MORTGAGE LENDERS

IN HOUSING PARTNERSHIPS

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INTRODUCTION

Mortgage lender participation in housing partnerships has developed largely as a response to the anti-redlining movements of the 1970's. The passage of the Home Mortgage Disclosure Act (HMDA) in 1974 and the Community Reinvestment Act CRA) in 1977 gave community groups experiencing disinvestment in their neighborhoods both a tool to evaluate the lending responsiveness of local institutions and an opportunity to use that tool to influence the lending community. Many of the partnerships that developed between lenders and community organizations did so after the community group flexed its muscle through demonstrations or CRA challenges, where the community group opposed a lending institution's move or its opening a branch on the grounds that it had not been adequately providing credit to its service community. Others came about through lenders' desire to improve their CRA records. Still others developed as a result of the lending institution's concern for stabilizing or improving its market area.

While most of these partnerships were not designed to specifically address fair housing, most do increase "fair housing" opportunities. Many partnerships are designed to reduce the cost of homeownership and thus make possible the option of homeownership to minorities, who are frequently among the lowest income groups in most parts of the country. Other partnerships are designed to provide resources for homeowner improvements to their neighborhoods or in their buildings. Still others lower the cost of rental housing to those most dependent upon the investment decisions of others.

Each partnership is created anew through negotiations between the parties and is based on the special needs and resources of each community. However, a number of patterns have emerged from the experiences, based on the programs and legislation that have existed over the last few years. These models include the following:

1) National Bank and Bank Holding Company Community Development Corporations: These are subsidiaries of banks, groups of banks or bank holding companies which are formed to carry out specific rehabilitation programs. Their partnerships with neighborhood groups can include neighborhood board members, formal partnership agreements for specific developments, and complementary activities. City government often participates by providing interest subsidies for CDC projects through its Community Development Block Grants, Urban Development Action Grants, or its tax-exempt borrowing capacities. Two examples of CDC's are the Buckeye-Woodland CDC in Cleveland and the North Carolina National Bank CDC.

2) Savings and Loan Service Corporations: These are subsidiaries of savings and loans or groups of savings and loan associations that may function like community development corporations to carry out housing development or rehabilitation. The service corporation or the individual members provide the project financing. Community-based development groups may form partnerships with the service corporations through joint ventures on specific projects. Other community groups may work with the service corporation in marketing the project or counseling affected tenants. City

government often provides grants or interest subsidies to specific projects. An example of a service corporation is RESCORP in Chicago.

3) Loan Pools: Loan pools are formed by groups of lenders for specific community revitalization purposes (often home purchase and rehabilitation programs). Sometimes local government or other types of corporations also participate in the pool. Community Development Block Grants frequently subsidize interest rates in these pools. Community groups may have a role as borrowers, counselors or marketers of the program. Examples are loan pools managed by Community Preservation Corp. in New York City and the Denver Family Housing Fund.

4) Tax-Exempt Financing: Usually initiated by local government or community groups, proceeds from sale of tax-exempt bonds or other tax-exempt borrowing are loaned for home purchase and rehabilitation at below market interest rates. Private lending institutions participate in program design and originate and service the loans which are then sold to the local government. Community groups often provide marketing and sometimes client counseling services. This technique is being widely used in many cities throughout the country. One example is the North Side Revitalization Program in Pittsburgh.

5) Linked Deposits: In this technique, public funds from state or local treasuries, or from lump sum drawdowns of Community Development Block Grant allocations are deposited in specific financial institutions, often at below prevailing interest rates. In exchange, the institution receiving the deposit agrees to carry out a specific lending program, usually including below market interest rate loans to specific projects or in target areas. Local government often further subsidizes these loans through CDBG or other sources, and community groups may participate in program design, market the program, and screen clients. The East Humboldt Park Mortgage Loan Program in Chicago is an example of the use of a linked deposit.

6) FNMA Triparty Agreements: The Federal National Mortgage Association (FNMA) is a private corporation which purchases mortgage loans from local lending institutions. It is promoting a technique in which the costs of housing construction, rehabilitation and purchase is reduced through the creation of a pool in which a lender makes a portion of the loan at market interest rate and the city makes a portion at a very low interest rate or interest-free through CDBG or UDAG. The lender then sells a large portion of the loan to FNMA. This effectively reduces the interest rates to the borrower and the risk to the lender. A non-profit or community-based group can borrow money under this program. An example is the Phillips Neighborhood Housing Trust in Minneapolis.

7) Neighborhood Housing Services: Neighborhood housing services programs throughout the country develop a neighborhood partnership of lenders, community residents, local businesses, and local government. Each participating neighborhood has a service office with staff to assist residents in upgrading their properties, and has a revolving loan fund to provide credit to borrowers considered to be high risk. Local government participates by contributing to the loan funds, by providing public

improvements to the area, and through code enforcement. Lenders provide bankable loans, contribute to the revolving loan fund and operating expenses, and serve on the boards. Community residents hold a majority of the seats on the boards.

8) Affirmative Marketing/Counseling/Technical Assistance: Many lending institutions, either individually or in groups, have established programs to market their services to minorities and low income groups who might not otherwise be aware of them, to provide credit and home ownership counseling, or to provide technical assistance for various housing and rehabilitation needs. Local government sometimes provides financial support, and community groups often refer clients. An example is the Home Loan Counseling Center in Los Angeles, Ca.

These categories provide a general summary of types of initiatives to date. Most are dependent on subsidies from the federal government, and most were initiated by community organizations or local government. To increase the effectiveness of these partnerships in providing quality affordable housing in stable neighborhoods to the poor and minorities, it is important to strengthen both regulatory enforcement and subsidy design and administration. The Community Reinvestment Act and all fair housing laws and regulations must be vigorously enforced, and the CRA extended to cover financial institutions not now regulated by it. Systematic enforcement provides both the carrot and the stick for voluntary compliance and creative approaches to satisfying the regulatory requirements.

Public programs can also be used in a number of ways to strengthen public-private partnerships. Neighborhood groups need resources to become true partners. Direct funding from HUD will enable them to acquire those resources and thereby strengthen their role in the partnership.

Subsidies for these programs must continue and be augmented. Orienting the administration of the Urban Development Action Grant program so that it can be used more readily for housing would expand the resources available. Tightening and enforcing the Community Development Block Grant regulations and enforcement to focus on the needs of low and moderate income and minority communities would increase the effective use of these resources as well.

Community groups and lending institutions must become better informed about the benefits, costs and risks of such partnerships, as well as of the mechanisms available to reduce costs and risks. Greater use of private mortgage insurance, for example, can lower the risks of certain mortgage loans to the lender. Knowledge of other groups' experiences with similar partnerships can help community groups know what they can reasonably ask of mortgage lenders and can help lending institutions and local government know how to respond to community credit needs.

Additional sources of capital need to be identified and brought into housing investment. Pension funds, insurance companies, private corporations and others can provide the capital that is no longer adequately available from savings deposits.

And finally, the changing nature of the banking industry must be considered. How will the "new" financial institutions such as Sears relate to their communities? What will be the effect of the increasingly large bank holding companies as compared to the independent neighborhood bank or savings and loan association? Will lender profitability increase as interest rates drop? Who will win the contest for savings deposits? All of these questions will affect the future of mortgage lender/neighborhood partnerships.

The examples that follow were chosen to illustrate the range of lender involvement in housing programs and the partnership types described above.

MORTGAGE LENDER CASE STUDIES

Case	Region	Model	Lenders	CBO	CD or UDAG
East Humboldt Park Mortgage Loan Program	4	Linked Deposit	Yes	Yes	Yes
Buckeye-Woodland Community Development Corporation	4	CDC	Yes	Yes	Yes
North Carolina National Bank Community Development Corporation	6	CDC	Yes	Yes	No
RESCORP	4	Service Corp.	Yes	No	Yes
Community Preservation Corporation	2	Loan Pool	Yes	No	Yes
Denver Family Housing Corporation	3	Loan Pool Tax Exempt Bonds	Yes	Yes	Yes
North Side Revitalization Program	2	Tax Exempt Bonds	Yes	Yes	Yes
Phillips Neighborhood Housing Trust	4	FNMA Tri-Party	Yes	Yes	Yes
Home Loan Counseling Center	1	Affirmative Marketing	Yes	No	No
Illinois Neighborhood Development Corporation	4	Community Development-oriented Bank Holding Company	Yes		Yes on a Pe Project Bas

EAST HUMBOLDT PARK MORTGAGE LOAN PROGRAM

East Humboldt Park is a working class neighborhood which houses the nucleus of Chicago's Puerto Rican community. It is a neighborhood made up of brick and frame cottages, greystone and brick two and three-flats, and larger three-story apartment buildings. While its housing stock is typical of Chicago's working class ethnic neighborhoods, East Humboldt Park is unlike many Chicago ethnic neighborhoods in that it has been visibly ravaged by arson, abandonment and demolition. Over the past decade, more than one-third of its housing stock has been lost.

In recent years, new threats have been added to the problems of this community. The eastern edge of the neighborhood has become the target of real estate speculation as young professionals and artists recognize the beauty of its architecture and its convenient location. National economic conditions have increased the already high unemployment, leaving many East Humboldt Park residents unemployed, and high interest rates and energy costs led to widespread disinvestment by building owners, accelerating the cycle of deterioration and abandonment.

In order to reverse the cycle of disinvestment in East Humboldt Park and to protect the current residents from displacement due to speculation and demolition, the Westtown Concerned Citizens Coalition (WCCC) undertook, in 1979, to examine the ways in which local hispanic residents could be assisted in becoming homeowners who would have a stake in maintaining their neighborhood. The WCCC first, with the help of the Woodstock Institute, examined the Home Mortgage Disclosure Act data to identify where local community lenders were making mortgage loans. Armed with the information that Pioneer Bank, which received much local business, was not making mortgage loans in the neighborhood, they arranged a meeting with the president of the bank. This meeting began negotiations which resulted in the establishment of the East Humboldt Park Mortgage Loan Program.

After considering a number of alternatives, it was decided to pursue a linked-deposit strategy which would link deposits from the Illinois State Treasury with below market interest rate mortgages in East Humboldt Park. The partnership would consist of the State Treasurer, the depositor; Pioneer Bank, the mortgage lender; two community-based organizations which would market the program, screen the applicants, and monitor compliance with the requirement that purchasers live in the homes; and the City of Chicago Department of Housing, which would make an interest-free rehabilitation loan available to purchasers of property under this program. The program was to be marketed to people already living in the community, but was to be available to anyone who would live in the property purchased and could meet the bank's normal loan underwriting criteria. Although most of the applicants have been low and modest income hispanics, there was no income or other requirement for program participation.

The State Treasurer already had a program in place which awarded state deposits to commercial banks at below market interest rates to leverage bank participation in specific community-oriented loan activities, particularly new construction of single-family detached housing. This program, however, had not yet been used in inner-city neighborhoods.

Lengthy discussions between the State Treasurer's office, the bank and the community resulted in agreement that the State Treasurer would deposit up to $1 million in Pioneer Bank on a reimbursement basis as the bank approved mortgages under the program. The reimbursement deposits earned 7 1/2% interest for one year, and would be renewed for a second year at the same rate. As a further incentive to Pioneer Bank to participate in the program, an additional $1 million of state money was deposited in the bank at an interest rate 1 % below prevailing rates, which would be renewed for one year.

The Bank's role in this program is to make up to $1 million in mortgage loans in the community at 10% interest per year. The bank uses its normal underwriting standards for these loans, with the understanding that the lower than normal interest rates will make the housing affordable to community residents. While the state deposits only remain in the bank for up to two years, the loans are amortized over 25 years with interest rates at 10% for ten years after which they are re-negotiated. The loans require a minimum 10% downpayment with private mortgage insurance if the downpayment is less than 20%. The private mortgage insurer insures the top 20% of the loan against foreclosure; therefore, the bank has less at risk than it would with a conventional loan. The borrower pays the premium of 1/2 percent of the unpaid balance until his/her equity exceeds 20%.

Two community organizations also play a role in this program. The Spanish Coalition for Housing, a HUD-certified counseling agency located within the neighborhood screens all program applicants and accompanies them to the bank for their application interview. The purpose of the screening is to save the bank staff time by discouraging ineligible applicants from applying, and to discourage real estate agencies involved in speculation or promoting gentrification in the neighborhood from using the program to their own ends.

The Westtown Concerned Citizens Coalition, the umbrella organization responsible for initiating the talks which led to the program's development, is responsible for marketing the program to area residents and monitoring both program operation and the residency requirement after houses purchased under the program are occupied.

Finally, the City of Chicago offers a Community Development Block Grant-funded rehabilitation loan which can be made by the bank to borrowers having incomes below median as a purchase/rehabilitation package. The rehabilitation loans are interest-free and structured as deferred payment loans; no payments are made by the borrower unless the building is sold.

The linked deposit technique, coupled with extensive community involvement and local government support was, in this example, a cumbersome one to set up, but a promising one for the future of the neighborhood. It involved effective use of public deposits, little risk for the bank, an opportunity for the bank to improve its relationship with its service community, and a real role for the community groups who, once they made the program happen, were able to continue to participate to insure its success. While the role of local government was less significant, its support was also important in establishing a precedent for future partnerships using this technique. Additional agreements between the partners can be made, based on this experience, to continue to supply housing ownership opportunities to the modest income Puerto Rican residents of this neighborhood, and the technique and structure set up for this program can be replicated in other neighborhoods and in other cities.

BUCKEYE-WOODLAND COMMUNITY DEVELOPMENT CORPORATION, CLEVELAND, OHIO

The Buckeye-Woodland CDC was formed after frequent demonstrations at banks and two long CRA challenges by community organizations in Cleveland led several of the major commercial banks to decide that it might be less costly to work with the community than to incur the legal and "good will" costs in fighting the community. The result was the creation of a for-profit community development corporation sponsored by four major Cleveland commercial banks (not those previously targeted by the community in its CRA actions)and a non-profit technical assistance organization working in tandem with a strong community organization able to effectively advocate the needs of the neighborhood residents.

The Buckeye-Woodland CDC was approved by the U.S. Comptroller of the Currency in 1982 as the first multi-bank community development corporation. It was created through the joint efforts of the Buckeye-Woodland Community Congress and the four sponsoring commercial banks--BancOhio National Bank, Central National Bank of Cleveland, Society National Bank, and Union Commerce Bank. Initial investment by the banks was $70,000. The purpose of the CDC is to rehabilitate housing and reverse deterioration in the Buckeye-Woodland neighborhood.

Buckeye-Woodland is a neighborhood made up predominately of single-family and two-family homes. Its population, in the last ten years, changed from 75% white ethnic to 75% black. Sections of the neighborhood vary from areas of moderate-income owner-occupied housing to very low-income areas with absentee landlord-owned buildings, many vacant lots, and generally deteriorated buildings. There are few major businesses in the community, and commercial areas are in need of revitalization.

The BWCDC is a for-profit corporation, initially capitalized by the sponsoring banks. Its Board of Directors is made up equally of bankers and community residents, with one additional member representing local government. The executive director is on loan two days a week from Central National Bank, and office rental and equipment have been donated by the sponsors. Profits from the first three years of operation will be reinvested in the corporation.

Working closely with BWCDC is the Buckeye Evaluation and Technical Institute (BETI), a not-for-profit corporation funded primarily through contributions from foundations. Equipment and office space are supplied by the lending institutions. BETI provides technical support to the BWCDC with market research, neighborhood outreach, building acquisition, specification writing, and construction supervision. In addition, it carries out projects independent of BWCDC but supportive of its general goals. A weatherization program carried out by BETI provides insulation and solar equipment to homeowners in the neighborhood at a cost 80% subsidized by local energy corporations and other contributors. A paint program to improve appearances of targeted blocks utilizes donated paint and the efforts of community residents.

In the year that the two organizations have been in existence, five houses have been purchased and have been, or are in the process of being rehabilitated. These rehabbed homes have been sold to neighborhood residents. Plans for the second year call for a major increase in homes rehabilitated to between 20 and 25. This increase is due, in part, to the availability of a line of credit at a 7% interest rate from the Local Initiative Service Corporation (LISC), a consortium of corporations and foundations. Also available to the program in the upcoming year is a pool of funds made available from the City of Cleveland's Community Development Block Grant allocation, which will be used to write down interest costs for home buyers.

The strategy of the program in the upcoming year will be to concentrate all of the available programs on a target area within Buckeye-Woodland, in order to stabilize a number of declining blocks. After that has been accomplished, attention will be focused on the most deteriorated sections of the area.

The combination of the three types of organizations--the community development corporation, the non-profit technical assistance organization, and the community-based advocacy organization--with support from the city and foundations, has been a successful one for Buckeye-Woodland. The community development corporation approach has brought a much greater contribution to the community from the lending institutions than a corporate gift of a few thousand dollars. The banks not only are applying their knowledge of banking and business to a public purpose, but have made a financial investment in the corporation and, therefore, have a larger stake in its success.

The non-profit technical assistance organization, Buckeye Evaluation and Technical Institute, is able not only to support the BWCDC in its efforts, but to marshall the resources of foundations and corporations and engage in non-profit activities important to the overall stabilization of the neighborhood.

The Buckeye-Woodland Community Congress, which started the whole process through its willingness to take action on behalf of its members, participates on the board of BWCDC and can apply the pressure of the citizens, when needed, on city government and on corporations and institutions important to the revitalization of the neighborhood.

COMMUNITY PRESERVATION CORPORATION, NEW YORK, NY

The Community Preservation Corporation was formed in 1974 by a group of financial institutions in New York who recognized the unmet need in some city neighborhoods for financing to preserve the deteriorating multi-family housing stock which provides much modestly-priced housing for the low and moderate-income residents of New York. They established a partnership of private capital, public subsidy and support, and private enterprise which pioneered a low-cost approach to multi-family housing rehabilitation.

Thirty-three financial institutions currently contribute to a $100 million capital pool for mortgage and rehabilitation loans originated and serviced by CPC. CPC staff work with existing building owners and potential investors in assessing their rehabilitation and financial needs, and in helping them to carry out moderate rehabilitation of occupied buildings. The rehabilitation includes replacement of major systems such as plumbing, heating and wiring, as well as weatherization, security and cosmetic improvements. Costs per unit are well below those of substantial rehabilitation or new construction, thus maintaining housing at reasonable costs.

The City of New York's Department of Housing Preservation and Development and other city agencies provide their support through tax abatements and exemptions, through the provision of Section 8 rent subsidies where available, through rent increase authorizations where necessary, and through provision of Community Development Block Grant-funded loans at 1% interest to bring down the costs of financing so that rents will not exceed the abilities of existing tenants to pay them.

While the program is designed for the for-profit investor, corporations spun off by two community institutions (a synagogue and a hospital) have also been developers under the program with the purpose of improving their neighborhoods and providing housing for their members. Community-based organizations are regularly informed of CPC's and the landlord's plans for building improvements and rent increases.

Since the inception of CPC, 216 loans have been made, totalling 9977 units and $92.8 million.

DENVER FAMILY HOUSING CORPORATION, DENVER, CO

The Denver Family Housing Corporation is a partnership of the public and private sectors and community organizations. The program provides below market rate home purchase financing through a combination of tax-exempt bonds and a fund made up of foundation contributions, corporate contributions and Community Development Block Grant funds. Community organizations are represented on the board of directors and operate neighborhood housing counseling centers which refer applicants to the program.

The home purchase loans are made available through two sources of financing. A first mortgage is funded through the sale of tax-exempt bonds by both the city and state governments. A separate second mortgage comes from the Family Housing Fund, a pool of $1 million made up of contributions from foundations, corporations and local government. Community development block grant funds make up 20% of the pool and have been loaned at zero interest. Other contributors to the fund include the Local Initiatives Service Corporation (LISC) and a major lending institution, Midland Savings and Loan. Second mortgage loans from the fund are made at an interest rate of 8 1/2%. Both first and second mortgages are originated by local lenders.

Community groups make up one-third of the board of directors-- an equal number to business and to corporation representation. Two community groups have also received contracts from the program to operate neighborhood counseling centers which, among other services, refer clients to the program.

NORTH SIDE REVITALIZATION PROGRAM, PITTSBURGH, PA

This program was formed by the City of Pittsburgh's Department of Housing in 1979 to address the need for construction, rehabilitation, and permanent mortgage financing in an ethnically and racially diverse group of six neighborhoods. The program, designed cooperatively by lenders, neighborhood groups, and city government, combine three components. The first provides below market rate first mortgage loans for purchase, new construction, rehabilitation, and refinancing with rehabilitation to investors and homeowners in the area. Funds for these loans come through the sale of tax exempt mortgage revenue bonds issued by the City's Urban Renewal Authority.

Equity participation loans funded with Urban Development Action Grants and Community Development Block Grants make up the second program component. These provide special second mortgages which can either make up 15% of the total costs for low and moderate income homeowners or close the appraisal gaps in buildings where the cost of the rehabilitation needed plus the purchase price exceeds the appraised value of the building. In the first case, the loan is repayable only at sale of the building. In the second, the loan is repaid through monthly installments.

A construction loan fund completes the program. The Urban Renewal Authority borrows money for this loan fund from local banks at a tax exempt rate to make construction loans within the North Side area. Construction loan repayments are returned to the fund to be used on a revolving basis.

All of the loans for the program are originated and serviced by participating local lenders. Six neighborhood groups have formed a federation called the North Side Development Alliance to market the program within the neighborhoods, to monitor the progress of the program, and to advise the City on program performance.

PHILLIPS NEIGHBORHOOD HOUSING TRUST, MINNEAPOLIS, MN

The Phillips Neighborhood Housing Trust in Minneapolis is a non-profit, community-owned organization which has arranged a partnership with the Minneapolis Community Development Agency, David C. Bell Investments, a mortgage company, and the Federal National Mortgage Association (FNMA) through its Municipal Tri-Party Participation program for financing the rehabilitation of 36 units of rental housing for low income people in a declining inner-city neighborhood. The project, costing just over $1 million, will receive about two-thirds of its financing from the mortgage company at conventional lending rates and one-third from the City of Minneapolis through its Community Development Block Grant program. Part of the City funds will be structured as a no-interest, thirty-year second mortgage, and the remainder will be structured as a grant. This will lower the effective interest rate to around 10%. FNMA will purchase the loan from the mortgage company.

Phillips Neighborhood Housing Trust will act as the developer and will manage the buildings after work is completed. The rehabilitated buildings, mostly two-family and a few single-family houses, will be available to low-income tenants through the Section 8 moderate rehabilitation program, which will guarantee that the rents will remain affordable to low income tenants for fifteen years.