-existing mortgage(s), so that payments on all the outstanding debts on the property are combined into a lump-sum payable in installments to the wrap-mortgagee who provided the new pmm. The wrap-around mortgage specifies that the mortgagee can claim the rent monies generated by the building if the mortgagor (buyer-landlord) fails to keep up with his loan payments.

WRAP AROUND MORTGAGES IN A BRONX NEIGHBORHOOD

Prepared by: Louis Zaneri

Editors: Polly A. Smith, Reinvestment Unit
and
Thomas Bryant III, Research Division
New York City Commission on Human Rights

Acknowledgments:

Dr. Art Sullivan, Fordham University, Graduate School of Business Administration

Dorothy Krynicki, Fordham University, Graduate School of Political Science

For Further Information Call:

Polly A. Smith
Reinvestment Unit,
Neighborhood Stabilization Program
New York City Commission on Human Rights
(212) 566-0765/69