

Testimony

of

Ann Ashburn

President
AmeriDream, Inc.
Gaithersburg, Maryland

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Hearing on Homeowner Downpayment Assistance Programs
and Related Issues

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Good morning, Chairwoman Waters and Ranking Member Biggert. Thank you for holding this hearing to examine innovative ways in which the private market and charities are helping low and moderate income families to purchase homes. I very much appreciate the opportunity to testify on this important and timely subject.

AMERIDREAM – WHO WE ARE

My name is Ann Ashburn, and I am President of AmeriDream, Inc., a 501(c)(3) charitable entity which is dedicated to helping low and moderate income families achieve their dream of purchasing their own homes.

AmeriDream was established in 1999, and is based in Gaithersburg, Maryland, but provides housing programs throughout the United States. AmeriDream provides a wide range of programs to benefit the families it serves, including homebuyer education, loss mitigation counseling, community development, and privately-funded down payment gift assistance. Through those various programs, AmeriDream not only seeks to help families to purchase homes, but also to provide those families, many of whom are first time homebuyers, with the education and other resources needed to help them meet the responsibilities of homeownership. In turn, those responsible, committed homeowners help build safe, thriving communities.

AmeriDream exists to serve low and moderate income (LMI) individuals and families. Our mission is to permit these aspiring homeowners, a disproportionate number of whom are first-time homebuyers, minorities, legal immigrants, women headed households, and single-parents, achieve homeownership. Since 1999, we have educated 61,346 homebuyers through our homebuyer education course, counseled and assisted 1,200 people to retain their home regardless of their mortgage product, and built 68 affordable housing units in our inner cities, most notably right here in Southeast DC, and committed over \$30 million to these projects. Most significantly, we have provided critical down payment assistance to over 200,000 low and moderate income homebuyers, enabling them to purchase their homes, the majority for their first time.

OVERVIEW OF PRIVATELY-FUNDED DOWNPAYMENT ASSISTANCE & THE FHA PROGRAM

Congress created the Federal Housing Administration (FHA) to establish and implement crucial policy initiatives to assist low and moderate income individuals and families make the transition from tenants to homeowners. To help achieve that worthy goal, the FHA guarantees certain loans for moderately priced homes. That single program, the FHA loan guarantee, is perhaps the most important federal initiative to promote homeownership among families with limited means. Significantly, low and moderate income borrowers who qualify for FHA-backed loans are able to get credit at reasonable rates from reputable lenders. They do not fall prey to predatory lenders.

To qualify for FHA loan guarantees, both the homes and the prospective purchasers must meet certain criteria, among which is the statutory requirement that the

homebuyer must make a down payment of at least 3% of the purchase price of the home. That criterion has proven to be an insurmountable obstacle for many otherwise qualified low and moderate income families seeking to purchase their own homes. Even families who have pristine credit histories, steady employment, and sufficient income to meet mortgage payments nonetheless often have trouble setting aside a significant portion of their paycheck to meet the FHA's down payment requirement. As a result, the FHA program, though highly commendable, nonetheless has failed to benefit many of the very families which it was designed to serve. As a result, families who have been denied access to FHA-backed loans are left with two options, both very unfavorable: resort to potentially predatory, sub-prime loans, or do not purchase a home at all.

To the credit of both Congress and the FHA, they have long recognized that the down payment requirement would prove too burdensome for many of the families whom they sought to help. For that reason, prospective homebuyers are expressly permitted to use monetary gifts to make the required down payments, provided that those gifts come from certain specified sources, including family members, employers, labor unions, and charities certified by the Internal Revenue Service pursuant to section 501(c)(3) of the tax code. As a practical matter, for many aspiring home purchasers—whose relatives also have modest means, who do not belong to a union, and do not have employers who provide the requisite gifts—the only source of down payment assistance on that list to whom they may have recourse are charities.

Beginning in the mid-1990s, a number of 501(c)(3) organizations began to step up to meet this need. Faith-based organizations first took the lead, initiating programs to provide needed down payment assistance to these low and middle income aspiring homebuyers, typically from the very communities in which the churches were based.

From those modest beginnings, down payment assistance programs grew very rapidly to meet the pent up demand of hundreds of thousands of families who longed to purchase their own homes, and qualified for FHA loans in every respect except for the required down payment.

I certainly acknowledge that the extremely fast growth led to a measure of disorganization among down payment assistance providers, and, in some cases, excesses by certain individuals involved with those entities. AmeriDream, and other down payment assistance providers have sought to address those problems, and we welcome further regulation and oversight from the government to ensure that we adhere scrupulously to our charitable mission.

I also acknowledge that, as the scale of the down payment assistance programs quickly grew beyond the means of the traditional donor base of the churches and other providers of down payment assistance, providers turned to other sources of support, particularly within the real estate industry. However, I view that as an unequivocally positive development. An expanded donor base has permitted down payment assistance to be extended to far more families, who then are able to purchase homes at valuations

validated by HUD-certified appraisers. Moreover, an expanded donor base has permitted down payments assistance programs to grow without taxpayer dollars.

By any quantitative measure, down payment assistance programs have proven to be an enormous success.

- To date, approximately one million low and moderate income individuals and families in every state have received down payment assistance which has allowed them to buy their own homes, usually for the first time.
- Down payment assistance to these low and moderate income families was given entirely from private sources; no government funds were used.
- Down payment assistance programs are targeted at low and moderate income purchasers purchasing modestly priced homes in neighborhoods which would particularly benefit from an increase in owner-occupied housing.
- The average down payment gift amount is approximately \$3,600.
- The average sales price of homes purchased with down payment assistance is currently \$128,000.
- Down payment assistance has been given to deserving, credit worthy borrowers who, notwithstanding their limited incomes, are able to meet their mortgage payments. They are only unable to come up with the required down payments. Nationally, approximately 94% of down payment assistance recipients have met their mortgage obligations without undue difficulty.
- Transactions which utilize down payment assistance now reportedly comprise approximately 40% of FHA's loans.
- Down payment assistance programs have been crucial to achieving record levels of homeownership, both among the general population and among groups which historically have been denied the ability to purchase their own homes.

In the balance of my testimony, I hope to describe in greater detail how down payment assistance currently works, and to present further data which illuminates the benefits down payment assistance provides. I also hope to address legitimate questions which have arisen concerning the provision of down payment assistance, for which I believe there to be equally legitimate responses.

In the end, however, I ask this Committee to bear in mind one proposition. Down payment assistance works.

No one disputes that these programs have enabled many hundreds of thousands of low and moderate income families to purchase homes for the first time. No one questions

whether the beneficiaries of these programs have received every penny promised. No one doubts that these programs have been instrumental in lifting homeownership rates to record levels, particularly among minority groups. This is a new charitable sector, barely a decade old, and it has experienced significant growing pains. AmeriDream and other reputable down payment assistance providers not only welcome, but have aggressively sought out, additional guidance and even regulation from HUD and the IRS to ensure that the providers scrupulously adhere to their charitable mission. Unfortunately, however, that outreach has been rebuffed, and down payment assistance providers have been confronted with policies, drafted without their input, which seek to shut them down. I respectfully suggest to this Committee that such a result would be calamitous not just for down payment assistance providers, but for the families we serve, and would be a major setback for the work of this Committee to promote homeownership for all Americans.

HOW THE PROGRAM WORKS

Charitable organizations raised the seed money to make the down payment gifts to LMI homebuyers on a waiting list. The program is designed and operated to protect the integrity of the fund and in compliance with HUD regulations. Organizations provide down payment gifts to qualifying homebuyers from this fund. The money is sent directly to the closing attorney and placed in the homebuyer's escrow account in advance of the loan closing. . After the loan closes and the real estate transaction is complete, the seller of that property often pays the organization a service fee which is typically 7 to 10 days after the closing is complete. The service fee is deposited into the organization's fund for down payment assistance and is later used for new homebuyers requesting down payment assistance, other charitable programs, and administrative costs.

In 1998, HUD's Office of General Counsel reviewed the down payment assistance process, the distribution of funds to a homebuyer and the post-settlement payment of a service fee from a seller and found that it was in compliance with HUD's guidelines.

*“HUD’s Office of General Counsel has advised that the timing of the payments is a key point in whether there is a seller inducement to purchase. If a gift is made from a nonprofit entity (either directly or through an entity such as a closing agent), from the nonprofit’s own funds, prior to the completion of the closing, the gift becomes the homebuyer’s property so the buyer can make the three percent required down payment. After the completion of the closing, a seller makes a contribution (perhaps through the closing agent as well) from the gross sales proceeds to the nonprofit entity. The donation is commingled with other nonprofit funds that later become a source of donations to buyers other than the buyer who has just closed the purchase of the seller’s property. **Because the buyer has not received funds from the nonprofit that can be traced to the seller’s contribution, there has not been an inducement to purchase provided by the seller.**”*

Because downpayment assistance overcame one of the largest barriers to entering homeownership, which is accumulating a significant sum of money for the

downpayment, and because privately-funded downpayment assistance (DPA) was reliable to have continuous funds and not run out of money to fund the downpayments, the program grew rapidly. Within a few years privately-funded DPA made up 40% of all FHA transactions.

It is important for the committee to understand that DPA is not sub-prime lending and DPA does not provide subprime loans. DPA is a very safe program for homebuyers that supplements FHA's 97% Loan -To-Value product. The three largest DPA organizations together comprise almost half of FHA/DPA totals. Without DPA, FHA's homebuyers would not be served and would likely have turned to subprime loans or remained renters, and revenues for FHA would have been cut significantly.

HELP PROVIDED BY DPA

No one has denied the social and economic benefit that DPA provides. It is consistently acknowledged that FHA and DPA serve the same population of homebuyers. FHA and DPA jointly serve the working yet struggling class to include lower income, minorities, women headed households and first time homebuyers. Approximately 35% of the DPA recipients are minorities, 70% are low income and 85% are first time homebuyers. The Washington Post has reported that DPA has helped boost national homeownership rates to near-record 69% in the past 6 years. And reported that the program has helped hundreds of thousands of low income households buy their first homes.

- DPA is a good program that works and provides significant benefit to LMI homebuyers using the program.
- DPA is now a mainstream affordable housing program with lenders, builders, and real estate agents to help LMI homebuyers achieve the American Dream.
- HUD, itself, has used AmeriDream DPA in selling 7 of its REO properties where AmeriDream gave the buyer the down payment gift and HUD paid our service fee.

ISSUES RELATING TO DPA

Because the industry evolved very rapidly and under the auspices of charities, early management was not accustomed to managing large and complex organizations. The beginning years are marked by disorganization and management problems. However, in no instance has it ever been alleged that benefits did not go to recipients. As potential issues arose, DPA organizations sought to address the issues on their own and invited HUD and others to provide input and recommendations on how they would like the issues addressed. While DPA was able to address many of the issues themselves, two issues have continually remained.

Claims on FHA Insurance – HUD has suggested that DPA has led to a burden of FHA because of default rates of homes purchased using DPA. When foreclosure is being reviewed, one must always look at the “claim” rate. Often “default” rate numbers are cited which are considerably higher than actual claim rate numbers. A claim is when the FHA fund actually pays out money. Two independent studies determined that when claim rate is used there is no statistical difference in claim rate between homeowners who received a down payment gift from a privately-funded down payment assistance program and homeowners who received a down payment gift from a family member. Claim rate for these two groups represent a 94% and 95% success rate, respectively. One study was conducted by George Mason University Center for Regional Analysis and the other by the Reznick Group.

Furthermore HUD has repeatedly gone on record stating that borrowers who rely on non profit down payment assistance are representative of the population that FHA was established to serve. FHA has determined that additional requirements or restrictions that would prevent these borrowers from obtaining FHA financing would not be beneficial, leaving this population with financing options that are more costly and riskier than FHA.

More fundamentally the DPA program resulted in several billion dollars of savings to the government. DPA gave FHA a less risky program that had an equity safety net for homebuyers compared to certain subprime programs. Additionally, over the past 10 years DPA has generated billions of dollars for FHA that has funded the national Treasury.

Home Prices – Concern arose that potentially sellers were increasing the sales price of their home to include the service fee payment to the DPA which could cause the home to be over valued. In addressing this concern, AmeriDream made it known that this was not the proper use of DPA programs and has internal policies and training so that homebuyers are not buying a house that is overvalued. Through the home sale process using FHA all homes are required to have a HUD-certified appraiser conduct an official written appraisal on the home. DPA programs do not have any contact with the appraiser. AmeriDream also recognized that home price appraisals were an issue throughout the entire lending industry and not unique to DPA. AmeriDream proposed strengthening the appraisal process by adding additional requirements that appraisers be assigned randomly from a large group similar to VA’s blind draw process. In addition, AmeriDream has advocated its support for appraisal reform as evidenced by promoting Congressmen Wilson and Clay’s Appraisal Reform bill.

OUTREACH TO HUD AND EXECUTIVE AGENCIES

AmeriDream and other DPA organizations have collectively reached out to HUD and other agencies as far back as 1999 through current day to protect homeownership opportunities for LMI families and create official standards for DPA programs. All agencies have rebuffed outreach for 10 years.

As with any new program, changes are sometimes needed to make the program better, this includes enforcing penalties to curtail wrongful practices, and creating outreach opportunities with public and private partners to discuss problems and challenges, and work collectively towards long-term solutions and success. As issues arose, the major DPA programs evolved and addressed these issues by creating better management structures, governance, code of conduct, and shared best practices to enhance their programs and continued to proactively reach out to agencies in the Executive branch for guidance.

In contrast, since 1999 HUD has been trying to eliminate privately-funded DPA.

In 2003, AmeriDream met with the IRS and voluntarily sought the IRS guidance on its operations. In 2004, the IRS granted AmeriDream its final determination letter confirming the organization as a 501(c)(3) entity. Additionally, AmeriDream sent letters, in 2004, 2005, and 2006 to the IRS requesting to participate in any guidance that would be developed for down payment assistance. The Service ignored all outreach. It was not until mid-2006 that the IRS issued its interpretation of tax law as it related to down payment assistance in Revenue Ruling 2006-27.

By now you are probably aware of the IRS's latest pronouncement regarding DPA: Revenue Ruling 2006-27. The ruling was issued following a years-long guidance project that, as far as we know, never considered the views or input of DPA organizations that are doing this charitable work every day. Instead, the agency published this ruling, its own interpretation of the law, and now attempts to apply it with the effect of shutting down DPA organizations solely because they have as part of their charitable operations support from private parties in the real estate industry. We must be careful not to treat the ruling as if it were a settled statement of law. Revenue rulings do not carry the precedential authority of a statute, a court decision, or even a regulation. Rather, they represent merely the IRS's interpretation of the law. The Supreme Court has addressed the precedential weight of revenue rulings: “the ‘Service’s interpretive rulings do not have the force and effect of regulations,’ and they may not be used to overturn the plain language of a statute.”¹ As of this writing, the 2006 Ruling has not yet been reviewed by a court of law on its merits. Absent a court decision upholding the 2006 Ruling, it cannot be considered to have settled the issue of when down payment assistance is “charitable” for tax purposes. Thus, the IRS's position, as reflected in the Revenue Ruling, does not warrant the deference it receives in HUD's proposed rulemaking.

¹ *Commissioner v. Schleier*, 515 U.S. 323, 336 n.8 (1995) (citing *Davis v. United States*, 495 U.S. 472, 484 (1990)). See also *Estate of Kosow v. Commissioner*, 45 F.3d 1524, 1529, n.4 (11th Cir. 1995)(a revenue ruling “is merely an opinion of an IRS attorney”); *Stubbs, Overbeck & Assoc., Inc. v. United States*, 445 F.2d 1142, 1146-47 (5th Cir. 1971) (“[a] ruling is merely the opinion of a lawyer in the agency and must be accepted as such.”); *Sprang Industries, Inc. v. United States*, 791 F.2d 906, 913 (Fed. Cir. 1986) (“a revenue ruling is entitled to some weight as reflecting the Commissioner’s interpretation of the regulation, but does not have the same force as a regulation.”).

The Office of Management and Budget (OMB) has also ignored outreach. When it became public that HUD had submitted draft language for the current proposed HUD rule to OMB for review, AmeriDream sent a letter to OMB requesting a meeting to discuss down payment assistance. The letter made it clear that any change that would impact this program would be a significant matter for LMI homebuyers, the housing sector, and AmeriDream. No response came from OMB.

PROPOSED HUD RULE

As the proposed rule relates to privately-funded down payment assistance, it focuses on the mechanics of the program as opposed to FHA's mission of housing policy and the social and economic good of achieving homeownership. HUD has implemented the public rule making process that could begin to achieve regulations that have been requested for almost 10 years. However, the proposed rule language seeks to eliminate the DPA program, which has proven its success over 10 years.

The proposed rule would eliminate 30-40% of FHA's homebuyers and 30-40% of FHA's business. It would remove one of the only remaining programs geared to helping LMI homebuyers. Private market/subprime options have been reduced significantly and housing professionals are returning to FHA coupled with DPA. The proposed rule has the very real potential to create further stress on the overall housing industry and the national economy. The unintended consequence will be LMI homebuyers returning to risky and sometimes predatory sub-prime products, if available, or remain renters and continue to lag behind in creating financial stability through home equity.

The proposed rule would also have a national effect on mortgage companies, real estate companies and builders across the country. DPA beneficiaries are 85% first time homebuyers. First time homebuyers are the most important link in the chain of home purchases. The first time homebuyer represents more than 40% of home purchases over the past 10 years. The entry of the first time homebuyer into the housing market begins the ripple effect of allowing current homeowners to sell their home and move to their next home. Without the entry of the first time homebuyer the housing market will decline even more.

DPA has become a mainstream program. Almost all mortgage companies are familiar with DPA and like using the program for their LMI homebuyers. Otherwise lenders would simply not use DPA and opt for an alternative 100% financing program perhaps through Fannie Mae's "My Community" or Freddie Mac's "Home Possible" program. DPA is an optional program. If problems existed lenders would have stopped using DPA years ago.

Mortgage companies can adjust loan program parameters to offset almost any problem resulting in almost immediate results. FHA and HUD have never attempted to constructively fix the alleged issues with DPA over the past 10 years.

The proposed rule states that the primary concern is over valuation of the property. HUD's primary concern of an appraisal issue does not warrant the elimination of a program that has been undisputed in the help it provides to many hard-working yet struggling American families. Valuation is a problem that can be fixed with some rules and regulations about the appraisal process as we have requested for 10 years. This type of programmatic change would fix HUD's primary concern and would be a less costly, less disruptive, and more easily implemented as opposed to the current proposal that would harm LMI homebuyers, disrupt the housing market, reduce revenue that is currently generated into local, state, and national treasuries and harm nonprofit organizations and their constituents, to name a few.

PROPOSED HUD RULE COMMENT PERIOD

The proposed rule calls for a public comment period until July 10, 2007. As of June 20, 2007, there have been 7,042 Americans from across the country, from every state, and from every Congressional district using the public comment period to voice their support for DPA and have requested HUD to withdraw the rule. The subcommittee has been provided a copy of these 7,042 comments. The committee has also been given copies of the 16 comments that support the proposed rule.

It is important to mention that the public comment process could be compromised at this time. Two weeks ago HUD Secretary, Alfonso Jackson, said in the interview that HUD intends to approve the new rule by the end of the year even if the agency receives critical comments.

RECOMMENDATIONS OF AMERIDREAM AND NEHEMIAH

AmeriDream and the one million gift recipients respectfully request that the committee instruct HUD to withdraw its proposed rule so that the committee can have time to review our recommendations to improve DPA and work with us to achieve Congressional sanctioned regulations for DPA.

Nehemiah's and AmeriDream's collective ideas are offered to highlight the various options available to HUD or other branches of the government to create approval guidelines to regulate providers and programs associated with privately-funded downpayment assistance. Through a thorough and collaborative process, the non-profit DPA providers and the government should be able to develop these and/or many more ideas. The result will be sound policy, positive outcomes, a successful mission-driven public-private partnership committed to increasing homeownership opportunities. These suggestions include:

- Mandatory homeownership education for all downpayment assistance recipients either in person or online paid for by the seller.
- Mandatory loss mitigation counseling and mortgage insurance for all downpayment assistance recipients paid for by the seller.

- Mandatory prohibition of the inflation of sales price.
- Refine the current appraisal process. A few suggestions include: implement a blind draw process similar to the Veterans Affairs process; require that the appraisal account for and recognize the DPA gift and include it in the assessment; require the lender, seller, and appraiser to sign a fair appraisal document that no coercion or manipulation of the value was taken under penalty of perjury and monetary fine.
- Expand list of allowable sources for providing down payment gifts to include other organization structures.
- Require certain financial thresholds, annual disclosures for participating organizations, and accountability.
- Require certain organizational experience such as 5 years experience in providing downpayment assistance programs to at least 10,000 families for all downpayment assistance providers that raise funds from private sellers that operate in states other than their own home state.
- Require background and financial check of officers and board members to include financial requirements and “Clean Hands”.

On behalf of the million DPA assisted homeowners, AmeriDream’s employees, AmeriDream’s Board of Directors, and myself, we affirm to you that our down payment assistance program is not the abusive program that some paint it to be. In our pursuit of excellence, we come before you to request your assistance in allowing us to continue doing things right for America’s homebuyers.

Thank you again for your time and attention to this very important matter.