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Property Flipping Remediation Yields Investment-grade Security

by Mark Thomsen, SocialFunds.com October 10, 2001

SocialFunds.com -- A three-year property flipping scheme in Minneapolis and St. Paul, Minnesota (see yesterday's article) affected a total of over 500 families. While some were able to regain their credit, many lost their homes. However, about 50 families, despite all odds, had managed to hold on to their houses. In a few cases they have staved off foreclosure by making partial payments.

The Family Housing Fund (FHF), a nonprofit that promotes affordable housing in Minneapolis and St. Paul, realized that these 50 families might have a chance of keeping their homes if they received the right help. This help would have to go beyond the scope of the Property Flipping Task Force, a multi-organization initiative that FHF launched to help victims of the scam.

In the summer of 2000, members of FHF met with the Board of Pensions of the Evangelical Lutheran Church in America to discuss how new mortgages might be financed. At the meeting, the Board of Pensions said it was looking for investments that had ERISA-compliant features, which ruled out options such as purchasing below-market mortgages. **William Cunningham, Manager of Social Purpose Investing at the Board, suggested creating a Fannie Mae or Freddie Mac product.**

Fannie Mae (ticker: FNM) and Freddie Mac (FRE) are government-backed corporations that purchase mortgage loans in the secondary mortgage market. **Mr. Cunningham was fresh from testifying the month before on Capitol Hill regarding Fannie Mae's and Freddie Mac's lack of involvement in addressing special housing-related issues such as predatory lending.**

FHF and other Property Flipping Task Force participants then went to work, starting a dialogue with Fannie Mae through its partnership office in the Twin Cities. In the spring of 2001, FHF convened a larger group to address the problems of these fifty families. In addition to social services organizations, the group included the Board of Pensions and local mortgage lenders.

The group proposed counteracting the families' bad credit and lack of financial sophistication by raising charitable dollars to fund extensive homeowner counseling. New mortgages would be made to these 50 homeowners contingent upon their promise to attend homeowner counseling sessions.

Although the plan involved a significant deviation from its typical loan guidelines, Fannie Mae agreed to the arrangement. It would purchase and securitize the loans made by primary lenders, even though some of the homeowners did not meet its credit history underwriting standards. Thus was born the Home to Stay program. In return for signing an agreement to participate in the counseling sessions, the families would get a 30-year fixed mortgage.

The Community Reinvestment Fund (CRF), a non-profit that provides capital to community development lenders in low- to moderate-income communities, is servicing the loans. The Home to Stay program administration is very strict about attendance to the counseling sessions; families are called the next day if a session is missed. The counseling, which started in late April, is administered by the Family Housing Fund and is offered by Lutheran social services.

Of the initial 50 families, there are now 38 in the program. Eleven of the refinance loans have been closed, and the others should close this month. The 30-year mortgages are being processed by three primary mortgage lenders in the Twin Cities. Each will take about one-third of the applications, originate the loans, and then sell them to Fannie Mae.

Fannie Mae will then take the mortgages, pool them, and create government-backed securities that the Evangelical Lutheran Church and United Methodist Church pension funds will purchase as investments.

Since most of the houses are dilapidated, renovating them is an important part of the Home to Stay program. The 30-year mortgages are based on an after-renovation appraisal value. The goal is to have the first mortgages be no more than 80 percent of the after-renovation value; this makes the mortgages more attractive to Fannie Mae. There are three nonprofits working with the families to coordinate the repairs.

Money for the renovations comes in the form of a junior mortgage, which is interest-free and can be paid back when the house is sold. There are two other junior mortgages with the same payback conditions; one for closing costs and the other for those families that have insufficient income. Twin Cities Habitat for Humanity and the Minnesota Housing Finance Agency are among the sources of funds for these junior mortgages.

Besides teaching the basics of home ownership, Home to Stay has helped the families get through the mortgage application process, as well as obtain estimates on the necessary renovations. According to FHF, the hot housing market in the Twin Cities made it a challenge to get reasonable and timely bids on the renovation work.

Mr. Cunningham is pleased that the Board contributed to realizing a high-impact community investment. "We are glad to see an investment we outlined come to life," he said. "The Family Housing Fund and CRF carefully listened to what we suggested, and did the hard work required to make it happen."

He is also excited about what Home to Stay means for future victims of such scams. "This is a complicated process, since it is the first time that any type of investment-grade predatory loan remediation has been done," he explained. "We hope to work with other church pension funds to replicate this program around the country."

Community development and social services organizations that would like to get more information about the Home to Stay program can contact the Family Housing Fund.