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## **THE RECESSION AND YOUR MUNICIPALITY: AN UPDATE ON FORECLOSURES, VACANT PROPERTIES, LIENS AND RELATED ISSUES**

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### **I. Introduction.**

The mortgage foreclosure crisis gripping borrowers nationally has serious implications for communities trying to prevent the repossession of homes on one hand and manage the resulting vacant properties, increases in crime, homelessness, and other problems that stem from family financial crisis. This outline will provide an overview of the challenges to municipalities caused by the recent wave of foreclosures, discuss tools cities have at their disposal, examples of best practices from around country, and finally summarize recent enacted and pending legislation designed to assist municipalities in addressing the impacts of foreclosures.

### **II. Tools Available to Municipalities to Address the Impact of Foreclosures.**

Relying on common law tradition and the statutory grant of general police power, modern cities have a variety of powerful tools available to combat the negative impact foreclosures on individual homes and neighborhoods. When foreclosed homes become vacant due to abandonment or eviction they often quickly succumb to the forces of nature and the elements; grass and weeds grow long, swimming pools become stagnant public health hazards, landscaping dies from lack of attention or grows out of control, windows break, and exteriors suffer damage from normal wear-and-tear and vandalism. The domino effect of one distressed home having a negative impact first on neighboring residences and then on entire neighborhoods is familiar to city officials. When this occurs, municipalities must aggressively enforce local codes.

#### **A. Property Maintenance Codes.**

Many localities have adopted property maintenance codes to regulate community standards for the interior and exterior condition of structures (e.g. the International Property Maintenance Code published by the International Code Council). Typically these codes require that the exterior of properties and accessory structures be maintained in a clean, safe, and sanitary condition; that weeds and plant growth be limited; that sidewalks and stairs be maintained.

Property maintenance codes often cover everything from window glazing to abandoned cars. Codes are enforced by building or property maintenance departments and authorize the appointment of staff and inspectors to administer regulations. Code enforcement officials have the right to enter structures at reasonable times and assess fines for non-compliance.

The strength of these codes varies from city to city and from state to state. For example, until recently, the Illinois Municipal Code only permitted cities to cut weeds when the owners of real estate either refused, or neglected, to maintain properties themselves. Now municipalities may collect the reasonable costs of cutting grass, and trimming or removing nuisance trees and bushes. The cost of maintenance becomes a lien against the real estate and is superior to all other liens except tax liens.

### **B. Vacant Building Ordinances and Registries.**

Illinois is one of the top ten states in the nation for mortgage foreclosures. The Village of Bellwood is an example of one community that has proactively managed the challenge. While failure to make utility payments is often the first sign of an impending foreclosure, abandonment and eviction mark the start of the serious headaches for local government. Empty houses become an invitation for squatters, criminal elements, and vandals.

Many communities like Bellwood have adopted specific ordinances to address the unique problems posed by vacant structures. The Bellwood Neighborhood Preservation Ordinance was enacted as a way to:

(A) prevent the deterioration and abandonment of housing in transitional neighborhoods; (B) preserve, coordinate and concentrate maintenance efforts by the village in designated neighborhoods; (C) promote private investment in housing in those neighborhoods; and (D) promote community involvement in all such activities.

In order to maximize the program's effectiveness, each neighborhood in the village is studied with input from community representatives. The program is administered by the Department of Community Relations which develops and implements a residential housing recycling program in designated areas to ensure a safe, clean and viable housing market.

Among the core functions of Neighborhood Preservation is the management of vacant properties. Under the ordinance, vacant buildings must be registered with the village within 30 days of becoming vacant. Registration requires the personal contact information of the owner or another responsible party who may be personally liable "...for any violation therein, existing or occurring, or which may have existed or occurred, at or during any time when such person is or was the person owning or managing, controlling, or acting as agent in regard to said buildings or premises and is subject to injunctions, abatement orders or other remedial orders." Owners under the ordinance include any person who controls, or directs the control, of the maintenance of structures. That can include banks who have foreclosed on the property, property management companies hired to manage the property, and other organizations or individuals with some form of control over the property. Responsibilities of owners of vacant properties are extensive and

include maintaining the building in a safe and secure condition, posting contact information on the structure, and keeping the building insured.

The International Property Maintenance Code similarly contains administrative tools for local jurisdictions to manage vacant properties including the requirement that vacant structures be maintained in a clean, safe, secure, and sanitary condition; and that they be closed up so they do not become attractive nuisances.

Some cities have added creative aspects to traditional property maintenance codes. Dearborn, Michigan, for example, requires “decorative board-ups” rather than standard and unsightly plywood.

### **C. Administrative Adjudication of Code Violations.**

Even in communities with good public education efforts and diligent property maintenance inspection departments, some property owners (for a variety of reasons) become non-compliant. Most states recognize the administrative burden placed on local units of government and allow the recovery of costs through fees and fines. Illinois law, for example, authorizes both home rule and non-home rule municipalities to establish systems for the administrative adjudication of most code violations. 65 ILCS 5/1-2.1-8 and 5/1-2.2-55. However, non-home rule communities do not have the authority to adjudicate building code and traffic violations.

In some large cities, administrative adjudication departments can rival the court system in scale and scope. Often employing hundreds of people and processing thousands of violations each year, these systems relieve pressure from already burdened municipal courts and allow respondents due process with less formality and usually without an attorney. They can also play an important role in expediting cases and the payment of fees and fines, which can be substantial. Multiple violations can accumulate into the thousands of dollars and be recoverable through the filing of liens and the eventual sale of the property.

### **D. Municipal Liens.**

When the best efforts of local building and property maintenance departments fail to achieve the cooperation and compliance of owners, municipalities can file liens to recover their costs for securing and maintaining problem real estate. In Illinois, municipalities may file liens against property for unpaid water and sewer fees 65 ILCS 5/11-139-8; the reasonable costs of cutting grass and weeds, trimming and removing trees and bushes 65 ILCS 5/11-139-8; the removal of garbage and debris 65 ILCS 5/11-20-13; and unpaid municipal taxes 65 ILCS 5/8-13-15.

Traditional liens are typically junior lien holders in foreclosure suits with the exception of demolition liens. Note that the Illinois General Assembly recently enacted legislation to authorize municipalities to record “priority” liens that are junior only to tax liens, as discussed in Section IV of this outline. Recovery can often be difficult after higher priority lien holders such as banks are paid in full. Sometimes lenders are eager to resolve municipal code violations in order to avoid complications in remarketing the property however. Cities frequently levy payment of a transfer tax and require the issuance of transfer stamps to close real estate transactions, which can provide some leverage when working with lenders.

### **E. Demolition, Repair, Enclosure, or Remediation.**

After all reasonable efforts to work with property owners to achieve compliance with building and property maintenance codes have failed and a property continues to present serious and even dangerous conditions the last resort of municipalities is demolition, repair, enclosure, or remediation. Under Illinois law:

The corporate authorities of each municipality may demolish, repair, or enclose or cause the demolition, repair, or enclosure of dangerous and unsafe buildings or uncompleted and abandoned buildings within the territory of the municipality and may remove or cause the removal of garbage, debris, and other hazardous, noxious, or unhealthy substances or materials from those buildings. 65 ILCS 5/11-31-1(a).

Judicial approval is required; however, hearings on applications to the court for demolition, repair, enclosure, or remediation must be expedited and given precedence over all other suits. The costs of these remedies are born by the property owner and can include court costs, attorney's fees, and all other costs related to the enforcement of municipal codes.

### **F. Land Banking.**

Land banking is a land management technique frequently used by local government in the economic development context to control future development. In the case of the foreclosure crisis, land banking can be a useful tool to stabilize neighborhoods particularly hard hit by foreclosures. Land banking involves the purchase of parcels of land by a unit of local government. The land bank is a governmental entity that focuses on conversion of tax delinquent, tax reverted, and abandoned properties into productive use. Land banks allow local government to overcome some of the legal restraints that prevent them from converting public land and public liens on private land into performing (tax generating) assets.

Some of the benefits of the land bank include: (a) providing land and buildings for affordable housing; (b) putting property back on the tax rolls; (c) stabilizing declining neighborhoods by repairing, removing, or redeveloping abandoned, blighted property; (d) developing green spaces; (e) creating developable sites for income generating business by collecting and joining abandoned lots into a business-able sized site; (f) facilitating the revitalization of brownfields; (g) cleaning up the tax rolls and resolve some of the mystery of abandoned, unused properties; (h) providing property owners a way out from under tax delinquent property.

The benefits of land banking go beyond the property itself. While abandoned and vacant properties depress property values, discourage property ownership, and attract criminal activities in the surrounding area, a land bank provides tools to quickly turn these tax-reverted properties back into usable parcels that reinvest in the community's long-term vision for its neighborhoods. Land bank programs act as an economic and community development tool to revitalize blighted neighborhoods and business districts. Land banks can benefit urban schools, improve tax revenues, expand housing opportunities, remove public nuisances, assist in crime prevention and promote economic development.

By transferring vacant and abandoned properties to responsible land owners through a land bank program, local governments benefit because they avoid the significant cost burden of property maintenance, like mowing and snow removal, as part of their nuisance abatement responsibilities. In addition, local governments benefit from increased revenue because the new property owners pay taxes on the property. Also, the local schools benefit because they receive more funding when there is an increase in property owners in their school districts. Land bank programs can increase the variety of mixed-income housing offered and provide more opportunities for affordable housing. Also, land bank properties, which become owner-occupied, discourage criminal activity thereby benefiting public safety and decreasing the cost burden on the local police and fire departments. Finally, the more residents and businesses that occupy property in a neighborhood, the more services and amenities will be needed, which boosts local economic activity.

Many cities like Atlanta, Georgia; St. Louis, Missouri; Genesee County, Michigan; and Cleveland, Ohio have established land bank programs to redevelop vacant and abandoned land as a productive use for their communities. These communities are using land banks as a tool to reuse their urban land and stimulate economic development and neighborhood revitalization.

For example, in Flint, Michigan, a new land-banking program allowed the city and county to leverage \$2 million worth of investments into \$35 million worth of renovations on derelict foreclosed homes. The city's program was authorized by state statute, the Michigan Land Bank Enabling Law. This statute created a "Land Bank Fast Track Authority" that authorizes counties to create land banks through intergovernmental agreements with the state authority. The law defines all land banks as "brownfields" and provides tax exempt status for the properties. More important, it provides cities with express authority to sell properties at less than fair market value, or to lease, demolish, maintain, and/or rehabilitate the properties for resale.

While land banking can be a very useful tool for municipalities desiring to purchase, maintain, and then eventually resell properties when the market rebounds, most states (including Illinois) do not have specific statutory authority for this type of action beyond the general power of municipalities to acquire land for public purposes. Nor do they have the funding to administer a land bank program or to acquire the properties.

#### **G. Tax Increment Financing.**

While sometimes controversial, and nearly always unpopular with local school districts, tax increment financing can provide needed funds to improve and redevelop blighted areas including housing. TIF districts establish boundaries around blighted or underdeveloped areas, including areas with dilapidated and deteriorated buildings and structures, or buildings that do not meet modern or minimal code requirements.

### **III. Prevention of Foreclosures: What State And Local Governments Are Doing.**

According to the Joint Economic Committee of Congress, the cumulative cost of a foreclosure to the homeowner, lender, surrounding property owners (due to the decrease in property value), and municipal government can add up to \$80,000, while the cost of preventing foreclosure is approximately \$3,300. Chicago estimates that vacant and abandoned homes annually cost the

city \$34,000 each on average for inspections, legal action, greater demand for law enforcement, unpaid taxes and utilities, and demolition.

While most proposals to address the foreclosure crisis are national in scope, and focus on the banking industries, state and local government can make a difference, and information is frequently the key. The Village of Bellwood, Illinois, has retained an attorney to provide free advice and community based seminars to residents facing foreclosure. Lenders are sometimes willing to work out distressed loans with the informed cooperation of homeowners. In the State of Ohio where 1 in 58 households is facing foreclosure, the state has recruited 1,300 public and private attorneys to help homeowners negotiate settlements with lenders to avoid foreclosure.

New York City is coordinating non-profit agencies and safety-net programs, offering specific home financing counseling for families confronting foreclosure. Broward County, Florida sponsors counseling and public awareness campaigns and appointed a task force to study solutions, including public service advertising, increased education and early intervention, required communication with lenders before foreclosure, and direct financial assistance.

Other communities are offering direct assistance. Minneapolis is offering forgivable loans of \$10,000 to home buyers for the purchase or rehabilitation of residences in neighborhoods hard-hit by foreclosures. The City of Lawrence, New Hampshire, recently proposed (and later suspended due to cost) a plan to purchase foreclosed homes with the intent to rent back to former homeowners. Berkeley, California, has established a portal website for foreclosure crisis resources including links to credit counselors approved by the US Department of Housing and Urban Development, and information on avoiding fraud in the recovery process.

Cities like Baltimore, Maryland, and Cleveland, Ohio, and states like Illinois, are taking a more aggressive tact by suing banks alleging a variety of discriminatory lending practices that precipitated the crisis in their communities.

#### **IV. What Municipalities Need – Financial and Legislative Assistance.**

While municipalities have a variety of options to reduce the number of foreclosures and tools to deal with the burden on neighborhoods created by vacant and abandoned homes, additional steps need to be taken. As the number of foreclosures continues to grow so do opportunities for the unscrupulous to take advantage of sometimes already financially unsophisticated homeowners. Tighter regulation of so-called foreclosure consultants and lenders is necessary. The foreclosure process should be modified to require pre-foreclosure communication and mandatory work-out consultations. Regional action can be beneficial to avoid patchwork solutions that simply shift burdens from one community to another. Most importantly, appropriate state and federal enabling legislation and funding sources for municipalities are critical to address what has essentially become an unfunded mandate on municipal governments across the country attempting to deal with the fall out from a nation-wide housing crisis.

While the federal government has proposed various legislation (some of which has passed) to address the foreclosure crisis, most of it focuses on solutions for the banking crisis or dealing with individual homeowners. While this type of legislation is clearly needed, there is also a need for the state to enact legislation to provide municipal authority and funding to address not just the

individual foreclosure situation, but the impact that each individual foreclosure has on the community as a whole.

Over the past year, the state legislature has taken some steps to provide Illinois municipalities with additional tools to deal with the impacts of foreclosures. These steps include the introduction of bills to address foreclosures, a few of which were recently enacted and effective, as described below.

**A. New Legislation Recently Enacted.**

**1. Notice to Municipalities of Mortgage Foreclosures (Public Act 96-856)**

One of the concerns raised frequently by municipal staff is that there is no system in place to notify municipalities of foreclosure proceedings of property within their communities. Municipal employees must continuously review court records, county recorded documents, and public notices to find out what properties are entering the foreclosure process. This new legislation, which became effective March 1, 2010, requires that notice of a foreclosure proceeding be provided to a municipality in which the property is located. First, a copy of the notice of foreclosure must be mailed to the municipality in which the property is located at the time the foreclosure proceedings are initiated. Second, notice of the confirmation order (completion of the foreclosure proceedings) must also be mailed to the municipality.

The new law requires a municipality to “clearly publish on its website a single address” where both the notice of foreclosure initiating the proceedings and the notice of confirmation order completing the proceedings should be sent. If a municipality does not maintain a website, it must “publicly post in its main office a single address” where the notice should be sent. There is a “default notice” provision in the new law that provides that if a municipality fails to comply with the notice requirements of this new law, notice must be provided in the same manner as for the service of summons in lawsuits.

It is recommended that a municipality promptly post on its website (or at the village or city hall, if there is no website) an address where these foreclosure notices should be sent. The municipality should also determine who the appropriate contact person is to receive these notices. A sample posting might be as follows:

<p style="text-align: center;"><b><i>Notices of Foreclosures and Confirmation Orders Should Be Sent to the Following Address:</i></b></p> <p style="text-align: center;"><i>Attention: [Contact Person] [Address]</i></p>
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**2. Priority Liens for Property Maintenance Activities on Vacant Property (Public Act 96-856)**

Another issue that has confronted municipalities is recovery of costs when a municipality performs property maintenance activities on vacant properties, such as weed and grass control and garbage removal. While municipalities have authority to record a lien against the property for costs incurred in these activities, these liens are junior to mortgages and usually extinguished

in a foreclosure proceeding. The new law amends various provisions of the Illinois Municipal Code to establish a “priority lien” process for certain property maintenance costs, such as weed removal and grass cutting, pest extermination, removal of infected trees, and garbage removal. These liens would have priority over all other liens in a foreclosure proceeding, except tax liens, and would be paid out of the sale proceeds. This new lien procedure applies only to property maintenance activities performed *after* the effective date of the new law (March 1, 2010).

The process for recording and enforcing a priority lien is set forth in 65 ILCS 5/11-20-15.1, and is summarized below:

- The municipality must record the lien within one year after the cost is incurred.
- The notice of lien must include a sworn statement setting out:
  - (1) a description of the abandoned residential property;
  - (2) the cost of the maintenance activities;
  - (3) the date or dates of the activities;
  - (4) a reference to the statutory authority for the priority lien (i.e., garbage removal or weed removal statute).
- The municipality must keep records of the following:
  - (1) a dated statement of a finding that the property was abandoned;
  - (2) the date when the property was first observed to be vacant;
  - (3) a description of the actions taken by the municipality to contact the legal owner of the property, and a statement that no contacts were made with the legal owner;
  - (4) a dated certification by a municipal official of the necessity and specific nature of the work performed;
  - (5) a copy of the agreement with the person or company performing the work, including the rates and estimated cost of the work;
  - (6) detailed invoices and payment vouchers for the work;
  - (7) a statement as to whether the work was competitively bid, and if so, a copy of all proposals submitted by the bidders.

The new law did not eliminate the traditional liens (such as “weed liens” or “garbage liens”) that are authorized by 65 ILCS 5/11-20-15. Many municipalities have established a process for these traditional liens in their municipal codes. Consequently, a municipality can still choose to record and enforce these traditional liens for property maintenance activities, with the understanding that these liens have a lower priority in a foreclosure action than the new priority liens.

A municipality that wants to take advantage of this new “priority lien” authority should consider adopting an ordinance to amend its municipal code to establish the process for these priority liens consistent with the new law.

### **3. Authority to Secure and Enclose Vacant Structures.**

This new law amends the Illinois Municipal Code to provide additional authority to municipalities to take action to secure or enclose abandoned residential properties without having to obtain a court order through a demolition statute action or other court action. The statute specifically allows a municipality to take actions to ensure that an abandoned building and property are made inaccessible to the general public by boarding up or otherwise closing off windows or other entrances to a building and by enclosing an abandoned property with a fence or other wall. The law authorizes a municipality to record and enforce a priority lien to recover its costs for these activities.

A municipality should consider adopting an ordinance supplementing its existing property maintenance regulations (or its vacant property ordinance if a municipality has one) to include this additional authority and to reference the priority lien procedures discussed above.

### **4. Consolidation of Property Maintenance Liens (Public Act 96-462) and (Public Act 96-856)**

Last year, the General Assembly amended the “traditional” lien statute to authorize a municipality to consolidate or combine into a single lien the costs for all property maintenance activities performed within the course of a year on a particular property.

The new law, effective March 1, 2010, expands this authority to the new priority lien procedure so a municipality can also consolidate or combine into a single lien the costs for all property maintenance activities performed within the course of a year on an abandoned or vacant property.

A municipality can take advantage of the new “lien consolidation” authority for both traditional and priority liens by simply following the statutory procedure for these liens without having to record a separate lien for each property maintenance activity. While a municipality could legally consolidate an entire years’ worth of invoices into a single lien, a municipality should use caution not to wait too long to record a lien or risk a challenge that a subsequent owner did not receive timely or adequate notice prior to purchase.

Municipalities should consider establishing a procedure for consolidation of invoices such as monthly or quarterly recording of liens on a particular property. These activities can be tracked as part of a municipality’s vacant property ordinance and registration records, for those municipalities that have adopted these ordinances.

### **B. Pending Bills.**

There are a number of other bills that have been proposed and are pending before the General Assembly relating to foreclosures. It is not clear which, if any, will be passed in this session

(similar bills were proposed last year but were never enacted). Two of these bills are summarized below.

**1. Vacant Property Ordinance Authority.**

House Bill 1195 and Senate Bill 2101 would amend the Illinois Municipal Code to authorize municipalities to establish rules and regulations for the maintenance and security of vacant properties and to impose registration fees for vacant properties and fines for failure to comply with these regulations. These regulations would allow a municipality to hold the property owner *and* the lender responsible for maintenance and security of the vacant property.

Although there is no express statutory authority for municipalities to enact vacant property ordinances that impose registration requirements, many communities have, nevertheless, already enacted vacant property registration requirements based on a municipality's authority to regulate and abate nuisances. In preparing these ordinances for our clients, we have been careful to draw on existing municipal authority to support the regulations. Of course, having express statutory authority to enact these regulations will enhance existing authority for non-home rule municipalities, particularly with respect to the imposition of registration fees.

**2. Land Banking Authority.**

House Bill 1195 and Senate Bill 2101 would authorize municipalities to create "land banks" to acquire and "bank" (or hold) vacant properties to ensure these properties are adequately maintained and until the properties can be sold and returned to productive use. These bills would authorize a municipality to create a "land bank authority," an entity separate from the municipal corporate authorities, to exercise the powers authorized by statute.