THE PHILADELPHIA MORTGAGE PLAN:
TESTING TRADITIONAL PERCEPTIONS
OF INNER CITY LENDING

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Introduction

The purpose of this paper is to present an analysis of the Philadelphia Mortgage Plan (PMP), a cooperative effort initiated in October, 1975 by the following financial institutions: Philadelphia Savings Fund Society, First Pennsylvania Bank and Philadelphia National Bank. PMP was designed to adjust the lending policies and practices of participating institutions in order to provide conventional home mortgage financing throughout the city of Philadelphia to creditworthy individuals, especially those individuals seeking to purchase single family property in older residential neighborhoods. A PMP mortgage is defined as a mortgage of $ 15,000 or less.

In an era where there is an increasing realization that the revitalization of the inner city primarily depends on the initiative of the private sector, this paper presents a case study of a private sector reinvestment effort initiated without government participation or subsidy. This paper is designed to provide planners and neighborhood advocates with ideas for motivating the private sector in various cities to engage in investment activities intended to ameliorate inner city disinvestment. Neighborhood disinvestment is a process by which institutions and individuals systematically withdraw financial resources from a neighborhood perceived to be declining.

Methodology

This analysis of PMP is based on information obtained through interviews with representatives of participating financial institutions; staff members of the Greater Philadelphia Partnership, a not-for-profit civic organization which played an interstitial role in creating PMP; and public interest groups and neighborhood residents who have been active in monitoring PMP. The data analysis presented is based on raw data collected by the Greater Philadelphia Partnership and a survey of financial institutions conducted by the Institute for the Study of Civic Values, a not-for-profit public interest group based in Philadelphia. Other sources which were employed included a literature search of selected periodicals, and a review of Congressional testimony and speeches presented by PMP representatives.[1]

The basic questions which this paper attempts to answer are listed below.

1) What are the goals of the Philadelphia Mortgage Plan?

2) Who are the key actors involved in PMP?

3) Has PMP caused participating lenders to alter their lending policies and practices?

4) Has PMP increased the supply of conventional credit in Philadelphia neighborhoods?

5) Who was responsible for initiating PMP?

6) Why was PMP created?

7) Does the experience of PMP participants validate or invalidate the assumption that inner city lending is a high-risk activity?

8) What is the potential for a PMP type effort to be initiated in other cities?

Goals of PMP and Participants

The basic goal of the Philadelphia Mortgage Plan is modification of traditional lending practices in order to make them more responsive to the credit needs of older Philadelphia communities. The two key components of this effort are the commitment of senior bank management to the goal of the Plan, and the development of a candid working relationship between lenders and neighborhood groups engaged in monitoring PMP.

PMP was not created to be an ongoing special "high risk" lending program separated from the ordinary lending procedures of participating financial institutions. Instead, it was designed to be an effort to adjust, on a permanent basis, policies concerning the underwriting and appraisal of all mortgage applicants and property.

Initially, PMP was assumed by some observors to be an effort where financial institutions were "donating" a special pool of credit to be used to accomplish a "social purpose." In response to such misunderstandings of PMP, James Bodine of First Pennsylvania Bank made the following statement:

> I lament the tendency of some to regard PMP as a special charitable "do-gooder" effort. This is precisely what the PMP is not. It is a sound business proposition and should continue to be a good investment for Philadelphia's financial institutions. Banks can earn a profit on the lending activity that has been stimulated through the PMP.[2]

After the initiation of the Philadelphia Mortgage Plan by the three founding institutions, other local financial corporations began to join the effort. Currently, the following lending institutions are involved in PMP: Beneficial Savings, Central Penn Bank, Community Federal Savings and Loan Association, Fidelity Bank, First Pennsylvania Bank, Girard Bank, Industrial Valley Bank, Lincoln Bank, Philadelphia National Bank, Philadelphia Savings Fund Society, Provident Bank and Western Savings.

Although PMP has been successful in attracting the support and participation of local commercial and savings banks, it has only been able to secure the participation of one savings and loan association. According to the Insured Savings Association of the Delaware Valley (ISA), which represents seventy-eight associations, the savings and loan industry has not particpated in PMP for three reasons. First, associations prefer to devote their reinvestment efforts to the two local Neighborhood Housing Service programs.[3] Secondly, ISA contends that most associations already employ PMP underwriting criteria.[4] Thirdly, ISA members were concerned that the addition of numerous associations to the PMP partnership might complicate the oversight process which has been established between the small number of lenders currently participating and concerned community organizations.[5]

Another factor not stated by the ISA, but of concern to PMP participants, is the savings and loan industry's impression that PMP is viewed by the public as a commercial and savings bank effort. Consequently, associations may be reluctant to join because they would be forced to share publicity with their competitors. Given this concern and the fact that state and federal regulators of financial institutions are beginning to view inner city reinvestment initiatives favorably in reviewing applications for structural changes, associations desire to support efforts, such as NHS, which are viewed as reinvestment strategies primarily facilitated by the savings and loan industry.[6]

In addition to attracting the participation of primary lenders, the three founding institutions were faced with the task of encouraging the involvement of the private mortgage insurance (PMI) industry.[7] Although PMP participants were optimistic about the risk of inner city lending, they are required by regulatory agencies to compel mortgagors who receive mortgages which are for more than 80% of the value of the property financed to purchase private mortgage insurance. Since PMP participants desired to reach that portion of the market which had less than a 20% downpayment, they were dependent on the participation of private mortgage insurance companies to make the Plan work. Fortunately, the private mortgage insurance industry was willing to insure 25% of the difference between the downpayment and the total value of the property purchased.[8]

Organizational Structure

The Philadelphia Mortgage Plan is a voluntary confederation of fourteen financial institutions which is committed to improving the housing stock and condition of inner city neighborhoods through the provision of conventional credit to creditworthy borrowers. All participants have agreed to use underwriting criteria established by the three founding institutions. They also have made a commitment to participate in both a peer and public review of their performance in extending credit to residents of inner city neighborhoods.

The peer review system involves the review of all rejected mortgage applications for \$ 15,000 or less by a committee consisting of a loan officer from each participating institution. The loan officer from the institution which rejected a given mortgage application presents his rationale to the review committee. Another member of the committee may feel that the application should have been accepted. This committee member can suggest that the rejecting institution reconsider the loan or suggest that his institution would favorably entertain the application. However, the committee does not have the authority to force an institution to reconsider a rejected loan application.

The public review process consists of quarterly meetings between community representatives and participating lenders. During these meetings, the Greater Philadelphia Partnership presents the latest data on the volume and location of mortgages granted and applications rejected by PMP participants. The meeting is then opened for general discussion concerning the performance of PMP. Although there is a committee of community representatives which monitors PMP performance, this committee has no formal authority over the conduct of the Plan.

PMP Underwriting Reforms

The most heralded aspect of the Philadelphia Mortgage Plan has been the underwriting reforms which have been undertaken by PMP participants. For decades, inner city neighborhoods have been disadvantaged by underwriting practices which devalue inner city property and unjustifiably discriminate against moderate income families which are disproportionately located in the inner city.[9]

In determining whether or not to grant a mortgage loan, lenders engage in a process referred to as loan underwriting. Loan underwriting is divided into two components: credit underwriting and property underwriting.

Credit underwriting is a process whereby a loan officer determines if a mortgage applicant possesses a high probability of repaying the credit extended plus interest. A lender investigates the applicant's credit references, employment history, income, assets and current debts. Prior to the passage of the Equal Credit Opportunity Act (ECOA), lenders refused to consider welfare payments, child support payments or the income of working wives as effective household income.[10] Despite the existence of the ECOA, which prohibits discounting such income, some lenders allegedly continue to refuse to consider welfare income in analyzing an individual's ability to meet monthly debt service. Since households which receive welfare income are disproportionately located in the inner city, inner city neighborhoods are likely to be disadvantaged by standards which prevent the extension of credit to families subsidized by welfare programs.

Prior to the initiation of the Philadelphia Mortgage Plan, some Philadelphia financial institutions did not recognize the income of the co-mortgagor or consider welfare income to be effective income. In 1975, however, PMP participants began to consider such income in credit underwriting. As Herb Bowers, an Assistant Vice-President of Philadelphia National Bank once stated, "what is better confirmed income than welfare? You don't even have to work for it; it's there."[11]

Consequently, PNB and several other lenders established a twice monthly mortgage payment program which was designed to encourage borrowers on public assistance to make their mortgage payments as soon as they receive their checks.

The other part of the analysis performed by a loan officer in analyzing a mortgage application is property underwriting. The purpose of property underwriting is to insure that the value of the property is equal to or greater than the sale price. This is done to protect the lender's investment in case the borrower is unable to repay the mortgage and the lender is forced to take the property through foreclosure. In such cases, the lender must be able to sell the property for a price equal to or greater than the sum equal to the mortgage amount plus the lost interest, and the cost of servicing the loan and selling the property.

Prior to the establishment of the PMP, <u>some</u> Philadelphia financial institutions, like many institutions throughout the country, maintained the following property underwriting standards:

1) No mortgages were granted for properties 75 years of age or older;

2) No mortgages were made in the inner city;

3) No mortgages were granted for the purchase of properties with a sale price of less than $ 15,000.[12]

The cumulative effect of these standards was to withhold conventional mortgage credit from a number of Philadelphia neighborhoods, and to deny conventional financing to a substantial number of moderate-income and lower-income households.

Assuming that the property which a mortgage applicant desired to purchase is not rejected because of the lender's initial property standards, an appraisal of the property will be undertaken. An appraisal is necessary to insure that the market value of the subject property is equal to or greater than the sale price.

On the basis of his professional judgment and available data, an appraiser estimates the value of the property in question. If the appraised value of the property is equal to or greater than the sale price, then the lender may grant a loan, usually for an amount equal to 80% of the sale price. However, if the appraised value is less than the agreed upon sale price, then a loan may be offered for only 80% of the appraised value. Consequently, the borrower would have at least three options: secure the funds required for a larger downpayment; negotiate a reduction in the sale price; or void the purchase contract.

Appraisers have been accused of underappraising property in inner city neighborhoods because of their belief in models of neighborhood decline which implicitly or explicitly suggest that the presence of minorities or low-income residents in the neighborhood where the subject property is located, or in an adjacent neighborhood, represents an inevitable decline in property values.[13] Consequently, appraisers devalue property in such areas on the basis of their <u>perception</u> of the future.[14]

If appraisers believe that property values may decline in the near future and appraise properties for an amount significantly less than the agreed upon sale price, then they alone may reduce property values in that neighborhood. By acting upon their assumptions that values will decline, appraisers can create a self-fulfilling prophecy which often results in neighborhood deterioration. Neighborhoods which incur such pressures are likely to be placed at a competitive disadvantage relative to other areas, particularly exurban areas which appraisers do not perceive to be declining. Neighborhoods which are devalued by appraisers may experience disinvestment by property owners since they will be unable to assume that the value of their properties will appreciate and will therefore be reluctant to make improvements or maintain their properties.

Before the creation of the Philadelphia Mortgage Plan, Philadelphia financial institutions utilized appraisers which employed traditional and accepted appraisal practices which were based on the inevitability of the decline of neighborhoods which were populated, in part, by low- or moderate-income or minority families, or were adjacent to such neighborhoods.

However, during the planning stage of the Philadelphia Mortgage Plan, the initiators of the Plan realized the role that self-fulfilling appraisal practices had played in neighborhood disinvestment. The following comment by Todd Cooke, President of the Philadelphia Savings Fund Society, underscores this point.

> Disinvestment has occurred in the past, not only because banks were reluctant to risk depositors' funds in older neighborhoods, but also because they were hesitant to encourage a prospective homeowner to make an investment which might depreciate owing to the location of the house in a declining neighborhood. In this process,

> the exercise of propert caution -- perhaps, in some instances, excess caution, caused whole neighborhoods to become suspect. The new policies retain the same concern, for home buyer and depositor, but are based on a closer, block-by-block, house-by-house analysis. Essentially, the approach avoids tarring all the properties in one neighborhood with the same brush.[15]

The Philadelphia Mortgage Plan established new appraisal criteria which must be employed by all participating banks as well as appraisers that are hired by PMP banks. The PMP appraisal changes involved the appraising of a given property according to the structural condition of the subject property and all other property located on the immediate block. Consideration of the surrounding "neighborhood" was no longer permitted.

The following statement by Herb Bowers, an Assistant Vice-President of PNB and a certified appraiser, expresses the perspective PNB participants had undertaken in approaching local appraisers.

> ....we talked to the appraisers -- those open-minded, lovable chaps -- about how the neighborhood works on the economic bell scale -- good, excellent, and ugh..... what we said was: 'Okay, we want you (to forget the neighborhood and) appraise the remaining economic life of this block, on the bricks and mortar of the block. We want to know how long the damned house (and other houses on the block) will be there, irrespective of who the occupant is... If behind the block are the headquarters of the Mafia, forget it. We want two sides, corner to corner.[16]

In analyzing the block on which the subject property is located, PMP participants have suggested that appraisers regard the following criteria as favorable to mortgage lending and the appreciation of property values.

1) Abandonment and vacancy rate of no more than 10% in the immediate block;

2) Median property value of $ 6,000 in the immediate block;

3) The existence of a strong and cohesive neighborhood organization which considers the block on which the subject property is located to be part of its area of concern;

4) The presence of a non-profit developer who is rehabilitating abandoned units, or the existence of other ongoing programs by public agencies, lenders or private groups to improve or rehabilitate housing and;

5) Cooperation of absentee owners with neighborhood residents to improve housing and make needed repairs.[17]

Initially, this revisionist approach to the appraisal of inner city property was not well received by appraisers. However, after realizing that participating financial institutions would not hire appraisers who did not employ PMP appraisal criteria, most appraisers had a dramatic change of heart.

Impact of the Philadelphia Mortgage Plan

City of Philadelphia

One method of measuring the impact of PMP on the city of Philadelphia is the total number of mortgages which have been granted. From October 1, 1970 to December 31, 1977, the lenders participating in the Philadelphia Mortgage Plan had received 4,750 applications with an aggregate value of $ 50,019,827.[18] PMP participants had granted 2955 mortgages valued at $ 31,563,615, and had rejected 1,010 applications valued at $ 9,831,405.[19] The average mortgage granted was for $ 10,538.

Although fourteen financial institutions currently participate in the Plan, Table I indicates that the three institutions which created PMP have made 58% of all PMP mortgages as of July, 1977.[20] This is probably due to the participation of these institutions since the first day of the Plan; their continuing commitment; and the fact that they have more resources than other local lenders.

The value of PMP mortgages has ranged from $ 3,000 to $ 15,000.[21] Sixty-three percent of all mortgages granted as of December, 1977, were between$ 7,000 and$ 13,000, while 37% ranged from$ 7,000 to$ 13,000.22 Forty-five percent of the mortgages were for 95% of the appraised value of the property, 42% of the mortgages were for 90% of appraised value, and 14% were for 80% or 85% of value.[23]

Twenty-one percent of the mortgage applications received were rejected. Thirty percent of the rejections were caused by insufficient income, 26% were due to poor credit, 19% were due to the condition of the subject property, and 12% were the result of the condition of the block in which the property was located.[24]

The racial composition of PMP mortgage applicants has been 70% black, 20% white, and 10% other (Spanish, Oriental, etc.).[25] Two-thirds of all applicants were couples, while one-third were female-headed households.[26] The total family income of applicants ranged from $ 9,000 to $ 15,000 per year.[27]

Although the application rejection rate appears to be high,

Table I

PMP Performance

(October 1977 to July 1977)

Financial Institution	No. of Mortgages Granted	Dollar Amount of Mortgages	Average Mortgage Amount
Philadelphia Nat'l Bank	426	$ 4,356,925	$ 10,227
Philadelphia Savings Fund Society	424	4,722,700	11,138
First Pennsylvania Bank	393	4,239,200	10,786
Girard Bank	248	2,680,100	10,806
Fidelity Bank	167	1,750,515	10,482
Industrial Valley Bank	106	1,125,150	10,614
Continental Bank	105	1,222,050	11,638
Beneficial Savings	81	822,000	10,148
Germantown Savings	67	693,450	10,350
Provident National Bank	65	653,370	10,051
Western Savings	55	568,295	10,332
Central Penn Nat'l Bank	13	149,000	11,461
Frankford Savings	12	112,000	9,333
Community Federal Savings and Loan	0	0	--
Totals	2,162	$ 23,127,755	$ 10,697

Source: The Greater Philadelphia Partnership one has to realize that prior to the initiation of PMP, very few of the households which have obtained mortgages through PMP were able to obtain conventional financing. According to James Bodine, the high rejection rate is, in part, due to the initial perceptions of many real estate brokers who assumed that the Plan was a give away.[28] Bodine has contended that brokers "attempted to sell some badly deteriorated, junk properties through the bank."[29] Allegedly, brokers were performing "sloppy screening jobs" and referring individuals without sufficient income to support the debt service.[30] Since the initial misunderstanding of PMP was ameliorated by Bodine and other lenders, brokers have reportedly been more discriminating about the properties which are referred to PMP participants.

A second measure of the impact of PMP is to examine the distribution of mortgage loans granted by PMP participants. A comparison of mortgages granted in Philadelphia during 1975 with mortgages extended in the city during the first six months of 1976 indicate whether participants shifted their lending emphasis from the suburbs to the city. As indicated in Table II, one institution, Girard Bank, has dramatically shifted from a suburban to an inner city focus, while two other lenders, First Pennsylvania and PSFS, have continued to increase their activity in the city.[31] The other four participants surveyed revealed that almost two-thirds of their mortgage lending during 1975 was in the suburbs.[32] Two of these institutions, Beneficial and Western increased the percentage of their total mortgage lending in the city during the first half of 1976.[33] However, Germantown Savings Bank's portfolio did not change while Provident's record reflects a de-emphasis of city lending relative to suburban lending.[34]

Table 2

Comparison of Mortgage Lending Activity in City and Suburbs by PMP Participants

	1975		First Six Months of 1976	
Financial Institution	City	Suburbs	City	Suburbs
Girard Bank				
# of mortgages	32	63	67	12
% distribution	34%	66%	85%	15%
First Pennsylvania Bank				
# of mortgages	320	142	332	69
% distribution	69%	31%	83%	17%
Philadelphia Savings Fund Society (PSFS)				
# of mortgages	802	727	669	360
% distribution	52%	48%	65%	35%
Beneficial Savings				
# of mortgages	314	558	160	205
% distribution	33%	67%	44%	56%
Western Savings				
# of mortgages	19	39	15	21
% distribution	33%	67%	42%	58%
Germantown Savings				
# of mortgages	219	467	159	324
% distribution	32%	68%	33%	67%
Provident Bank				
# of mortgages	42	55	39	83
% distribution	43%	57%	32%	68%

Source: Institute for the Study of Civic Values

A third measure of the impact of PMP on the city of Philadelphia is the opinion of various community representatives who have actively monitored the Plan.[35] Generally, comments have been favorable although there has been increasing concern regarding the inability of PMP participants to extend credit to very low income groups and their unwillingness to finance the purchase of properties in blocks which do not meet the minimum block criteria established by PMP. Other concerns involve the need for a rehabilitation program and the fear that displacement of poorer residents may be caused by rising property taxes due to the appreciation of property values. Despite these concerns, community spokespersons acknowledge that PMP is pumping some conventional mortgage money into areas which previously were unable to attract conventional credit.

On the basis of the three measures discussed above, particularly the total number and value of PMP mortgages, it appears that several PMP participants have had a significant impact on the moderate income neighborhoods of Philadelphia. By providing conventional credit to households desiring to purchase property in neighborhoods previously considered imprudents risks, PMP has helped to create equity stakes for a number of prudent, but moderate-income, residents.

Impact on the Lending Industry

In addition to increasing the supply of conventional credit in Philadelphia, the experience of the Philadelphia Mortgage Plan has begun to raise doubts concerning the lending industry's negative assumptions about urban lending. Most lenders regard inner city lending as characterized by high risks. They also suggest that there is little, if any demand for conventional credit in city neighborhoods. Recently, these perceptions have been reinforced by the writings of two consultants to the lending industry, Andrew Brimmer and George Benston.[36] On numerous occasions, the findings of these two experts have been cited by lenders as rationale for refusing to extend credit in inner city areas. Brimmer and Benston, however, have overlooked the demand for credit which has been generated by the Philadelphia Mortgage Plan. They have also ignored the low default, reasonable return experience PMP supporters have had with the mortgages they have extended.

Since the start of PMP, a number of participating lenders have actively marketed the availability of credit to brokers, residents of inner city neighborhoods and community organizations. Marketing activities have involved the distribution of flyers (Figure 1), brochures (Figure 2), and advertisements in community and metropolitan newspapers. Some participants have also made presentations to neighborhood groups concerning the goals and operation of PMP. As a result of these activities, a demand for conventional credit was generated which amazed participating lenders.

For years, PMP participants, like their colleagues throughout the country, had assumed that there was little demand for conventional credit in the inner city. However, when they reoriented their lending policies by making flexible loans, and then marketed these loans, they encountered a demand that allegedly did not exist.

One mortgage officer involved in processing PMP mortgages expressed his view of PMP's marketing success in the following manner:

> A new market has been created because of the Plan. This is a market that, contrary to expectations, has prospective buyers with reliable income sources (although small) and genuine commitment to own a home. They are purchasing properties that, although low priced, are in livable and respectable condition.[37]

The skeptics in the lending industry assumed that if this latent demand for credit was met, then PMP lenders would shortly be faced with a high rate of foreclosures. Such gloomy predictions were based on experiences such as the high volume of foreclosures in the FHA single-family mortgage insurance programs and the high rate of abandonment in inner city neighborhoods.

The success of PMP during its first two years of operation will probably force such pessimists to rethink their perceptions concerning the risk of inner city lending. As of December, 1977, PMP institutions had extended 2955 mortgages and have had to foreclose on only one property.[38] According to PMP spokespersons, part of the reason for the low foreclosure rate is the use of pre- and post-purchase counseling programs for many of the mortgage recipients.

Despite the ominous predictions of excessive foreclosures, the experience of PMP has indicated that it may be possible to extend credit, without subsidies, to moderate income households and obtain a reasonable return on investment. Such an experience in Philadelphia suggests that there are opportunities

FIGURE 1

A new look at mortgages

The Philadelphia Mortgage Plan is stemming neighborhood deterioration in Philadelphia and giving a new lift to our town.

Civic leaders and the Greater Philadelphia Partnership conceived the Plan. PSFS and two local commercial banks undertook to make it work. And the Plan *is* working.

Mortgage policies have been revised to relate real estate appraisals to individual blocks rather than entire neighborhoods. Applicant qualifications have been liberalized as well. Co-mortgagor and welfare incomes are now counted, for example.

But what is involved here is not charity; it's business. The Philadelphia Mortgage Plan offers financing in older neighborhoods on the same terms as the participating banks are offering elsewhere. Competitive rates are charged on all loans which are generally covered by private mortgage insurance. Since October, 1975, over 1,100 mortgages have been granted for a total of $12,000,000.

PSFS, the other participating mutual and commercial banks (now numbering 12), neighborhood associations, churches, counseling agencies and real estate interests have joined together to carry forward this unusual undertaking in community cooperation. PSFS is proud to have played a part in this effort.

PSFS®
THE SAVER'S BANK

The Philadelphia Saving Fund Society
Member FDIC

EQUAL HOUSING LENDER

Prepared by Weightman Inc. PS-1623 Rev. I
7" x 10"—1977

FIGURE 2

THE PHILADELPHIA

MORTGAGE PLAN

What It Is

The Philadelphia Mortgage Plan is a cooperative effort by major local financial institutions to adjust lending policies to residential mortgage needs as they exist today in Philadelphia.

Under the Plan, the participating banks have adopted revised and uniform lending guidelines to assure that each application for home mortgage financing is considered on an individual basis.

What It Does

Overall, the goal of the Philadelphia Mortgage Plan is to improve housing conditions in Philadelphia. More specifically, it seeks to accomplish this by making mortgage funds available to creditworthy prospective purchasers of residential properties in potentially healthy city neighborhoods which have fallen victim to deterioration and consequent disinvestment.

Lending Criteria

The banks participating in the Plan have modified their lending policies to ensure that decisions are based on evaluations of both property and applicant.

Regarding Applicants:

...Income of borrower's spouse/co-mortgagor will be recognized as effective income.

...Confirmed income from official welfare agencies will also be recognized. (As a general rule, however, support orders will not be considered as such.)

...Loan-to-value ratios of up to 90-95% will be acceptable, provided there is adequate mortgage insurance. Maximum loan amount will be $15,000 and maximum sales price $17,500.

...Amounts necessary to cover annual taxes, fire insurance and private mortgage insurance will be collected monthly.

...Mortgage terms will be based on loan amount and ability to repay.

...Uniform loan application and appraisal forms will be used by the participating institutions.

Regarding Properties:

Homes for which mortgages are sought will be appraised according to their structural state and that of other housing units in the immediate block, and not on generalized perceptions of housing conditions in larger adjacent areas. Prospects for mortgage financing will be most favorable for homes on blocks in which: (1) the median property value is at least $6,000, and; (2) the combined abandonment and vacancy rates do not exceed 10%. However, in cases where these conditions are not present, properties may still be eligible for mortgage funds where a combination of the following factors exists:

...The presence of a strong and cohesive neighborhood or community organization;

...The existence of a rehabilitation or other ongoing housing improvement program by either a non-profit developer, public agency or recognized private group, or;

...A cooperative effort by absentee owners with neighborhood residents to improve housing conditions and make needed repairs on existing dwellings.

How The Program Works

Those seeking mortgage financing should go to any one of the offices listed below and on the back page of this brochure. Trained housing counselors are available to answer questions and assist in the preparation of mortgage applications. For special assistance in the preparation of mortgage applications, or in cases where mortgage financing cannot be provided, participating banks may refer applicants to qualified community organizations and counseling agencies.

Office Locations and Key Personnel of the Philadelphia Mortgage Plan:

Beneficial Savings Bank
1200 Chestnut, Philadelphia, Pa. 19107
Telephone: 923-0700
James J. Connor, Assistant Treasurer

Central Penn National
Public Ledger Building
7th and Chestnut Streets, Philadelphia, Pa. 19106
Telephone: 854-3294
Walter C. Hebden, Assistant Vice President

Continental Bank
Broad and Nedro Streets, Philadelphia, Pa. 19141
Telephone: 823-6494
Louis Pauzano, Assistant Vice President

Fidelity Bank
15th & Sansom Streets, Philadelphia, Pa. 19102
Telephone: 985-7668
John Schultz, Vice President

in other cities for extending credit to moderate income, but creditworthy families in older neighborhoods.

Lenders in other cities have begun to acknowledge the short-run success of PMP, but are generally withholding judgment until the mortgages are four to five years old. A rule of thumb employed by lenders is that once a mortgage is five years old, the probability of default dramatically declines with each additional year.

In the cities of Seattle and Detroit, lenders have initiated programs which are based, in part, on the Philadelphia Mortgage Plan.[39] In both cases, the programs were started after a review of the experiences of PMP.

Potential for Implementation of PMP Typology in Other Cities

Although the principals involved in the Philadelphia Mortgage Plan believe that PMP type strategies can and should be implemented in other cities, such assumptions are questionable. In an article in Banking Magazine, James Bodine of First Pennsylvania Bank stated the following view of the potential for PMP replication in other cities.

> Seattle and Detroit have already modeled programs after PMP, and there is no reason why other cities cannot do the same. Queries have come from Chicago, New York and Washington, D.C.[40]

In order to assess the potential for the creation of efforts like PMP in other cities, it is necessary to analyze the environment in which PMP was created.

PMP evolved from the participation of three Philadelphia lenders in the Greater Philadelphia Partnership which was engaged in a search process for two neighborhoods which would serve as target areas for Neighborhood Housing Service programs. The three lenders were Todd Cooke, President of the Philadelphia Savings Fund Society; James Bodine, Chairman of First Pennsylvania Bank; and Frederick Heldring, President of Philadelphia National Bank. During the search process, these lenders developed a relationship with several indigenous community leaders who had been protesting the practices of Philadelphia's financial corporations which were allegedly accelerating neighborhood deterioration. The lenders and neighborhood representatives participated in a mutual learning experience where lenders learned of the problems of neighborhoods and the neighborhood people realized the intricacies of lending and risk analysis.

After an extensive search process, the lenders and neighborhood representatives collectively concluded that given the large number of disinvested neighborhoods which they had witnessed, more than two Neighborhood Housing Service programs were needed. Consequently, an effort was undertaken to establish a city-wide approach to stabilizing Philadelphia's neighborhoods, which culminated in the creation of PMP.

In forty-six cities, Neighborhood Housing Service programs have been established through the partnership approach which was used in Philadelphia. Lenders and community representatives, along with public officials, have cooperated in each of these cities to select one or two neighborhoods to serve as NHS target areas. However, only in Philadelphia did lenders undertake the initiative to design a serious strategy to revitalize numerous disinvested neighborhoods which they had found during the NHS search process.

On the basis of interviews with PMP participants and a careful review of their public speeches and congressional testimony, the author has found that the following factors played a significant role in the creation of PMP.

First, the principal officials of the three institutions which founded PMP began to realize that the future financial success of their institutions was directly linked to the condition of Philadelphia's economy. Unlike many lenders in other cities who have only begun to understand the relationship between their prosperity and the prosperity of the central business district, the PMP founders also realized the necessity of insuring the vitality of the city's existing residential neighborhoods in order to insure the soundness of their consumer deposit base. They realized that if something was not done immediately to reverse the blighted condition of many inner city neighborhoods, then the city's economy and their institutions would be in deep trouble. The following statement by Todd Cooke exemplifies this understanding:

> ...A bank, unlike many other businesses, is pretty much rooted to a particular community or group of communities. My bank, Philadelphia Savings Fund Society, simply cannot pack up and move to the Sun Belt. We don't want to, but that is just as well because we can't. We have had a

> 160-year association with Philadelphia and the Greater Philadelphia area, and we hope to continue to do business in this community for many years to come. Since this is the case, it is clearly in our interest that the community in which we operate grows and prospers. An essential element in such growth and prosperity is a sound stock of housing sustained by a healthy flow of mortgage financing.[41]

A second significant factor in the creation of PMP was the belief by the participants that the extension of mortgage credit could make a difference in many of the neighborhoods which were beginning to experience deterioration. Unlike much of the lending industry, PMP participants no longer assumed that most of the city was too deteriorated for lending institutions to make a difference. They began to distinguish, on a block-by-block basis, among deteriorated blocks which represented prudent credit risks and those blocks which did not.

A third factor which at least played a role in the involvement of the Philadelphia Savings Fund Society in PMP was the assumption that banks are licensed to serve the <u>needs</u> of the public. The following statement by Todd Cooke explains this often overlooked principle of banking:

> Banks, as components of the service industry, have a marketing <u>opportunity</u> and "franchise" <u>obligation</u> to serve the public. That is what we are set up to do; that is what state regulators, in effect, license us to do, and I think serving the public means just that -- attempting to meet a <u>full range</u> of financial needs as the public perceives them, not simply offering a selection of these services which we, as bankers, find easy and profitable to provide. Older urban neighborhoods need mortgage financing. Banks, as financial service institutions, should attempt to meet that need. (emphasis added)[42]

Although the PMP founders appear to be relatively enlightened concerning the role of financial institutions in stabilizing neighborhoods, until 1975 they were not fulfilling their acknowledged role in many of the city's neighborhoods. Like some of their associates throughout the country, they too were refusing to extend all but a minimal amount of credit in neighborhoods perceived to be declining. Why did they change their policies in 1975 after years of withdrawing from many neighborhoods?

Throughout the early 1970s, Philadelphia, like most major cities, experienced a considerable amount of activism on the part of citizen's groups protesting the refusal of many lenders to extend credit in older neighborhoods. Initially, many of the lenders which now participate in PMP were defensive when they were attacked by neighborhood groups which had experienced redlining. In early 1975, however, local financial institutions began to respond in a constructive manner to criticisms from neighborhood advocates. Perhaps they were swayed by the arguments of community leaders or they were jolted into rediscovering their commitment to the city by two other forces which were affecting or could potentially affect the banking industry and the city of Philadelphia.

A potential threat to the banking industry was the fear of federal or state legislation mandating inner city lending. This may have strongly encouraged the PMP lenders to find a way to meet neighborhood credit needs. In 1975, the Home Mortgage Disclosure Act was passed, despite the massive efforts of the banking lobby, one of the most powerful interests in Washington, to kill the legislation. Consequently, some lenders assumed that almost anything was legislatively possible given the sudden influence of the pro-neighborhood lobby.

Another factor, which directly influenced the city of Philadelphia, may have also stimulated the creation of PMP. This concerned the alleged inability and unwillingness of local government to do anything to reverse the decline of Philadelphia's neighborhoods.

According to some neighborhood leaders, the election of Frank Rizzo as mayor of Philadelphia initiated a process of public disinvestment in neighborhoods, particularly black neighborhoods, which did not support Rizzo. Neighborhood groups contend that as a result of the withdrawl of city services and the cancellation of capital improvements, many neighborhoods began to rapidly deteriorate and financial institutions consequently withdrew support. The ultimate effect of such practices was predicted by many to be the collapse of the city as deterioration spread and destroyed the residential and commercial tax base.

Assuming that local lenders agreed with neighborhood groups which were accusing Rizzo of such practices, the creation of PMP may have been an effort to reverse the deterioration which was allegedly produced, in part, by the practices of the Rizzo administration.

In the process of investigating PMP, this author found no evidence or statements by PMP lenders which explicitly accused Philadelphia's political administration of such practices. The only reference to the significance of local government support for city neighborhoods was found in the following statement by Todd Cooke:

> An important contribution of local government is to provide the same range and quality of services -- police and fire protection, sanitation, and so on -- in low income neighborhoods as in more affluent areas. With all due respect to local governments, this is sometimes not the case.[43]

Although PMP founders probably did not share the conspiratoral theory of the Rizzo administration maintained by many neighborhood groups, the absence of city representation in PMP, which in effect aids the creation of equity stakes for minority residents, is noteworthy.

The key to the creation and continued performance of PMP, and the development of PMP-type programs in other cities, is the willingness of the senior management of local financial corporations to meet with neighborhood leaders and learn about the problems which neighborhoods are experiencing. It is particularly important for lenders to understand the problems resulting from private and public investment practices which appear neutral on their face, but are discriminatory in effect towards certain neighborhoods. Such practices often accelerate the demise of inner city housing stock and neighborhood commercial districts. Lenders must also be enlightened with regard to the practices of their institutions which are not only accelerating housing and commercial deterioration, but are also stimulating the decline of their deposit base and their labor force as residents and businesses leave disinvested areas.

If such educational partnerships between neighborhood leaders and lenders can be found, then the potential for a successful PMP-type effort will be enhanced provided that the senior management of financial corporation is committed. Otherwise, any effort will represent no more than a paper strategy with little chance of meaningful implementation.

Interested parties in other cities who desire to establish strategies similar to PMP should attempt to foment working partnerships through reasonable discussion. Confrontation tactics might be utilized if attempts to structure reasonable dialogue fail. However, the nature of such an approach may permanently prevent the development of constructive cooperation between lenders and neighborhood people.

The Philadelphia Mortgage Plan is probably the most significant organized, multi-bank reinvestment program in any single city. Groups in other cities interested in fomenting such a strategy, however, should be aware that the goals and potential success of PMP in revitalizing neighborhoods are limited.

At the close of 1977, PMP had successfully begun to extend conventional credit for the purchase of <u>single-family housing</u> in formerly redlined neighborhoods without incurring even minor losses. Philadelphia, like Baltimore, is a city which is primarily characterized by single-family housing. Consequently, PMP is an appropriate response to the <u>housing</u> related credit needs of Philadelphia. Most of the other older cities of the Northeast and Midwest, however, are plagued by the massive problems of multi-family housing deterioration and abandonment. In cities like New York, Chicago and Boston, large apartment buildings anchor many inner city neighborhoods. Once such buildings deteriorate, then the surrounding neighborhood composed of single-family and smaller multi-unit housing may quickly follow.

Unlike neighborhoods exclusively composed of single-family housing, neighborhoods which consist of both single-family and large multi-unit housing are extremely difficult to revitalize. To date, there have been few successful efforts to slow the deterioration of such neighborhoods. Cities experiencing rapid deterioration of their multi-family housing stock should consider focusing their time and talent on the creation of vehicles to extend credit for the acquisition and renovation of multi-family buildings. The lessons learned from PMP regarding single-family mortgage lending should be implemented by concerned lenders in conjunction with their regular, everyday business without exhausting precious time and talent required to design an unnecessary plan.

Even in Philadelphia, PMP alone will not be sufficient to stabilize the decline of the city's neighborhoods. Additional initiative must be taken by participating lenders to finance the improvement of the small business establishments which populate the major streets of the city's neighborhoods. Concerned lenders must also stimulate the creation of new businesses and meet the credit needs of existing small business entrepreneurs who will employ or are currently employing existing inner city residents. Unless such steps are undertaken, PMP single-family loans may become less than secure.

PMP represents a landmark effort which has indicated that the extension of single-family mortgages in neighborhoods perceived as marginal investment opportunities is both prudent and profitable. Single-family mortgage lending is a necessary first step, but it is not sufficient to insure the future viability of the city of Philadelphia or any other city.

Footnotes

[1]The literature search consisted of a review of editions of the following publications published since January, 1976: American Banker, Banking Magazine, Business Week, Forbes, Fortune, Journal of Housing, Philadelphia Bulletin, Philadelphia Inquirer, Philadelphia, Planning, Practicing Planner and the Wall Street Journal.

[2]James F. Bodine, "Good for people, good for banks: The Philadelphia Mortgage Plan," Banking Magazine, July, 1977.

[3]The Center for Community Change, The Lifeblood of Housing, (Alexandria, Virginia: Mt. Vernon Publishing Company, Inc., 1976), p. 71.

[4]Ibid.

[5]Ibid.

[6]Due to the passage of the Housing and Community Development Act of 1977, financial institutions are concerned about generating favorable publicity concerning their inner city lending performance. Title VIII of the Act requires federal regulatory agencies to examine each lending institution's performance in meeting the credit needs of all segments of the community in which it is located. Regulatory review of credit performance will occur whenever an institution applies to a regulatory authority for permission to make a structural change (e.g. branching, merger). Theoretically, a regulatory agency can reject such an application if the applicant institution is not sufficiently meeting the credit needs of its community.

[7]Private mortgage insurance provides lenders with insurance on a specified percentage of a mortgage loan for a fee. If the borrower defaults on the loan and foreclosure occurs, then the lenders will be reimbursed by the private mortgage insurance company for that portion of the loan which it had insured.

[8]Continental and MGIC were the two private mortgage insurance companies which have been involved with PMP since its inception.

[9]For a more complete analysis of these underwriting practices see: Calvin Bradford, An Analysis of Underwriting and Appraisal Practices and Their Impaction on Credit Availability, (Chicago, Illinois: Woodstock Institute, 1977).

[10]The Equal Credit Opportunity Act (ECOA) (15 USC 1691) became effective on October 28, 1975 and was implemented by Regulation B (12 CFR 202). ECOA was amended on March 23, 1977. Regulation B prohibits discrimination with respect to any aspect of a credit transaction on the basis of race, color, religion, national origin, sex, marital status, age, receipt of income

from public assistance programs, and good faith exercise of any rights under the Consumer Credit Protection Act.

[11]Herb Bowers, Presentation before Governor's Conference: From Redlining to Reinvestment, Chicago, Illinois, September 1976. Transcript available from the Woodstock Institute, Chicago, Illinois.

[12]May Long, "Community Groups, Banks," Journal of Housing, January 1977, p. 23.

[13]For an analysis of the historical development of contemporary appraisal practices see: Bradford, supra., note 9.

[14]For an understanding of the subjectivity of appraisal practices concerning future value see: Stanley L. McMichael, McMichael's Appraising Manual (Englewood Cliffs, N.J.: Prentice Hall, Inc., 1931). McMichael's Appraising Manual is one of the most frequently used training textbooks in the appraisal industry.

[15]Todd Cooke, Presentation before the Governor's Conference: From Redlining to Reinvestment, Chicago, Illinois, September, 1976.

[16]Bowers, supra., note 11.

[17]Long, supra., note 12.

[18]Greater Philadelphia Partnership, The Philadelphia Mortgage Plan Report, IX, December 31, 1977.

[19]Ibid.

[20]Greater Philadelphia Partnership, The Philadelphia Mortgage Report VII, September 30, 1977. This was the last report which indicated the number of mortgages made by each PMP participant.

[21]Supra., note 18.

[22]Ibid.

[23]Ibid.

[24]Ibid.

[25]Bodine, supra., note 2.

[26]Ibid.

[27]Ibid.

[28]Ibid.

[29]Ibid.

[30] Ibid.

[31] Jane Shull and Hilde Jeffers, Mortgage Money in the City: An Analysis of Mortgage Disclosure Data, (Philadelphia, Pa.: Institute for the Study of Civic Values, 1977).

[32] Ibid.

[33] Ibid.

[34] Ibid.

[35] Such community representatives include Father Joseph Kakalec, the organizer and first president of a city-wide council of community organizers; Shirley Dennis, director of the Housing Association of Delaware Valley; and Reverend William Gray, member, Greater Philadelphia Partnership.

[36] See Andrew Brimmer, Risk vs. Discrimination in the Expansion of Urban Mortgage Lending (Chicago, Illinois: U.S. League of Savings Associations, April, 1977).

[37] Long, supra., note 12, p. 24.

[38] Supra., note 18.

[39] Bodine, supra., note 2.

[40] Ibid.

[41] Cooke, supra., note 15.

[42] Ibid.

[43] Ibid.

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