

## Credit Scoring: Friend or Foe?

Credit scoring, a statistical method used to predict the probability that a loan applicant will default or become delinquent, was introduced in the 1950s and was used primarily to evaluate credit card applications. Because of advances in technology and the increase in the number of large banks that can afford such technology, the use of credit scoring has expanded over the years and now includes consumer lending, such as auto, personal unsecured, and home equity loans. More recently, it has been used to help evaluate applications for mortgages and small-business loans, sparking renewed controversy. Supporters see credit scoring as an important tool in reducing expenses and speeding loan processing. Opponents argue that an automated

system will not consider the unique needs of low-income and other non-traditional borrowers. As a result, opponents believe, loan denial rates will increase.

### **Creating a Scoring System**

The first step in developing a scoring system is to determine which pieces of information correlate with future credit performance. In selecting the factors that will be scored and the points awarded to each factor, the model builder wants to find the combination that results in final scores that are best correlated with actual credit performance. When a typical application scorecard is developed, 50 or 60 factors may be identified as having some stand-alone predictive value. However, usually only eight to 12 vari-

ables will be used in the final scorecard because they are the factors with the highest predictive value.

And while risk weights assigned to these factors may vary from system to system, there are normally some common elements. Credit history scoring systems, which are based primarily on individuals' credit histories, consider number of credit lines, current and historic delinquencies, and public records (bankruptcies, foreclosures, or judgments). Application scoring systems, which look at both credit bureau information and information submitted on an application, consider employment stability, debt-to-income ratios, assets (particularly cash), and loan-to-value ratios (if the loan is for a mortgage).

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## Consumers Urged to "Know the Rules, Use the Tools"

Declaring that the attorney general's office "will not tolerate credit abuse in Pennsylvania," Mike Fisher, the Commonwealth's attorney general, kicked off a meeting sponsored by his office in conjunction with the U.S. Food and Drug Administration. The meeting, which was held at the Federal Reserve Bank of Philadelphia, was part of National Consumer Protection Week in February.

At the meeting, representatives from city and state government as

well as community organizations and consumer advocacy groups exhorted consumers to "know the rules, use the tools" and warned them of the dangers of credit fraud.

Issues involving credit and credit fraud generate a large number of complaints to the Federal Trade Commission (FTC), the government agency that enforces a variety of consumer protection laws. Consumer discontent also arises from a host of other sources,

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including problems with appliances, car sales, and home-improvement contracts.

But fraud represents one of the biggest problems. Credit card fraud alone costs the economy \$436 million a year. When other types of fraud are factored in—stock manipulation, money laundering, and other “white collar” crimes—the figure approaches \$1 trillion, according to a 1997 article in the *Philadelphia Inquirer*.

Third District states, unfortunately, stand out in this area: Figures compiled by Visa show that Pennsylvania, New Jersey, and Delaware all rank in the top 10 states for credit card fraud. The good news is that all three states vigorously prosecute cases involving consumer rip-offs.

In the credit fraud game, unscrupulous persons prey not only on consumers but also on companies. Depository institutions are often prime targets of those who engage in fraudulent practices. Check fraud, including counterfeit, altered, forged, or stolen checks, costs the U.S. banking industry more than \$1 billion a year. Fraud involving ATMs and identity theft add to the losses. A recent survey by the American Bankers Association stated that in the past few years alone, fraudulent checks carried a face value of \$4 billion. A 1996

study by the Federal Reserve Board, reported in the *American Banker*, claimed that DFIs lost \$615 million to fraudulent checks in 1995. The same study noted that thrifts suffered

the greatest losses from bad checks, with banks and credit unions faring only slightly better.

Community organizations should be familiar with the “rules and tools” so that they can help steer their clients away from potential fraud or point them to resources should they fall victim to a ruse. Banks, too, must maintain vigilance against potential scams.

The FTC’s web site ([www.ftc.gov](http://www.ftc.gov)) is a good source of information about consumer protection laws and gives consumers access to various publications and news releases. The Federal Reserve Bank of Philadelphia’s Community and



**Dede Myers, Vice President and Community Affairs Officer, Federal Reserve Bank of Philadelphia, and Michael Fisher, Attorney General of the Commonwealth of Pennsylvania, shown here at the National Consumer Protection Weekmeeting, which was held at the Philadelphia Fed in February.**

Consumer Affairs Department also responds to consumers’ complaints about the banking and lending practices of depository institutions and nonbank lenders. In addition, Consumer Affairs staff also answer inquiries and advise callers of their credit rights under various consumer banking laws. The Philadelphia Fed’s consumer representative is Rose Howe; her number is 215-574-6116. The Bank also publishes several pamphlets on consumer issues, including “Your Credit Rights” and “Frauds and Scams: Protect Yourself and Your Money.”

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### Advantages

Proponents of credit scoring cite several points in its favor. First, credit scoring involves identifying underwriting parameters and applying them consistently, which allows a level of objectivity. Because loan officers differ in their experience and in their views regarding

the relationships between risk and specific credit characteristics of applicants, an institution cannot be certain that its underwriters are approving all applications that have risk profiles consistent with the institution’s objectives. By reducing judgmental review, scoring can promote fair lending by helping lenders

ensure that they are applying the same underwriting criteria to all borrowers.

Second, scoring decisions differ from most judgmental decisions in that scoring has built-in compensatory features. Judgmental systems often involve a series of “knock-out” rules that may reject an applicant

## FAIR LENDING ISSUES

Another concern with credit scoring involves fair lending issues. The courts have defined three types of discrimination. The first, overt or blatant discrimination, means that lending decisions are explicitly made on the basis of some prohibited factor such as race or gender. Lenders who use credit scoring as the sole basis for their decisions have, in essence, a safe harbor from claims of overt discrimination so long as their model does not contain any factor that is prohibited *per se*.

The second, disparate treatment, means that even though there is no explicit use of a prohibited factor, applicants who qualify similarly on the basis of all legitimate factors are nevertheless treated differently in some respect. But credit-scoring models treat similarly situated applicants the same—by assigning them the same score.

Therefore, any assault on credit scoring would be launched under the third type of discrimination, the so-called effects test or disparate impact doctrine developed under Title VII of the Civil Rights Act of 1964, as amended.

The effects test, as applied to credit scoring, permits discrimination claims based on a credit-scoring system's overall disproportionate negative impact on a protected class. The effects test can also be applied to individual factors used in a credit-scoring system. That is, specific scoring factors could be challenged as being substantially disadvantageous to protected groups and as hindering their ability to qualify for credit under the overall scoring system.

For example, requiring that applicants have incomes in excess of a certain amount to qualify for an overdraft line of credit could mean that women and minority applicants will be rejected at a higher rate than men and nonminority applicants. If there is a demonstrable relationship between the income requirement and creditworthiness for the level of credit involved, however, use of the income standard would likely be permissible.

Cases dealing with the effects test have generally involved a three-step test. The first part of the test requires the plaintiff to show that the use of the challenged criterion has a disproportionate impact on a protected class.

If the plaintiff meets the burden of showing that a disparate impact exists, the second part of the test shifts the burden to the defendant to demonstrate a business justification for the challenged criterion. A credit-scoring model makes it easier for the defendant to document the business reason for using a factor that might have a disproportionately negative impact on a protected class of applicants. The weights in the model give a measure of the relative strength of each factor's correlation with credit performance, given the other factors contained in the model. In fact, both the Federal Reserve Board and the Office of the Comptroller of the Currency have supported credit-scoring models that have been empirically developed to predict risk as having valid business justification under the test for disparate impact.

The third part of the test shifts the burden back to the plaintiff to show that there is an equally effective but less discriminatory alternative available and that the defendant has refused to adopt that alternative.

based on only one criterion. With scoring, a low score on one factor can be made up in other areas.

Third, credit scoring requires less time to underwrite and approve loans, resulting in faster service to the consumer and lower cost to the lender.

Fourth, the reduction in time required to underwrite high-quality loans allows originators to focus their underwriting resources on exception credits. This added time,

which can be dedicated to the more marginal applications, can potentially increase the percentage of loans approved because it enables lenders to better assess default risk and to implement lending policies designed to mitigate potential losses.

### **Disadvantages**

On the other side of the credit-scoring debate, opponents point out that a model's reliability depends on the accuracy, completeness, and

timeliness of the information used. If the baseline population used in the scoring model is not sufficiently diverse, scores may lack predictive power for the underrepresented segments of the overall population. For example, scoring models may leave out rent, utility, and other nonstandard payment histories, which are often considered an important part of the payment record of low- and moderate-income populations.

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## Rural Housing Development

Higher rates of substandard housing, fewer banks, and reduced access to money from foundations and corporations are just some of the special problems developers of rural housing face. Furthermore, residents of these areas often can find only minimum-wage jobs, sometimes rendering even affordable housing unaffordable for them. In rural Delaware, for example, available employment means work in the service or agricultural sector, areas not known for high-paying jobs. Such circumstances just add to developers' frustration levels.

As if these barriers aren't enough to overcome, recent estimates from the U.S. Census Bureau indicate that new home construction in rural areas fell almost 5 percent from 1996 to 1997. Figures for Pennsylvania show that in 1997 rural areas of the state saw 8,610 new residences go up, while the number in urban areas was nearly three times higher (24,900).

The three brief articles that follow outline some initiatives currently under way in rural parts of Pennsylvania and Delaware that attempt to solve some of these problems, as well as others, to make affordable housing more accessible to people who live far beyond the city's boundaries.

### ***Delaware Nonprofits Form Consortium to Meet Special Challenges of Rural Housing***

Seven nonprofit developers in Delaware have realized the truth in the saying about strength in numbers.

After discussing the difficulties involved in rural development in Delaware at a roundtable sponsored by NCALL Research in Dover, Delaware, these seven groups discovered that they all faced similar barriers in trying to develop housing in rural areas: lower incomes and a wider affordability gap in the rural part of Delaware, fewer government housing

resources, and a higher rate of substandard housing. Consequently, the seven formed the Delaware Rural Housing Consortium.

The consortium provides its members with increased access to technical assistance on housing development, fund-raising for operations and housing development, strategic planning, product development, networking, and pre-development funds. This year, the consortium is seeking to establish an endowment fund to support the housing development work of its members and plans to campaign for additional state and other resources for rural housing. It also plans to



***Better Homes of Seaford, Inc., developed a 27-unit project for the elderly and a community center with assistance from the Delaware Rural Housing Consortium. Better Homes is developing another 26-unit residence for senior citizens. Both projects are in Seaford, Delaware.***

expand a fund of last resort to help families faced with eviction retain their homes.

Joe L. Myer, executive director of NCALL Research, a nonprofit housing developer, said in an interview, “Alone, we have tunnel vision. Together, we think creatively. I find that some of our most creative time is spent in our monthly steering committee meetings.” He recalled that Better Homes of Seaford articulated the need for additional financing to double the capacity of a multipurpose community center that’s part of an 88-unit project being developed for the elderly. A fund-raising consultant retained by the consortium proposed a grant campaign and raised \$87,000 from two foundations and the Greenwood Trust Company. Today, the center is the nucleus for a dozen key services to residents. The consultant separately raised \$25,000 for a hardship fund for one of the developments in the project.

Myer explained that a consortium work group is studying ways in which rental housing in rural Delaware can be made more affordable. One concept under exploration is that of a rural rental trust in which an endowment would provide a stream of earnings for operations of selected developments. Myer said that NCALL had developed a 28-unit complex in Snow Hill, Maryland, employing such a concept.

NCALL Research is the administering agency for the consortium, which initially was funded by a half-dozen Delaware foundations. The consortium members are Appoquinimink Development, Inc. (ADI), Middletown; NCALL Research, Inc., Dover; Delmarva Rural Ministries, Inc., Dover; Milford Housing Development Corporation, Milford; Better Homes of Seaford, Inc., Seaford; Millsboro Housing for Progress (MHP), Millsboro; and the Interfaith Mission of Sussex County, Inc., Ocean View. ADI and MHP are all-volunteer nonprofits.

***For further information, contact Joe L. Myer, Executive Director, NCALL Research, Inc., P.O. Box 1092, Dover, DE 19903; Telephone: (302) 678-9400; web site: [www.ncall.org](http://www.ncall.org)***



***This 16-unit two-bedroom project for residents 55 and over in Mifflinburg, Pennsylvania, was developed using the USDA’s Rural Rental Housing Program and the Federal Home Loan Bank of Pittsburgh’s Community Investment Program. West Milton State Bank helped finance the project.***

#### ***USDA Introduces Two Programs for Rural Housing***

The United States Department of Agriculture (USDA) has announced two new tools to help ease some of the problems faced by developers of rural housing.

The first, the Rural Direct Loan Leveraging Program, allows the USDA to offer funding jointly with lenders of single-family mortgages in rural areas.

Under this new program, participating lenders may hold and service their portion of the financing, or they may sell that portion to Fannie Mae. Two sets of loan documents are required. Loan amounts may not exceed HUD’s maximum mortgage limits for a county, in effect as of September 30, 1998.

USDA has selected two nonprofit organizations in Pennsylvania—the Housing Development Corporation (HDC) in Lancaster, Pa., and the Alliance for Better Housing (ABH) in Kennett Square, Pa.—for a set-aside within the leveraging program. USDA will finance about 75 percent to 80 percent of each loan, with the remainder coming from the bank. The set-aside of \$319,000 for HDC and \$490,667 for ABH represents additional funding for the USDA portion of loans.

The two nonprofits are counseling applicants and packaging loans under this program. HDC is working with Fulton Bank, which is providing first mortgages, usually through the Pennsylvania Housing Finance Agency, and with the Lancaster Housing Opportunity Partnership, which is providing down payment

assistance through HOME funds. Meschelle Sensenig-Roten, director of Home Sales at HDC, estimated that the set-aside would enable five buyers to purchase homes. Using set-aside funds, HDC has developed and is currently marketing a 98-unit townhouse subdivision in Manheim Township, Lancaster County, Pa.

Alliance for Better Housing, working in partnership with The Peoples Bank of Oxford, in Oxford, Pa., will use the set-aside to assist in home purchases by seven or eight additional low-income first-time buyers, according to ABH's president, Howard Porter.

***For further information on this USDA program, contact Frank Wetherhold, Single Family Housing Program Director, USDA, Rural Development, One Credit Union Place, Suite 330, Harrisburg, PA 17110; Telephone: (717) 237-2279; E-mail: [fwether@rdmail.usda.gov](mailto:fwether@rdmail.usda.gov)***

The second new tool from the USDA's Rural Housing Service attempts to meet the difficult challenge of developing rental housing in rural areas. The Section 538 Guaranteed Rural Rental Housing Program allows lenders to underwrite and originate



***James Thomas, executive director of the Columbia County Housing Authority, congratulates Cathy Gipe, who bought her first house with the assistance of the authority's down payment and closing cost program. At far right is Vonda Laubach, assistant treasurer of First Columbia Bank and Trust Company.***

loans in eligible rural areas, to perform all loan-servicing functions, including asset management and liquidation, and to monitor rent levels. The program provides lenders with loan guarantees of up to 90 percent.

Loans can be used for new construction, moderate or substantial rehabilitation, acquisition of buildings that meet special housing needs, combination construction and permanent loans, and construction of a wide variety of housing types, including mobile homes and congregate housing. Tenants' income must be below 115 percent of the area's median income at the time of initial occupancy; no income verification is required afterward. Rents must not exceed, on average, 30 percent of the area's median income, adjusted for family size.

Guarantees may be used in conjunction with other subsidy programs, such as the low-income housing tax credit program. Eligible lenders are FHA-, Fannie Mae-, and Freddie Mac-approved multifamily lenders and others with multifamily lending experience.

Robert P. Yoder, Sr., vice president of Warrior Run Development Corp., in Turbotville, Pa., said in an interview that he thought the program would become a key to rural development in the future, especially since federal appropriations for direct funding of rental developments have been steadily declining. Yoder expects that banks, which have not been very active in rural multifamily development for the past decade, will show significant interest in the program. He observed that banks and mortgage companies that previously provided only single-family financing are now taking a look at multifamily lending.

Banks that are members of the Federal Home Loan Bank System can apply for Community Investment Program (CIP) funds in Section 538-financed projects, thereby controlling their interest rate and credit risk, Yoder said. Both Section 538 and the CIP can serve residents with up to 115 percent of area median income, allowing the two programs to be used harmoniously. CIP funds represent critical interest rate savings on project development costs and make it possible to charge lower rents, Yoder explained.

In fact, Warrior Run is already working with three different community banks in Pennsylvania on



***Photo shows the interior of one of the townhouses in Manheim Township, Lancaster County, developed by the Housing Development Corporation, Lancaster, Pa.***

developments using the two programs. West Milton State Bank is helping to finance a 16-unit project for residents 55 and over in Mifflinburg, Pa. Jersey Shore State Bank, Williamsport, Pa., is financing an eight-unit family complex in Lock Haven, Pa. Columbia County Farmers National Bank, Bloomsburg, Pa., is financing a 24-unit local complex for residents 55 and over.

***For further information on the Section 538 Guaranteed Rural Rental Housing Program, contact Gary Rothrock, Multi-Family Housing Program Director, USDA, Rural Development, One Credit Union Place, Suite 330, Harrisburg, PA 17110, Telephone: (717) 237-2281; E-mail: [grothroc@rurdev.usda.gov](mailto:grothroc@rurdev.usda.gov)***

### ***Housing Authority Program in Rural Pennsylvania Assists First-Time Buyers***

An unusual first-time homebuyer program involving a local housing authority and community banks in Columbia County, Pa., has enabled 105 low- and moderate-income buyers to purchase homes that they otherwise could not afford.

The Columbia County Housing Authority (CHA) initiated a down payment and closing cost assistance program in 1991 using its excess funds and grants from the state and from Pennsylvania Power and

Light, one of the state's major utility companies. The program has provided an average of about \$5500 in deferred-payment second mortgage loans to income-eligible buyers who have purchased houses costing about \$55,000, explained Jim Thomas, the authority's executive director. Many times, these families' rental expenses are higher than the new mortgage payment.

Buyers obtain financing from area banks or nonbank mortgage companies. The banks have been very cooperative in working with the program, Thomas commented. The most active banks since the program's inception, Thomas said, include Columbia County Farmers National Bank, First Columbia Bank & Trust Co., The First National Bank of Berwick, First Federal Bank (based in Hazleton, Pa.), and PNC Bank, N.A.

Lenders assist applicants in completing the application form and forward it and supporting documentation to the authority, which reviews the application and determines eligibility. The authority issues a letter of eligibility to applicants and sends copies to the lender.

Paul E. Reichart, president and chief executive officer of the Columbia County Farmers National Bank in Bloomsburg, Pa., said that the program has been quite successful and that delinquencies are rare.

Reichart, who is chairman of CHA, said that the program would be substantially funded in the future with Act 137 (the Pennsylvania County Housing Trust Fund Program) transfer tax payments to the county. Reichart has been a CHA board member since its founding in 1969.

Enhancements to the program include a home ownership education program that will be instituted this year and modeled after a home owner institute operated by the Union County Housing Authority. Reichart added that one challenge is to increase awareness of the program among buyers and real estate agents.

Ed Christiano, executive director of the Northumberland County Housing Authority and president of the Eastern Pennsylvania Association of Housing Authorities, said that Northumberland's was the only other home buyer assistance program operated by a housing authority in the 36-member association. That program, which provides closing costs but not down payment funds, has assisted about

45 families since it was started in 1995.

Christiano explained that an increasing number of housing authorities are looking for additional financial resources and are interested in working in partnership with banks. For example, the Northumberland authority is looking to work with banks that might donate or negotiate sale of defaulted properties to the authority, which in turn would make repairs and sell them to low- or moderate-income buyers, he said.

***For information on the Columbia County program, contact Jim Thomas, Executive Director, Columbia County Housing Authority, 700 Sawmill Road, Bloomsburg, PA 17815; Phone: (717) 784-9373. For information on the Northumberland County program, contact Ed Christiano, Executive Director, Northumberland County Housing Authority, 50 Mahoning Street, Milton, Pa. 17847; Telephone: (570) 742-8797***

***Keith Rolland wrote this article.***

## ***Ways to Work Program Gets Help from Consortium of Banks in South Jersey***

Twelve financial institutions that serve southern New Jersey have entered into a ground-breaking consortium with Family Service Association (FSA), a private nonprofit community-based agency headquartered in Absecon, New Jersey, to implement the Ways to Work Family Loan Program.

Ways to Work is an innovative program that has proven to be effective in helping families move from welfare to work. In a cooperative effort between the national Alliance for Children and Families in Milwaukee, Wisconsin, and the McKnight Foundation of Minneapolis, Minnesota, the successful 14-year-old program is now being replicated in other sites throughout the nation.

The purpose of the program is to provide small loans to low-income parents who are making the



***Twelve financial institutions are contributing funds to the Family Service Association's loan pool and/or operating expenses. Shown (left to right) are Vincent Nolan, Vice President, First Union National Bank, Camden, N.J.; Peggy Massey, Vice President, The Woodstown National Bank and Trust Company, Salem, N.J.; Dawn Kosko, Vice President, Summit Bank, Brigantine, N.J.; Theresa Lance, Branch Manager, Fleet Bank, N.A., Absecon, N.J.; Joyce Harley, Senior Vice President and Community Development Officer, Fleet Bank, N.A., Newark, N.J.; and Keith Rolland, Community Development Advisor, Federal Reserve Bank of Philadelphia.***

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## **Credit Scoring ...continued from page 3**

Thus, scores for these populations may not reliably assess individual risk.

In addition, the data on which the scoring system is based need to include both well-performing and poorly performing loans and must be up-to-date. Builders of credit-scoring models report that a model's performance deteriorates over time and that periodic validation is necessary. For example, if a lender that uses scoring increases its applicant pool through mass marketing, the lender must ensure that the new pool of applicants behaves similarly to the pool on which the model was built. Indeed, according to the Equal Credit Opportunity Act, a credit scoring system must be "periodically revalidated by the use of appropriate statistical principles and methodology and adjusted as necessary to maintain predictive ability."

Another concern is whether scoring models that were developed during good times will work if the economy takes a turn for the worse. Those who create scoring models acknowledge that applicants, as a group, will tend to score lower because characteristics used in the model will reflect the change in behavior brought about by difficult economic times. However, they point out, the user of a scoring model can adjust the cutoff score. Furthermore, regardless of the underwriting process, whether judgmental or scoring, a downturn in the economy will result in a greater

number of defaults and denials than one would expect to experience in relatively good times. Nevertheless, the concern remains that the model itself may not be valid in a declining economy.

### **Who's Using It**

In spite of the ongoing debate, credit-scoring models are gaining in popularity and sophistication. In 1995, both the Federal Home Loan Mortgage Corporation (Freddie Mac) and the Federal National Mortgage Corporation (Fannie Mae) encouraged mortgage lenders to use credit scoring. Also in 1995, Fair, Isaac and Company, Inc., a major provider of credit-scoring models, introduced its Small Business Scoring Service (SBSS).

In 1997, Fair, Isaac and Company, Inc., and CRI ProServices, Inc., announced that they would offer a credit analysis tool that would increase the speed and efficiency of underwriting small-business loans and, ultimately, would enable financial institutions to take advantage of small-business loan securitization services, allowing the loans to be rated and sold in the secondary market.

Despite the enhanced sophistication of the models, many people, including some bankers and community leaders, remain skeptical that the objectivity in scoring will benefit low-income individuals. However, surveys of various databases conducted by Freddie Mac

and Fair, Isaac show that credit scoring, when compared to judgmental screening, would have provided a substantial increase in acceptance rates. Also, three economists at the Board of Governors of the Federal Reserve analyzed a large sample of mortgage loans and showed that the relationship between a borrower's income and loan performance appeared to be slight. Credit score and, to a lesser extent, loan-to-value ratio appeared to be much stronger predictors of foreclosure rates. The fact remains that people with lower credit scores pose higher risks to lenders.

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**Sources used for this article were:**  
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**Fair, Isaac and Company, Inc. "Low to Moderate Income and High Minority Area Case Studies," *Discussion Paper* (August 26, 1996).**  
**Mester, Loretta. "What's the Point of Credit Scoring?" *Business Review, Federal Reserve Bank of Philadelphia* (September/October 1997), pp. 3-16.**

**Don James wrote this article and the accompanying box on fair lending issues.**

## **City of Bethlehem and ABC Join Forces On the Bethlehem Home Ownership Project**

Alliance for Building Communities (ABC), a nonprofit organization based in Allentown, Pennsylvania, and the City of Bethlehem have

teamed up to renovate and "deconvert" 15 houses, 10 on Bethlehem's South Side and five on the city's West Side. Other partners in the

Bethlehem Home Ownership Project are the Northampton County Housing Trust Fund, the Community Action Committee of the Lehigh Val-



***This house on West 4<sup>th</sup> Street in Bethlehem, Pennsylvania, was renovated and deconverted through a program sponsored by the Alliance for Building Communities.***

ley, and First Union, Lafayette Ambassador, and Summit banks.

According to Ed Pawlowski, executive director of ABC, deconversion, which involves restoring to single-family dwellings houses that have been chopped up into apartments, presents its own set of challenges. In addition to the usual rehabilitation needs—new roof, rewiring, paint—contractors must also contend with taking out extra kitchens and bathrooms, removing dividing walls, and restoring utilities to one-household use.

Furthermore, it's harder to keep costs to a minimum with deconversion projects. For one thing, Pawlowski points out, there's a fixed amount of subsidy per house, so deconversion efforts are often more difficult than other nonprofit housing ventures.

However, deconversion has two primary benefits: it cuts down on urban density and provides roomy, but affordable houses for low-income people with large families.

Most of the properties acquired

were in bad shape. Pawlowski attributes the deterioration, at least in part, to the fact that most of them were rental units. He noted that cities tend to have "huge rates of renting. In Bethlehem, the figure is about 51 percent." Rates are even higher in Allentown, where Pawlowski has completed a similar project involving 12 houses, and they're higher still in Reading, where ABC has set its sights for its next venture. He blames some of this high rate on the collapse of the housing market in the 1980s. Back then, one way to pay off the mortgage on a large house was to create several rental units out of the dwelling.



***Interior of a house renovated by ABC.***

Consequently, Pawlowski thinks, many people "became reluctant landlords, and properties deteriorated, either intentionally or unintentionally."

Helping ABC finance the costs of the renovations—thereby keeping these properties affordable for low-income people—are the other partners involved in this project. First Union is providing a \$500,000 line of credit and Lafayette Ambassador a \$250,000 line, both collateralized against 80 percent of the value of the rehabilitated structures. Lafayette also sponsored the project’s application to the Federal Home Loan Bank of Pittsburgh, which contributed a \$67,500 grant to reduce the acquisition price of houses purchased for the program. Summit Bank has sup-

plied a \$10,000 grant for home-buyer counseling. In addition, the City of Bethlehem is kicking in a \$20,000-per-house subsidy, and the Northampton County Trust Fund is contributing an additional subsidy of \$2000 per house.

The Community Action Committee of the Lehigh Valley is performing energy audits on all the properties, and all will have updated, efficient energy systems.

Ultimately, Pawlowski observed, the project has three main purposes: revitalizing the community, reducing density, and providing

large, affordable living space for low-income families. He added, “If we concentrate on an eight-block area on Bethlehem’s South side where there might be 100 houses, and we re-do 10 or 15 of them, that has an impact.”

***For more information about ABC and its projects, contact Ed Pawlowski, Alliance for Building Communities, 830 Hamilton Mall, Allentown, PA 18101; (610) 439-7007.***

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## **Ways to Work Program ...continued from page 8**

transition from welfare to work and who cannot get loans elsewhere. The loans are designed to help family members succeed in their jobs. Loans can be used to pay for clothing, transportation, or unexpected expenses that could interfere with a family member’s ability to keep a job or stay in school.

The consortium that has been developed in South Jersey, with the assistance of the Federal Reserve Bank of Philadelphia, is unique in that it will serve a larger geographic area than the other Ways to Work sites. The program is available to families who live in Atlantic, Burlington, Camden, Cape May, Cumberland, Gloucester, and Salem counties.

The banks that have contributed to the loan pool and to operating expenses for the innovative venture are The Bank of Gloucester County,

Cape Savings Bank, Commerce Bank, N.A., Equity Bank, N.A., The First National Bank of Elmer, First Union Foundation, Fleet Bank, N.A., The Pennsville National Bank, Summit Bank, Sun National Bank, and The Woodstown National Bank & Trust Company. Also providing support for operating expenses are the Sovereign Bank Foundation; the Gold Foundation; the Atlantic City Hilton; Bally’s Park Place, a Hilton Casino Resort; and the Showboat Casino Hotel.

A 10-year evaluation of program operations in Minneapolis showed that transportation in and of itself was key to helping people keep their jobs and stay in school. Also, while approximately three-fourths of the borrowers were receiving governmental aid at the time of their loan application, their use of public assistance dropped 40

percent within two years. Fewer than 1 percent of the borrowers have become new users of public assistance since getting their loans. Repayment rates in some areas have reached 90 percent, but the average in metropolitan areas is about 76 percent.

The program is based in FSA’s Consumer Credit Counseling Service of South Jersey. Successful program applicants will receive credit and budget counseling.

***For more information on the Family Loan Program, contact Jerome Johnson, President and Chief Executive Officer, Family Service Association, or Tony Marinaccio, Manager, Consumer Credit Counseling Service of South Jersey, 312 E. White Horse Pike, Absecon, NJ 08201; Telephone: (609) 652-2377.***

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For program and registration information, please contact Cynthia Burnett Howard at (415) 974-2968.

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