

Montana Board of Housing
Homeownership: Encouraging New Production

Habitat for Humanity Special Financing Program

Description of the Program: From September of 1997 through June of 2009, the Montana Board of Housing had a partnership with local Habitat for Humanity Chapters in Montana to finance first mortgage loans for new Habitat homebuyers at a 0% interest rate. Over the years, the program financed 74 homes with eight Habitat Chapters around the state. These homes went to homeowners below 60% of median income, a target group that MBOH cannot reach with its regular financing programs, especially in urban areas. Selling these loans to MBOH allowed the local Habitat chapters to recoup the construction costs of the homes immediately rather than receive payment over the life of the 30-year mortgage. With cash in hand, Habitat Chapters were able to turn around and build another home for another Habitat family, thereby increasing the numbers of families they were able to serve.

However, as the impact of the housing collapse began to affect state housing finance agencies, MBOH realized that it could not continue to offer 0% financing for any program, no matter how effective in reaching lower income households. As a whole loan state that does not service its own loans, MBOH needed a loan product that would come from the originator looking like a standard MBOH loan bearing an interest rate of 2%.

MBOH advisors suggested a loan arrangement in which the MBOH first mortgage loan at 2% would be complemented by a Habitat "wrap around" second mortgage loan at 0%, the principal amortization on which is deferred and forgiven to the extent the MBOH loan principal payments are timely made. The total principal amount of the two loans would be the amount that the borrower would have borrowed from Habitat directly at 0% if Habitat had kept the loan in its portfolio. The example that follows illustrates how this would work for a typical Habitat home. Habitat also carries a third mortgage on the home for the difference between the amount the borrower qualified for at 0%, and the full appraised value of the home. The amount of the MBOH loan is always well below 80% LTV, so the MBOH loans do not require mortgage insurance.

This financing mechanism was tried in a pilot program beginning in October of 2009. Thus far, six Habitat Chapters have financed one borrower each with MBOH loans at 2% and Habitat wrap around loans at 0%. The MBOH loans ranged from \$75,000 to \$107,026 on homes with appraisals that ranged from \$145,200 to \$179,000 and served households with incomes from \$16,380 to \$30,690.

Responsiveness to award criteria:

Innovative- This is a new form of financing that generates interest income for MBOH while meeting Habitats needs for cash to invest in another home

Replicable - Other finance agencies that would like to help Habitats but can't afford to do 0% loans can use the same financing mechanism, assuming they can do loans under 80% LTV without mortgage insurance and can accept interest earnings on the loan in the 2-2.5% range

Respond to important state housing need – Habitats have found fundraising for new homes to be very difficult in the recession. This allows Habitats to continue to serve under 60% LTV homebuyers at a time when Habitat resources would otherwise be scarce.

Demonstrate measureable benefits to HFA-targeted customers – This program allows MBOH to serve households below 60% median income, particularly in urban areas.

Have a proven track record of success in the marketplace - with six participating Habitat Chapters having each completed one loan, the program has been accepted by lenders and Habitats alike. The Coalition of Habitat Chapters in Montana requested and received approval from MBOH to continue the program when the pilot expired in June of 2010.

Provide benefits that outweigh costs – The benefits of helping Habitat families are well-known; this program allows MBOH to continue the program at cost affordable to MBOH in the post-housing market collapse environment.

Demonstrate effective use of resources – MBOH has recycled bond funds that it is using for this program and will be getting a higher interest rate on these loans in the short term than it can get by investing the funds; Habitats receive, in effect, the present value of the income they would have received over time from mortgage payments, allowing them to reinvest immediately in a new home for another Habitat family

Effectively employ partnerships – MBOH valued its partnership with Habitats, and Habitats valued their long-standing partnership with MBOH. This program allows that partnership to continue in another form that is in keeping with the more stressful economic times.

Example: MBOH Loan for Habitat Borrower at 2% with Habitat Wrap-Around Loan at 0%

Goal: To give the borrower an effective 0% interest rate mortgage amortization payment on the amount they are borrowing to purchase the home from Habitat; to have Habitat receive funds at closing equal to or more than the typical present value of the purchase price if paid over 30 years; to have 2% interest on MBOH loan.

Example: Habitat Sale price of \$125,000 - must be equal to appraisal

Total "cash" loan amount is \$100,000 (If Habitat were keeping the loan to the borrower in the Habitat loan portfolio, this would be the amount of the loan)

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Habitat has lien in 3rd position for \$25,000 difference from the sale price and the “cash” loan Borrower payment at 0% on \$100,000 for principal and interest = \$277.78 a month

Under the MBOH program, the “cash” loan is split into two loans; the first from the Montana Board of Housing and the “wrap around” second from Habitat, as follows:

Mortgage loan in first position from MBOH for \$75,153

This loan has a Note for \$75,153 at 2% for 30 years.

The monthly payment on this Note is \$277.78/ month (same payment as above)

There is no MI on this loan as the LTV using the sale price is 60%

“Wrap-Around” Mortgage loan in second position from Habitat for \$24,847, at 0%

This loan has a Note and has no payments unless the home is sold early or borrower becomes delinquent on the MBOH first. Amortization is calculated as the difference

between \$100,000 at 0% and \$75,153 at 2% for each monthly payment. See Visual Aid:

Summary of Habitat Wrap-Around 2nd Amortization

MBOH purchases the first mortgage for \$75,153. The borrower’s payment of \$277.78 goes through the servicer to MBOH every month. From MBOH’s and lender perspective, the loan is no different than any other MBOH loan, just with a lower interest rate.

Habitat has Note on its Wrap-around second that is tied to the MBOH first, and a Trust Indenture as a second lien. Habitat receives: \$75,153 of cash up front to do more homes; a silent second lien of \$24,847 at 0% that will allow Habitat to recoup some portion of the \$24,847 should the borrower sell the house and pay off the loan early; and a silent 3rd lien for the top \$25,000 of the purchase price that is forgiven over time, at 0% with no payments.

From the borrower’s perspective, they are paying \$277.78 on \$100,000. If they were to sell the house in year 10, how do MBOH and Habitat reconcile the amount of principal left with the borrower’s expectations? At 0% after 120 payments, the principal balance on a loan of \$100,000 would be \$66,667. However, on a \$75,153 loan at 2%, after 120 payments the principal balance would be just \$54,909. The borrower pays the \$66,667, of which \$54,909 goes to MBOH and the difference of \$11,756 goes to Habitat.

The Visual Aid shows a summary of the amortization schedule for this example Habitat Wrap-Around Loan, as well as the first 17 payments. The payment on \$100,000 at 0% is \$277.78. This payment actually goes to the MBOH loan, and determines the principal amount of MBOH loan by entering the \$277.78 payment at an interest rate of 2% into an amortization calculator, then solving for principal. In this case, the principal amount of the MBOH loan is \$75,153. The balance on the Habitat loan is the difference between the \$100,000 at 0%, and the MBOH loan of \$75,153 at 2%. Amortization of the Habitat loan is the difference between the amortized declining balances of the \$100,000 and MBOH loan over time.