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CHAIRWOMAN

United States House of Representatives
Committee on Financial Services
2129 Rayburn House Office Building
Washington, D.C. 20515

PATRICK MCHENRY, NC
RANKING MEMBER

May 3, 2019

Memorandum

To: Members, Committee on Financial Services

From: FSC Majority Staff

Subject: May 8, 2019, "A Review of the State of and Barriers to Minority Homeownership"

The Subcommittee on Housing, Community Development and Insurance will hold a hearing entitled, "A Review of the State of and Barriers to Minority Homeownership," at 10:00 a.m. on Wednesday, May 8, 2019, in room 2128 of the Rayburn House Office Building. This will be a single-panel hearing with the following witnesses:

- **Alanna McCargo**, Vice President, Housing Finance Policy, the Urban Institute
- **Nikitra Bailey**, Executive Vice President, Center for Responsible Lending
- **Joseph Nery**, Partner, Nery & Richardson LLC and Past President of the National Association of Hispanic Real Estate Professionals (NAHREP), current National Board Member
- **Jeffrey Hicks**, President, National Association of Real Estate Brokers
- **Carmen Castro-Conroy**, Managing Counselor, Montgomery County, Housing Initiative Partnership, Inc.
- **JoAnne Poole**, 2019 Vice Chair, Multicultural Real Estate Leadership Advisory Group, National Association of Realtors
- **Joel Griffith**, Research Fellow, Financial Regulations, the Heritage Foundation

Historical Background

Prior to the passage of the Fair Housing Act in 1968, federal, state, and local governments actively and explicitly enforced policies that discriminated against racial minorities seeking homeownership opportunities, making it harder for them to purchase homes in certain neighborhoods or to obtain financing on fair terms.[1] During parts of the 20th century, state and local governments promoted segregation in neighborhoods across the nation by actively enforcing racially restrictive covenants, which were legally enforceable provisions in property deeds that prohibited racial minorities from purchasing homes in white residential neighborhoods. In 1933, the Franklin D. Roosevelt administration created the Home Owners' Loan Corporation (HOLC) to help homeowners that were about to default as a result of the depression. HOLC created color-coded maps that identified high risk areas in red; communities were also colored red if racial minorities lived there. Similarly, when the Federal Housing Administration (FHA) was established in 1934 to help expand homeownership opportunities, the agency classified neighborhoods as too risky and therefore ineligible for FHA mortgage insurance if it was a racially mixed neighborhood, or

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[1] *See e.g*. Richard Rothstein, "The Color of Law: The Forgotten History of How our Government Segregated America," May 2017.

if it was a white neighborhood near a minority neighborhood. As Richard Rothstein sums it up in his book, *The Color of Law*,

> Racial segregation in housing was not merely a project of southerners in the former slaveholding Confederacy. It was a nationwide project of the federal government in the twentieth century, designed and implemented by its most liberal leaders. Our system of official segregation was not the result of a single law that consigned African Americans to designated neighborhoods. Rather scores of racially explicit laws, regulations, and government practices combined to create a nationwide system of urban ghettos, surrounded by white suburbs.

After the passage of the Fair Housing Act, discrimination in the homeownership market was no longer as overt but continued to exist in different forms that have had incredibly harmful impacts on minority borrowers and communities. This is perhaps most clearly demonstrated by several studies and lawsuits that have documented the practice of reverse redlining in the lead up to the 2008 financial crisis.[2] Specifically, minority borrowers were targeted for predatory mortgage products or products with less-than-favorable terms, setting them up to be disproportionately affected when the housing market crashed. For example, the Center for Responsible Lending found that African American and Latino borrowers were much more likely to receive high interest (subprime) loans and loans with features that are associated with higher foreclosures even after controlling for credit scores.[3] A study by the Wall Street Journal found that most borrowers who received predatory loans in 2006 would have qualified for better, more sustainable loans.[4]

These trends set the stage for a crisis of starkly different proportions for minority homeowners compared to white homeowners. By 2011, during the height of the foreclosure crisis, about a quarter of African American and Latino homeowners had lost their homes to foreclosure or were seriously delinquent, compared to just under 12 percent for white homeowners and just under 14 percent for Asian homeowners.[5] Also by 2011, 25 percent of black homeowners and 28 percent of Hispanic homeowners had underwater mortgages, a home purchase loan with a higher principal than the free-market value of the home, compared to just 15 percent of white homeowners.[6] Even for minority homeowners who were able to remain current on their mortgages, the effects of the financial crisis was particularly devastating. Patterns of racially segregated neighborhoods in conjunction with higher rates of foreclosure in those

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[2] *See e.g*. Department of Justice press release, "Justice Department Reaches Settlement with Wells Fargo Resulting in More Than $175 Million in Relief for Homeowners to Resolve Fair Lending Claims," July 12, 2012, available at: https://www.justice.gov/opa/pr/justice-department-reaches-settlement-wells-fargo-resulting-more-175-million-relief

[3] Debbie Gruenstein Bocian, Wei Li Carolina Reid, & Roberto G. Quercia, "Lost Ground, 2011: Disparities in mortgage Lendng and Foreclosures," the Center for Responsible Lending, November 2011, available at: http://www.responsiblelending.org/mortgage-lending/research-analysis/Lost-Ground-2011.pdf

[4] Rick Brooks and Ruth Simon, "Subprime Debacle Traps Even Very Credit-Worthy: As Housing Boomed, Industry Pushed Loans To a Broader Market," the Wall Street Journal, updated December 3, 20117, available at: https://www.wsj.com/articles/SB119662974358911035

[5] Debbie Gruenstein Bocian, Wei Li Carolina Reid, & Roberto G. Quercia, "Lost Ground, 2011: Disparities in mortgage Lendng and Foreclosures," the Center for Responsible Lending, November 2011, available at: http://www.responsiblelending.org/mortgage-lending/research-analysis/Lost-Ground-2011.pdf

[6] Center for Global Policy Solutions, "Beyond Broke: Why Closing the Racial Wealth Gap is a Priority for National Economic Security," May 2014. This report further found that racial gaps remained in terms of whether or not a homeowner in underwater even after accounting for several mortgage characteristics including age, education, income, marital status, and living in a crisis state.

neighborhoods contributed to greater losses in home values due to compounding issues such as blight. From the height of the housing bubble to the bottom, communities of color saw their home values drop significantly more than white communities, with a 46 percent drop in Hispanic communities, and a 32 percent drop in African American communities, compared to a 24 percent drop in white communities.[7] African Americans and Asian Americans lost nearly half of their wealth (45 percent and 48 percent respectively) as a result of their crisis and Latinos experienced an even greater loss at 58 percent of their net worth, compared to just 21 percent among white households.[8]

Current Trends and Future Projections

Today, a persistent gap in homeownership rates remains between minority and white households. According to the most recent Census Bureau data (2018), the homeownership rate is 73 percent for non-Hispanic white households, 42 percent for African American households, 47 percent for Hispanic or Latino households, and 58 percent for Asian or Native Hawaiian/Pacific Islander households.[9] In the past 15 years, black homeownership has seen the most dramatic drop of any racial or ethnic group and it is now as low as it was when discrimination was legal.[10] Hispanic households have experienced some modest improvement over the same time period but continue to see a significant gap compared to white homeownership rates.[11] The U.S. Census Bureau only recently started to track Asian homeownership separately, which used to be counted in the "Other" category, so it is more difficult to see those trends over time. (See Appendix for homeownership rates over time)

As homeownership continues to be a primary means for American families to gain wealth, the lagging rates of minority homeownership has significant implications for the racial wealth gap. The most recent Census Bureau data available on the wealth gap (2014) showed that non-Hispanic white households had an average net worth of $130,800, while black households had an average net worth $9,590 and Hispanic households had $17,530.[12] Asian households had an average net worth of $156,500 when looking at the aggregate, but they are also the most economically divided racial or ethnic group in the U.S., with Asians in the top percentile having median income of $133,529 in 2016, compared with $12,478 for those in the bottom percentile. On the whole, this means that on average, white households held over 13 times the amount of wealth of black households, and more than seven times that of Hispanic households. The Institute for Policy Studies and Prosperity Now project that if current trends continue and the racial wealth divide is left unaddressed, median black household wealth is on a path to hit zero by 2053, median Latino household wealth is projected to hit zero twenty years later (or by 2073), while median white household wealth is expected to climb to $137,000 by 2053 and $147,000 by 2073.[13] Due to the projected growth of minority households in the coming decades and the importance of the housing market to our national economy, some analysts have argued that a failure to address the gap in minority

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[7] Zillow, "A House Divided: How Race Colors the Path to Homeownership," January 2014.
[8] Center for Global Policy Solutions' analysis of Census Bureau data in "Beyond Broke: Why Closing the Racial Wealth Gap is a Priority for National Economic Security," May 2014.
[9] Census Bureau data available at: https://www.census.gov/housing/hvs/data/ann18ind.html
[10] *See e.g*. Alanna McCargo, "A five-point strategy for reducing the black homeownership gap," Urban Institute, February 14, 2019.
[11] *Id*.
[12] Census Bureau data available at: https://www.census.gov/data/tables/2014/demo/wealth/wealth-asset-ownership.html
[13] Dedrick Asante-Muhammad, Chuck Collins, Josh Hoxie, & Emanuel Nieves, "The Road to Zero Wealth: How the Racial Wealth Divide is Hollowing Out America's Middle Class," Prosperity Now & Institute for Policy Studies, September 2017.

homeownership and corresponding wealth gap is not only a major civil rights issue, it is a threat to the America's economic security.[14]

Ongoing Systemic Barriers

Systemic barriers to increasing minority homeownership continue to exist, such as the continued existence of predatory products that are targeted at racial minorities, policies that unnecessarily keep immigrants out of homeownership, and FHA policies that unfairly burden minority borrowers with additional costs.

Rent-to-Own Contracts

Historically, rent-to-own contracts (also known as land contracts or lease-to-own transactions) have a long history of having predatory terms and being marketed to racial minorities as an alternative path to homeownership in the absence of affordable and available mortgage credit or down payment assistance.[15] In general, a rent-to-own contract includes a standard lease agreement for a specified period of time, during which the title to the house remains with the landlord, and after which the tenant has an option to purchase the property. Despite the fact that a rent-to-own contract term begins with a standard lease agreement, state landlord-tenant laws generally do not apply during this period, allowing sellers to convey dilapidated properties to tenants and shift the obligation for maintenance, taxes, and substantial structural repairs to the tenant.[16] Other common problems with these contracts include inflated purchase prices, issues with conveying title due to failure to disclose liens and mortgages, and evictions when the costs of maintenance and rent become too onerous.[17] According to the National Consumer Law Center, these issues are going overlooked by a patchwork of state laws that govern these contracts.[18] While it is difficult to identify the scope of the issue as there is no national database tracking the prevalence of rent-to-own contracts, several recent press articles have reported on the rise of these predatory contracts.[19]

Access to Homeownership for DACA Recipients

On December 14, 2018, BuzzFeed reported that the Trump administration was quietly denying FHA loans to recipients of Deferred Action for Childhood Arrivals (DACA),[20] which is a federal policy that allows children who were brought to the U.S. as children to remain in the country. In response to letters from Members of Congress, expressing concerns, HUD insisted that it had not made any formal changes to their policies.[21] Although HUD may not have made any *formal* changes to its policies, based on the Buzzfeed article and other press reports, it appears that HUD may have made an *informal* policy change to interpret its own existing regulations and guidance to consistently deny DACA recipients whereas previously some lenders had been able to originate loans for DACA recipients with HUD's approval for years. Fannie Mae has responded by clarifying that DACA recipients are eligible for loans

[14] *See e.g.* Center for Global Policy Solutions, "Beyond Broke: Why Closing the Racial Wealth Gap is a Priority for National Economic Security," May 2014.
[15] *See e.g.* Jeremiah Battle, Jr., Sarah Mancini, Margot Saunders, & Odette Williamson, "Toxic Transactions: How Land Installment Contracts Once Again Threaten Communities of Color," the National Consumer Law Center, July 2016.
[16] *Id*.
[17] *Id*.
[18] *Id*.
[19] *See e.g.* Alana Semuels, "A House You Can Buy, But Never Own," the Atlantic, April 10, 2019.
[20] Nidhi Prakash, "The Trump Administration is Quietly Denying Federal Housing Loans to DACA Recipients," BuzzFeed, December 14, 2018.
[21] *See e.g.* Ben Lane, "HUD to lenders: We are not denying mortgages to DACA Dreamers" April 30, 2019.

that they guarantee.[22] It does not appear that Freddie Mac or USDA have responded to clarify their policies on DACA recipients.

[22] *See e.g.* MBA NewsLink Staff, "Fannie Mae Issues Guidelines for Non-Citizen Borrowers, Including DACA," March 26, 2019.

FHA Premiums

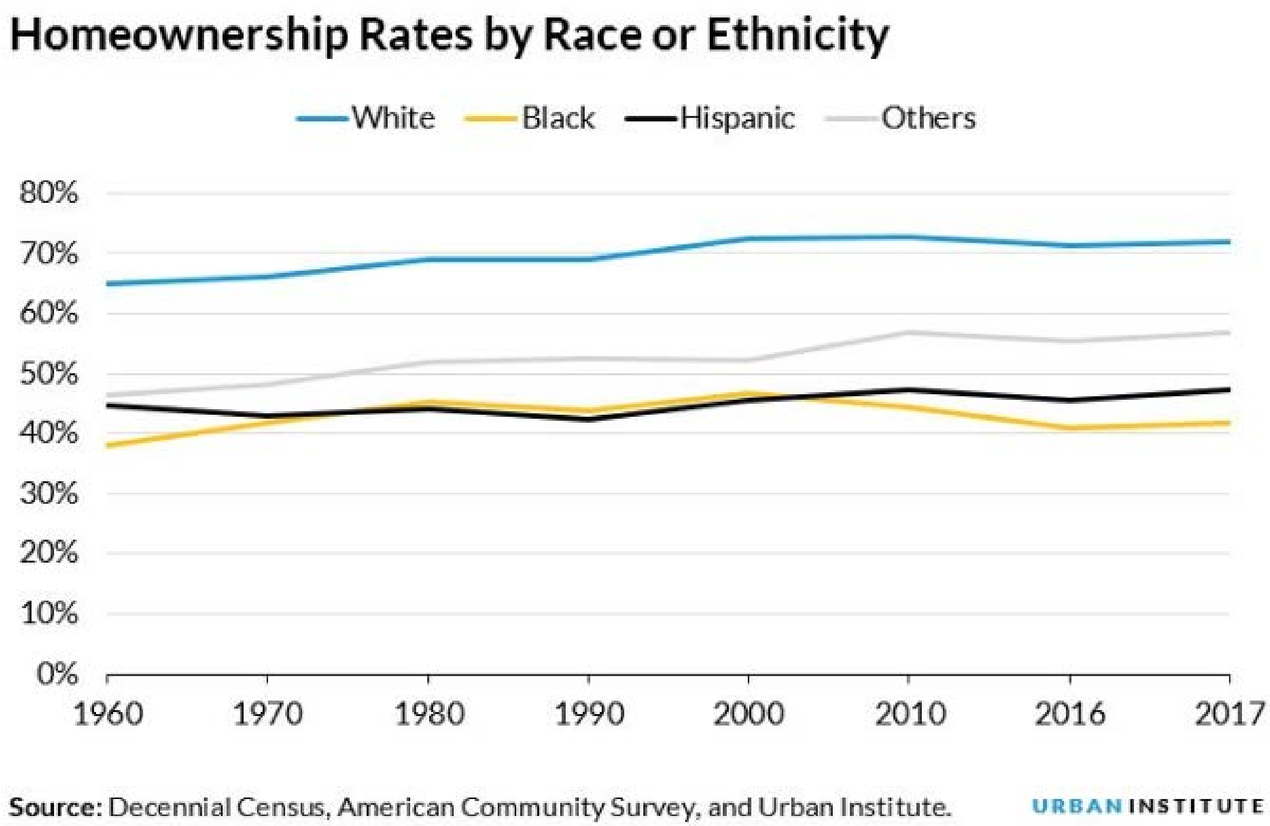
Under current law, private mortgage insurers are required to cancel premiums once the outstanding principal balance reaches 78 percent of the original home value. In contrast, the FHA requires its borrowers to pay mortgage insurance premiums for the life of the loan. This means that FHA borrowers can pay far more in premiums over time than non-FHA borrowers. Moreover, the FHA disproportionately serves minority borrowers, meaning that the FHA's policy of charging premiums for the life of the loan is disproportionately harming these same households. The FHA has required borrowers to pay the annual premiums for the life of the loan since June 3, 2013.[23] Prior to that, the FHA was aligned with the private mortgage insurance industry in charging premiums only until the outstanding principal balance reached 78 percent of the original home value.[24] The FHA's justification for the change in its policy was that it was consistent with its efforts to strengthen the Mutual Mortgage Insurance Fund (MMIF), which had dipped below the statutorily mandated capital ratio of 2 percent in the wake of the housing crisis. However, the FHA is currently in strong financial health and has remained over the 2 percent threshold for four consecutive years. Moreover, the policy of charging premiums for the life of the loan incentivizes those with the financial means to refinance into a non-FHA loan to avoid ongoing premium payments which may weaken the MMIF by causing FHA to lose some of the lower risk loans in its portfolio.

Legislative Proposals

- H.R. 2162. This bill introduced by Reps. Beatty and Stivers would provide a discount on FHA mortgage insurance premiums for first-time homebuyers if they complete a HUD-approved housing counseling program.
- HOUSFIN_001. This discussion draft from Rep. Vargas would ensure that DACA recipients are eligible for loans backed by FHA, USDA, Fannie, and Freddie.
- TLAIB_013. This discussion draft from Rep. Tlaib would establish a basic federal standards for rent-to-own contracts to help eliminate predatory practices.
- HOUSFIN_002. This discussion draft from Rep Phillips would eliminate FHA's current policy of charging premiums for the life of the loan and reinstate the FHA's previous policy of only requiring borrowers to pay premiums until the outstanding principal balance reaches 78 percent of the original home value.

[23] HUD Mortgagee Letter 2013-04
[24] HUD Mortgagee Letter 00-38

Appendix


Homeownership Rates by Race or Ethnicity
White
Black
Hispanic
Others
80%
70%
60%
50%
40%
30%
20%
10%
0%
1960
1970
1980
1990
2000
2010
2016
2017
Source: Decennial Census, American Community Survey, and Urban Institute.
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