Using Mortgage Refinance to Protect Middle Neighborhood Households

Homewise, Albuquerque NM
Intend Indiana, Indianapolis, IN

Mortgage refinancing strategies are proving to be solid approaches for strengthening neighborhoods and preventing displacement of families who are locked into substandard or even unscrupulous loans. Two Community Development Financial Institutions (CDFIs), located in Albuquerque (NM) and Indianapolis (IN), have developed refinance products to help homeowners who have seller-financed contracts (also known as land contracts or real estate contracts) transition to safer and more affordable loans. The effort fits well with their overall goal to protect the equity of owner-occupants and retain affordable housing in the community.

Homewise is a large CDFI that began in 1986 serving New Mexico with a mission to help create successful homeowners and strengthen neighborhoods so that individuals and families can improve their long-term financial wellbeing and quality of life.

Homewise (Albuquerque, NM): In recent years, many homebuyers in Albuquerque have been taken advantage of through alternative, owner financing. Many deals are nearly predatory, involving two- or three-year balloons, high down payments ($20,000 or $30,000) and high interest rates. Upon noticing the increase and looking a little deeper, Homewise found that most borrowers were native Spanish-speaking. Many thought they could not qualify for a conventional mortgage because they were applying with ITIN[1] numbers, so they turned to alternative financing. Many did not understand the terms and conditions of the contracts and found themselves in risky and even predatory situations. With these types of deals, missed payments can cause contracts to revert to tenant-landlord law, meaning just one or two late payments can trigger an eviction and buyers lose all payments they have made.

Homewise completed several refinances for households that came in for counseling, and quickly realized there were more Real Estate Contracts (REC) than they thought. Customers let family members and friends know about the program, and news spread. As Home Purchase Advisors started getting more and more inquiries, Homewise began investigating and realized how difficult it is to pinpoint the scope of the problem. REC's are not filed as public record, so data is essentially unavailable and easily missed. If a deal falls through, and the homebuyer is displaced through a silent eviction, there is no public record of that either. No policies or legal protections exist for these buyers; they essentially have no rights once they enter an owner-financed REC.

Homewise kicked off an official outreach campaign through Spanish-speaking television and radio ads, and inquiries exploded. As Homewise realized how

[1] An Individual Taxpayer Identification Number (ITIN) is a tax processing number issued by the Internal Revenue Service. The IRS issues ITINs to individuals who are required to have a U.S. taxpayer identification number but who do not have, and are not eligible to obtain, a Social Security number from the Social Security Administration because of their immigration status. Individuals with ITINs pay income taxes and can use their tax returns to prove income for a mortgage with some lenders.

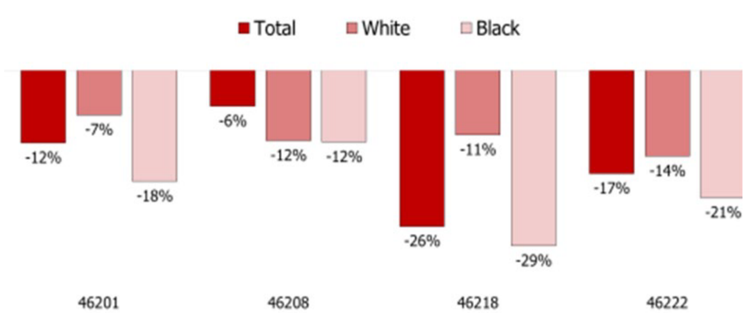
seriously underserved these households were by conventional lenders, they started adding more information on REC's to pre-purchase education and counseling sessions to inform buyers before it's too late. Homewise changed how they talked about the issue with potential buyers, public entities, lending partners, Realtors, and nonprofit organizations in the community. This focus on prevention was as important as intervention options.

The Loan Product. All components of the refinance are done in-house, including origination, processing, underwriting, closing, and loan servicing. These borrowers become clients for life, which allows Homewise to provide support or early delinquency prevention if needed. Homewise services over 7,000 loans and its overall delinquency rate is approximately 1.37 percent. Homewise sells 80% of these refinance loans on the secondary market to its lender partner, Self-Help Credit Union.

Elena Gonzales, Senior Director of Policy and Resource Development at Homewise, says real estate contracts can work if they have reasonable, good terms. However, they often do not. Offering a refinance product to help families out of the situation is an anti-displacement strategy that is important to protecting middle neighborhoods; it helps people achieve stable homeownership, addresses the racial wealth gap, preserves affordable housing options, and helps preserve wealth. "It is important for CDFIs to get involved," says Gonzales. "We have the ability to adapt our products for a good purpose and help families save the wealth they have worked so hard to build."

Intend Indiana (Indianapolis, IN): Intend Indiana had a similar problem with homes purchased on land contract. Since the 2008 recession, Indiana lost about 30% of its homeowners, and the homeownership rate for Black and Brown households dropped significantly more than other groups. The overlap of redlined communities, vacant properties and race was obvious, and the problem spiked again during the pandemic. While the city was offering a rental assistance program and the state was offering a mortgage relief program, households with land contracts and predatory mortgages were not being served. Intend Indiana decided to launch a refinance strategy to solve the problem: "We needed a way to help those who were temporarily out of work and maybe missing a few payments," said CEO, Steven Meyer. "Those families needed help getting caught up like so many others."

Intend Indiana – formerly known as Renew Indianapolis – supports community development through innovative financing and housing development solutions. It operates two CDFIs whose goals include creating and preserving affordable housing, revitalizing neighborhoods, and supporting small business development.



Causes were linked to several factors including 'zombie foreclosures' (when vacant properties owned by banks sit empty because the foreclosure is incomplete), and an increase in investor purchases. Investors were buying homes for next to nothing and then renting them for as much as possible without doing any real maintenance or upgrades. The city saw an uptick in 'lease to purchase' scenarios that required tenants to invest $10,000 or more in improvements but ended soon after with eviction because of a technical default. Intend Indiana began receiving reports from the local fair housing agency about this and answered with its refinance strategy, called IndyAMP (Indianapolis Affordable Modification Program).

The Loan Product. Intend Indiana partnered with local banks and the City of Indianapolis to design the refinance program. Homeowners must live in the city of Indianapolis, the home must be their primary residence, and the owner must have existing mortgage debt. Bank partners originate and underwrite the loans, using the Fannie Mae HomeReady mortgage product guidance (with some exceptions and overlays). Refinance loans offer a 3% fixed interest rate and serve households earning up to 120% of the area median income. The amount is limited to $200,000 and borrowers are allowed up to 44% for the debt-to-income ratio. Once the refinance is in place, the first payment is not due until 90 days after closing, to give clients time to catch up on other bills. To be eligible, the customer needs to be current on payments and have a credit score of at least 600. Lender partners do not require appraisals but instead use broker price opinions (BPOs) which helps get to closing faster with less expense. They also established an alternate way to verify income since people were out of work during the pandemic; they annualize incomes based on the past 30 days of paystubs, rather than two years. There is no PMI since Intend Indiana's CDFI subsidiary, Edge Fund, is holding the loan in portfolio and homeowners are generally able to pay the loan off quickly with this model.

Intend Indiana also allows borrowers to roll a portion of non-mortgage debt into the loan if they need a better debt-to-income ratio to qualify. For example, if a borrower's debt-to-income (DTI) ratio is 50%, and the refinance requires a DTI of 44%, they can roll some of that debt into the loan to decrease the DTI and be able to qualify for the loan.

Lending Partners: Several partners helped to make this program possible. The Edge Fund, managed by Intend Indiana, is the starting point for all refinance loans; the application is started through its website, and they are the repository for all documents. The Kheprw Institute is an outreach partner that works to raise awareness about the program, plus provides housing navigation services including help filling out applications. Intend Indiana determines program eligibility for all applicants; they do the initial application review and turn it over to the bank who applies agreed-upon underwriting criteria. Two partner banks – Stock Yards Bank and Trust and Merchants Bank of Indiana - determine if the borrower is eligible and complete the underwriting process and approval. Intend Indiana signs off on each loan and upon closing, buys the loan back to hold it in house, essentially acting as a secondary market to the bank. This approach could be useful for a nonprofit that does not have loan origination capacity. For Intend Indianapolis, Merchant's Bank services the loans. A third lender, Woodforest National Bank, supported the program by providing senior debt at the start, to enable cash flow for the program.

Offering a refinance option can be a lot to coordinate, but it works for Intend Indianapolis. In one year, the organization closed 20 loans worth about $3M. The average monthly savings to borrowers was $175, which was a huge savings for borrowers; calculated over a 30-year mortgage, that's about $60,000. Plus, these homeowners now have a safe loan that offers protections.

The benefits of the program were quick and obvious so Intend Indiana will keep the program going. Refinance is a long-term anti-displacement strategy that works and is a great wealth building strategy for homeowners. "Coordinating low interest refinance loans can be difficult," said CEO Steven Meyer, "but they can have the same or even greater impact as money invested into future loans."

Lessons Learned

Realize the multiple benefits	Refinance options are not only a great anti-displacement strategy, the savings over time for buyers is significant. The strategy also helps to prevent gentrification by allowing people to stay in their homes.
Invite broad partnerships	Bank partners are essential and generally willing to help if the organization can buy the loans back or provide some method for getting the loans off the books until they can be sold to a conventional secondary market. It's a safe model and allows banks to satisfy their CRA requirements through normal business operations.
Pay attention to CRA updates	Changes to CRA requirements are coming soon. The current plan, which will likely take effect in 2023, states that banks will need to track and support programs serving low-income areas and overlay plans with minority borrowers. These new requirements will make partnerships with nonprofits even more valuable.
Include prevention strategies	Intervention is important but prevention should also be part of the program. Inform all pre-purchase clients and classes about the dangers of real estate contracts and focus on strategies for becoming mortgage eligible for conventional financing.
Do the research	If you are unsure about the rate of real estate contracts in your area, check with local real estate companies, check foreclosure data, and reach out to local fair housing and other nonprofits working with displaced families. Talk to neighborhood residents directly to gather details and share information.
Do the outreach	Build a solid public relations team to get the word out to the community. Partner with nonprofits and share information regularly as well as success stories. Create a solid promotional campaign and include how much money will be saved with a more affordable loan.
Build trust	Since many individuals are confused about the mortgage process and skeptical of banks, it is important to focus on building trust. Build relationships with neighborhood leaders as well as trusted organizations and businesses.

Questions?

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