



## Responsible Homeownership Programs

Elements of a Sustainable Homebuyer Program



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### Caveat Venditor!

- Homebuyer activities have been very popular in the HOME Program
- But market conditions have slowed sales, and stuck some programs with inventory that cannot be sold (& nonprofits are perishing)
- As we have said in other session, before you assist development of more homeownership units, make certain your market needs them



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### HOME Homeownership

- HOME can fund homebuyer activities:
  - Development assistance
  - Buyer assistance
    - Downpayment & closing costs
    - Second mortgage assistance
    - 1st mortgage subsidies (interest subsidy or guarantees)
- PJs responsible for ensuring wise investment of HOME funds, including assistance to buyers
  - The underwriting imperative
  - The sustainability imperative



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## The Underwriting Imperative

- Regulatory bases of underwriting:
  - Cost reasonableness (“necessary & reasonable”)
  - Subsidy layering
  - Compliance
  - Repayment
- PJs need policies/standards to determine appropriate level of assistance to buyers
  - Require subrecipients to follow; monitor/review loan decisions/files




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## The Sustainability Imperative

- Real estate recession/foreclosures highlighted risks of unsustainable homeownership
- If assisted homeownership not sustained:
  - NAHA requirements not achieved (affordability period)
  - Household loses equity & credit is damaged
  - Neighborhood property values hurt
    - Chicago: foreclosure w/in 1/8 mile = -0.9% impact on values
    - JCHS: impact within ¼ mile; 1% within 1/20 mi.; foreclosure discount ave. 27%
- PJs need sustainable underwriting




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## HOME Foreclosures

- Study of HOME homebuyer unit foreclosures
  - 5000 buyers, 107 PJs
- Annual foreclosure rates: 1.7 - 5.3%
  - Below FHA, other gov’t programs, but...
- Foreclosure rates lower when:
  - Higher buyer equity required
  - PJ underwriting (credit scores & 1st mortgage)



[www.huduser.org/publications/hsgfin/addi.html](http://www.huduser.org/publications/hsgfin/addi.html)

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## Sustainable Underwriting

- Can homebuyers sustain ownership over compliance period/loan term?
  - Post-closing cash: avoid the post-closing credit squeeze
  - Ability to manage mortgage/financial obligations: good loan terms, reasonable ratios
  - Energy efficiency: control utility costs
  - Ability to maintain: quality/useful life of structure, systems & finishes (PITIUM)
  - Market viability: ability to sell & recover funds over time



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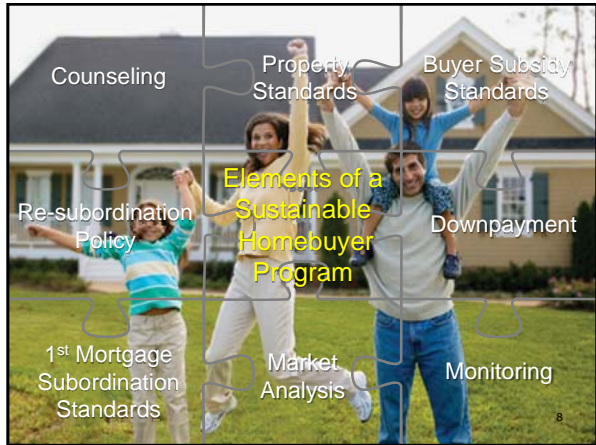
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**Elements of a Sustainable Homebuyer Program**

- Counseling
- Property Standards
- Buyer Subsidy Standards
- Re-subordination Policy
- Downpayment
- 1<sup>st</sup> Mortgage Subordination Standards
- Market Analysis
- Monitoring

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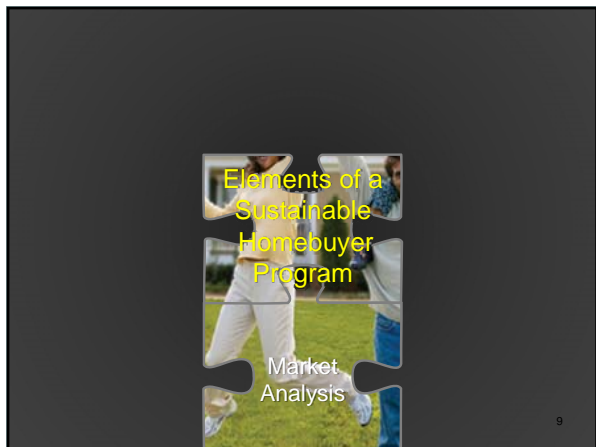
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**Elements of a Sustainable Homebuyer Program**

- Market Analysis

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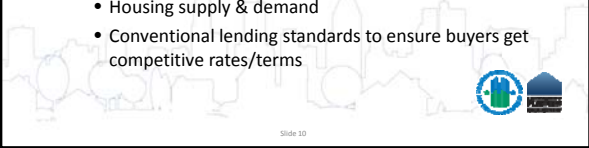
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## 1. Market Analysis

- Why market analysis?
  - Ensure buyers get fair prices & won't be upside down
  - Help buyers get reasonable loans
  - Make sure that HOME investments have reasonable collateral security
- What should be tracked?
  - Housing supply & demand
  - Conventional lending standards to ensure buyers get competitive rates/terms



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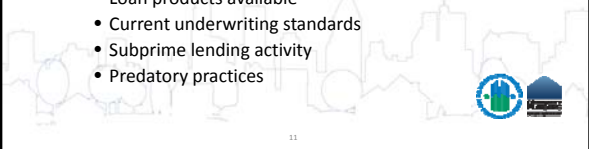
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## Understanding Your Market

- Which way the market is heading:
  - Vacancies
  - Sales prices
  - Activity level (& listing-to-sale time)
  - Status of foreclosures (& the shadow inventory)
- The status of mortgage lending:
  - Loan products available
  - Current underwriting standards
  - Subprime lending activity
  - Predatory practices



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A graphic consisting of three interlocking puzzle pieces. The top piece is dark gray with the word "Counseling" in white. The bottom piece is dark gray with the words "Market Analysis" in white. The middle piece is a photograph of a woman in a white shirt and pants running on a green lawn, with the text "Elements of a Sustainable Homebuyer Program" overlaid in yellow.

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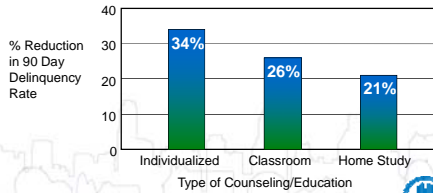
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## 2. Counseling

- Not a HOME requirement, but recommended
- Significant impact on foreclosure rate



Source: *A Little Knowledge is a Good Thing: Empirical Evidence of the Effectiveness of Pre-Purchase Homeownership Counseling*, Freddie Mac, 2001.

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## Counseling, cont.

- Most helpful if counseling precedes home search and mortgage shopping
  - Qualified counselors & current curricula
  - More is better
- Eligible HOME project cost if purchase occurs
- Post-purchase relationship & support is an important consideration for sustainability
  - But HOME can't fund it

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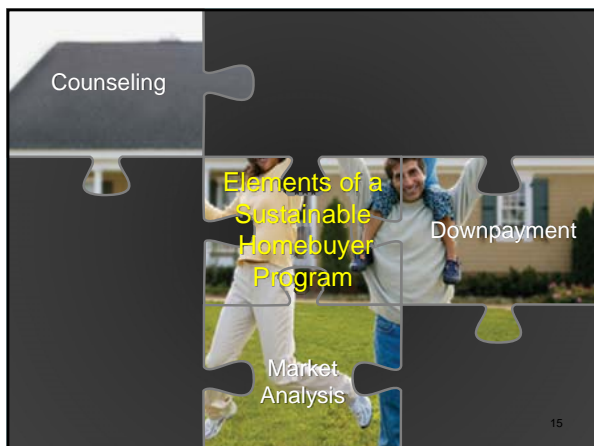
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### 3. Downpayment

- Importance of downpayment
  - Skin in the game
  - Reduce mortgages
  - Demonstrate ability to save for other costs of owning
- But downpayment all but disappeared
  - 33% of all mortgages were 100%+ LTV (2006)
  - 42% of 1<sup>st</sup> time buyers bought with no \$ down (2005)
  - Seller-financed DPA artificially inflated prices
- Lenders now back to 3.5%+ DP
  - Proposed QRM rule: 20% down for best rates



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### Downpayment & DPA

- CDBG/NSP limit DPA to 50% of lender-required downpayment
  - Requires buyers to save for ownership
- Downpayment analysis:
  - Analyze total cash needs: downpayment, closing costs, post-closing cash
  - Develop asset standards: assets required for purchase, excessive asset levels that disqualify for assistance



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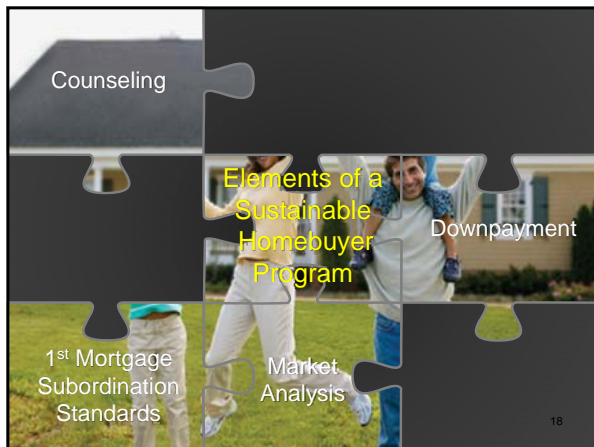
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## 4. Subordination Standards

- 1<sup>st</sup> mortgage terms affect your security
  - You don't have to lend behind any mortgage they find
- PJs should establish subordination standards:
  - Acceptable 1<sup>st</sup> mortgage loan terms:
    - competitive interest rate & terms (for buyer risk)
    - predatory loan terms prohibited
  - Type of mortgages permitted:
    - fixed rate
    - (if necessary) hybrid ARMs (stable rate in early years)
  - LTV/TLTV limits
    - 1<sup>st</sup> mortgage LTV affects downpayment & mortgage insurance
    - TLTV: affects PJs collateral security



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## 5. Buyer Subsidy Standards

- PJs must ensure “adequate but not excessive” buyer subsidy based on:
  - Affordability
  - Sustainability
- PJ must have buyer underwriting standards, considering:
  - Sales price
  - Financing
  - HH income & debt
  - Buyer contribution (downpayment) & assets



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## Buyer Subsidy Standards

- Home approved for purchase
  - Price supported by value
  - Meets household needs (HH size/home size)
- “Optimized” first mortgage
  - Mortgage amount & terms competitive/reasonable
  - “Reasonable” ratios: maximum front & back ratios, but also minimum front ratio (so other debt not excessive)
- Reasonable downpayment based on:
  - Purchase price & loan requirements
  - Buyer assets & ability to meet cash requirements

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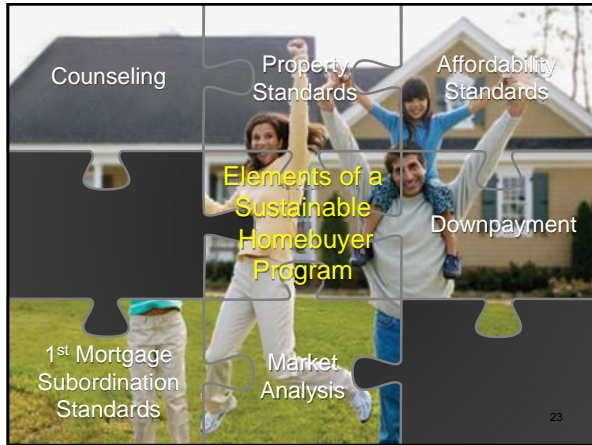
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## 6. Property Standards

- HOME has property standards
  - But existing housing standards are limited
- Sustainable homeownership addresses utility, maintenance & replacement costs
  - Energy efficiency
  - Useful life of systems & structural components
  - Quality/durability of finishes & materials

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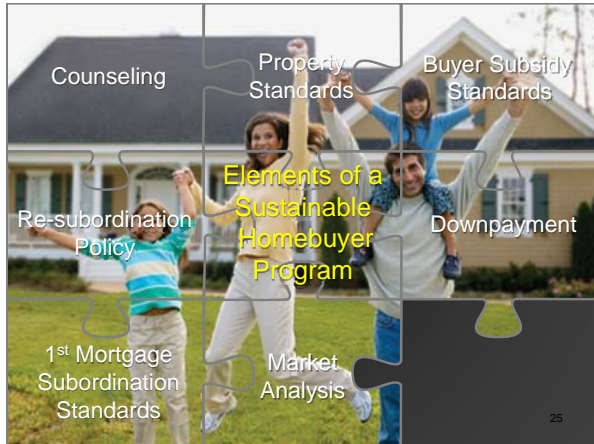
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### 7. Re subordination Policy

- Refinancing: common until prices/equity dropped
  - Better rates/terms
  - Equity takeout: "house as ATM"
- Re-subordination: agreeing to subordinate HOME loan to new loan
- Policy needed:
  - To forewarn buyers
  - To ensure fair treatment



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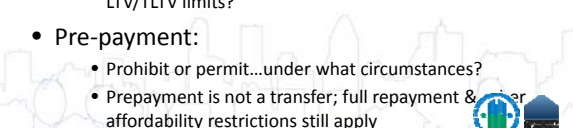
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### Re subordination Policy

- Re-subordination permitted for:
  - Better rates & mortgage qualification standards?
  - Equity takeout: under what circumstances?
- Standards to approve re-subordination:
  - Limits on types of lenders/loans? Conventional rates? LTV/TLTV limits?
- Pre-payment:
  - Prohibit or permit...under what circumstances?
  - Prepayment is not a transfer; full repayment & affordability restrictions still apply



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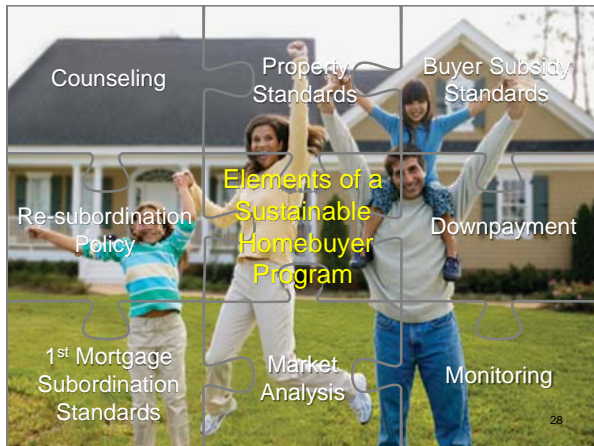
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### 8. Monitoring

- PJs are responsible for all HOME investments made by their subrecipients, CHDOs and other developers
- PJs need to impose buyer assistance program policies & standards
- PJs need to review/monitor buyer assistance provided
  - Part of ongoing risk-based monitoring strategy



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### Wrap Up

- Watch for/read the HOMEfires
- Get back to basics: analyze your market & program design
- Review/revise/update your homebuyer lending policies
- Establish review/monitoring procedures to ensure reasonable buyer assistance



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