

## **2009 NCSHA Annual Awards for Program Excellence**

Category: Homeownership: Empowering New Buyers  
HFA: Nebraska Investment Finance Authority (NIFA)  
Program: Advanced Buyer Credit (ABC) Loan Program

### **NIFA's ABC Loan Program: The Sweet Ingredient in Monetizing the Federal First-Time Homebuyer Tax Credit**

#### **The Problem**

In a tricky financial market with complicated lender restrictions, how does an HFA create a Homebuyer Tax Credit Monetization loan that does not penalize the borrower with higher interest rates...and does not significantly increase risk to the lender?

#### **Introduction**

Imagine you are sitting down to enjoy a slice of warm apple pie. Your mouth waters as you take your first bite, and then your face turns sour as you realize someone forgot to add the sugar! The delicious aroma, flaky crust and juicy apples are there but the key ingredient, sugar, is missing, making all the difference in the world!

In Nebraska our available housing stock, a basic component of this market, is large and home prices have firmed. Rates are at historic lows. The Federal First-Time Homebuyer Tax Credit (Federal Tax Credit) is exciting new buyers.

But while all of the pieces seem to be in place, borrowers continue to struggle with a key element to the purchase of their first home – money down at closing. So what is the missing ingredient needed to sweeten the rest? A monetization of the Federal Tax Credit!

#### **The Lead-Up**

In reality, the Federal Tax Credit does not put money in the buyer's pocket at closing to assist in the purchase of a home. The availability of a cash refund eight to ten weeks after closing, or even longer, does little to fill the funding gap buyers face without the availability of 100% financing products. This challenge keeps many would-be homebuyers out of the ownership market and exacerbates the problem of stagnant home sales.

NIFA immediately realized the need to develop a loan product to monetize this credit, but we also knew a prudent approach in developing the program would ensure the best benefits to our low and moderate income borrowers. In designing this new program, the challenge was to minimize potential losses to NIFA on a temporary second mortgage loan structure, but not penalize the borrower with an increase in payments or interest rate for 30 years on a tax credit monetization loan.

With a unique "step-down" mortgage in mind, NIFA staff and its legal team contacted the Federal Housing Administration (FHA) to explain the new concept and receive assurance that the "step-down" ABC Loan Program would be eligible for FHA insurance. FHA was a catalyst for the program by quickly providing NIFA with the guidance and approval it needed to move forward.

US Bank, the master servicer for the NIFA single family program also quickly rose to the challenge by modifying servicing structures for the ABC Loan Program. The US Bank team members were

encouraging and constructive partners as we wound our way through the complex parameters of the new program.

With the aid of these key partners, NIFA was able to rollout a new, one-of-a-kind program on June 5<sup>th</sup>, 2009 offering borrowers a non-punitive second mortgage loan product in anticipation of the receipt of their Federal Tax Credit.

The ABC program provides the missing ingredient – cash at closing.

### **The ABC Program**

With the Advanced Buyer Credit (ABC) Loan Program, NIFA provides both a first and second mortgage loan. The second mortgage loan, in an amount up to 8.5% of the purchase price of a single-family residence (not to exceed \$6,800), is available to assist the homebuyer with down payment and closing costs. This second mortgage loan, a monetization of the Federal Tax Credit, has been designed with the expectation that the homebuyer will repay the second mortgage loan upon receipt of the cash payment of the Federal Tax Credit. **If the second mortgage loan is, in fact, repaid within 120 days of loan closing, the interest rate on the first mortgage will step-down (be reduced) by one-half percent.**

This “step-down” feature offers an extraordinary benefit to our borrowers. Rather than penalizing a borrower for accessing their Federal Tax Credit, the step-down rate structure provides positive economic incentive to the borrower to **payoff** the ABC second mortgage upon receipt of their Federal Tax Credit. When they do so, the interest rate on their first mortgage loan is reduced, **decreasing the borrower’s monthly mortgage payment and saving them thousands of dollars of interest over the life of their mortgage!**

NIFA decided to take a “no-harm” approach in the development of the ABC loan product. At origination, the second mortgage loan interest rate is set at the same rate as the first mortgage loan. If the second mortgage loan is not repaid in full within 120 days after loan closing (we anticipate from proceeds of the Federal Tax Credit), the borrower’s combined monthly payment (on the first and the second loans) continues on in the same amount. The portion of the monthly payment allocated to the second mortgage loan repays NIFA in full after ten years.

Thus the goals of the ABC program were achieved. ABC provides benefits to the borrower and encourages repayment of the monetization loan. The buyer receives the needed funds at closing to assist in purchasing their first home, and the borrower is positively incented to use the cash from the Treasury to payoff the second loan. There is increased equity in the home and their interest rate is reduced. **This is good for the homebuyer and NIFA.** The early payoff of the second mortgage loan returns to NIFA our General Operating Fund moneys used to make the loan.

### **Rationale**

With the financial savings to be realized by the homebuyer, the homebuyer is positively incented to pay the ABC second mortgage loan once funds from the Federal Tax Credit are received. But the option to pay, or not pay, the second mortgage remains with the borrower. Our belief is that the “step-down” rate structure and a lower monthly mortgage payment will encourage most homebuyers to elect an early payoff to take advantage of this positive financial reward.

To encourage **responsible borrowing**, all buyers must have a minimum investment of \$1,000 and must complete a homebuyer education course prior to closing. NIFA will also follow up with each homebuyer to encourage the repayment of the second ABC mortgage. A maximum second mortgage amount of up to

8.5% of the purchase price (not to exceed \$6,800) ensures that the borrower will have access to additional capital after closing to pay for any unexpected expenses.

The amount of the rate reduction (½ of 1%) provides a financial incentive to the buyer to pay off the second mortgage without being punitive. The following example illustrates the “step-down” structure of the ABC program:

Initial Borrower Qualification

|  |                 |
|--|-----------------|
| \$100,000 first mortgage P&I @ 6.25% initial rate: | \$615.72        |
| \$6,800 second mortgage P&I @ 6.25%:               | <u>\$ 56.14</u> |
| Borrower’s combined monthly mortgage payment:      | \$671.86        |

When ABC second mortgage is paid with Federal Tax Credit

|  |                             |
|--|-----------------------------|
| \$100,000 first mortgage P&I @ 5.75% step-down rate: | \$583.57                    |
| Second mortgage P&I (paid off)                       | <u>                    </u> |
| Borrower’s new monthly mortgage payment:             | \$583.57                    |

Total reduction in borrower’s monthly payment with step-down rate:    **\$ 88.29**

**The 30-year interest savings on this same mortgage when a borrower pays off the ABC second mortgage amounts to approximately \$13,585.** NIFA is confident this financial reality provides a great incentive to buyers to payoff the ABC second mortgage with the cash derived from the Federal Tax Credit.

**Dynamics**

Since launching the ABC program, NIFA has received requests from **ten financial institutions** expressing interest in becoming a participating lender in the NIFA single family program, specifically so they can offer the ABC program to their clients. Our office has been fielding, on average, approximately **25-30 calls** per day from borrowers, realtors, sellers, homebuilders, non-profits and others interested in learning more details about the ABC loan program. In less than two months, NIFA’s Single Family Department has taken **65 reservations for a total of \$7 million in ABC program loans.**

The program is replicable because of the rapid consent of our national partners. **FHA** approved a step-down interest rate structure (specifically conditioned upon a subsequent event – the payoff of the second mortgage loan within 120 days of closing). Our master servicer and partner in this program, **US Bank**, helped NIFA to develop the program, and they are able to use this experience to assist their many other housing finance agency clients. NIFA will share information about this innovative homeownership tool with our counterparties in other states.

**Closing**

NIFA’s goal is serving the people of Nebraska with innovative programs that provide extraordinary value. That goal has been achieved in the creation of the ABC loan program. The missing ingredient for many first-time homebuyers is a source of cash to assist them with down payment and closing costs. **NIFA’s ABC Program moves the Federal Tax Credit to the closing table in a positive, cost-efficient and innovative way.** Nebraska’s housing market is already being invigorated by this distinct program and the financial benefit it provides to our borrowers. The ABC loan program **is** the missing “sweet ingredient” that completes the recipe for first-time homeownership.