

# **BUILDING TEXAS COMMUNITIES**

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## **A Guide for Home Mortgage Lending to Immigrant and Low-income Families**



**Texas Appleseed**

**Project made possible through funding from the Ford Foundation.**

**September 2005**



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## ACKNOWLEDGEMENTS

This report is generously supported by a grant from the Ford Foundation. We would also like to thank all of the financial institutions, organizations, and individuals who gave us their time to further our understanding of the issues involved in serving immigrant and low-income communities. We are particularly grateful to Rebecca Lightsey and Community Resource Group; Gerald Buechler and Scott Kimpel of Akin Gump Strauss Hauer & Feld LLP; Matt Hull of the Texas Association of Community Development Corporations; Mark Vanderlinden, Director-Community Lending with Fannie Mae; and Woody Widrow of the Texas IDA Network, a project of the Covenant Capital Corporation, for their guidance in developing this report. We would also like to offer a special thanks to all those interviewed for this report.

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**Texas Appleseed Mission**

Texas Appleseed works to promote justice for all Texans by using the volunteer skills of lawyers and other professionals to find practical solutions to broad-based legal and social issues. Texas Appleseed was founded in 1996 and is one of 17 Appleseed Centers throughout the United States and Mexico. Texas Appleseed leverages the skills and resources of lawyers and firms across Texas to address root causes of problems rather than individual symptoms and works to create viable solutions at a local level.

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## EXECUTIVE SUMMARY

There is growing interest among financial institutions in serving Hispanic immigrants and other low-income markets. These communities are largely unbanked, yet successful lending programs nationwide have demonstrated that they can be good credit risks and profitable to serve.

This report identifies characteristics of innovative home mortgage loan programs that have succeeded in meeting the needs of low-income and immigrant communities. According to the 2004 American Community Survey, 2.5 million Latin American immigrants currently live in Texas. The same survey shows that 42 percent of Texas households earn under \$35,000 per year. While low-income and recent immigrants in Texas often have access to home mortgage credit, many of the products available to them come with high interest rates, high fees, and pre-payment penalties that contribute to the likelihood of loan defaults. Instead of encouraging asset building, these products tempt people to take financial risks in order to participate in the American Dream of home ownership.

Today, there are market changes under way that make loans to these communities profitable for mainstream financial institutions while reducing the financial risk to low-income borrowers. Banks and credit unions have an important role to play in meeting the need for affordable home mortgage loans for Latin American immigrants and other lower income Texans.

### Barriers to Accessing Mainstream Credit

Latin American immigrants and other lower income communities face some of the same credit barriers. The one major barrier that is unique to immigrants is immigration status. The marketplace is starting to address this by expanding the availability of home mortgage loans accepting Individual Taxpayer Identification Numbers (ITINs) in place of Social Security Numbers. The Internal Revenue Service issues ITINs to individuals who conduct financial transactions with tax implications, but do not have access to a Social Security Number, in place of Social Security Numbers. Immigrant and low-income communities share four other major barriers to accessing credit:

- Lack of education about the United States banking and credit systems;
- Lack of credit or banking history;
- Limited access to conventional credit building tools; and
- Unique economic and family situations.

These barriers can be overcome, however, through both for-profit and community-based lending initiatives.

### Strategies for Overcoming Market Barriers

Overcoming barriers tied to immigration status is easily achieved, but remains outside mainstream market practice. Financial institutions that have accepted ITINs to make home mortgage loans have met with success. However, accepting alternative identification documents is only one of the elements of a successful lending program to immigrant markets. The other four credit barriers must also be addressed. A survey of lending programs in Texas and across the nation pinpointed six strategies that banks and credit unions have used to overcome the barriers to serving immigrant and low-income communities:

1. Building a relationship with the target community and connecting with its trusted organizations;
2. Providing financial education to help potential borrowers make informed decisions about their capacity to buy and retain a home and assist families that need time to build towards home ownership;
3. Using flexible loan underwriting criteria with little or no dependence on credit scores;
4. Offering flexible down payment options and low fee loans;
5. Providing flexibility in the debt-to-income ratios to take into account the specific circumstances of the borrower; and
6. Maintaining a relationship with the borrower after the loan closing in the event that the customer has problems making payments.

Since the popularization of credit scoring and the automation of loan processing, the above strategies have been considered too time consuming, unprofitable and cumbersome. The lending programs profiled in the next section demonstrate how financial institutions and community organizations in Texas have found ways to make these lending strategies work.

### Texas Lending Program Profiles

The chart on page vii presents summary information about the eight home mortgage lending programs profiled in this report. Each offers examples of different strategies that banks, credit unions, and community-based organizations can use to successfully serve low-income and immigrant markets. The profiles are divided into initiatives created and



run by financial institutions, by lender partnerships with community organizations, and by non-profits.

### Launching an Affordable Home Mortgage Lending Program in Your Community

In developing a successful home mortgage lending program in markets not reached by mainstream lending programs, it is helpful for financial institutions to consider these five steps:

1. Define the specific needs in your community.
2. Determine your capacity to meet those needs.
3. Develop the necessary partnerships to reach the target community.
4. Develop your lending paradigm with community partners.
5. Launch the program.

Recent immigrant and lower income communities can be good credit risks for home mortgage loans. Offering these loans is a “win-win” for these consumers and the financial institutions seeking to enlarge their customer base.

## Texas Lending Initiatives: Summary of Program Profiles

Program/Financial Institution	Program Type	Loan Type	Number of Loans	Target Customers	Loan Performance	Profitability
Community Development Lending/First National Bank	Market-based Initiative	30-year fixed rate and 15-year fixed rate; mix of Fannie Mae and portfolio loans	400	Varies depending on lending program; most low to moderate income	No foreclosures, few delinquencies	All programs profitable
Affordable Loan Program/Jefferson Bank	Market-based Initiative	30-year fixed rate, 15-year fixed rate, and 30/15 balloon.	200	80 percent or less of local median income; average income \$21,000; accepts applicants with ITIN	No foreclosures, few delinquencies	Self-sustaining in the short term, potential profitability in the long-term
ITIN Loans through Programa Libertad con TexasBank/TexasBank	Market-based Initiative	15-year fixed rate.	600	Applicants without access to a Social Security Number	Only three foreclosures	Profitable product for the bank
Affordable Home Ownership for Texas Pilot Program  Community Development Corporation of Brownsville/Ameriquest Partnership	Lender Partnerships	30-year fixed rate; during first four years of loan, rate will drop 50 basis points for every 12 consecutive months of on-time payment	16	Applicants with a credit score between 525 and 610	No information available because of short tenure of program	No information available because of short tenure of program
People Helping People Program  San Antonio Alternative Housing Corporation/San Antonio Federal Credit Union Partnership	Lender Partnerships	15-, 20- and 30-year fixed rate	200	Families at or below area median income	No foreclosures; monthly average of five loans past due 30 days or more	Self-sustaining in the short-term, potential profitability in the long-term
ACORN Loan Program  ACORN/ Bank of America Partnership	Lender Partnerships	30-year fixed rate	20 to 30 loans issued per month in Austin	Families at or below 100 percent of area median income	No information available	Long-term profit potential
Self-Help New Construction Program/ Proyecto Azteca	Non-Profit Subsidized Initiatives	Loan term varies based on ability to pay; average term of 20 years	600	Migrant farm workers with incomes averaging \$10,000	5 percent average delinquencies; few abandoned homes	Subsidized program
Affordable Housing Program/ El Paso Affordable Housing Credit Union Service Organization	Non-Profit Subsidized Initiatives	20- and 30-year fixed rate loan	100	50 to 80 percent of local median income, or \$15,000-\$30,000	One family unable to make payment; two loans over 30 days late	Not currently profitable; potential to become self-sustaining through increased loan volume



# Building Texas Communities

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## A Guide for Home Mortgage Lending to Immigrant and Low-income Families

### INTRODUCTION

Home mortgage lending to underserved low-income communities has long been a challenge for banks, credit unions, and governmental and community-based organizations. In recent years, immigrant communities have inspired new lender interest in non-traditional credit markets. This interest has been spurred largely by stiff competition in the mainstream markets, significant growth across the country in the number of Latin American and Asian immigrants, and the growing focus on the profitability of the large underserved low-income markets.

Texas has followed national trends, with a significant increase in its immigrant communities led by strong growth in the number of Latin American immigrants. According to the American Community Survey, there were 2.5 million Latin American immigrants living in Texas in 2004, a 14 percent increase over 2000.<sup>1</sup> Texas is also home to large communities with low to moderate income. In 2004 there were 3.3 million households with incomes below \$35,000, or 42 percent of all households in the state.<sup>2</sup>

The Hispanic immigrant community has been of particular interest to lenders in recent years. In March 2001, the Fannie Mae Foundation, in conjunction with the Georgetown University Institute for the Study of International Migration, published a detailed study of the unique aspects of home mortgage lending in immigrant communities and profiled successful models.<sup>3</sup> In May 2004, the American Bankers Association released a study profiling best practices in lending in immigrant communities.<sup>4</sup>

The National Association of Hispanic Real Estate Professionals released a report in October 2004 on the home ownership potential for undocumented immigrants from Latin America. The report estimated that there are 216,000 households that could afford to purchase a home if they had the opportunity.<sup>5</sup>

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<sup>1</sup> 2004 American Community Survey and 2000 U.S. Census.

<sup>2</sup> 2004 American Community Survey.

<sup>3</sup> Andrew Schoenholtz and Kristin Stanton, "Reaching the Immigrant Market: Creating Homeownership Opportunities for New Americans," Fannie Mae Foundation and Georgetown University Institute for the Study of International Migration, March 2001. See: [http://www.fanniemae.foundation.org/programs/pdf/rep\\_immigrant.pdf](http://www.fanniemae.foundation.org/programs/pdf/rep_immigrant.pdf) for a copy of the report.

<sup>4</sup> Moser Lauren and Esther Park, "Best Practices in Immigrant Lending," American Bankers Association, May 2004. See: [http://www.aba.com/aba/pdf/ImmigrantLending\\_May2004.pdf](http://www.aba.com/aba/pdf/ImmigrantLending_May2004.pdf) for a copy of the report.

<sup>5</sup> Rob Paral and Associates, "The Potential for New Latino Homeownership Among Undocumented Latino Immigrants," National Association of Hispanic Real Estate Professionals, October 2004, p. 17.

In fact, some of these immigrant households, both documented and undocumented, are purchasing homes through contract for deed, rent to own, and other arrangements outside of the mainstream lending system. According to the 2003 American Housing Survey, 13.5 percent of all Hispanic homeowners had a contract for deed or “land contract” mortgage, but the percentage is probably much higher because of the many undocumented immigrants with contract for deed purchase arrangements.<sup>6</sup>

Throughout Texas, colonias are sprouting in urban areas. The Texas Low Income Housing Information Service recently profiled a colonia near downtown Houston, where gravel and dirt roads are lined with densely packed homes, all purchased through contract for deed with predatory terms and improperly subdivided lots.<sup>7</sup> In Dallas, the Texas Attorney General recently pursued legal action in response to a housing scam where an individual was selling homes for cash, primarily to Latin American immigrants.<sup>8</sup> In most cases, the seller did not own the homes or hold good title to the homes. Many families paid between \$20,000 and \$25,000 in cash only to be evicted because of unpaid liens or condemnation of the property.

The studies described above underscore both the unmet lending potential of the immigrant market and the prevalence of predatory products that too often are the only options available to low-income communities. A recent report by the National Council of La Raza on predatory lending in the Hispanic market documents a dramatic increase—1,525 percent—in the number of Hispanics receiving subprime loans between 1993 and 2002, and highlights the general predatory characteristics of such loans.<sup>9</sup>

This report is designed to provide an overview of product options and successful loan components for serving immigrant communities in Texas as well as other low-income communities that do not meet the mainstream credit criteria for home mortgage loans. It includes specific strategies to help financial institutions successfully and fairly lend to these consumers.

The first section of this report provides an overview of barriers faced in establishing credit worthiness. The second section profiles common features of successful financial institution and community-based initiatives to provide home loans to immigrant and low-income communities. The third section profiles a selection of lending programs in Texas that serve recent immigrants and other low-income communities with non-traditional credit. It presents models for three different lending approaches: market-based initiatives, lender-community organization partnerships, and subsidized community-based initiatives. The final section offers guidance to financial institutions on how to develop an affordable home mortgage lending initiative.

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<sup>6</sup> American Housing Survey, 2003, Table 3-15.

<sup>7</sup> “Housing Matters,” Texas Low Income Housing Information Service, March 2005.

<sup>8</sup> “Attorney General Abbott Sues To Stop Housing Scam That Targeted Dallas-area Hispanic Consumers,” Office of the Texas Attorney General, April 11, 2005.

<sup>9</sup> Janis Bowdler, “Jeopardizing Hispanic Homeownership: Predatory Practices in the Homebuying Market,” National Council of La Raza, May 2005, p. 9.

The Appendix provides regulatory information on lending to foreign nationals. It addresses a range of issues including the Customer Identification Program under the USA Patriot Act, loan examination requirements, and the Community Reinvestment Act.

## **BARRIERS TO DEMONSTRATING CREDIT WORTHINESS IN IMMIGRANT AND LOW-INCOME COMMUNITIES**

Latin American immigrants often come to the United States with minimal assets and no experience with the U.S. banking and credit systems. They are used to dealing primarily in cash and obtaining credit through informal networks and pooled community and extended family resources. While they may soon realize that banking and credit are important to long-term financial success and integration and can provide a gateway to owning a home, many immigrants do not know how to access these financial services.

A study by the Tomás Rivera Policy Institute focused on three major barriers to homeownership for Latinos of Mexican origin: limited information about credit options, no relationship with financial institutions, and residency and citizenship issues.<sup>10</sup> Building on those findings and an analysis of successful lending initiatives, these four factors—in addition to immigration status—have been identified as major barriers confronting immigrant families seeking home mortgage credit:

1. Lack of education about the U.S. banking and credit systems;
2. Lack of credit or banking history;
3. Limited access to conventional credit building tools; and
4. Unique economic and family situations.

Many native-born, low-income Americans face these same four barriers to entering the financial mainstream.

### Lack of Education About the United States Banking and Credit Systems

When people do not understand how systems work, it is difficult for them to function successfully within those systems. For immigrants, understanding how to use a financial service account, learning what credit is, and understanding the benefits of having and maintaining good credit are essential first steps to becoming integrated as new Americans into our financial system.

### Lack of Credit or Banking History

Under conventional home mortgage loan underwriting criteria, many immigrant and low-income families do not qualify for credit. They often have no credit history or credit score and no banking history. Even issues like history of rent or utility payments can be difficult to obtain because of shared living situations and the inability of some

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<sup>10</sup> Jongho Lee, et al, “El Sueño de su Casa: The Homeownership Potential of Mexican-Heritage Families,” The Tomás Rivera Policy Institute, 2004, p. v.

immigrants, who lack a Social Security Number, to obtain the identification necessary to rent an apartment or have utilities in their own name. Often financial institutions will assume that they cannot help these individuals because they do not meet the established credit evaluation criteria.

### Limited Access to Conventional Credit Building Tools

Obtaining credit cards from banks or credit unions is one way to begin building credit towards a home mortgage loan, yet many people outside mainstream financial services do not have access to these because of their lack of any payment history. While immigrants may have more access to credit cards from retail outlets, these cards typically charge higher than average interest rates and can be a drag on credit if too many are obtained. Lower income consumers often do not have access to smaller secured loans, such as automobile loans, and, again, may face difficulties in documenting even the most basic means of building credit: rent and utility payments. For individuals who lack a Social Security Number, the challenges of building credit are even greater. They often lack access to formal systems that would enable them to build a positive credit history and obtain reasonably priced credit.

### Unique Economic and Family Situations

The mainstream lending system also is not accustomed to the workings of family networks in lower income and immigrant communities. Typically, lenders making an income assessment will disregard supplementary income from parents, grandparents, cousins, or children living in the loan applicant's household. Cash payments that cannot be documented through tax filing or W-2 forms often are not considered when calculating family income. Immigrants who lack a bank or credit union account frequently keep large sums of cash on hand, making it difficult for lenders to document the source of cash savings and how long it has been available to the potential borrower. Traditional mortgage loans usually require debt-to-income ratios of 28/36. For lower income immigrant families living with multiple wage earners in the household, these ratios—and particularly the limits on the house payment—can preclude their obtaining a loan despite the fact that they are paying more than 28 percent of their monthly income in rent and are able to make consistent rent payments.

These four barriers are all surmountable. There are programs, both through the Federal government and Fannie Mae and Freddie Mac, that facilitate lending to immigrants and lower income communities. Some banks and credit unions are taking the initiative to offer home mortgage credit to the ever growing low-income and immigrant markets. These loan products succeed because they tend to offer flexible guidelines for documenting work and credit history, assessing family income, and qualifying debt-to-income ratios.



## **COMMON FEATURES OF SUCCESSFUL HOME MORTGAGE LENDING TO IMMIGRANT AND LOW-INCOME COMMUNITIES**

There are a number of models nationwide for providing home mortgage loans to immigrant communities and Hispanic immigrants in particular. The two reports cited in the introduction provide a useful resource in examining model programs. This section highlights six key components of successful financial institution and community-based initiatives that have overcome the barriers to lending to these markets.<sup>11</sup>

1. Building a relationship with the target community and connecting with its trusted organizations;
2. Providing financial education to help potential borrowers make informed decisions about their capacity to buy and retain a home;
3. Using flexible loan underwriting criteria with little or no dependence on credit scores;
4. Offering flexible down payment options and low fee loans;
5. Providing flexibility in the debt-to-income ratios to take into account the specific circumstances of the borrower; and
6. Maintaining a relationship with the borrower after the loan closing in the event that the customer has problems making payments.

### Building Relationships in the Targeted Community

Having a relationship with a community, particularly an immigrant community that tends to distrust financial institutions, is a great marketing tool and a helpful way to learn about unique local needs and barriers to accessing credit. Understanding the community assists a lender in creating appropriate loan products and assessing effective and meaningful alternative underwriting procedures. The majority of the programs profiled in this report have strong community connections. Some established those connections by partnering with community-based organizations, and others by providing direct outreach and education in the target community.

Fostering community ties is particularly important to the small but increasing number of financial institutions now providing “ITIN” mortgages, or mortgages that use the

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<sup>11</sup> As part of our research, we conducted interviews and researched certain lending programs at Bank of America; Laredo National Bank; GMAC; Banco Popular; San Antonio Federal Credit Union; Self-Help Credit Union; El Paso Affordable Housing Credit Union Service Organization; the Community Development Corporation of Brownsville; Latino Community Credit Union, McAllen Affordable Homes, Inc.; Proyecto Azteca; TexasBank; Jefferson Bank; First National Bank; Mitchell Bank; and Second Federal Savings and Loan.

Individual Tax Identification Number as the identifying number for the loan. The ITIN also is used to verify tax payments and available credit history. These ITIN loans are performing well in Texas, often with exceptionally low foreclosure rates.<sup>12</sup> Banco Popular in Texas, which has an ITIN mortgage program with a 10-year track record, continues to market and make the loans because it is a profitable business. TexasBank in Fort Worth and Jefferson Bank in San Antonio, both profiled in the next section, also offer successful ITIN lending programs. For financial institutions looking to serve this new market, it is particularly important to build strong community relationships. Customers are attracted by word of mouth. Being involved in a community and having relationships with trusted organizations expedites the process of becoming known and trusted.

### Providing Financial Education

Financial education on the front end is important for successful lending to communities that do not fit standard credit profiles. Because many immigrants have no previous experience with a formal financial service system, financial education is a tool that can empower people financially and protect the financial institution's investment in a new customer. The vast majority of community-based organizations that provide home mortgage lending to lower income and immigrant communities include financial education as part of the process of determining loan eligibility. Completing required financial education courses helps potential homebuyers determine if they are ready to assume a home mortgage loan and learn how to manage their finances so that they can afford loan payments.

An added advantage of financial education on the front end of the home buying process is that it allows a financial institution to develop a closer relationship with potential customers. If the institution finds that an individual or family is not ready to purchase a home, it then has an opportunity to work with them to reach the goal of home ownership. For example, some immigrants with no credit history, including no alternative credit history under their name, may need a few years to build one. Financial institutions can help them create a history of consistent payments by offering secured credit cards or loans secured by a certificate of deposit.

Financial education is also an important lending tool to improve mortgage performance. According to a 2001 study by Freddie Mac, home mortgage delinquency rates for low- to moderate-income borrowers were reduced on average between 21 and 34 percent by homebuyer education. The highest percentage decrease resulted from individual, face-to-face financial education, with an average delinquency reduction of 34 percent.

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<sup>12</sup> Chicago's New Alliance Task Force profiled two lending programs that showed a zero percentage default and almost zero late payment rate. One of the profiled programs documented a five-year loan history (Second Federal), and another a one-year history (Mitchell Bank).

Classroom study lowered delinquency rates by 26 percent and home study by 21 percent.<sup>13</sup>

There are a number of free financial education resources available for prospective homebuyers. The Federal Deposit Insurance Corporation has developed a financial education curriculum called *Money Smart*, which is available in five languages, and the Federal Reserve offers a financial education workbook available in English and Spanish called *Building Wealth*. Fannie Mae provides a toll-free number for consumers to call to learn about loan products and special lending partnerships and initiatives.<sup>14</sup> Freddie Mac offers a curriculum called *Credit Smart*, which is available in English and Spanish. The Fannie Mae Foundation provides homebuyer guides in nine different languages, including English, Spanish, Chinese, Korean, Vietnamese, Russian, Polish, Portuguese, and Haitian Creole. In 1997, the Texas Department of Housing and Community Affairs was charged with developing a statewide homebuyer education program. The agency offers a toll-free number that interested consumers can call to learn about approved programs in their area.<sup>15</sup>

Some organizations have developed their own financial education curricula. The El Paso Affordable Housing Credit Union Service Organization, for example, developed a curriculum to support its home mortgage lending programs. A multi-state partnership of Appleseed Centers created a nine-brochure financial education series, *Bank on Your Future/Su Dinero Su Familia y Su Futuro*, geared towards the specific financial education needs of recent Latin American immigrants.

Financial institutions can partner with community-based organizations or utilize a city's financial education program. As part of the home loan process, banks and credit unions can require homebuyer education—either providing it themselves or using a state-certified education provider where available. If the financial institution is administering the lending program on its own, without a community-based partner, it is ideal if the bank or credit union can provide at least a portion of the financial education services. This can help the bank or credit union develop a supportive relationship with the borrower in the event that problems arise during the life of the loan

### Using Flexible Loan Underwriting Criteria

Over the past 10 to 15 years, credit scores have become the most common means of evaluating credit for home mortgage loans. However, this practice can exclude a large group of individuals with good credit potential from access to prime rate mortgage loans. Among those in the excluded group are more recent immigrants who often lack any conventional credit history and may lack a Social Security Number, which is the primary means of tracking an individual's credit.

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<sup>13</sup> Abdighani Hirad and Peter Zom, "A Little Knowledge is a Good Thing: Empirical Evidence of the Effectiveness of Pre-purchase Homeownership Home Counseling," Freddie Mac, May 22, 2001, p.15.

<sup>14</sup> The number to call for information is: 1-800-7Fannie.

<sup>15</sup> The number to call for more information is: 1-877-895-1093.

Without credit scores to rely on, some lenders have added flexible lending criteria to their underwriting models to reach out to immigrant markets. Common practice is to use one or more of the typical alternative credit assessment means: rent, utilities, cable, and—if available—some type of car payment or store credit. In addition, some lenders will accept a letter from an employer verifying employment and income in place of W-2 forms. Lenders also are becoming more flexible in accepting income contributed to the household by extended family living with the loan applicant. This contribution can be counted as rental income, enabling the loan applicant to show greater capacity to meet a monthly mortgage loan payment.

Some immigrants, including many who do not have a Social Security Number, face other barriers to establishing credit. Often groups of unrelated individuals will live in the same household with the lease in only one person's name, or in the name of a person who is subletting the home or apartment to the group. Before broad acceptance of the *matrícula* card, many immigrants who lacked a Social Security Number could not have utilities or leases in their name because of lack of proper identification. On the other side of the equation, the one family member with a Social Security Number may use his or her name and identifying information to obtain utilities, leases or even credit cards for a number of other family members. If family members do not make payments reliably, that individual's credit can be damaged.

In communities where such arrangements are common, some lenders will evaluate credit based on rental payment statements from landlords for persons without a traditional credit history. For those bearing the credit of an entire extended family, lenders will sometimes give minimal weight in the lending decision to late utility payments or other negative credit marks if there is compelling evidence that the individual was not responsible for them.

Often lenders will require one to two years of tax information and a minimum of a one- to two-year work history. For individuals without a Social Security Number, it is possible to file taxes using an Individual Tax Identification Number. Given the seasonal nature of work available to many recent immigrants, the work history does not always have to be with the same employer. Establishing consistent work in the same field can substitute for long-term employment with the same employer.

For immigrants who have lived in the U.S. for more than a few years, and particularly for those with children, medical debt can be another barrier to establishing credit for a home mortgage loan. These families often have two wage earners in the family, but none with a job that provides health insurance. Because of the high cost of health care, all it takes is one emergency or illness for a low-income family to incur significant debt. Depending on the needs of the lender, this issue has been addressed primarily in two ways. If the lender holds the loan, then medical debt can be ignored in the assessment of an individual's credit worthiness for a home loan. For loans that are sold on the secondary market, a debt payment plan must be arranged, but the lender does not have to use the medical debt as a negative credit indicator.

Lenders usually will require two to four sources of measurable credit. If such sources do not exist, some lenders will work with individuals to create a means of establishing credit in the future. One of the first steps is to encourage customers to open a bank or credit union account as a way of documenting deposits, savings, and expenditures. Opening an account also provides opportunities to build more traditional credit through CD loans and secured credit cards.

Although most of the lending initiatives serving immigrant communities have originated in community banks or credit unions, some national lenders and credit bureaus are reaching out to this market as well. Some of these are summarized below:

- **Settle America.** In 2003, GMAC Mortgage Corporation launched Settle America, a lending program specifically targeting immigrants lacking traditional credit histories. Under this program, income of extended family members living in the same household can be counted towards the individual's income, and rent and utility payment history can be used to measure credit if no credit score is available. Participation in Settle America requires legal status and a one-year U.S. employment history, and prospective customers must attend a pre-purchase financial education seminar.<sup>16</sup>
- **Bank One Pilot.** As part of a Fannie Mae New Immigrants Initiative pilot, Bank One launched a similar lending program in Houston in 1999. The program required that the borrower have a green card or pending application, accepted multiple and part-time job income when assessing credit worthiness, considered cash-on-hand for a down payment and asset assessment, and used the borrower's most recent hourly wage to determine qualifying income.<sup>17</sup> Fannie Mae has now incorporated many elements of the successful pilot into available loan products.
- **First American Corporation program.** The First American Corporation launched the Emerging Markets Initiative in October 2003 to expand access to home mortgages for lower income communities. The Greenlining Institute, a San Francisco-based coalition that encourages home ownership and economic development in America's inner cities, has officially endorsed the First American program. First American offers title insurance and mortgage and credit information, and is hoping to draw on its credit information business to create an alternative credit scoring system to expand the availability of Grade A mortgages to minority and immigrant communities.<sup>18</sup> First American has launched financial education programs and developed products that make it easier for lenders to use non-traditional credit to meet secondary market standards.<sup>19</sup>

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<sup>16</sup> "How to Buy a Home in Your New Homeland with Settle America," GMAC Mortgage Corporation. (Source: <http://www.gmacmortgage.com>, July 18, 2004).

<sup>17</sup> "Mortgage Company will Offer Immigrants Easier Path to Home Ownership," VISALAW.COM, November 16, 1999. (Source: <http://www.visalaw.com/99nov/16nov1999.html>, July 2, 2004).

<sup>18</sup> "First American and Greenlining Announce Comprehensive Program to Increase Minority Home Ownership," First American Press Releases, October 2003. (Source: <http://www.firstam.com>, July 18, 2004).

<sup>19</sup> For more information about the initiative, go to <http://www.emergingmarkets.firstam.com>.

This initiative combines information from proprietary national databases with tenant-screening and rental performance information, subprime and finance company databases, utility payments, and public records. First American expects that providing this alternative credit information to mortgage lenders will help them increase lending to first-time and moderate-income homebuyers.<sup>20</sup>

- **Pay Rent Build Credit.** Another national initiative to establish an alternative credit information database is called Pay Rent Build Credit. Based in Maryland, this credit bureau aims to establish a national database of rent, utility, cable, child care, international remittances, and other recurring payments that can be used to measure credit worthiness—a departure from conventional credit scoring models. Currently, individuals need to register and submit their own documentation of payments through locally approved verifying agents. The current network of agents, which includes financial institutions, is quite small, but the program hopes to expand to assist both consumers and lenders in all parts of the country.<sup>21</sup>
- **Citibank/ACORN Partnership.** In the fall of 2004, Citibank and the Association of Community Organizations for Reform Now (ACORN) announced an initiative to promote homeownership in low- and moderate-income neighborhoods. As part of the initiative, Citibank is making home mortgage loans more accessible to immigrant communities regardless of their immigration status.<sup>22</sup>

### Offering Flexible Down Payment Options and Low Fee Loans

There are currently many low down payment lending products available on the market, from loans insured by the Federal Housing Administration (FHA) to the community lending products offered by Fannie Mae and Freddie Mac. Typically a 3 percent down payment is the lowest available in secondary market products, although individuals with good credit can access zero down products. These lending programs take three approaches to help recent immigrants and the lower income meet down payment requirements: 1) accepting cash-on-hand and gifts for most or all of the down payment; 2) using down payment assistance programs available through the Federal Home Loan Bank or other local and national resources; and 3) offering subsidized, soft second mortgages to bring the loan-to-value ratio to 80/20.

The first approach is common to many lending initiatives targeting low-income families and recent immigrants. Because many immigrant families, and particularly those from Latin America, tend to be unbanked and hold much of their savings in cash, this

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<sup>20</sup> Jessica Sese, “Next Big Thing in Mortgage Technology,” *Top Economy News*, March 31, 2004.

<sup>21</sup> Michelle Singletary, “Earning Credit for Paying Rent,” *Washington Post*, February 22, 2004. (Source: <http://www.washingtonpost.com/ac2/wp-dyn?pagename=article&contentId=A59605-2004Feb21&notFound=true>, July 20, 2004). See: <http://www.payrentbuildcredit.com> for more information.

<sup>22</sup> “Citibank and ACORN Sign Historic Agreement,” *Acorn Annual Report 2004*.

provision is crucial in making loans accessible to them. Each of the initiatives profiled in the next section accept gifts and unseasoned savings for the down payment.

The second approach requires a proactive lender. The lender must either partner with community-based organizations that connect individuals with resources to facilitate the lending process, or have first-hand knowledge of these resources. Participating in the Federal Home Loan Bank is beneficial for lenders serving lower income immigrant communities. The Federal Home Loan Bank's down payment assistance is available to low-income borrowers through participating financial institutions regardless of their citizenship status.

The third approach is most commonly used by subsidized lending programs serving very low-income communities. Borrowers can contribute as little as \$500 towards the down payment and closing costs. The remaining cost is folded into an interest-free or low-interest second mortgage. The lender takes on all of the risk of the second mortgage, but is able to sell the loan on the secondary market because of the strong loan-to-value ratio. This approach also lowers the borrower's mortgage payment because PMI is not required.

Lenders holding home mortgage loans in their portfolio have more options regarding down payments and whether or not to require PMI. For example, the Self-Help Credit Union in North Carolina does not require PMI on any of its loans and has experienced very low default rates even though its loans are exclusively to low- and moderate-income individuals. Currently, loans to individuals without Social Security Numbers cannot be sold on the secondary market, and PMI is not available to this community in most parts of the country. Some lenders charge higher interest rates to compensate for the lack of PMI. As these loans gain more of a track record, it will be easier to appropriately price them. To date, they have very low default and foreclosure rates.<sup>23</sup>

Another strategy is to require low out-of-pocket payments, providing nearly full financing. Instead of using cash for the down payment, the lender requires families to put the 1 to 3 percent down payment amount into a savings account, so that the money is available to make loan payments in case of a cash flow emergency.

### Providing Flexible Debt-to-Income Ratios

The standard debt-to-income ratio of 28/36 may not be applicable to more recent immigrants, particularly the portion that reflects the maximum amount of monthly income to be expended on housing payments.<sup>24</sup> Lenders should be careful not to allow

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<sup>23</sup> The Self-Help Credit Union, TexasBank, Jefferson Bank, Second Federal Savings and Loan, and Mitchell Bank report close to zero foreclosure rates over the one to five years that they have offered these loans.

<sup>24</sup> The first number in the ratio indicates the percentage of total monthly pre-tax income spent on housing. The second number is the percentage of total monthly pre-tax income spent on all debt payments.

individuals to assume too high of a debt burden, however it may be appropriate to allow for a higher debt load that is directly tied to housing costs.

A general standard used to calculate how much of a housing payment a family can afford is to examine current rental payments and to allow no more than 25 percent above that amount. Generally, any increase in the allowable debt burden should be tied directly to housing expenditures, although specific circumstances may be considered. Debt-to-income ratios used by lenders serving low-income and immigrant communities are generally in the range of 33/38 to 45/45. Some programs use a ratio of 50/50 if the family has a history of successfully making rental payments that amount to 50 percent of their monthly income.

If a potential borrower cannot document a credit history and has no prior experience with bank or credit union accounts, the lender still has a tool to determine if home ownership is a realistic option. The bank or credit union can ask loan applicants to state their income and to disclose the duration and amount of savings. This informal documentation of a savings pattern can help the lender determine how large a housing payment the borrower can truly afford.<sup>25</sup>

#### Maintaining a Relationship with the Borrower After the Loan Closing

Making the loan is only a preliminary measure of a successful effort to expand homeownership in underserved markets. Real success comes with long-term retention of the home. This realization has prompted Fannie Mae, Freddie Mac, financial institutions, and researchers to devote resources to supporting and documenting best practices in helping borrowers retain their homes.

There are factors—both prior to the initiation of the loan and after the loan has closed—that can impact retention. If the home is poorly constructed, overvalued, or in a bad location, then there is a higher likelihood that the buyer eventually will stop making payments on the loan and be unable to sell the home to cover the loan value. On the back end, there are many instances of lower income individuals obtaining home mortgage loans on good terms, only to lose their homes because of a predatory refinance, such as a high fee and high interest home equity or home repair loan. Individuals of limited income are also vulnerable to financial crises, which can result in their losing their home unless the lender remains flexible in working with them.

Another complicating issue centers on marketing appeals to inexperienced recent homebuyers. Offers to create a bi-weekly payment plan or to purchase credit life insurance can be confusing. These marketing pitches often falsely appear to come from the financial institution, and homebuyers may feel obliged to participate even though they cannot afford or do not need the products. Others get into financial trouble when they

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<sup>25</sup> Andrew Schoenholtz and Kristin Stanton, “Reaching the Immigrant Market: Creating Homeownership Opportunities for New Americans,” Fannie Mae Foundation and Georgetown University Institute for the Study of International Migration, March 2001, p.52.



take advantage of a misleading refinance offer with terms that can cost them more money than their original mortgage in the long term. Recent immigrants are particularly vulnerable to these aggressive marketing schemes because they are not familiar with financial systems in the United States, and may not have had experience with banking institutions in their home country.

Banks and credit unions can help avert these problems. Key strategies include offering prospective buyers financial education during the loan-making process, encouraging diligence in obtaining a fair property appraisal, adequately assessing the borrower's financial limitations, maintaining a trusted advisor relationship throughout loan repayment, and working with borrowers to avoid default.

Though such intervention can be expensive, there are ways to approach it that may be worthwhile for a lender. The financial institution can partner with a community-based organization that can help struggling borrowers as needed. This model has proven effective where there is good communication between the lender, the community partner organization, and the borrower. If specified in the loan agreement, the lender can inform the community partner when a loan payment is late so that there can be immediate intervention before the loan goes into default.

Helping families work through a short-term crisis can save a financial institution's investment in a loan and an individual's home.<sup>26</sup> In June 2005, the City of Dallas partnered with mortgage lenders, non-profits, government agencies, and the Homeownership Preservation Foundation to launch the Dallas Homeownership Preservation Enterprise, a foreclosure prevention program. A toll-free number connects borrowers to credit counseling resources. The initiative is funded jointly by the city, mortgage lenders, and the Homeownership Preservation Foundation. The hope is to provide a resource for borrowers to address financial crises before foreclosure.<sup>27</sup>

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<sup>26</sup> For resources on post-purchase intervention, see: Mark Wiranowski, "Sustaining Home Ownership Through Education and Counseling," Neighborhood Reinvestment Corporation Joint Center for Housing Studies of Harvard University, 2003; Information on the Second Phase of Fannie Mae's American Dream Initiative. (Source: <http://www.fanniemae.com/newsreleases/2004/2945.jhtml>); Lucy Gorham, et al, "Effective Practices in Post-Purchase Foreclosure Prevention and Sustainable Homeownership Programs," Fannie Mae Foundation, April 2004; and Amy Crews Cutts and Richard K. Green, "Innovative Servicing Technology: Smart Enough to Keep People in Their Houses?" Freddie Mac Working Paper Series, July 2004.

<sup>27</sup> Kim Horner, "City Joins With Lenders, Foundation to Keep Owners in Homes," *The Dallas Morning News*, June 8, 2005.

## **PROFILES OF TEXAS LENDING PROGRAMS**

There is great demand in Texas for home mortgage credit that takes into account the unique credit profile of the state's large immigrant and low-income communities. The programs profiled in this section demonstrate how the six components of a successful lending program have been applied by Texas financial institutions and community-based organizations. They span market-based approaches, lender/community organization partnerships, and non-profit subsidized initiatives. All of the profiled programs offer flexible loans that are designed to accommodate the borrower's unique circumstances. They are all successful, with very low late payment and foreclosure rates.

### Market-based Initiatives

The market-based initiatives profiled here are for-profit or profit-neutral programs developed by financial institutions to meet a low-income market need in their lending area. The profiled financial institutions have developed relationships within their target communities and have helped borrowers obtain down payment assistance. These programs challenge the popular belief that "high touch" lending relationships and alternative underwriting systems are cumbersome and too expensive for financial institutions.

The loans profiled are a mix of subprime and prime loans. The subprime programs target borrowers who do not qualify for prime rate secondary market products because of credit deficiencies or lack of legal immigration status. They do not, however, mimic many of the common predatory loan features—including over-inflated interest rates, prepayment penalties, and high points and fees. Origination fees are not generally charged, and many of the closing costs are subsidized or adjusted by the lender. The programs also offer options to refinance the loan at a prime rate if the borrower meets secondary market standards during the loan term.

### Lender/Community Organization Partnerships

Partnerships between lenders and community organizations allow lenders, with capital to devote to mortgage lending to immigrant and low-income markets, to outsource program marketing and screening of applicants to an entity that knows the community the best. For community organizations, the partnership offers access to capital to serve their clients.

In two of the three programs profiled, the lender relies on the community organization to screen applicants, collect credit history, and provide financial education. In both cases, the lender services the loan. The third program relies on a community partner only for financial education. All three are portfolio loan programs, and most offer prime or better than prime rate loans. One program is for subprime borrowers and offers a low subprime rate with the option to reduce to a below-prime rate through a demonstrated payment

history on the loan. These partnerships were developed in response to problems that specific low-income communities were having in accessing credit.

### Non-profit Subsidized Initiatives

It is possible to serve very low-income families, with incomes in the \$10,000 to \$15,000 range, but such programs generally require subsidies and provide low or no-interest loans and substantial down payment assistance. One of the profiled programs was developed by eight credit unions in El Paso. It demonstrates how pooling resources can make affordable lending feasible, particularly to the lowest income families. The El Paso affordable housing program offers loans that are salable on the secondary market. The program has potential to become self-sustaining as its loan volume increases.

The other profiled initiative offers zero-interest loans and illustrates how loan products can be designed to meet the needs of low-income families. Instead of offering loans based on a risk assessment, the program offers loans to the neediest families and shapes the loan to fit the family income and payment capacity. Although this type of program could not operate without a subsidy, it provides interesting insights into successful lending to a community widely believed to be a bad credit risk.

Such initiatives provide avenues for financial institutions to contribute to affordable lending in their communities through donations and through potential collaborative lending efforts, where the loan risk is assumed largely by the non-profit organization. They also are models of successful asset-building loan products that meet the needs of underserved communities.

The following profiles are based on extensive interviews with program directors.

## **MARKET-BASED INITIATIVES**

# **First National Bank**

## *McAllen, Texas*

### **Community Development Lending<sup>28</sup>**

#### Background

First National Bank has its corporate headquarters in Edinburg, Texas, with mortgage operations based in McAllen. It has 46 branches throughout the Rio Grande Valley and in Corpus Christi, Dallas, El Paso, Houston, Laredo, and San Antonio. The bank was founded in 1934. It holds \$2.5 billion in assets and \$1.3 billion in loans.<sup>29</sup> The bank has been involved in home mortgage lending for many years using portfolio loans. They began making loans for sale on the secondary market in June 2002 to offer more competitive rates on long-term fixed-rate mortgages. Half of their lending is made using Fannie Mae My Community Mortgage products for first-time home buyers. On the border, the loans do not have any maximum income limitations; however, the majority of the borrowers are low- to moderate-income. The Community 100 loan, a zero down payment loan, is the product they use most often.

The flexibility of using Fannie Mae Community Mortgage products in conjunction with portfolio loans allows the bank to serve a broad spectrum of the low- to moderate-income community in its service area. The bank works with non-profits and local housing authorities to support various programs. The bank has successfully provided home mortgage loans to Section 8 program participants and for a lease-purchase program sponsored by the San Antonio Housing Authority.

First National Bank targets low- to moderate-income families for their mortgage lending initiatives. The bank was the only lender that stepped forward to make loans to support the Section 8 program in San Antonio. Lenders were reluctant to participate because the loan servicing was viewed as labor intensive, with part of the payment coming from the Department of Housing and Urban Development (HUD) and part from the borrower's own resources. There was also an unwillingness to take on the loans because the HUD subsidy lasts only for 10 years for most families.

The bank is comfortable with the risk associated with the time limit on the subsidy and has found a creative way to make loan servicing easier. All families are invited to open an account at the bank for direct deposit of their HUD check and auto debit of the loan payment after the HUD check arrives. Most of the participating families were previously unbanked, and many took advantage of the auto debit option. As a result of the success of the Section 8 program, the San Antonio Housing Authority invited the bank to provide loans for families that successfully complete the lease period of the Authority's lease-purchase program.

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<sup>28</sup> Interview with Jack Mooney, Senior Mortgage Officer, First National Bank, June 2, 2005.

<sup>29</sup> Texas Department of Banking, "Top 100 Banks in Texas by Asset Size Information as of December 31, 2004."

First National Bank views these lending programs as an opportunity to create an expanded financial service relationship with the borrowers. They make automobile loans and offer credit cards in addition to encouraging borrowers to open a checking or savings account.

Branches take the lead in conducting community outreach around mortgage lending. Some branches are very active in working with non-profits, which is their main strategy for reaching the community. Written and television advertisements have not proven effective, rather it is trusted community organizations and word of mouth that help promote the bank's business. As a service-oriented lender, relationships are central to their business success.

#### What community development loans does the bank offer?

First National Bank offers Fannie Mae My Community loans to their general customer base and includes those loans, where possible, in its program with the San Antonio Housing Authority. In the Section 8 and lease-purchase program, about one-third of the borrowers qualify for the Community 100 loan. The housing authority requires the seller to provide 3 percent of the sales price, and the closing costs can be paid by a non-profit or through a gift. Most loans are for existing homes. Borrowers will generally make their payments in cash at the teller window unless they are participating in a special program, such as the Section 8 purchase program, that encourages having a bank account.

Most of the home mortgage loans the bank makes are 30-year fixed. For those who do not qualify for a Fannie Mae loan, the bank structures the loan like a Fannie Mae loan with the goal of seasoning the loan for a few years and then selling it on the secondary market. In most cases, loans are held in portfolio—either because the credit score is too low or the borrower's income is not verifiable by Fannie Mae standards. The bank does not finance mobile home purchases.

The portfolio loan rates are currently ranging from 7.5 to 10 percent. For scores in the low 400's the 30-year fixed rate is between 9 and 10 percent. At 500, the rate reduces to 8 percent and decreases to 7.5 percent for the high 500's. At 600, the family can qualify for a Fannie Mae loan. If a borrower with a portfolio loan develops a history of on-time payments, the bank will work to refinance the loan with a Fannie Mae product.

There is a strong desire among borrowers to pay loans off early. When borrowers can afford it, they often choose a 15-year loan. The bank makes 15-year fixed rate portfolio loans at between 8 and 9 percent interest.

Alternative credit is accepted in underwriting the loans. For the Section 8 loans, down payment assistance is available. Under the lease-purchase program, the housing authority provides up to \$20,000 in down payment assistance and guarantees to repurchase the loan within 30 days if it is 90 days delinquent.

The majority of the borrowers under the San Antonio programs are single mothers with incomes ranging between \$1,200 and \$3,000 per month. The bank will make mortgage loans as small as \$16,000. Most homes are purchased for between \$71,000 and \$82,000.

### Community Development Lending Program: A Snapshot

Year of Program Inception and Number of Loans	Expanded low- and moderate-income home mortgage lending in 2002; currently servicing 400 loans.
Target Customers	Varies depending on lending program; most borrowers are low- to moderate-income.
Average Loan Size	\$70,000 to \$80,000, with loans as small as \$16,000
Loan Type	30-year fixed and 15-year fixed
Down Payment	As low as zero down. Accepts gifts, unseasoned savings, and city down payment assistance.
Interest Rate	Market rate for Fannie Mae loans, currently around 6 percent; 7.5 to 10 percent for loans held in portfolio depending on credit.
Fees	1 percent origination, \$300 processing fee, \$250 administrative fee, \$325 for appraisal, \$350 for survey, and \$20 for credit report
Debt-to-income ratio	60 percent maximum; 45 percent preferred
Credit Evaluation	Will accept credit score as low as 400's with good explanation. Assesses alternative credit; looks for four credit lines and two- to three-year work history.
Loan Performance	No foreclosures, few delinquencies.
Financial Education	Not required, except for Fannie Mae loans and Housing Authority requirements. Financial education provided informally through relationship with loan officer.
Profitability	All programs profitable.

The bank estimates that it costs between \$750 and \$1,000 to close a loan. The fees charged for all home mortgage loans include a 1 percent origination fee with a \$500 minimum fee, a \$300 processing fee, and \$250 administrative fee. The appraisal costs \$325, and \$350 is charged for the survey and \$20 for the credit report. The bank requires

escrow, which usually is in the \$1,500 range, when the loan-to-value ratio is above 80 percent or the borrower has not demonstrated an ability to save.

First National Bank's home mortgage lending programs are currently in a growth mode. Under the Section 8 program, the bank closes two loans per month. The bank anticipates closing 40 loans this summer and fall through the lease-purchase program. First National averages two to four My Community loans per month in the Valley, which makes up about 10 percent of their total new loans. The bank is still working to encourage more branches to use the Fannie Mae loans. Their lenders often prefer portfolio loans because of the lower documentation requirements and because it allows them to do one-time closings on new construction loans. Currently most of their underwriting is manual, and alternative credit is commonly used to underwrite loans.

#### How have the loans performed?

Since First National Bank launched its expanded lending program in 2002, there have been no foreclosures for loans made by the mortgage division in McAllen. On average, two out of the 400 loans the division services are in default each month. Most late payers make payments before the loan reaches 60 days delinquent. Approximately five loans per year are beyond 60 days delinquent. Homeownership is important to the low- and moderate-income families the bank serves. The bank has found that these borrowers will make every effort to pay their loan.

The bank reports that delinquencies are almost never due to neglect. Usually there is a triggering family emergency, such as a job loss, illness, or injury. One borrower recently called to let the bank know that he would be more than 30 days late on his loan because he was in the hospital. In such cases, the bank is usually able to work things out, offering some flexibility until the family situation is resolved.

#### What are the underwriting criteria for the loans?

Credit scores are used, but not emphasized in the bank's home mortgage lending. As the program director expressed, "I don't believe in credit scores. They are misleading. If people experience a tragedy, this can affect all of their credit." If the situation improves and the family has the ability and desire to make mortgage payments, the bank will make the loan.

For alternative credit evaluation, four credit lines are required. They can include rental verification, utility bills, and telephone bills. The mortgage lending division does not find it difficult or cumbersome to conduct an alternative credit evaluation. Using alternative credit has never held up a loan. The burden is on the borrower to obtain the credit information and provide it to the loan officer.



The bank is flexible in its underwriting criteria. First National Bank will often make loans in cases where desktop underwriter says “refer with caution” and, in some cases, will not make a loan approved by desktop underwriter because they feel the debt burden is too high for the borrower despite a strong credit rating. The bank can be flexible and successful in its lending because it takes a more in-depth look at the borrower. If the borrower has a realistic, acceptable explanation of credit problems with documentation to back up the explanation, the bank will often make the loan. “All of our loans are individual-based,” the program director explained.

The bank verifies employment through two or three years of tax returns, a verification of employment document, a letter from the employer, and year-to-date pay stubs. In the case of laborers who may not have consistent employment with one employer, they look for pay stubs or documentation that the person is being paid in cash. They only consider the income of family members who are included in the note, but they will consider informal income as long as the borrower can substantiate the income claim. Income from Social Security is increased by 25 percent.

In cases involving people with seasonal employment, such as migrant farm workers, the bank will accept a history of continuous employment and does not require a specified period of employment with the same employer or even in the same profession. For example, there are a number of people who travel to the northwestern United States to work in agriculture or the fish canning industry. They will be gone for half of the year and then return and receive unemployment until the season begins again. In such cases, the bank requires three years of income tax returns and W-2’s to document the employment pattern.

For a standard loan, they look for a total debt-to-income ratio of 45 percent. Ratios as high as 60 percent are acceptable if there is good credit, strong reserves, and job stability. Only a few of their low- to moderate-income borrowers have verifiable reserves.

The bank will lend to Mexican nationals who are legally in the United States. It is not uncommon to have a family with one spouse documented and the other undocumented. In such cases, the bank only considers the income of the spouse with legal status. For Mexican nationals who do not file tax returns in the United States, the bank will go to creditors in Mexico and get letters from them, as well as look at bank statements from Mexico if available. They look for 12 months of bank statements as a way to verify income and a profit and loss statement.

For portfolio loans, they will accept gifts and unseasoned savings for the closing costs and any required down payment. The bank will refer families to local down payment assistance programs if applicable. No private mortgage insurance is required on portfolio loans.

Financial education is not a required part of obtaining a portfolio loan except in the case of the housing authority loans. The Fannie Mae My Community loan program and the San Antonio lease-purchase program require counseling. First National sees a strong

benefit in housing counseling, and the feedback from families participating in homebuyer education classes has been very positive. These classes are generally provided for free by local non-profits.

#### Does the bank service the loans?

First National Bank services all of its loans, including those sold on the secondary market. They use Fannie Mae loan products and try to structure portfolio loans such that they can be sold on the secondary market after seasoning.

All servicing staff is bilingual, and delinquency notices are sent in both English and Spanish. If a loan is 15 days late, a lender supervisor will call the borrower to see if there is a problem that can be addressed. Delinquency notices are sent 60 days after the payment due date. If they are able to establish communication with the borrower, they are usually able to work with the borrower to bring the loan back into good standing.

First National Bank is flexible in working with borrowers. For portfolio products, the bank will accept interest only for a period of time or will roll a payment into the loan if it is clear that the borrower has a way out of the financial emergency contributing to loan delinquency.

Although there is no required program, the lender has found post-purchase counseling to be extremely beneficial, especially for borrowers with credit problems. The challenge is getting people to attend the classes. They are particularly successful in lease-purchase programs where the classes are required as part of the process of transferring ownership to the lessee.

#### Why is the program a success?

The success of the bank's lending programs is due, in part, to their flexibility in considering the entire picture when evaluating a borrower's financial situation and to their commitment to building relationships with borrowers. Lending partnerships with non-profits have allowed the bank to expand its services to low- and moderate-income borrowers they may not have reached otherwise.

Supportive senior management at the bank provides the mortgage division with the flexibility it needs to be successful. Rather than focusing only on high-dollar loans as the easiest way to make a profit, the bank's philosophy is that home mortgage lending to low- and moderate-income families is both a profitable business for the bank and an important service to an underserved community: "We are profit driven," said the program director. "We want to put as many low- to moderate-income families into homes as possible, and we feel that it is a market with very much opportunity."

# Jefferson Bank

*San Antonio, Texas*

## Home Owners Advantage Program<sup>30</sup>

### Background

Jefferson Bank was founded in 1946 and began mortgage lending in 1992. They have \$560 million in assets and loans totaling \$318 million.<sup>31</sup> The bank launched the Home Owners Advantage Program in October 2001 in an effort to better meet the needs of communities surrounding their branches. Many of their customers are families with moderate incomes, and they view the program as a way to better serve their entire customer base. The program serves low-income families in Bexar County. Borrowers must have 80 percent or less of the area median income.

In addition to offering a mortgage loan, the bank offers free accounts (checking and savings) to all mortgage customers in the program. To date, all of the program customers who did not previously have a bank account have opened one at Jefferson Bank, and many closed accounts with other banks to take advantage of the Jefferson Bank account offer. Approximately 65 percent of all mortgage customers open an account, and most customers both direct deposit their pay checks and use auto-debit to make their loan payments. The program director provides one-on-one financial education on the basics of managing a checking account, including samples that show first-time account holders how to write checks.

Community outreach is done through a number of avenues. Word of mouth from past customers is a major source of program referrals. Jefferson Bank is also involved in a variety of housing-related community initiatives, such as affordable housing fairs and Association of Community Organizations for Reform Now (ACORN) fairs. They work with affordable housing builders and realtors, and partner with the San Antonio Avenida Guadalupe and the Unitarian-Universalist Housing Assistance Corporation down payment assistance program.

### What is the Home Owners Advantage Program?

The Home Owners Advantage Program is a portfolio loan program. It is a 5 percent down home mortgage loan with no bank fees and flexible underwriting guidelines. The bank offers three loan products under the program: 30-year fixed, 15-year fixed, and a 30/15 balloon loan.<sup>32</sup> The 30-year fixed loan for the down payment assistance program carries an interest rate that is two percentage points above market rate. Those without

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<sup>30</sup> Interview with Mary Sanchez, Vice President, Home Owners Advantage Program, Jefferson State Bank, May 23, 2005.

<sup>31</sup> Texas Department of Banking, "Top 100 Banks in Texas by Asset Size Information as of December 31, 2004."

<sup>32</sup> A 15-year balloon loan with 30-year amortization.

down payment assistance can choose between a 15-year fixed rate loan or a 30/15 balloon loan, both at 9 percent interest.

### Home Owners Advantage Program: A Snapshot

Year of Program Inception and Number of Loans	Program began in October 2001. Currently 200 loans in portfolio.
Target Customers	80 percent of area median income or less; average income \$21,000; will accept applicants with ITIN <sup>33</sup>
Average Loan Size	\$65,000
Loan Type	30-year fixed, 15-year fixed, and 30/15 balloon
Down Payment	Requires 5 percent. Accepts gifts, unseasoned savings, and city down payment assistance.
Interest Rate	7.5 percent on 30-year fixed (with city down payment program); 9 percent on other loans
Fees	Bank pays most fees (\$1,500 per loan). Customer pays title insurance and prepaid property taxes and homeowner's insurance.
Debt-to-income ratio	50 percent maximum for total debt ratio; 45 percent preferred
Credit Evaluation	High 500's credit score, but will accept less with good explanation. Assesses alternative credit; looks for four credit lines and two-year work history.
Loan Performance	No foreclosures, few delinquencies.
Financial Education	Not required, but encouraged to attend city-offered classes. Loan officer provides basic education regarding the home-buying process and managing a bank account. Applicants are given a copy of the Fannie Mae Foundation home-buying booklet.
Profitability	Self-sustaining in the short-term; profit potential in the long-term.

<sup>33</sup> The ITIN, or Individual Taxpayer Identification Number, is issued by the Internal Revenue Service for individuals who need to file taxes in the United States but do not qualify for a Social Security Number.

Fifteen percent of their portfolio is through the down payment assistance program, 10 percent are 15-year fixed, and the remainder uses the 30/15 balloon loan. The average loan size is \$65,000, and average family income is \$21,000. Approximately one-third of the program's borrowers are single parents. Borrowers with a credit score tend to have a score between 500 and 600, with scores averaging in the high 500's.

The loan requires no private mortgage insurance, and the bank absorbs most of the fees. There is no origination fee or application fee. The bank pays approximately \$1,500 per closing—covering the survey, appraisal, attorney fees, and flood survey. The client pays the title fees, prepaid property taxes and homeowner's insurance, and the down payment. Client fees are generally under \$1,000. If a client qualifies for a conventional loan, the bank will refer the client to their lending department. Some customers will opt for this loan product despite the higher interest rate in order to avoid the usual closing costs.

At the program's inception, Jefferson Bank allowed people without Social Security Numbers to take out loans using the Individual Taxpayer Identification Number (ITIN). The program was so successful that limits were imposed. Realtors were actively promoting the program to would-be homebuyers, and word of mouth continues to bring in new referrals. The bank was closing eight to 10 loans per month just with ITIN borrowers. Because there is no secondary market for the ITIN loans, the bank decided to limit ITIN-based lending under the Homeowners Advantage Program to customers with a credit report. The types of credit that applicants generally have are from finance companies, gyms, and rent-to-own locations.

Ninety percent of the customers participating in this program are more comfortable conducting financial transactions in Spanish, and many cannot speak English. The bank offers the loan application and the U.S. Department of Housing and Urban Development homebuyer booklet in Spanish. They also offer a long-term relationship with the customer. Even after the closing, customers are encouraged to call the program director with a variety of financial questions. This relationship is helpful to the bank. It means that people will call if they have problems with a monthly payment, or if they get an offer related to their loan that they do not understand. Jefferson Bank strives to make customers feel comfortable at their bank. They close the home loans at the bank with the program director present. Most customers bring cash to the closing for the down payment. Closing the loans at the bank makes it possible to safely accommodate these cash transactions.

Since October 2001, approximately 200 loans have been made under the Homeowners Advantage Program. Between one-third and one-half of program loans are to customers with an ITIN instead of a Social Security Number. To date, 2004 was the peak lending year, with 93 new loans under the program.

### How have the loans performed?

There have been no foreclosures under the program. Only three loans have had 90-day delinquencies. If the program director sees an account is overdue, she writes a note to the customer. The bank sends an official letter if a customer is close to 90 days delinquent.

Loan payment problems generally arise from job loss or a medical emergency. The bank is willing to work with customers by modifying the loan and rolling a few payments into the loan principal. As long as the customer makes an effort to provide some payment, the bank will work with the customer. In the one case requiring this type of extensive intervention, the bank reports that the customer is now on track with loan payments.

### What are the underwriting criteria for the program?

The program is flexible regarding credit history and documentation of income and employment. The bank looks at credit scores where available and generally does not accept scores lower than the upper 500s. Jefferson Bank has made loans to people with scores of 522 or 565 if the customer has a good explanation for the low score. They accept total debt-to-income ratios of up to 50 percent.

For clients with a Social Security Number, the bank will accept four lines of alternative credit. They look for a good history of paying utilities, telephone service, or car or furniture rental. They will accommodate one delinquency in payment, as long as it does not reflect a pattern. A long job history can make up for other delinquencies. “People see their house as the most important thing,” says the program director. “They will make their house payment before paying other obligations.”

In examining credit history outside of the credit score, Jefferson Bank looks for at least two years in the same profession, although not necessarily with the same employer. The big picture—including the earning ability of the borrowers—is an important consideration. The bank uses standard forms or calls the employer to verify employment. The program does not consider income from household members other than the borrowers, but does include supplemental income not reported in formal documents if it is verifiable. For example, if someone mows lawns on the weekends, the income could be considered if they provide letters from clients. If income is non-taxable, it is increased by 25 percent, and the Earned Income Tax Credit is considered as income.<sup>34</sup> For loans based on the ITIN, the bank also requires at least one year of tax returns.

For the loan down payment, the bank accepts both gifts and unseasoned income. They also work with the city down payment assistance program when applicants qualify.

Basic homebuyer education is provided during the home loan process. The program director encourages buyers to attend Saturday classes offered by the City of San Antonio.

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<sup>34</sup> The Earned Income Tax Credit (EITC) is a federal tax credit designed to supplement the income of the working poor.

The program director also provides borrowers with the Fannie Mae Foundation booklet on home buying and reviews the information with them.<sup>35</sup>

#### Does the bank service the loans?

The loans are held in portfolio and serviced by the bank. In practice, Jefferson Bank services the entire financial relationship. The bank monitors accounts opened by borrowers to ensure they are not having problems with overdrafts and works with customers to help them manage their account.

For example, one customer frequently over-drafted her account because she did not understand that there is a delay between the time when the purchase is made on a debit card and when the amount is deducted from the account. The program director contacted the customer and together they decided that an ATM card might better meet her needs.

#### Why is the program a success?

Without this program, many of the people served would have no other options for home mortgages or pay very high interest rates and fees. Some refinance requests that came into the program had original interest rates of 12 to 18 percent, required mortgage insurance, and had closing costs in the range of \$8,000. Some contract-for-deed refinances had 12 to 18 percent interest and no title on the property.

The relationship with the customer is also an important part of success. Once people close their loan, they are immediately marketed various insurance and loan payment restructuring products that look like they are coming from the bank, but are in fact from separate companies. Customers will often call the bank and ask advice, which has helped them avoid costly and unnecessary expenditures.

The greatest limitation of the program is that the loans cannot be sold on the secondary market, and so the available capital is limited. Jefferson Bank would like to serve more people with ITINs and no credit scores, because the loans are performing well. The program is self-sustaining in the short-term—with long-term profit potential, and it provides the bank with a unique opportunity to expand its customer base.

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<sup>35</sup> The homebuying guide can be viewed on-line at: <http://www.homebuyingguide.com>.

**TexasBank**  
*Fort Worth, Texas*

**ITIN Loans through Programa Libertad con TexasBank<sup>36</sup>**

Background

TexasBank was formed in Weatherford, Texas in 1889. They currently have 25 branches in the Dallas/Fort Worth area. The bank holds \$1.5 billion in assets and \$1.1 billion in loans.<sup>37</sup> TexasBank began providing home mortgage loans in the early 1980's. Most of their home mortgage lending is done using Fannie Mae products.

Programa Libertad was launched in June of 2000. The program is designed to serve customers who do not have a valid Social Security Number, although other customers can choose to use the program. Some customers who qualify for Fannie Mae products have chosen the Programa Libertad loan because it requires less paperwork. Conversely, there have also been customers coming to apply for Programa Libertad, but ending up in a Fannie Mae loan.

Currently, all applicants without a Social Security Number must have an Individual Taxpayer Identification Number (ITIN), which is issued by the Internal Revenue Service. The bank developed Programa Libertad in response to a request from a local real estate agent who was looking for a loan product to help clients who could not qualify for a valid Social Security Number. The realtor was looking for a loan without many upfront fees and a lower interest rate than available options. She asked for no origination fee, no survey requirement for properties within the city, and no requirement for escrow of taxes and insurance. Initially the realtor made up all of TexasBank's business under this program, but in recent months they have begun soliciting other customers. Now, the realtor makes up half of the new business, and the bank intends to expand its marketing of the program.

In the past six months, the bank has begun accepting the Mexican consular identification card, the *matrícula consular*, to open bank accounts, as most loan applicants are of Mexican origin. TexasBank does not require a bank account for participants in the loan program—and at the program's inception, most did not have one. Now, two-thirds of the applicants have a bank account. TexasBank is working to attract more loan customers and is considering offering credit cards to the home mortgage program participants.

The bank also is working to expand Spanish language customer service. They currently have bilingual staff on the mortgage origination and servicing side and are working to increase bilingual staff on the banking side. Most of the marketing for the program is done through real estate agents and word of mouth.

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<sup>36</sup> Interview with Joe Barnhart, President/Mortgage Division, TexasBank, March 28, 2005.

<sup>37</sup> Texas Department of Banking, "Top 100 Banks in Texas by Asset Size Information as of December 31, 2004."



What is Programa Libertad con TexasBank?

Programa Libertad is a 15-year fixed rate mortgage product with a 10 percent down payment requirement. Customers are comfortable with the 15-year loan term because they want to pay the loan off quickly. Borrowers tend to pay between \$50 and \$100 extra every month in cash. The bank holds the loans in portfolio because there is currently no secondary market for home mortgage loans based on ITINs.

**Programa Libertad Loan Program: A Snapshot**

Year of Program Inception and Number of Loans	Program began in June of 2000. Currently 600 loans in portfolio.
Target Customers	Applicants without access to a Social Security Number
Average Loan Size	\$55,000-\$60,000
Loan Type	15-year fixed rate loan
Down Payment	Requires 10 percent. Accepts gifts, unseasoned savings, and city down payment assistance.
Interest Rate	9.5 percent; will reduce by 1 percentage point for \$200 fee after two years of on-time payments
Fees	No origination, processing or survey fees; \$27 application fee, \$295 appraisal, and attorney and other usual fees
Debt-to-income ratio	28-30 percent front end; 50-60 percent back end
Credit Evaluation	Assesses alternative credit; looks for four years of rental history and three credit letters. Emphasis on housing stability and two-year work history.
Loan Performance	Three foreclosures
Financial Education	Required to attend City of Fort Worth homebuyer education classes. One-on-one counseling provided by loan officer using the Fannie Mae Foundation home purchase education booklet.
Profitability	Profitable product for the bank.

The current interest rate for the loans is 9.5 percent. With two years of on-time payments, customers have the option to reduce their interest rate by one percentage point

(to 8.5 percent under current terms) for a \$200 fee. If borrowers become documented, the bank will modify the loan to a 30-year fixed rate loan at an A paper rate for a 1 percent origination fee and \$400 to cover transaction costs. Program applicants must provide both a picture ID with current address and an ITIN card. There is no private mortgage insurance for the loans, and they do not require a survey for properties in an established neighborhood. There is no origination or processing fee, and no prepayment penalty for the loans. They charge a \$295 appraisal fee, \$27 application fee, and charge attorneys fees and other customary closing costs. They will finance homes that are in poor condition, because they found that people will fix them up. Two-thirds of the loan applicants work in the construction business.

TexasBank looks for borrowers who take pride in where they live and credits this program with revitalizing neighborhoods. Alternative credit is used for underwriting most loans, and the loan officers view a long history of residence at the same location as one of the most important determinants in the success of the loan.

Six hundred loans have been made under Programa Libertad since June of 2000, for a total of \$25 million. New loan closings average about 18 per month. Most loans tend to be in the \$55,000 to \$60,000 range, with a high of \$120,000 and a low of \$20,000. TexasBank has staff whose job is to help connect borrowers to down payment assistance programs and take advantage of those programs when they can.

#### How have the loans performed?

There have been three foreclosures under the Programa Libertad. Delinquencies are higher than the Fannie Mae loans they service, but lower than other portfolio loan products despite the higher underwriting and down payment requirements for the other loans.

The first late payment notice is sent out if payment is not received by the 17th of the month to let the customer know that a late charge will be assessed. Phone calls are made to borrowers during the last week of the month if payment is not received. If loan officers are unable to reach the borrowers by phone, they often will drive by the property to try to contact the borrower. On the 45th day, bank staff will drive out to the property to make sure that it has not been abandoned. If it has been abandoned, then they initiate foreclosure proceedings. Otherwise, they wait until the 62nd day to send a delinquency notice.

As the low foreclosure statistics reflect, the bank is usually able to work out any payment problems. Most problems are the result of unemployment or a medical emergency, and the borrowers work in good faith to continue payments on the loan.

What are the underwriting criteria for the program?

In assessing credit worthiness, the loan program requires four years of rental history documented by letters from landlords, with a strong preference for residence in the same location for all four years. In addition, three alternative credit letters are required, but the letter of rental history may count as one of the three.

The 10 percent down payment and the closing costs must be in a savings or checking account and verified by a bank statement, but they do not have to be seasoned. The down payment may come from a gift or a down payment assistance program. The bank allows a 28 to 30 percent front end debt-to-income ratio and 50 to 60 percent back end ratio. They do not look for reserves because the borrowers generally have income and savings in addition to documented reserves.

The program requires two years of work history verifiable through W-2s and pay stubs. It is not important that the borrowers be employed by the same employer. Pooled household income is considered in making the loan, as well as part-time or undocumented income through the higher debt-to-income ratio. It is assumed that the documented income is only part of the total family income.

Borrowers are required to take homebuyer education classes offered by the City of Fort Worth. There is no charge for the classes. The loan officer also provides one-on-one counseling using the Fannie Mae Foundation homebuyer booklets.

Does the bank service the loans?

The bank services the loans in its portfolio, including Programa Libertad, and all of its Fannie Mae loans. Because the Programa Libertad loans are the only portfolio loans that do not require PMI, the bank has a particular investment in the success of the loans.

The bank will customize payment schedules to accommodate a family emergency. Their experience has shown that the vast majority of late payments are tied to unemployment or a medical emergency. To help people maintain their homes through such times, the bank will roll a payment into the loan or allow the customer to pay only interest for a designated period of time until they can resume full payments.

If payments are late, the bank will make a personal contact to try to resolve the situation. In one such case, it turned out that the borrower had signed up for a bi-weekly payment plan he thought was being marketed by the bank, and the plan had failed to make the payments. The borrower immediately made the necessary loan payments. This instance emphasizes the importance of communication and having a relationship with the borrower.

How is the program a success?

The program is a profitable initiative for the bank and provides an underserved community with the opportunity to own a home. Because of the strong performance of the loans, the bank is now exploring offering other financial services to mortgage customers, from increased marketing of basic accounts to credit cards and other services.

The greatest limitation on the bank's capacity to expand the lending program is the lack of a secondary market for the loans. However, the bank expects this lending market will expand and that interest rates will decrease as more financial institutions become interested in serving a community that has been shown to be a good credit risk.



**LENDER PARTNERSHIPS WITH  
NON-PROFIT COMMUNITY DEVELOPMENT  
CORPORATIONS  
&  
COMMUNITY-BASED ORGANIZATIONS**

**Community Development Corporation  
of Brownsville/Ameriquist Partnership**  
*Brownsville, Texas*

**Affordable Home Ownership for Texas Pilot Program<sup>38</sup>**

Background

The Community Development Corporation of Brownsville (CDC Brownsville) was established in 1974. The non-profit corporation both builds and finances affordable housing in southern Cameron County. In 2004, they partnered with Ameriquist, a subprime lender, and the Texas State Affordable Housing Corporation (TSAHC) to pilot an initiative to provide reasonably priced home mortgage credit to families with a low credit score.

Ameriquist, a privately owned subprime lender, has made \$83 billion in subprime loans. They accept credit scores as low as 500, but average around 620. They currently service 520,000 loans and have a 9 percent delinquency rate compared to the national subprime average of 14 percent. Loan servicing is an important part of their business. Texas is their sixth largest lending market in terms of capital and third largest in number of units.

Ameriquist has committed \$100 million to the Affordable Home Ownership for Texas Program, and TSAHC has committed \$1 million in down payment assistance. The program was developed based on the experiences of CDC Brownsville, which is the first pilot site. The CDC has a successful lending history. Over the past 10 years, they have serviced 700 loans under the Affordable Housing Loan Program with only three foreclosures. However, they were only able to serve four out of every 10 people who walked in their door. The greatest barrier to providing loans was credit problems. The CDC found that the only products available to serve these borrowers were subprime loans issued through mortgage brokers, who often maximize interest rates and fees.

“We want to have a broad-based impact on the market to push down prices of subprime loans,” said the program director. To achieve this goal, CDC Brownsville created a program with Ameriquist and TSAHC designed to offer a subprime loan product that more closely reflects true lending costs and risk and provides the borrower with an opportunity to lower the interest rate on the loan by demonstrating a good payment history.

What is the Affordable Home Ownership for Texas Program?

The program is designed to serve first-time home buyers with credit scores ranging between 525 and 610 and with incomes at or below 80 percent of the area median family

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<sup>38</sup> Interview with Don Currie, Executive Director of CDC Brownsville, March 1, 2005.

income. Alternative credit and stated income of up to 25 percent is considered, but the borrower must have a credit score. The lender wants to ensure that participants cannot qualify for prime loans. No mobile homes or homes in rural areas can be financed through the program. It is designed primarily for new or recent construction. Ameriquest underwrites and issues the first lien and services the loan. Brownsville CDC finds and screens potential borrowers, provides most program financial education, and connects qualified borrowers to down payment and closing cost assistance programs.

### **Affordable Home Ownership for Texas Program: A Snapshot**

Year of Program Inception and Number of Loans	Program began in late 2004. To date, 167 loans have been issued.
Target Customers	Applicants with a credit score between 525 and 610
Average Loan Size	\$70,000 to \$80,000
Loan Type	30-year fixed rate loan. During first four years of loan, rate will reduce by 50 basis points for every 12 consecutive months of on-time payments.
Down Payment	10 percent—and 3 percent of must come from borrower's own funds; remaining 7 percent may come from gifts or down payment assistance programs.
Interest Rate	275 basis points above the rate of a 10-year Treasury note
Fees	\$500 lender fee to Ameriquest. CDC receives about 3 percent of loan value origination, processing, and other fees.
Debt-to-income ratio	50 percent back end ratio
Credit Evaluation	Must have a credit score between 525 and 610.
Loan Performance	One loan late over 30 days.
Financial Education	Required to attend Brownsville CDC counseling and education classes and a class provided by ACORN.
Profitability	No information available because of short tenure of program.

The loan requires a 10 percent down payment, with the borrower contributing at least 3 percent from personal funds. TSAHC provides 7 percent through a second lien that is



amortized over 10 years. The seller is required to contribute 3 percent of the sales price towards closing costs, which is a common term for new construction. Closing costs may be rolled into the loan as long as the loan-to-value ratio does not exceed 90 percent. The minimum loan amount for the program is \$50,000. To date, 17 loans have been made under the program, averaging \$70,000 to \$80,000. A total of \$20 million in capital is available for the pilot project, with the goal of making 150 loans over the next 18 months.

The first lien is a 30-year loan that is fixed after the first four years of payment. The initial rate is set at 275 basis points above the 10-year Treasury rate on the 15<sup>th</sup> of the month that preceded the loan commitment date. The second lien, from TSAHC, is set at 4 percent interest. The payment for both loans is combined into one monthly payment. The interest rate for the 30-year loan is designed to provide an incentive to the borrower to make on-time payments. For each year of timely payments in the first four years of the loan, the loan interest rate drops by one-half of 1 percent. The total possible drop is capped at 2 percent. After the first four years, the loan rate is fixed. As of March 2005, the initial rate offered on the loans was 6.35 percent, with a potential drop to 4.35 percent at the end of four years of timely payments. Escrow of taxes and insurance is required. There is no private mortgage insurance.

CDC Brownville is advertising the program through outreach to area builders. They are also able to find borrowers simply through word of mouth.

#### How have the loans performed?

Currently, there is little data on loan performance. The first loans were made in the spring of 2005. Loan performance will be assessed at the end of the 18-month pilot to determine if any changes in the loan structure or underwriting are needed.

#### What are the underwriting criteria for the program?

In order to qualify for the program, the borrower must have a valid Social Security Number and have documented income from the U.S. Non-citizens with legal work status may qualify.

The average credit score of the borrower or of the highest wage earner, if there is more than one, must reflect a credit score ranging between 525 and 610.

One year of rental history with no late payments is required unless borrowers can document they are living rent-free with parents or others. If a rental history is unavailable, borrowers must present a completed budget worksheet or provide proof of three months cash reserves.

Twelve months of job history is required. It does not have to be with the same employer as long as there is documentation of continuous or increasing income. Seasonal

employment may be considered. Employment income is verified through two years of bank statements or two years of tax returns, W-2's, and a statement or pay stub with year-to-date earnings. Twenty-five percent of total income may be stated income, supported by a letter. The Earned Income Tax Credit is considered as part of the stated income allotment and must be documented through tax returns.

The program permits charge offs of under \$5,000. All open judgments and tax liens must be paid off, and delinquent lines of credit must be paid off or made current. Any payments on collections, with the exception of medical collections, are calculated at a 3 percent per month rate and included in the debt-to-income ratio. It is not necessary to resolve medical collections to close on the loan. The maximum total debt-to-income ratio is 50 percent. The 3 percent down payment that must come from the borrower's own funds must be deposited in a bank account 30 days prior to closing.

Ameriquest receives a lender fee of \$500, and the CDC receives a 1 percent origination fee. There is a \$350 application fee, and a \$105 fee for processing and document preparation. In total, the CDC receives approximately 2 percent of the loan amount in fees.

Financial education is required for the loan. The Brownsville CDC provides free counseling for prospective homebuyers. Homebuyers must also attend a supplemental financial education class offered by ACORN in partnership with Ameriquest.

#### Which partner services the loans?

Ameriquest holds and services the loans. They have a center in California that specializes in loan servicing. Their servicing style is hands-on and focuses on early intervention. Three days after the payment due date, servicing center staff will call the borrower to see if there is a problem. They also offer early delinquency intervention counseling with the goal of bringing borrowers back into their regular payment schedule before problems get out of control.

#### Why is the program a success?

The program is still a new initiative. There has not been enough time to quantify its success or impact. It does offer an innovative opportunity for families with a problem credit history to access fairly priced credit and have the chance to work towards a prime rate loan through a demonstrated payment history. The director of Brownsville CDC commented, "It is still a new program, but the hope is that we will be able to serve more people walking in the door and create healthy competition for the over-priced subprime market."

**San Antonio Alternative Housing Corporation/San Antonio  
Federal Credit Union Partnership**  
*San Antonio, Texas*

**People Helping People Program<sup>39</sup>**

Background

The San Antonio Alternative Housing Corporation (SAAHC) was founded in 1993. They own rental housing for low-income families, develop new affordable single-family homes, and provide home buyer and home owner financial counseling and classes. San Antonio Federal Credit Union provides home mortgage loans to families who qualify to purchase homes built by SAAHC and provides financing to SAAHC for the home construction and land purchase costs.

San Antonio Federal Credit Union (SACU), founded in 1935 for military civil service employees, is a large credit union with \$1.8 billion in assets. They began offering home mortgage loans in 1975 and currently hold a \$450 million real estate loan portfolio. They currently have 14 branches in San Antonio and two branches in Houston. Their members in the San Antonio area include local, state, and federal government employees; students at post-secondary institutions; employees at financial institutions; and families of credit union members. There are also 1,500 companies and community organizations in Houston and San Antonio that qualify people for membership. Borrowers in the People Helping People loan program qualify for membership through their affiliation with SAAHC.

SACU launched the People Helping People Program as a result of efforts to target unmet financial service needs in the San Antonio community. They partnered with Dolores Catholic Church to conduct focus groups with low-income San Antonio families. Out of this process came a new partnership with the non-profit housing corporation to provide affordable housing loans to support new home development. “If you can’t provide affordable housing to your community, then that is the first step to the downfall of the community. We tried to design a program in tune with specific community needs, instead of asking the community to conform to our product,” said the SACU program director.

The People Helping People Program is targeted for low- to moderate- income residents in San Antonio. Families cannot exceed the area median income set by the U.S. Department of Housing and Urban Development—and most are at or below 80 percent of median income levels.

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<sup>39</sup> Interview with Chuck Smith, First Vice President, Director of Lending, San Antonio Federal Credit Union, June 20 and 21, 2005.

SACU also encourages borrowers to open a free checking account at the credit union. Approximately half of the borrowers maintain a checking account. They also offer borrowers access to other conventional financial service products, such as car loans. Twenty-five percent of the borrowers have used additional credit union financial services.

Outreach for the lending program is done through the San Antonio Affordable Housing Corporation. The corporation identifies and screens potential borrowers. They also provide all of the counseling and homebuyer education and collect all of the credit history required for the loan. The credit union then assesses the credit information and makes loan approval decisions.

### People Helping People Program: A Snapshot

Year of Program Inception and Number of Loans	Began in 1997. To date, 200 loans have been issued.
Target Customers	Families at or below area median income
Average Loan Size	\$50,000
Loan Type	15-, 20-, and 30-year fixed rate
Down Payment	1 percent minimum; \$500 must come from borrower's own funds
Interest Rate	Conventional Fannie Mae rate, locked 7 days prior to closing
Fees	No lender fees. Negotiated \$100 discounts for survey, appraisal, and attorney fees.
Debt-to-income ratio	45/50
Credit Evaluation	Conducted on case-by-case basis; alternative credit accepted.
Loan Performance	No foreclosures. Average of five loans per month are 30 days or more past due.
Financial Education	Required to attend a seven-class series offered by the San Antonio Affordable Housing Corporation. Post-purchase and delinquency counseling also offered.
Profitability	Self-sustaining with long-term profit potential.

### What is the People Helping People Program?

The People Helping People Program offers a 1 percent down fixed rate home mortgage loan amortized over 15, 20, or 30 years. Most purchasers opt for the 30-year loan and have between \$10,000 and \$15,000 in down payment assistance through the City of San Antonio. The down payment assistance is offered as a low-interest or zero percent interest loan. Borrowers must provide at least \$500 or 1 percent of the loan amount from their own funds. The average loan amount after down payment assistance is in the \$50,000 range. The minimum loan amount is \$10,000, and the maximum is \$90,000.

The credit union asks borrowers, currently residing rent free with a parent or another person, to deposit \$500 per month into a savings account to become accustomed to making a monthly mortgage payment. Because the financing is for new construction, it usually takes six months to close on the house after being accepted into the program. This gives these borrowers time to save up to \$3,000—a financial safety net that can be used to purchase a refrigerator and other appliances that a new homeowner needs.

No private mortgage insurance is required for the loan. For borrowers with less than 80 percent loan-to-value, a mortgage insurance risk premium is added to the loan's interest rate. As part of the closing process, down payment funds that come from the borrower must not be seasoned and may be a gift. SAAHC works to pull together down payment assistance resources. Escrow of taxes and insurance are required as part of the closing costs. The credit union works to minimize other closing costs. They do not charge an origination fee for the loan or any processing, closing, or escrow fees. They also negotiate discounts on the surveyor, appraisal, and attorney fees. Each service offers a \$100 discount.

To date, 200 loans totaling \$10 million have been made under the People Helping People Program. Most of the loans have been issued in the past four years. They tend to be issued in groups, as each new development is completed. There is no limit to the number of loans issued under the program. The People Helping People Program finances home purchases for all of the new SAAHC affordable housing developments. Currently, a 131-unit subdivision is under development. Approximately 10 to 15 homes are completed and financed every month.

### How have the loans performed?

The loans have performed as well or better than other portfolio loans. To date, there have been no foreclosures. If a family has problems paying, they are offered post-purchase counseling options. If there is no way for the family to maintain payments, SAAHC works within the community to bring a new family into the home.

Delinquent payment statistics are also very low. In the most recent month, five of the 200 loans were 30 days or more past due, a typical scenario for the program. The delinquency statistics for this portfolio program are better than for other portfolio loans.

The program covers its costs and will be moderately profitable in the long-term. It pays additional long-term dividends to the credit union as a result of cross selling products.

What are the underwriting criteria for the program?

To qualify, borrowers must be pre-screened by SAAHC and cannot have income in excess of the San Antonio area median income, which is currently \$51,500 a year. SAAHC collects all credit information and submits it to the credit union.

The program considers both full and alternative credit documentation. Credit is assessed on a case by case basis. The credit union relies on SAAHC to screen candidates and refer only those who appear to have sufficiently good credit to qualify for the program. SAAHC will work with people to improve their credit. As a general rule, the credit union does not accept credit scores below 600 for this program. Twelve months of rental history documented by receipts or canceled checks is required. There can be no rental delinquencies in the past 12 months, and only one delinquency in the past 24 months.

Employment income must be verified with the most recent pay stub and two years of W-2 forms. For the self-employed, two years of personal and business tax returns and a profit and loss statement are required. It is not necessary to be employed in the same profession as long as the income level is maintained or improves over the two-year period. Pooled income from other household members is considered as a compensating factor if it can be established that the additional income earners have a history of living with the borrower and will continue to be part of the borrower's household. Informal employment will also be considered if it can be documented by a letter. The maximum housing debt-to-income ratio is 45 percent, and the maximum total debt-to-income ratio is 50 percent.

The interest rate is set at the conventional Fannie Mae rate for the loan based on the loan-to-value ratio. The current rate for a 30-year loan is approximately 5.65 percent.

Financial education and counseling are required as part of the loan and are provided by SAAHC. They offer a seven-session financial education class that covers a range of topics, from basic budgeting to understanding the loan, from home maintenance to insurance issues. Once the home is purchased and the loan closed, SAAHC offers an extended home ownership counseling program. They maintain monthly contact with homeowners over the first three years and address a range of issues tied to owning and maintaining a home and to creating a thriving community.

Which partner services loans?

SACU holds all of the People Helping People loans in portfolio and collects payments both on the first lien and any second lien through the down payment assistance programs.

If a payment is late, the credit union contacts SAAHC. SAAHC intervenes to determine the source of the problem and attempt to resolve the delinquency.

SAAHC offers delinquency counseling as part of their home ownership counseling services. They work with borrowers through one-on-one counseling to resolve the delinquency. SACU's policy is to begin foreclosure proceedings after the loan is 60 days delinquent and to complete the foreclosure when the account is 90 days past due.

“We are in the business to make loans and get repaid,” said the program director. In that vein, the credit union is flexible with the borrower and will adjust loan terms, including extending the period of the loan or folding a payment into the loan, in order to assist borrowers through short-term crises. They work in partnership with SAAHC. SAAHC provides direct services to the borrower, and the credit union offers flexibility in the loan. In extraordinary situations, the credit union will intervene to help borrowers stay in good loan standing. In one instance, the credit union raised funds to make payments for a borrower who was hit by a car and could not go to work.

#### Why is the program a success?

The People Helping People Program was developed with direct input from the target community. It has been successful in providing home ownership opportunities for people who would otherwise have continued renting. “If you don't give people the opportunity to buy real estate, they will keep renting and not build wealth,” commented the program director. “If you provide a stable place to live for a family, then other good things start happening.”

## **ACORN/ Bank of America Partnership** *Austin, Texas*

### **ACORN Loan Program<sup>40</sup>**

#### Background

The Association of Community Organizations for Reform Now (ACORN) was founded in Little Rock, Arkansas in 1970. It is a social justice organization that works to create better housing and job opportunities, improve access to health care, create safe neighborhoods, and meet other community needs. There are 175,000 members and 850 neighborhood chapters across the country and around the world.

The Bank of America/ACORN loan partnership was launched as a way to help Bank of America better reach low-income communities. Bank of America holds approximately \$36.4 billion in assets and has a large banking presence in Texas.<sup>41</sup> The partnership was launched 10 years ago, and Bank of America offers ACORN loans in many different markets. In Texas, the program was first launched in Houston, Dallas, and San Antonio. The Austin program began operation in 2003.

The program targets families at or below 100 percent of the area median income. In Austin, families earning \$68,400 or less qualify for the loan program. In addition to the loan program, Bank of America offers a full array of banking services to borrowers. All borrowers qualify for the Advantage Checking Account, which includes free checks. They also qualify for a free savings account and safety deposit box. Most unbanked borrowers and some who already have a bank account take advantage of the offer.

Outreach for the program is done through realtors, home builders, and church groups. ACORN also conducts outreach through its networks. Many referrals come through word of mouth.

#### What is the ACORN Loan Program?

The loan program is a partnership where Bank of America offers the loan, and ACORN offers pre- and post-purchase financial education and counseling. The loan offered is a 30-year fixed rate loan priced at 75 basis points below market rate for a 97 percent loan-to-value product. A 3 percent down payment is required, with a minimum of \$500 from the borrower's own funds. The maximum sales price to qualify for the loan is \$175,000,

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<sup>40</sup> Interview with Cindy Baranowski, Senior Vice President, Sales Manager Mortgage Lending, Bank of America, Austin, Texas, March 30, 2005, and interview with Yaisa Johnson, Manager of the ACORN Partnership with Bank of America, Consumer Real Estate Regional Marketing Director, Bank of America, June 10, 2005.

<sup>41</sup> Texas Department of Banking, "Top 100 Banks in Texas by Asset Size Information as of December 31, 2004."



with an average loan size of \$140,000. Between 20 and 30 ACORN loans, valued at \$2 million to \$3 million, are made per month in the Austin market.

The bank charges a \$250 application fee, \$719 for a loan closing fee, \$75 for tax service and \$11 for a flood certificate. The application fee and any other accrued fees are refunded if the loan is not finally approved. The bank does not require private mortgage insurance. Closing costs average about \$2,000 per loan plus the down payment and the required escrow of taxes and insurance. Bank of America will accommodate borrowers who wish to participate in the city down payment assistance program, but does not actively pursue such funds for borrowers. Approximately one-third of all loan

### ACORN Loan Program: A Snapshot

Year of Program Inception and Number of Loans	Available in various Texas cities since 1995. In 2003, program opened in Austin; 20 to 30 loans are currently issued there each month.
Target Customers	Families at or below 100 percent of the area median income
Average Loan Size	\$140,000
Loan Type	30-year fixed rate.
Down Payment	3 percent minimum; \$500 must come from borrower's own funds
Interest Rate	75 basis point below conventional mortgage rate for 97 percent loan-to-value product
Fees	Lender fees approximately \$1,000, in addition to customary title fees.
Debt-to-income ratio	38/45
Credit Evaluation	Alternative credit allowed, with a maximum of two non-housing delinquencies over 12 months. With debt ratios over 38 percent, will not approve loans with payments exceeding 25 percent of the borrower's rent payment.
Loan Performance	No information available.
Financial Education	Required to attend home ownership financial education classes offered by ACORN in San Antonio.
Profitability	Long-term profit potential

applications are rejected because of credit problems. The average documented income of borrowers is \$30,000 per year, and most applicants work in the service industry.

How have the loans performed?

“Bank of America is pleased with the ACORN product and partnership,” commented program staff. No specific information was provided regarding loan performance. Pre-purchase counseling is viewed as an important factor in mitigating the risk of the loans.

What are the underwriting criteria for the program?

The loans have flexible underwriting guidelines. Many program applicants have no credit score, and so the program depends primarily on alternative credit for underwriting loans. Generally, the bank looks for 12 months of decent credit. No more than one 30-day and one 60-day late payment over the last year are accepted. The bank will accept bankruptcy and repossessed vehicles that have been seasoned for two years with reestablished credit. They will accommodate a few small collections at closing. Medical collections are not counted against the borrower, but must be paid at closing. In addition, all borrowers must have a bank account by closing. The down payment and closing costs above the required \$500 borrower contribution may be a gift from a family member or a non-profit organization. All closing costs must be documented in a bank account prior to closing.

For alternative credit certification, three trade lines are required with no more than two late payments in the non-housing lines. There should be no late rental payments. One year of rental history must be certified with a letter from the landlord. The bank also looks at utility payments, rent-to-own payments, and other ways of verifying a credit history. They prefer that both housing and utilities be in the name of the borrower, but will accept just one in cases where housing is shared.

Two years of employment history must be verified with W-2's and tax returns. More than one family member's income may be used to underwrite the loan, and the bank will accept up to \$1,200 per month of income that is not documented by a W-2 or other official form. The bank looks for two years of work in the same industry, but not necessarily for the same employer.

The maximum housing debt-to-income ratio is 38 percent, and the total ratio is 45 percent. They will not approve a house payment that is more than 25 percent above what the borrower was paying in rent.

Financial education is required as part of loan program. ACORN provides the financial education classes for a \$20 fee.

Which partner services the loans?

Bank of America holds the loans in portfolio for a designated seasoning period and then can offer the loans on the secondary market. The bank services the loans. ACORN conducts follow-up counseling for the first year of the loan.

How is the program a success?

The program is a success for Bank of America on two different levels. It provides them an opportunity to serve an underserved demographic in their community and gain credit for the Community Reinvestment Act exam. It is also an opportunity to develop future customers. People who purchase homes through the ACORN program tend not to sell in the short term, preferring instead to build towards a long-term asset. Keeping a home over the long-term can be a source of stability for families.

**NON-PROFIT  
SUBSIDIZED INITIATIVES**

## **Proyecto Azteca** *San Juan, Texas*

### **Self-Help New Construction Program<sup>42</sup>**

#### Background

Proyecto Azteca is a non-profit organization established in 1991 to help members of the United Farm Workers improve their economic status. Proyecto Azteca offers home mortgage loans as part of the Self-Help New Construction Program.

The self-help program was launched to fund infrastructure improvements in farm worker communities and to provide a better system of financing the construction of homes that farm workers were already building themselves. The philosophy behind the program is to provide a middle class financial support system and access to credit to a poor community.

The target population for the program is low-income migrant farm workers with incomes ranging from \$8,000 to \$10,000 per year. In addition to the self-help loans, the Azteca Community Loan Fund (ACLF) provides micro entrepreneurial loans for informal business enterprises, emergency family support loans, medical loans, an individual development account (IDA) program, a savings incentive program, loans for processing immigration paper work, and Earned Income Tax Credit matches to support asset building.

Proyecto Azteca also has a special program with First National Bank, an ACLF partner on the IDA program. The bank offers free savings and checking accounts with a \$50 minimum deposit and minimum balance. Participants are given a \$100 grant to deposit in the checking account and \$50 for the savings account. If the total balance drops below \$50, there is a \$10 fee to maintain the accounts. The savings account interest rate is 1 percent. Both Proyecto Azteca and the bank provide financial education on how to write checks and manage the accounts. “Poor people do not go to banks because they have been told ‘no’ too many times,” said the director of Proyecto Azteca. “If one in 20 people qualify for a product, then it doesn’t work.” This account program is an opportunity for people to have a positive experience with a bank, he said. First National Bank launched the program as a way to reach low-income people in their community and introduce them to the benefits of financial services.<sup>43</sup> One thousand accounts have been opened through the program, and 30 percent have remained open after the required six-month period.

Outreach for Proyecto Azteca and ACLF programs is done largely through word of mouth. “If you provide a service to a community that is realistic in the context of their lives, then they will come,” commented the program director. Thirty new families approach them for assistance each day.

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<sup>42</sup> Interview with David Arizmendi, Director of Proyecto Azteca, March 7, 2005.

<sup>43</sup> Interview with Dianna Treviño, First National Bank, April 8, 2005.

What is the Self-Help New Construction Program?

The Self-Help New Construction Program offers zero percent no fee home mortgage loans to low-income migrant farm workers for homes that are constructed by the family. All homes financed under this program have three bedrooms and one bath, but families may personalize certain design elements. The design is meant to meet family need at an affordable price. The market value for the homes is approximately \$35,000, and most loans under the program are for approximately \$23,000.

**Self-Help New Construction Program: A Snapshot**

Year of Program Inception and Number of Loans	Began in October of 1991; currently 600 loans in portfolio.
Target Customers	Migrant farm workers with incomes around \$10,000
Average Loan Size	Under \$23,000
Loan Type	Loan term varies based on ability to pay; term averages 20 years.
Down Payment	Zero to \$1,000 based on ability to pay
Interest Rate	Zero percent
Fees	None
Debt-to-income ratio	Monthly payment capped at 10 percent of income.
Credit Evaluation	None; serves families based on need.
Loan Performance	Delinquencies average 5 percent; few abandoned homes.
Financial Education	Required classes; focus on dispelling misconceptions about home ownership and financial services.
Profitability	Subsidized program

Because the program serves the neediest families, with annual incomes frequently under \$10,000, Proyecto Azteca has structured a highly flexible program. The loan term and loan payments are based on annual family income. The total monthly payment is set at 10 percent of monthly family income. The total loan amount is divided by the monthly payment to arrive at the loan term. Monthly mortgage payments range from \$50 per month to \$150, averaging at \$100 per month for approximately 20 years.

To date, approximately 600 loans have been made under the program. Families that can afford it are required to pay a small down payment, between \$500 and \$1,000. This payment helps to fund assistance to even lower income families.

#### How have the loans performed?

The delinquency rate for monthly payments averages at 5 percent, increasing to 7 percent around Christmas time and decreasing to 3 percent during tax season because of the Earned Income Tax Credit. To date, three homes have been abandoned, and the bank has worked to avoid foreclosure by moving new families into the homes.

Borrowers are generally employed in seasonal work, and so the program works with them to plan for periods of unemployment. Borrowers are expected to increase mortgage payments during work periods to compensate for the lack of payments when there is little income. Over 40 percent of the portfolio is three months to more than a year ahead in their payments. The extra payments are escrowed and applied to future months to provide consistent monthly payments.

Loans are not considered late until they are 180 days past due. At 90 days past due, a letter is sent to the borrower. Because they have a personal relationship with their lender, borrowers will contact the lender if a problem develops and will work to keep the home loan in good standing. The Azteca Community Loan Fund can lend money to cover unexpected expenses and help the borrower get back on his feet.

#### What are the underwriting criteria for the program?

The program does not look at credit but rather at the consumer's ability to pay. It responds to need rather than manages risk. The focus is not to get repaid, but rather to customize a loan that works for the borrower's particular circumstances.

There is no private mortgage insurance for the loans, but homeowner's insurance is mandatory. Families are required to escrow taxes and insurance. Approximately 60 percent of the borrowers escrow tax and insurance payments. Property taxes average \$1000 per year. If that payment is too high for the borrower, then the loan terms are adjusted to make the entire cost affordable.

Financial education classes are required to participate in the program. Low-income families tend to think in the short-term, and so it is particularly important to offer financial education that is tangible and addresses common misperceptions. For example, one common misperception is that a loan is all that is required to own a home and that people can get away with not paying property taxes. To teach people about property taxes, Proyecto Azteca brings in an employee of the county tax assessor's office to provide information about paying property taxes and challenging the tax value of homes. They also address predatory borrowing and how such loans set people up for failure.

Having a presenter from the tax assessor's office makes the process more tangible and gives people a familiar face to approach if they have any questions or problems in the future.

#### Does Proyecto Azteca service the loans?

The loans are held in portfolio and serviced by Proyecto Azteca and ACLF. As a result, there is significant flexibility in dealing with post-purchase problems. For loans over 180 days late, they work with the borrower to help remedy the financial crisis that caused the delay. They will provide emergency loans, restructure loans, and alter the maturity date on loans if necessary to get the borrower back on track.

#### Why is the program a success?

The program is not about money, but about people. It recognizes that there is a "basic needs" threshold that people must be able to meet before they can cover other expenditures. The program demonstrates that even the lowest income borrowers can and will make payments if the loan product is structured correctly and risk is managed, not through credit evaluations, but through relationships.

Through the Self-Help New Construction Program, Proyecto Azteca has been able to make their borrowers feel that they can have a future and that middle class life is within their reach. "I don't want people to go through the housing program and still feel that they are poor. We help people to see the world in a different way," commented the program director.

Although Proyecto Azteca is not a profit driven initiative, there is mainstream potential for the product offerings and for the borrowers. Predatory lenders have met financial success in serving low-income markets. Through collaboration among non-profits, the government, and financial institutions, the Proyecto Azteca model could serve as a template for an alternative that helps build low-income communities rather than drain already scarce resources.



# **El Paso Affordable Housing Credit Union Service Organization**

*El Paso, Texas*

## **Affordable Housing Program<sup>44</sup>**

### Background

The El Paso Affordable Housing Credit Union Service Organization (CUSO) was launched in January 2002 and began closing home mortgage loans five months later. The CUSO was launched collaboratively by eight credit unions in the El Paso area. It was originally intended to provide an affordable loan option to people who could not fit into conventional loans—and to get them out of the subprime market. It has since expanded its mission to include community financial education. The two CUSO missions fit well together. Families often require financial education and counseling to establish or clean up their credit and help them learn to better manage their finances in order to qualify for loans with better terms and rates than the subprime market.

The CUSO developed its own financial education curriculum in both English and Spanish and works through local government, non-profit housing, and social service organizations to deliver the classes. “We have a financial education program with tools to empower people,” commented the program director. The primary reason people attend the classes is because they want to buy a home. Currently, the CUSO provides financial education to 1,500 adults and youth per year. The U.S. Department of Housing and Urban Development and the National Credit Union Foundation provide funding for the financial education classes, counseling, and for the operations of the CUSO. The CUSO is currently looking for ways to become self-sustaining and is trying to develop a portfolio of loans large enough to subsidize operating costs.

Community partners are central to the CUSO’s strategy to maximize their capacity and provide the greatest benefit to the community. They conduct program outreach through their community partners and serve more than 1,500 people every year. They have access to a \$5 million line of credit for mortgage loans from the local credit unions and leverage that in combination with funds from other programs in El Paso. They generally target families at 50 to 80 percent of local median income, or earning \$15,000 to \$30,000 annually. The CUSO’s goal is to create a loan that is workable for a family with major financial limitations.

Because of the CUSO’s ties to local credit unions, they are able to help people access conventional banking services in addition to home mortgage loans. If they see a family that can take advantage of any conventional credit union product, they refer them to a local credit union. Under a First Accounts Grant from U.S. Department of Treasury, the CUSO worked with local credit unions to open 3,600 new accounts over a two-year

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<sup>44</sup> Interview with Larry Garcia, Director of El Paso Affordable Housing Credit Union Service Organization, May 12, 2005.

period for low-income adults. They also have opened 4,000 youth accounts. Most of these accounts are still open. They also help people with short-term debt. For example, one CUSO client had a two-year loan from a finance company at an 85 percent interest rate. A local credit union was able to refinance the loan at a much lower rate, saving the client hundreds of dollars. Eighty-eight percent of CUSO clients have high cost loans with annual percentage rates averaging 85 percent. The clients, after being assessed, are referred to credit unions, and many of the high interest rate loans are refinanced at significantly lower rates.

### **El Paso CUSO Affordable Housing Program: A Snapshot**

Year of Program Inception and Number of Loans	Began in June 2002. Currently 100 loans—mix of portfolio and loans sold to Fannie Mae.
Target Customers	50 to 80 percent of local median income, or \$15,000 to \$30,000 annual earnings
Average Loan Size	\$40,000 to \$50,000
Loan Type	20- and 30-year fixed rate loan
Down Payment	1 to 2 percent; 5 percent for lease-purchase
Interest Rate	3.75 to 7.5 percent
Fees	Attempts to use down payment assistance programs to cover closing costs and fees.
Debt-to-income ratio	45 percent total preferred; will go as high as 50 percent if loan payment close to rent.
Credit Evaluation	Assesses alternative credit. Looks for two years of rental history and three credit letters. Emphasis on strong rental payment history and stable employment.
Loan Performance	One family unable to make payments; two loans over 30 days late.
Financial Education	Required to attend the CUSO's free 10-hour (two hours per day) class series.
Profitability	Not currently profitable, but potential to become self-sustaining.

The CUSO also runs free tax preparation sites and has prepared 250 tax returns for a total refund amount of \$500,000. They encourage people to save their refunds in an Individual Development Account (IDA) to use towards a mortgage loan. Savings in an IDA is not used to assess eligibility for public benefits, thereby alleviating fears that saving for a home will jeopardize assistance in meeting other basic needs.

### What is the Affordable Housing Program?

The El Paso CUSO works with a number of different local affordable housing initiatives to combine resources to issue home mortgage loans. They worked with Fannie Mae to create three approved pilot programs and so are able to sell most loans on the secondary market. The pilot programs support projects in Sparks, San Elizario, and Tornillo colonias. Since June 2002, the CUSO has made a total of 100 loans worth \$6 million under different programs.

El Paso CUSO will lend to families where one spouse is undocumented, but the loan can only be in the name of the documented spouse and can only be based on the documented person's income. The loan term is usually between 20 and 30 years with a fixed rate. Most rates are market, although the lease-purchase program has a higher rate. The rates range from 3.75 percent to 7.5 percent.

One loan program is carried out in partnership with the local Empowerment Zone to develop housing in blighted areas of El Paso to help revitalize the economy. By pooling their capital resources with the Empowerment Zone, the CUSO was able to create a loan program that provides two 10-year loans each at 7.5 percent interest. The first lien amortizes for the first 10 years, and the second lien amortizes for the second 10 years, creating in effect a 20-year loan at 3.75 percent interest. The loan requires a 1 to 2 percent down payment.

Working with the Empowerment Zone, the U.S. Department of Housing and Urban Development, and the University of Texas at El Paso, the CUSO launched a program in the Tornillo colonia to convert contract-for-deed property purchase agreements to conventional home mortgage loans and to replace existing homes, usually mobile homes, with new construction. The CUSO received a grant to provide financial education, buy out the contract for deed, and get a warranty deed to cover closing costs on the refinance loan and to demolish the old home after the new one is built. The new homes are energy efficient, have up to four bedrooms, and cost \$53,000 for a maximum 1,400 square feet.

In the San Elizario and Sparks colonias, El Paso CUSO works with people who already own their lots. The CUSO originates home mortgage loans for housing constructed by community college students studying home construction. The homes cost \$43,000 to build. El Paso CUSO also provides financial education to program participants and negotiated a pilot program with Fannie Mae to sell the loans on the secondary market.

### How have the loans performed?

To date, El Paso CUSO has not foreclosed on any properties, although one foreclosure is likely. Only two borrowers have been more than 30 days delinquent on their loan.

An important part of their success is responding quickly to late payments. The CUSO collects payments on all their loans. If a loan is five or 10 days late, they reach out to the

borrower to see if there is a problem. The program director emphasized that “a hands-on approach is important for the first two years.”

What are the underwriting criteria for the loans?

El Paso CUSO looks primarily for job stability and a good rental history. They require verification of a two-year rental history. There must be zero late payments over 30 days in the last 12 months, and they accept one late payment in the last 24 months. In verifying employment, they look for one year of employment with the same employer, but will also accept a history of consistent employment in the same profession. They also require three lines of alternative credit and do not consider credit scores.

The CUSO gives strong consideration to undocumented income and counts the Earned Income Tax Credit over the prior two years as supplemental income. The program accepts gifts and unseasoned savings to go towards the down payment.

In the pilot loan programs with Fannie Mae, borrowers are allowed a variance for \$3,000 in unpaid medical collections and up to \$1,200 in non-medical unpaid collections, such as loans from pay day lenders or finance companies. The rationale behind these variances is that most low-income working families cannot afford health insurance. Most of the low-income families had unpaid medical bills, and those delinquencies were keeping them from qualifying for prime loans. The CUSO does not require repayment plans on the medical delinquencies at closing, but prefers it. They do require repayment plans on the non-medical debt and count that as part of the debt-to-income ratio.

For revolving credit, the CUSO will accept two 30-day late payments in the last 12 months and no more than five 30-day late payments in the last 24 months. For non-traditional credit, there must be at least a one-year history and no late payments in the last 12 months.

The program permits a total debt-to-income ratio of 45 percent, but will go as high as 50 percent if there is a history of payments to support that ratio or if the household has disability income. The loan-to-value ratio on the first lien is 80 percent, but often rises to 100 percent with a soft second lien.

The program works to minimize closing costs by covering them with down payment assistance funds. All borrowers must provide at least some of their own funding for the purchase. Most programs require a 1 to 2 percent payment. The lease-purchase program requires a 5 percent payment. Private mortgage insurance is required on some of the loans with a loan-to-value ratio greater than 80 percent.

Financial education is required as part of the lending process. Potential borrowers must attend a course that lasts two hours per day for five days. The CUSO provides the classes at no cost and uses a curriculum created in-house.

### Does the CUSO service the loans?

The CUSO services the portfolio loans that they hold. The loans sold to Fannie Mae are serviced by partner credit unions. In order to ensure that borrowers are making their payments, the CUSO collects all payments and intervenes if a payment is five to 10 days late. All payments are made with a check or money order.

If an emergency arises and a borrower cannot pay, the CUSO will arrange a small loan with a one- to two-year payment period to help the family through a 30- to 60-day period.

The program does not offer customized payment schedules to accommodate seasonal work. Their goal is to teach the borrower to be a disciplined spender and to manage finances within the established system.

### How is the program a success?

The greatest success of the program has been the CUSO's capacity to provide financial education to so many people. People call the CUSO to take financial education classes. Greater participation in formal financial institutions is an outgrowth of this emphasis on education.

## **STRATEGIES FOR LAUNCHING AFFORDABLE LENDING PROGRAMS**

The programs profiled in the previous section demonstrate that it is possible to lend successfully and profitably to immigrant and other low-income communities. Texas financial institutions, both large and small, have found innovative ways to provide positive alternatives to predatory subprime loans, rent-to-own arrangements, and contract-for-deed purchases.

The programs profiled in this report have issued a combined 2,600 loans, most of them in the last two to five years. While there are other programs serving this market, this customer base is largely untapped. Even if there were 800 programs with a loan volume similar to those profiled here, they could not meet the demand created by the 2.5 million Latin American immigrants and 3.3 million lower income households in Texas.

### Meeting the Market Need

Texas financial institutions can increase affordable lending in their communities through a variety of approaches. Although banks have the added incentive of obtaining a positive Community Reinvestment Act (CRA) rating for serving the low- and moderate-income families, such lending does not have to be a charitable venture. When considering launching or expanding an affordable home mortgage lending program, there are five steps that are helpful for financial institutions to consider:

1. Define the specific needs in your community.
2. Determine your capacity to meet those needs.
3. Develop the necessary partnerships to reach the target community.
4. Develop your lending paradigm with community partners.
5. Launch the program.

These steps serve as a guide to meeting lending needs in immigrant or other low-income communities. The process is fluid, and new opportunities or needs may arise that necessitate changing an approach or lending paradigm.

### Define the specific needs in your community.

There are many ways to approach defining community needs. CDC Brownsville noticed a trend of people coming to a financial institution and being unable to qualify for the available loan products. TexasBank saw unmet need when they were approached by a realtor who was serving an immigrant community that did not have access to formal loans. In the case of the San Antonio Federal Credit Union, their work with a local

Catholic church serving lower income families inspired focus groups to further hone in on unmet needs. Jefferson Bank assessed their market base and realized that there were communities around their branch locations that were not being served by existing bank products. It is important to determine if the need for affordable home mortgage loans is based solely in a lack of access to credit or if it also includes a lack of affordable housing stock.

#### Determine your capacity to meet those needs.

Once needs are defined, it is important to assess capacity in meeting them. Financial institutions can develop their own lending programs, partner with a non-profit organization, or subsidize the work of a local housing initiative.

If there is a lack of affordable, well-constructed low-income housing, the lender can consider partnering with a reputable homebuilder, a for-profit version of the San Antonio Federal Credit Union or CDC Brownsville programs. Also, a large number of recent Latin American immigrants work in construction and are good candidates for self-help housing programs or for purchase of low-cost houses in need of repair.

#### Develop the necessary partnerships to reach the target community.

It is helpful for lenders to partner with organizations or individuals who have the trust of the target community. Depending on how the lending program is structured, financial institutions may want to partner with religious organizations, community-based direct service agencies, housing authorities, community development corporations, reputable realtors, or immigrant hometown associations. These partners are also valuable in connecting lenders with local down payment assistance programs and in helping develop a program that meets community needs.

#### Develop your lending paradigm with community partners.

With the community needs, approach, and partners defined, the next step is to develop program specifics. For new loan programs, it is important that the credit assessments and the loan terms be in line with community capacity and meet viable lending standards. The profiled programs provide helpful templates for lending to recent immigrant and low-income communities. Financial education, alternative credit assessments, and an ongoing relationship with borrowers should be a part of any new home mortgage lending program. There should also be options for intervention after the loan is made to help families retain their homes through short-term financial difficulties.

Most of the profiled programs discount medical debt in the credit assessment process and accept a low number of delinquencies. The most important credit indicators for the programs are a solid rental history and job stability. A final consistent characteristic of

the loan programs is that each program evaluates borrowers individually, assessing personal circumstances as opposed to fitting each borrower into a tightly set template.

### Launch the program.

The previous four steps should provide a solid basis from which to launch an affordable housing lending initiative or to participate in an existing community program.

There is a great need in Texas for expanded access to fairly priced home mortgage loans. The fast-growing Latin American immigrant market is one that is particularly underserved, although all lower income Texans stand to gain from greater availability of non-predatory credit. The eight programs profiled in this report offer some options for accomplishing this goal.

Studies have shown that home ownership is highly correlated with improved family and economic circumstances.<sup>45</sup> The prevalence of predatory loan products in Texas, both within and outside of the formal lending system, attests to the desire for homeownership among low-income and recent immigrant families and the lack of a sufficient number of affordable options.<sup>46</sup> As the number of fair affordable housing loan programs increases and successful underwriting criteria are established, the hope is that the price of market-based loans will come down—resulting in greater homeownership and stability for low-income families, new profitable markets for Texas financial institutions, and a stronger Texas economy.

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<sup>45</sup> John Harkness and Sandra J. Newman, “Homeownership for the Poor in Distressed Neighborhoods, Does this Make Sense?” *Housing Policy Debate*, Volume 13, Issue 3, Fannie Mae Foundation, 2002.

<sup>46</sup> Six of the top 10 cities nationally for subprime home refinances are located in Texas: El Paso, Corpus Christi, Laredo, Beaumont-Port Arthur, Killeen-Temple, San Antonio, and Galveston-Texas City. Source: Calvin Bradford, “Risk or Race? Racial Disparities in the Subprime Refinance Market,” Center for Community Change, May 2002, p. 28.



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Cindy Baranowski, Senior Vice President, Sales Manager Mortgage Lending, Bank of America, March 30, 2005.  
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Don Currie, Executive Director, CDC Brownsville, March 1, 2005.  
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Larry Garcia, Director of El Paso Affordable Housing Credit Union Service Organization, May 12, 2005.  
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Yaisa Johnson, Manager of the ACORN Partnership with Bank of America, Consumer Real Estate Regional Marketing Director, Bank of America, June 10, 2005.  
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Jack Mooney, Senior Mortgage Officer, First National Bank, June 2, 2005.  
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Mary Sanchez, Vice President, Home Owners Advantage Program, Jefferson State Bank, May 23, 2005.  
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Chuck Smith, First Vice President, Director of Lending, San Antonio Federal Credit Union, June 20 and 21, 2005.  
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Dianna Treviño, First National Bank, April 8, 2005.  
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## **APPENDIX**

### **HOME MORTGAGE LENDING TO FOREIGN NATIONALS:**

#### **A SUMMARY OF REGULATORY ISSUES**

## **HOME MORTGAGE LENDING TO FOREIGN NATIONALS: A SUMMARY OF REGULATORY ISSUES<sup>47</sup>**

There are myriad regulations affecting home mortgage lending practices generally. There are several regulatory issues, however, that are unique to lending to both permanent and non-permanent resident aliens. These are addressed in the following:

- the Customer Identification Program (CIP) rules required under Section 326 of the USA Patriot Act;
- the examination guidelines used by federal financial institution regulators to evaluate the credit quality of mortgage loans; and
- the Community Reinvestment Act (CRA) requiring financial institutions to meet the credit needs of the communities they serve.

This summary will also address Suspicious Activity Reporting under the Bank Secrecy Act as well as the recently enacted Real ID Act of 2005.

### CIP Rules—Home Mortgage Lending to Foreign Nationals<sup>48</sup>

The CIP rules are issued jointly by the regulatory agencies supervising federally insured depository institutions. They broadly require that institutions implement procedures to verify the identity of persons and entities opening accounts or obtaining loans at banks, savings associations, credit unions, private banks, and trust companies. These rules are intended to prevent activities associated with money laundering and the financing of terrorism.

Compliance with these rules has been required since October 1, 2003, and the broad features of these rules are by now well understood by financial institutions. There are, however, several aspects that may not be fully understood in the context of home mortgage lending to foreign nationals. Some of the important considerations in this area are addressed below.

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<sup>47</sup> This information is provided as a matter of public service for informational use, but it does not constitute legal advice and should not be used as such. Financial institutions are strongly urged to confer with regulatory counsel in evaluating these issues.

<sup>48</sup> The CIP rules can be found at 31 CFR §103.121. Additional information can be found in the publication, *Interagency Interpretive Guidance on Section 326 of the USA Patriot Act*, April 28, 2005, [http://www.ffiec.gov/bsa\\_aml\\_infobase/documents/BSA\\_AML\\_FAQ.pdf](http://www.ffiec.gov/bsa_aml_infobase/documents/BSA_AML_FAQ.pdf).

*What are the rules for existing vs. new customers?*

In many cases, a home mortgage loan applicant may already have an existing relationship with an institution. In these cases, the CIP identification rules require only that the institution have a reasonable belief about the identity of its customer. However, an existing relationship must meet the definition of an “account,” and occasional services provided to an applicant—such as check cashing, money order purchases and wire transfers—alone do not meet that definition. More formal banking relationships—such as a checking account, savings account, loan account, as well as providing a safety deposit box or custodial or trust services—will qualify the loan applicant as an existing customer.

*What are the timing considerations for complying with the rules?*

The CIP rules do not apply until a loan applicant establishes an account. In the case of mortgage loans, an account is not established until the loan application is accepted and approved, or when the financial institution enters into an enforceable agreement to provide a loan to the applicant. In this context, undocumented foreign nationals may be particularly intimidated by the loan application process if they are asked to provide identification information required by the CIP rules at the inception of the loan application stage. Institutions can help overcome this problem by requesting CIP information only after a loan application is accepted and approved, and then working with their new customer to develop the kind of documentation and information required by the institution’s CIP policies.

*What are the rules for U.S. vs. Non-U.S. Persons?*

The CIP rules require financial institutions to determine whether the applicant is a U.S. citizen, but it is important to remember that this requirement is *solely* for the purpose of determining the type of information that may be required from the applicant. This requirement is not intended to identify the nationality or lawful U.S. residency status of applicants who are not U.S. citizens. In fact, under the CIP rules, institutions have a broader range of choices as to the type of information they may accept from non-U.S. persons, including an Individual Taxpayer Identification Number (ITIN) issued by the Internal Revenue Service to foreign nationals for tax paying purposes, passport number and country of issuance, alien identification card number, or a foreign government-issued document—such as the *matricula consular* card—evidencing nationality *or* residence and bearing a photograph or similar safeguard. The *matricula consular* card is issued by Mexican consular offices in the U.S. In addition, if the applicant has applied for an ITIN (by filing IRS Form W-7) but has not yet received it, the financial institution may accept documentation indicating that the W-7 has been filed. In any event, the CIP rules are not intended, nor should they be used, to discriminate against any foreign national, regardless of residency or other immigration status in the U.S.

*What other sources of identification can be used?*

The CIP rules permit an institution to accept “non-documentary sources of identification.” These include verification of information through credit bureaus, public databases, and utility bills as well as through employment records. These sources of information may be particularly useful and appropriate when an applicant is unable to provide more formal identification at the time the “account” is established. If the financial institution identifies any discrepancy in information supplied from any source, the CIP rules allow the institution a reasonable period of time to resolve it.

*How flexible are these rules?*

The CIP rules are intended to give financial institutions flexibility in how they identify their customers. The institution can tailor its approach to fit the institution’s size, location, and type of business. A “one size fits all” policy is neither required nor intended. Institutions interested in serving immigrant communities can include provisions in their CIP policy that allow them to accept ITINs and *matricula consular* cards, delay the completion of CIP documentation until after loan approval, and help applicants complete a W-7 or obtain a *matricula consular* card.

#### Community Reinvestment Act (CRA)<sup>49</sup>

The CRA imposes a general requirement upon financial institutions to serve the banking needs of low- and moderate-income communities in their service areas. The CRA is important in this context because it conditions certain types of regulatory approvals upon a CRA rating that is at least “Satisfactory.” Thus, the regulatory approval required to open a new branch, acquire another institution, or engage in new banking activity may be denied institutions that have not demonstrated sufficient compliance with the CRA’s principles. This is particularly true in the mortgage lending area, because it comprises an important part of the composite CRA rating an institution receives. Institutions may improve their CRA rating by making home mortgages available to low- to moderate-income immigrant communities.

#### The Bank Secrecy Act—Suspicious Activity Reporting<sup>50</sup>

*Do violations related to immigration status require Suspicious Activity Reporting (SAR)?*

The SAR rules have their origins in the provisions of the Bank Secrecy Act and were created almost 10 years ago by the Financial Crimes Enforcement Network, or FinCEN.

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<sup>49</sup> Information on the new CRA rules can be found at

<http://www.federalreserve.gov/boarddocs/press/bcreg/2005/20050719/default.htm>

<sup>50</sup> Additional information can be found in the June 2005 report of the Federal Financial Institutions Examination Council, *Bank Secrecy Act Anti-Money Laundering Examination Manual*,

[http://www.ffiiec.gov/bsa\\_aml\\_infobase/documents/BSA\\_AML\\_Man.pdf](http://www.ffiiec.gov/bsa_aml_infobase/documents/BSA_AML_Man.pdf).

In general, these rules require a financial institution to submit a SAR when it suspects a violation of federal law in a transaction involving minimum specified sums.

Although the SAR requirements technically are not part of the CIP rules, the SAR rules are mentioned briefly in this context because of recent reports of uncertainty about whether an institution is required to submit a SAR upon discovery of a lawful banking transaction involving a person suspected of residing in the U.S. illegally. There is currently no specific official guidance on this point from the regulators, however, the informal consensus among the regulators at this point is that the unlawful residency status of an institution's customer or applicant, *by itself*, is not within the scope of unlawful activity intended to be detected under the SAR rules, and no SAR submission is necessary under such circumstances.

### Loan Examination Requirements

Institutions should be concerned about the guidelines the examiners will use in reviewing loans to foreign nationals. Having (i) successfully qualified the credit worthiness of a new customer; (ii) obtained all of the information required to document compliance with the institution's CIP policy; and (iii) closed and funded the new mortgage loan, the financial institution will not want to see the loan adversely classified as a result of issues related to the borrower's immigration or U.S. residency status.

*What are the federal examination guidelines regarding loans to foreign nationals?*

The current loan examination guidelines used by federal regulators make no distinction between home loans made to U.S. citizens and those made to foreign nationals. In the context of determining credit quality of a home loan or compliance with lending regulations, the citizenship, nationality or immigration status of borrowers is not considered relevant. Accordingly, home loans to foreign nationals are examined in the same manner and on the same basis as home loans to U.S. citizens. The examiners will be concerned about the institution's compliance with the CIP rules discussed above, but these concerns will be addressed through a separate CIP compliance examination. The examinations discussed in this section relate to loan examinations only.

*Are there special documentation requirements for these loans?*

Home loans to foreign nationals often will involve a "layered" underwriting process by the lending institution, requiring documentation of the borrower's available funds from multiple non-traditional sources, including the borrowers' family members, employers, community housing programs, and local government housing authorities, as well as "soft" second mortgages for down payments. In such cases, the underwriting process must be performed manually, as the documentation requirements for these loans are not compatible with typical automated loan underwriting software applications. Because of the increased volume and complexity of the documentation required for these loans, there



is greater opportunity for human error and greater care must be taken to avoid adverse classification of the loan—not because of any underlying credit risk—but simply on the grounds of inadequate or incomplete loan documentation.

*Is there a secondary market for these loans?*

There is currently no widespread secondary market for ITIN loans. The principal secondary market providers, Fannie Mae and Freddie Mac, as a practical matter, currently do not accept ITIN loans, unless the borrower can produce a visa permit or other proof of lawful immigration status. Fannie Mae does offer several programs intended to serve non-U.S. citizens, provided that borrowers can demonstrate their lawful residency status.

Some lenders have set aside a portion of their resources to provide ITIN loans on a portfolio basis, where the originating institution continues to hold the mortgage; there are also a few special local and regional programs that provide limited resources for the purchase of ITIN loans. Freddie Mac is reportedly reviewing its current policies in this regard and possibly may provide some liquidity for ITIN loans in the future. However, institutions originating ITIN loans in the current market generally expect to hold them indefinitely.

*Is mortgage insurance available for these loans?*

Although HUD and FHA do not currently insure mortgage loans to borrowers who cannot demonstrate lawful residency status, Mortgage Guaranty Insurance Corporation (MGIC), a private mortgage insurer, has been pursuing this market aggressively with its new Building A Life In America program. Under this program, MGIC employs non-traditional credit underwriting guidelines tailored to the circumstances of immigrants. This program is aimed specifically at ITIN loans and may significantly reduce the credit risk aspect of ITIN lending for financial institutions and the risk of adverse regulatory classification of these credits.

*What are the important points to remember about examination issues?*

Although the federal regulators' loan examination guidelines do not intend to distinguish generally between mortgage loans made to U.S. citizens and those made to foreign nationals—regardless of immigration status—loans made to foreign nationals still may present special loan examination issues. The relative complexity of the underwriting and documentation required for these loans, together with the current general lack of a widespread secondary market for ITIN loans, means that institutions should take special care in this area of lending to avoid an inadvertent adverse classification of these credits.

## The Real ID Act of 2005<sup>51</sup>

### *What is the impact of the Real ID Act of 2005?*

The recently enacted Real ID Act of 2005 will become effective in 2008 and imposes sweeping new uniform standards for states as to the kinds of identification required in issuing driver's licenses and identification cards. This law will generally deny a driver's license or identity card to persons who cannot produce documentation evidencing lawful residency in the U.S. The law prohibits federal agencies from accepting non-complying forms of identification. Persons who lack the required identification may be prohibited, for example, from entering federal buildings or boarding commercial aircraft. States may issue special driver's licenses to those who cannot demonstrate lawful U.S. residency. The new law does not mandate that financial institutions require a prospective customer to produce one of these new driver's licenses or identity cards when conducting banking business.

### Other Policy Considerations

#### *What immigrant reform legislation is being proposed?*

New immigration reform legislation, currently under discussion, has the potential to dramatically affect the immigration status of millions of immigrants in the U.S. While this topic has been discussed only in general terms, it appears that key features may involve a grant of conditional amnesty and eligibility for U.S. citizenship for many undocumented immigrants, coupled with a new documented worker program that could allow incoming foreign nationals permission to lawfully work and reside in the U.S. under specified conditions.

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<sup>51</sup> The Real ID Act was signed into law in May of 2005 as part of the Emergency Supplemental Appropriations Act for Defense, the Global War on Terror, and Tsunami Relief, 2005. The text of the Act can be viewed at [http://frwebgate.access.gpo.gov/cgi-bin/getdoc.cgi?dbname=109\\_cong\\_public\\_laws&docid=f:publ013.109](http://frwebgate.access.gpo.gov/cgi-bin/getdoc.cgi?dbname=109_cong_public_laws&docid=f:publ013.109)



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