



June 24, 2008

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U.S.-Backed Mortgage Program Fuels Risks

FHA Struggles To Eliminate Loans For Zero Down


By NICK TIMIRAOS
June 24, 2008; Page A1

Mortgages that allow consumers to put little if any money down when buying a home have largely disappeared as a financing option available from private lenders. But they are still available -- and growing more popular -- through a government-backed program.

That's raising concerns among critics who blame no-money-down mortgages for many of today's housing market woes. And while federal housing officials are moving to end the practice, for now home builders are promoting the programs to move unsold inventory.

"I just smell a massive taxpayer burden coming," says Sen. Christopher Bond (R., Mo.), who calls the programs "too good to be true."

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Risky Business

Down-payment assistance from nonprofit providers has grown in popularity...

Source of down-payment funds for FHA-insured mortgages



But some argue that it increases the risk for early loan delinquency

Default rate on FHA-insured loans in the first two years of ownership, by down-payment source



The offers -- including "100% financing" -- are made possible due to down-payment assistance programs run by nonprofit organizations. These programs are funded largely by home builders and also by private homeowners desperate to sell. The seller-funded

groups provide enough down-payment money to buyers that they can qualify for a mortgage backed by the Federal Housing Administration, which requires at least a 3% down payment.

Supporters of the down-payment programs say they help the FHA fulfill its goal of assisting first-time home buyers. But critics say the programs will burden the government agency, and taxpayers, with bad loans. The FHA, which essentially is filling the void left by the collapse of the subprime market, renewed a push to eliminate the programs this month, after warning that above-average default rates for seller-assisted down-payment programs will force the agency to request a government subsidy for the first time in its 74-year history. The agency says it will need \$1.4 billion next year.

DISCUSS¹

- Experts predict a long battle ahead for opponents of down-payment assistance. Join the discussion on [Developments](#)², WSJ.com's real-estate blog.

The FHA estimates that down payments provided by nonprofit groups account for 34% of all 200,000 loans backed by the FHA so far this year, up from 18% in all of 2003 and less than 2% in 2000. And the agency says that borrowers are two to three times as likely to default on their payments when they receive a down payment from a nonprofit.

D.R. Horton Inc., the nation's largest home builder by volume, is touting "100% financing" for its two- and three-bedroom condominiums near the beach in Maui, Hawaii, which start at \$498,000. In the Seattle area, local builder Quadrant Corp. is advertising townhouses that can be purchased with as little as \$500 down. "Use your coffee budget to move into a new home," says an online promotion. In the St. Louis area, Vantage Homes recently promoted its suburban developments with ads suggesting a new home should be on the list of things to buy for those "looking for something to spend your economic stimulus check on."



Vantage Homes tells prospective homebuyers that they can afford a new house with down payment assistance by cashing in their economic stimulus check.

A flier promoting D.R. Horton's Maui development, for example, says that funds for the down payment would be provided by Nehemiah Corp. of America, the largest private down-payment assistance provider. D.R. Horton, based in Fort Worth, Texas, didn't return calls seeking comment. Scott Syphax, president and chief executive of Nehemiah, a nonprofit organization, said D.R. Horton is one of 95,000 companies and individual home sellers that have participated in the assistance program.

To critics, mortgages with down-payment assistance are similar to no-money-down subprime loans, which have triggered a wave of foreclosures. Most bankers believe defaults are so high because borrowers who encounter financial difficulties are more willing to walk away from a home when they didn't put much of their own money into the purchase.

"The inescapable fact is that seller-funded down-payment assistance is particularly susceptible to losses," says Howard

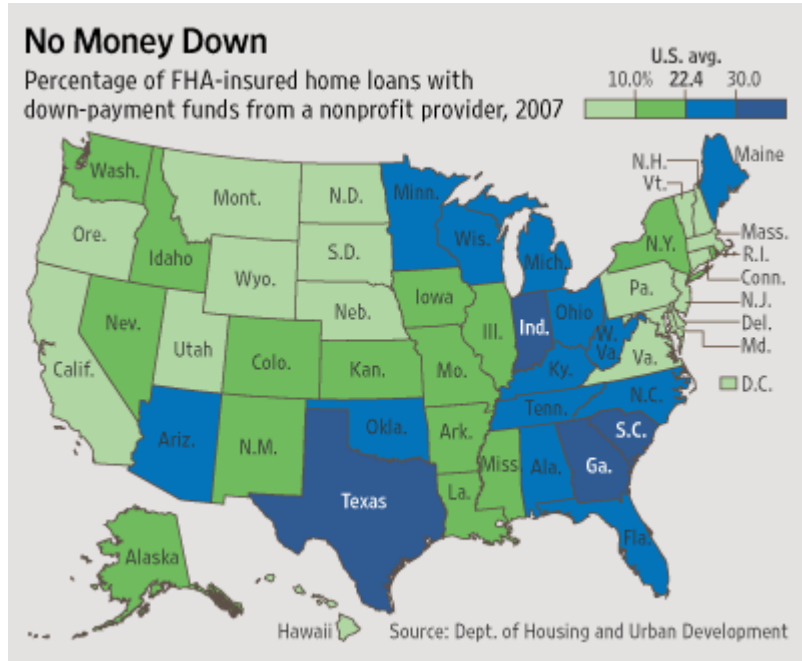
Glaser, a mortgage-industry consultant and former official at the Department of Housing and Urban Development. "Too often today's seller-funded loan is tomorrow's foreclosure."

Stalled Home Sales

Several years ago, during the height of the housing boom, some of the nation's biggest builders curtailed use of seller-funded assistance programs because lenders offered 100% financing, often via their subprime divisions.

But home builders are again embracing the programs because home sales have stalled, the subprime market is largely shut and traditional lenders are requiring large down payments. Under the down-payment assistance programs, a third-party nonprofit provides the money to the buyer and is then reimbursed by the seller. The seller's contribution to the program isn't tax deductible as a charitable contribution. FHA regulations prohibit sellers from providing direct cash gifts to buyers, due to concerns that the value will be added to the price of the home, inflating its value.

Home builders say touting no- or low-money-down financing helps bring in new customers, even if they ultimately choose more conventional financing. "The bottom line...is these promotions work," John F. Eilermann Jr., chief executive of McBride & Son Enterprises Inc., the parent company of Vantage Homes, said in an email. He said the current marketplace demands flexibility, and he credits "creative marketing," such as promotion of its \$500-moves-you-in program, with increasing new home sales in 2007 from the previous year.



Advocates of down-payment assistance say the programs are also good for the broader economy. Nehemiah's Mr. Syphax calls the FHA program an "economic stimulus." Home builders fear that eliminating the programs will cripple sales. "It would chill the market here," says Jeff Johnson, sales manager for Maracay Homes in Phoenix.

Dick Whitmore, a 47-year-old construction superintendent in Phoenix, put up just \$250 to move into a three-bedroom home that he purchased in March for \$189,000. He says the down payment and closing costs, which came to about \$12,000, were paid by the family selling the home via AmeriDream Inc., a down-payment-assistance program based in Gaithersburg, Md. "My wife and I are hardworking people, but to come up with five or six grand, that's next to impossible," he said.

Gloria Harris, a 57-year-old human-resources consultant, says she couldn't have bought her \$216,000 two-bedroom condo in McLean, Va., in January without the \$16,000 contributed by the seller to cover the down payment and closing costs. "I was having a hard time just trying to save because I was spending from week to week trying to live," she says.

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To sell Maui condos, home builder D.R. Horton touts its relationship with Nehemiah Corp., a seller-funded down payment assistance provider.

that eliminating seller-funded down payments would leave borrowers with "options that are more costly and riskier than FHA."

They also reject criticism that they are responsible for the FHA's recent shortfall. "We are a convenient scapegoat," says Mr. Syphax.

Seller-funded groups and supporters in Congress say that such programs should be regulated but not shut down, a proposal that HUD hasn't shown much interest in in recent years. "If there's a problem, let's fix it," says Rep. Gary Miller (R., Calif.), a vocal defender of the program and a former home builder and developer.

In the past, nonprofit groups have consistently outmaneuvered Congress and the regulatory agencies that have tried repeatedly to shut them down, thanks in part to a well-coordinated lobbying effort by a coalition of the nonprofit companies, low-income housing and minority groups and home builders. "I have holes on my shoes from walking around Washington," says Mr. Syphax.

The two sides have a long history of doing battle. Housing officials backed down from a fight in 1999, and earlier this year courts rejected a similar attempt to shut down the program.

The nonprofit groups have the backing of several influential members of Congress, including Reps. Maxine Waters (D., Calif.) and Barney Frank (D., Mass.). The Congressional Black Caucus and the Congressional Hispanic Caucus sent letters this month to House and Senate leaders urging that the programs stay intact, citing their role in improving minority home-ownership rates.

In current versions of the FHA modernization bill, the Senate would eliminate the down-payment programs and a vote on the bill is expected this week; the House version keeps the program in place. Rep. Frank said in an interview that he believed a compromise could be reached with the Senate that would preserve the program but with tougher lending requirements. "No one is talking about leaving it untouched," he says.

To be sure, the overwhelming majority of subprime loans in default are adjustable-rate mortgages. FHA-backed loans, including those with down-payment assistance, are fixed-rate loans with income verification requirements, which have better track records.

Assistance providers say their products helped keep low-income families away from subprime loans that reset to higher rates. The FHA had as recently as 2005 warned

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gets you into
a new home.

Use your coffee budget
to move into a new home

QUADRANT HOMES
5000 moves you in
Lower interest rates
Choose your glass, bread and freshies

In Washington state, Quadrant Homes' Web address, www.500movein.com³, spells out its promotion for little money down on new homes.

Write to Nick Timiraos at nick.timiraos@wsj.com⁴

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<http://online.wsj.com/article/SB121426681678998589.html>

Hyperlinks in this Article:

- (1) <http://blogs.wsj.com/developments/2008/06/24/long-battle-ahead-for-opponents-of-down-payment-assistance-programs/>
- (2) <http://blogs.wsj.com/developments/2008/06/24/long-battle-ahead-for-opponents-of-down-payment-assistance-programs/>
- (3) <http://www.500movein.com>
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