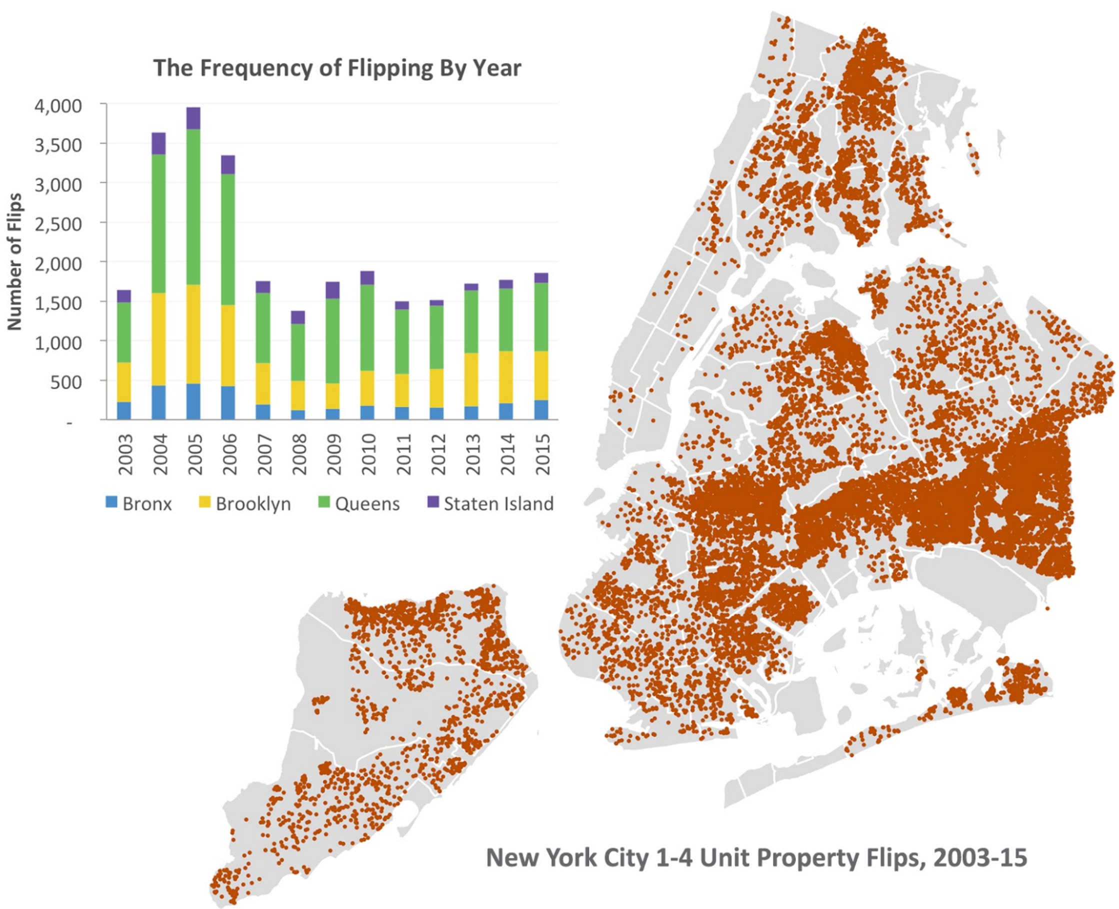
CENTER for NYC NEIGHBORHOODS

The Impact of Property Flipping on Homeowners and Renters in Small Buildings

This analysis explores the impact of real estate speculation on the residents of small homes by analyzing property flipping of 1-4 unit residential properties in New York City from 2003-2015. For this analysis, a flip is defined as a home that is bought and sold in an arm's length transaction within a 12-month period. The analysis excludes condominium and co-op sales for consistency when comparing trends across neighborhoods with varying housing stocks. The analysis has resulted in the following findings:

Property flipping is re-emerging from the collapse of the housing market

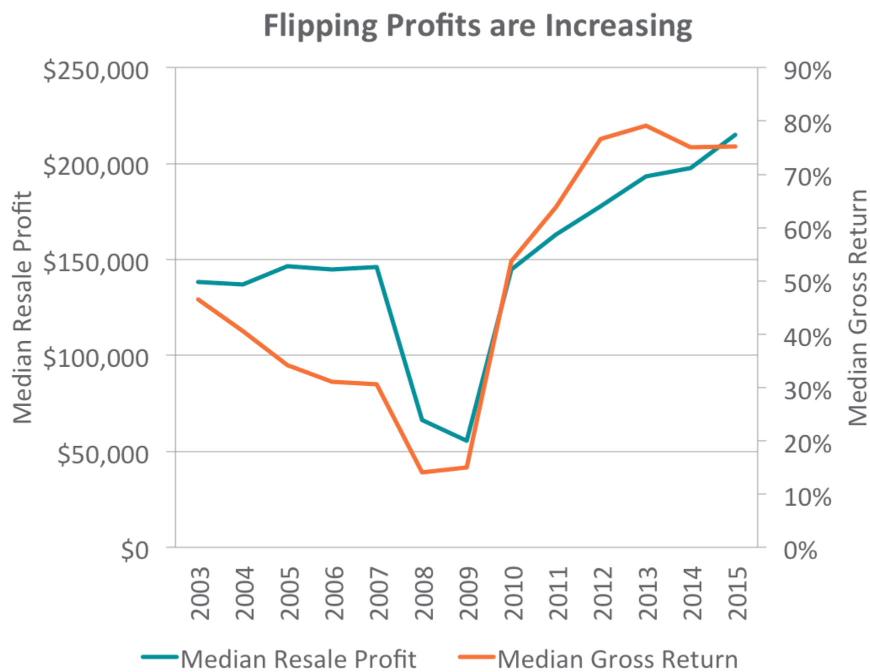
The frequency of flipping peaked in the years immediately preceding the housing crash, then declined dramatically. Today, flipping is creeping back up with over 1,800 1-4 unit properties flipped in 2015.



New York City 1-4 Unit Property Flips, 2003-15

Property flipping in New York City is becoming increasingly profitable

Flipping is more profitable now than it was at the peak of the housing bubble. In 2015, flipped properties produced a median resale profit of $215,000 or a 75% gross return (appendix 1). By comparison, according to a March study by RealtyTrac[1], 2015 home flips countrywide yielded an average of $55,000 in resale profits and a 46% gross return.



Flipping is concentrated in Central Brooklyn and Southeast Queens

East New York, which had more flips than any other neighborhood in 2015, has joined Bedford-Stuyvesant as a focal point of flipping activity in Brooklyn. Southeast Queens contains several neighborhoods where flipping has been concentrated for years: Jamaica (91 flips in 2015); St. Albans (81); and Springfield Gardens (74).

Neighborhoods with the Highest Volumes of Flips

2015 Rank	Neighborhood	# of Flips
1	East New York, Brooklyn	94
2	South Jamaica-Baisley Park, Queens	91
3	St. Albans, Queens	81
4	Bedford Stuyvesant, Brooklyn	75
5	Springfield Gardens, Queens	74

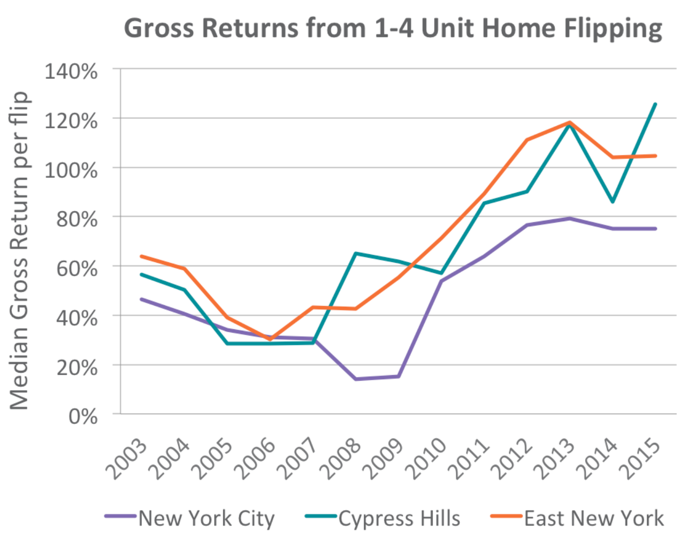
[1] http://www.realtytrac.com/news/real-estate-investing/2015-year-end-and-q4-u-s-home-flipping-report/

Returns from flipping vary by neighborhood

The largest gross returns from flipping occurred in Brooklyn neighborhoods with rapidly rising property values. Cypress Hills led all neighborhoods in 2015 with a median gross return of 125% and, since 2008, the profitability of flipping in Cypress Hills and East New York has increased well beyond the city's median.

The Top Neighborhoods for Gross Returns

2015 Rank (at least 20 flips)	Neighborhood	Median Gross Return	# of 1-4 unit home flips
1	Cypress Hills, Brooklyn	125%	32
2	Flatbush-East, Brooklyn	117%	36
3	Bushwick, Brooklyn	106%	58
4	South Jamaica-Baisley Park, Queens	106%	91
5	East New York, Brooklyn	105%	94



Flipping takes affordable homes off the market

Flipping reduces the quantity of affordable homeownership opportunities on the market by moving homes to significantly higher price points. The median initial purchase price of flips in Brooklyn in 2015 was affordable to families making about $75,000 or 95% of AMI for a family of three. The significantly inflated median resale price was affordable to families making about $125,000 or 163% of AMI for a family of three. That means that while a moderate income family could afford many of these properties before they were purchased by a flipper, the homes are unaffordable by the time they are reintroduced to the market, only months later. This shrinks the stock of affordable homeownership opportunities in the city.

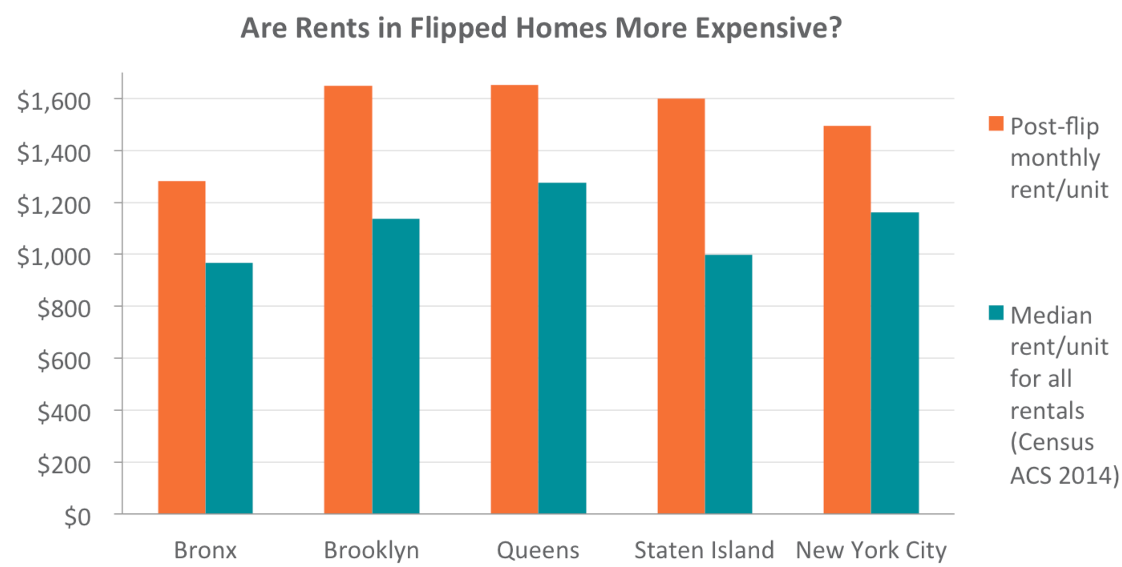
To buy a home in 2015 at the median sales price of flipped properties, a household will need ***at minimum****:*

	Income to afford Sale 1	% of AMI for family of 3 to afford Sale 1	Income to afford Sale 2	% of AMI for family of 3 to afford Sale 2
Bronx	$74,000	95%	$95,000	122%
Brooklyn	$74,000	95%	$127,000	163%
Queens	$60,000	77%	$93,000	120%
SI	$77,000	99%	$105,000	135%

Sale 1 reflects the price at initial purchase while *Sale 2* reflects the price of the resale months later. See methodology section.

Flipping impacts the affordability of rentals in small homes

Small homes are a significant source of affordable rental housing in the city. In 2015, the 1,837 1-4 unit properties that were flipped contained 3,150 units. Rental units in small homes that have been flipped are often subject to sharp increases in rent as new investor owners look to maximize profits. Renovations and added bedrooms command rents far above those claimed by the previous owners, often working class owner-occupant families.



The rents required to sustain the resale prices of flipped properties (appendix 6) far exceed the median rents in their boroughs (see Methodology for full explanation). For families renting in small homes, a flip likely means a rent increase beyond their capacity if not an outright eviction.

Recommendations for limiting small homes speculation and preserving affordability

As demonstrated in the above analysis, New York City house flipping is on the rise, is increasingly profitable, and negatively impacts housing affordability. Taken together, these trends raise concerns that flipping is taking small homes out of the hands of moderate-income homeowners and their tenants and turning them into investment properties with rental units priced increasingly out of range for most New Yorkers. Given New York City's housing affordability crisis, more must be done to deter flipping and therefore promote affordable housing in small buildings.

Anti-Speculation Tax

One way to limit house flipping is to tax speculative transactions at a higher rate. An anti-speculation tax would create a disincentive for property flipping while also generating new tax revenues that could be used to fund programs and services, including foreclosure prevention, home repair, and energy efficiency, to help stabilize homeowners and their tenants at risk of displacement. The tax would modify the existing Real Property Transfer Tax (RPTT) by taxing sales that occur in rapid succession at higher rates than those that follow long periods of ownership. The precise percentages should be determined through a careful study, but proposals in San Francisco and Philadelphia lay out a promising framework: a sale that occurs within one year of the previous sale will receive the highest transfer tax rate, properties resold within two years will receive a somewhat lower rate and so on until a base rate is reached at year four or five.

Citywide Cease-and-Desist Zone

A cease and desist zone creates a mechanism for homeowners to protect themselves from real estate professionals who scour neighborhoods by mail, phone and on foot in search of homes to buy. In a cease and desist zone, homeowners can opt-in to a no-solicitation registry to stop harassment from brokers and scammers seeking to pressure them into selling their homes. If solicitors persist, the homeowner can report them to an enforcement agency which can punish violators through fines and license revocation. Since 1989, the Secretary of State has the authority to create cease and desist zones but today there are no active cease and desist zones in New York City. New cease and desist legislation from the City Council could go beyond the State's program to create a comprehensive, citywide and user-friendly initiative. Unlike an anti-flip tax, cease and desist legislation could come from the City Council and would not require authorization by the State legislature.

Foreclosure Prevention

Many flips begin when an investor arranges for the purchase of a home in foreclosure at a below-market price. Too many homeowners who sell in such transactions are not getting the housing counseling and legal services support they need to pursue loan modifications or other mortgage workouts. Others, for whom homeownership is not financially sustainable, need guidance through the short sale process. Since stabilizing distressed homeowners also means stabilizing renters in those properties, foreclosure prevention services is an important investment in housing affordability for the whole neighborhood.

Methodology

We define a flip as a home that is bought and sold in an arm's length transactions within a 12-month period. An arm's length transaction is a sale that occurs via the market and not between actors who are related or otherwise inclined to carry out transactions at non-market prices. The analysis focuses on 1-4 unit homes and excludes condominium and co-op sales for consistency and to maintain the integrity of our data for comparisons across years and neighborhoods.

Median Resale Profit: This figure is calculated as the median of the difference between the price at which a property was bought and the price at which it was sold for all flips. Both sales prices are adjusted for inflation. Resale profit is not necessarily the final profit to the flipper since we do not know how much was invested in renovations and improvements.

Median Gross Return: Gross return, also known as gross return on investment (ROI), is the difference between the price at which a property was bought and the price at which it was sold divided by the initial purchase price. The median gross return is the median of gross returns for all flips within a given neighborhood or year.

Impact on Homeowner Affordability: This analysis reflects the incomes of real New York City homebuyers who used FHA loans in 2014. Homebuyers using conventional (non-FHA) loans in 2014 had substantially higher incomes while buying equally priced homes. Thus, these numbers reflect the absolute minimum a family would need to buy; most buyers would need higher incomes. To determine the affordability of flipped properties to homeowners, we used the most recent Home Mortgage Disclosure Act data (2014) to identify the relationship between incomes and sales prices in each borough. Our analysis began with a median sale price for both the initial and second sales. From that, we subtracted a downpayment (assuming 3.5% to reflect an FHA mortgage accessible to moderate income buyers). We then used that imputed mortgage value at origination to find comparable mortgages from the HMDA data, taking the median of the incomes associated with mortgages within $5,000 of the target mortgage amount.

The Impact of Flipping on Rents: To impute the monthly rent per unit for rentals in flipped properties, we derived the net operating income (NOI) of each flip by applying a cap rate of 5% to the resale price of the flip plus 5% of that value in renovation costs. From the NOI, we subtract 14% for operating expenses and 3% for vacancy to reach an annual rent roll for the property. From that we divide by the number of units and by 12 for a monthly rent per unit.

Our data, which includes sales from 2003 to 2015, is drawn from the City Department of Finance's annualized sales data. Neighborhood boundaries are derived from the same source. We created a number of filters to exclude transactions that were not at arm's length (for example, the sale of a property from parent to child). We excluded sales for less than $100,000 and those properties that were bought and sold within five days.

We use medians rather than averages to dull the influence of outliers in the data and give more accurate comparisons between neighborhoods and years.

The year of the flip is defined as the year in which the resale occurred. So if a property was purchased in December 2014 and sold again in February 2015, it is described as a 2015 flip.

Finally, all dollar amounts have been adjusted for inflation to reflect 2015 dollars so that we can compare changes in flip profitability across time.

Appendix 1

Returns on Flipping in 2015 by Borough

	Median Resale Profit	Median Gross Return
Bronx	$214,496	84%
Brooklyn	$305,000	90%
Queens	$196,882	74%
SI	$103,824	38%

Appendix 2

The Top Neighborhoods for Resale Profits

2015 Rank (at least 20 flips)	Neighborhood	Median Resale Profit	# of 1-4 unit home flips
1	Bushwick, Brooklyn	$500,039	58
2	Crown Heights, Brooklyn	$427,292	36
3	Bedford Stuyvesant, Brooklyn	$415,936	75
4	Ocean Hill, Brooklyn	$367,320	44
5	Cypress Hills, Brooklyn	$320,507	32
… 7	East New York, Brooklyn	$272,308	94

Appendix 3

The Top Neighborhoods for Gross Returns

2015 Rank (at least 20 flips)	Neighborhood	Median Gross Return	# of 1-4 unit home flips
1	Cypress Hills, Brooklyn	125%	32
2	Flatbush-East, Brooklyn	117%	36
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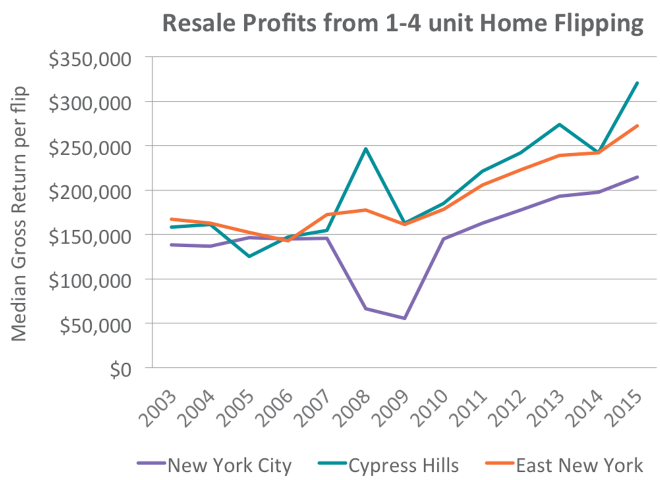
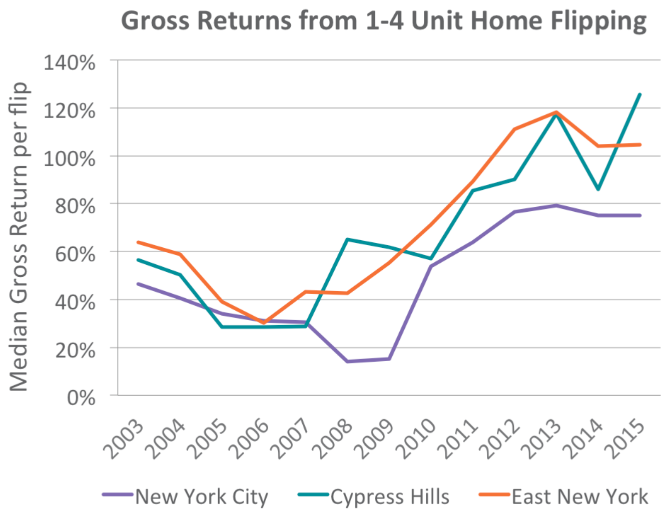
Appendix 4



Appendix 5



Appendix 6

Post-Flip Rents in the Boroughs and Select Neighborhoods

	Post-flip monthly rent/unit	Median rent for all rentals (Census ACS 2014)
Bronx	$1,281	$967
Brooklyn	$1,649	$1,136
Queens	$1,653	$1,276
Staten Island	$1,600	$997
New York City	$1,495	$1,160
Bed-Stuy	$2,326	
Bushwick	$2,371	
Canarsie	$1,300	
Crown Heights	$1,996	
Cypress Hills	$1,435	
East New York	$1,175	
Laurelton	$1,260	
Ocean Hill	$1,756	
South Jamaica	$1,318	
Woodhaven	$1,687	