

**Leveraging the Federal Housing Administration (FHA) Loans to Build Wealth in Latino Communities**

Presented at:

**The “Expanding American Homeownership Act of 2007”: H.R. 1852 and Related FHA Modernization Issues**

Submitted to:

**U.S. House Committee on Financial Services  
Subcommittee on Housing and Community Opportunity**

Submitted by:

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My name is Lot Díaz, I am Vice President of Community Development for the National Council of La Raza (NCLR). For more than 20 years I have been working in the community development field on behalf of low-income families. At NCLR, one of my main responsibilities is to oversee the NCLR Homeownership Network (NHN). NCLR is the largest national Hispanic civil rights and advocacy organization in the U.S. dedicated to improving opportunities for Hispanic Americans. I would like to thank Chairwoman Waters and Ranking Member Biggert for inviting NCLR to share our views on the expansion of Federal Housing Administration (FHA) home loan opportunities. NCLR fully supports a revitalized FHA program. In 2005, 10% of Latino families relied on FHA loans to purchase their first home.

For more than two decades, NCLR has actively engaged in relevant public policy issues such as preserving and strengthening the Community Reinvestment Act (CRA) and the Home Ownership and Equity Protection Act (HOEPA), supporting strong fair housing and fair lending laws, increasing access to financial services for low-income people, and promoting homeownership in the Latino community. In addition to its policy and research work, NCLR has been helping Latino families become homeowners for nearly ten years as a sponsor of housing counseling agencies. The NCLR Homeownership Network (NHN), a network of 42 community-based counseling providers, works with 20,000 families annually, nearly 3,000 of whom become homeowners. Our subsidiary, the Raza Development Fund (RDF), is the nation's largest Hispanic Community Development Financial Institution (CDFI). Since 1999, RDF has provided \$400 million in financing for locally-based development projects throughout the country, building the capacity of local nonprofits and creating opportunities for Latino communities. These relationships have increased NCLR's institutional knowledge of how Latinos interact with the mortgage market.

We commend Congresswoman Waters and Chairman Frank for their work on H.R. 1852, the "Expanding American Homeownership Act of 2007." The bill includes several improvements over H.R. 5121, the version of the bill that was passed by the House in 2006. While the bill passed with overwhelming bipartisan support, we believe several of the added provisions will help put Latinos and other underserved borrowers on a path to sustainable homeownership and wealth-building. Generally considered the ticket to the middle class, affordable loan options that promote homeownership often do not meet the needs of many low- and moderate-income Latino homebuyers. The number of Latinos with FHA loans has been decreasing while the number of Latinos with subprime loans has been increasing. Recently, the subprime market has been dominated by high costs and risky mortgage products.

In my testimony today, I will discuss the importance of a strong and competitive FHA program to Latino homebuyers, highlight the increased counseling opportunities included in the bill, and underscore other provisions in the legislation of significance to Latino families.

### **Federal Housing Administration**

For more than 70 years, FHA has served low- and moderate-income families, often representing their only affordable loan option. During that time, FHA has often changed the face of the affordable lending market through its product innovations, such as the 30-year amortizing mortgage and low-downpayment requirements. While the private market has evolved to offer

more affordable products, FHA is unique in its social mission to provide homeownership opportunities to underserved communities. However, it has not been without its challenges. In the mid-1990s, FHA loans were often cited as the vehicle for flipping scams. It has also had higher foreclosure rates than conventional lenders.

Recently, FHA has experienced a dramatic reduction in its market share. In 2001, for example, one in four Latinos with a mortgage had an FHA loan. In 2005, that number dropped to just more than one in seven. In the meantime, the share of Latinos accessing subprime mortgages has grown dramatically. In 2005, 40% of Latinos had subprime mortgages. In many cases, Latino families have been steered unnecessarily toward these more expensive, and often riskier, loan products. Now we are seeing studies that project a foreclosure rate as high as 12% for Latinos.

Despite FHA's troubled past, a revitalized FHA program could once again spur market innovation. For many Latino homebuyers, having access to safe and affordable home loans can mean the difference between building wealth and facing unmanageable debt and foreclosure. Many Latino families looking to purchase their first home face unique barriers. For example, 22% of Latinos do not have enough payment information on file to generate a credit score and more than one-third do not have traditional banking or savings accounts. Multiple wage-earners and sources of income in one household are also common characteristics of first-time Latino homebuyers. In an automated world, many loan originators do not take the extra-time required to connect these families to flexible mortgage products that accommodate these qualities. As a result, many Latino families are unfairly steered toward products that are expensive and sometimes risky. A stronger, more flexible FHA program that is widely available would serve as an affordable alternative to costly loans.

### **“Expanding American Homeownership Act of 2007” (H.R. 1852)**

“Expanding American Homeownership Act of 2007” would make a number of changes to the FHA program, introducing a new risk-based pricing system, creating new counseling and loss mitigation opportunities, rewarding on-time payments, lowering downpayment requirements, and increasing access through higher loan limits. NCLR supports a strengthened and more competitive FHA, but such expansion must be approached with caution.

The new opportunities to access homeownership counseling included in H.R. 1852 are important for Latinos in this respect. Research has shown that access to homeownership counseling reduces the chances of default. In a study evaluating NHN,<sup>1</sup> families who received services from NHN organizations cited one-on-one counseling as one of the most important determining factors in their ability to purchase their first home.<sup>2</sup> After ten years in the business, NHN organizations have helped more than 25,000 families purchase their first home. Pre-purchase homeownership counseling can help ensure that as FHA incorporates zero downpayment and other potentially risky products – such as some adjustable rate mortgages (ARMs) and those that

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<sup>1</sup> The NCLR Homeownership Network was created in 1997 to provide homeownership counseling services to low-income Latino communities in an effort to increase Latino homeownership.

<sup>2</sup> Johnson, Ryan and Elsa Macias, *Home-to-Own: A New Model for Community-Based Low-Income Mortgage Lending*. Tempe, Arizona: Morrison Institute for Public Policy, 1995.

include interest-only options – that borrowers receive these products when they are ready and fully aware of their alternatives.

FHA must also be prepared to assist borrowers who experience financial hardship and default on their mortgage payments. Families in this situation can benefit from timely loss mitigation services. Although FHA currently offers a strong loss mitigation program, the services are little use to a family that does not receive them. Often families in financial crisis are too embarrassed or too distracted by their life events that they avoid their servicer and never learn about the repayment tools available to them. In other cases, servicers do not take the time necessary to determine the needs of the family and provide them with foreclosure prevention services. The “opt-in” provision included in H.R. 1852 begins to address this by helping counseling agencies and servicing companies overcome the privacy laws that prohibit information sharing. In many cases, an independent, community-based counseling agency is in a better position to outreach to borrowers in default. The opt-in provision is a waiver presented to FHA borrowers at closing that gives the servicer permission to share their information with a Department of Housing and Urban Development (HUD)-certified counseling agency in the event they become delinquent. When borrowers are reached early in the delinquency stage, they still have many options available to them to overcome their situation.

Inherent in FHA’s mission is a responsibility to ensure that FHA loans build sustainable wealth and are widely accessible to the communities that need them. There are three provisions of H.R. 1852 that work toward this goal. First, there is the payment incentive. FHA borrowers who choose one of the riskier loan products, such as the zero downpayment product, will pay a higher premium. The payment incentive will reduce the insurance premium rates for borrowers with these products who have made timely payments for five years. It also offers a refund to high-risk borrowers for the difference between the higher and the standard rate premiums upon repayment of the loan. Second, increasing the FHA loan limits will increase the accessibility of FHA-insured loans, especially for Latinos. Many Latinos live in high-cost areas. H.R. 1852 increases the maximum principal allowed under the FHA program to the area median home price. This will allow families in high-cost markets to access FHA. Third, the cap placed on fees in the new risk-based pricing model is helpful. This ensures that FHA’s target borrower – one who is arguably more vulnerable than the average consumer – is not overcharged. While FHA must remain flexible to serve as many borrowers as possible, it also has a responsibility to protect borrowers and place them in sustainable loans.

Overall, we consider H.R. 1852 to be an improvement over the original bill from the 109<sup>th</sup> Congress (H.R. 1521). Through NHN, NCLR serves thousands of Latino borrowers who fit the target FHA profile. We understand the needs of this market. In this spirit, we offer three recommendations below to further strengthen this legislation.

- **Increase authorization levels for the HUD Housing Counseling Program to \$100 million.** Across the country, housing counselors are seeing an increased demand for their services. Many NHN organizations went from one or two calls a week to five a day from families seeking foreclosure prevention services. While we see the counseling provisions in this legislation as highly positive, we have to ensure that the counseling agency has the capacity to serve the market. Increasing rates of foreclosure also weigh heavily on the

counseling industry. We recommend an increase in counseling funds, and that portions of this increase be set aside to fund foreclosure prevention and special outreach efforts to vulnerable populations, including language minorities.

- **Solidify the incentive for borrowers to receive counseling.** Families who receive housing counseling are less likely to default. Therefore, borrowers who successfully complete homeownership counseling in a timely manner before the closing of their mortgage should receive a “discount” on their insurance premium in the form of a credit enhancement. To accomplish this, we recommend that the committee instruct HUD to consider whether a family has received counseling as part of its risk-based pricing equation. In addition, to guarantee that FHA borrowers in need of loss mitigation services actually receive them, we recommend that the loss mitigation program make homeowners’ ability to save the home when facing foreclosure HUD’s clear priority. This can be done by adjusting servicers’ fee schedules to provide at least equal compensation for loss mitigation services and a short sale or other loss of the home. HUD should penalize servicers that do not provide loss mitigation services according to HUD regulations.
- **Ensure the FHA program remains true to its social mission.** As discussed, FHA’s unique social mission is one of its strongest assets to underserved communities. As FHA seeks to expand its reach and explores a variety of origination channels, NCLR recommends that HUD institute an originator code of ethics. Through such a code of ethics, all FHA originators would pledge to uphold FHA’s mission and responsibilities. The code of ethics would serve as a quality control tool and should protect the integrity of the borrower-broker relationship, promote transparency in the mortgage transaction, prohibit pressure sales tactics, and ensure that borrowers have access to accurate and timely information regarding the price of their loan. In the past, NCLR has also recommended HUD put in place monitoring techniques similar to the tactics used by other market players, including random audits for its originators and interviews with FHA borrowers shortly after closing.

Finally, although outside the scope of this legislation, we encourage members of this committee to see their efforts to combat predatory lending as a complementary endeavor. All too often we see our families fall prey to abusive loans when they could have qualified for a safe and affordable product. Thank you.