



# Technical Briefs

*Federal Reserve Bank of Philadelphia  
Community Affairs Department*

## **Home-Improvement Loans: The Homeowner Housing Rehabilitation Loan Program**

In recent years, there has been a great deal of emphasis on creating first-time home-buyer programs for low- and moderate-income individuals and families. Offering below-market rates, waiving private mortgage insurance, and expanding qualifying ratios are some of the ways that lenders help people who would not otherwise qualify to buy a house. Creating home-improvement loan programs for low- and moderate-income people, however, has not normally been a priority, despite the fact that many home owners may not otherwise be able to afford needed repairs.

According to the 1990 Census, 23.1 percent of the population of Johnstown is 65 years of age or older, compared with 15.4 percent in the entire state of Pennsylvania, which has the second-highest number of senior citizens of any state. Many of the seniors are on fixed incomes and make up part of the 56.5 percent of the city's low- and moderate-income households. In fact, 28.1 percent of the city's households are below the poverty level, and 16.1 percent receive public assistance. When one considers as well that the median age of Johnstown's housing stock is more than 60 years old, it is clear that some type of home-improvement loan program targeted at low-income borrowers is needed.

In response, Johnstown's Department of Community and Economic Development identified this need and created the Owner-Occupied Rehabilitation Program in 1981. Using community development block grants (CDBG) from the U. S. Department of Housing and Urban Development (HUD) and HOME funds from the Pennsylvania Department of Community and Economic Development, the city offers loans to low- and moderate-income home owners in Johnstown for correcting code violations and improving energy conservation. The maximum loan amount is \$15,000, and the maximum term is seven years. The interest rate is 0 percent, and no monthly payments are required. Repayment of the principal may be forgiven if the property remains free of code and energy violations and the borrower owns and occupies the property for the term of the loan. This loan program proved to be very popular and, by the fall of 1998, had a three-year waiting list.

Because the city wanted to shorten the waiting list, it asked U.S. Bank, headquartered in Johnstown, to join it in offering another program—the Homeowner Housing Rehabilitation Loan Program—which was introduced in March 1999. Under this program for low- and moderate-income borrowers, the city uses HOME funds, which must be matched dollar for dollar by the home owner. In providing the match, the home owner may borrow funds from a special installment-loan pool provided by U.S. Bank. The maximum amount of HOME funds available per borrower is \$7500 at 0 percent interest for a maximum term of seven years. The city's portion of the loan is forgiven if the borrower occupies the property for the entire term of the loan and keeps the property free of code violations after repairs have been completed. U.S. Bank's portion of the loan, which is also capped at \$7500, is provided at 1 percent below its normal market rate for home-owner rehabilitation loans with a maximum term of 10 years. The borrower, who is subject to U.S. Bank's normal underwriting criteria, may choose a shorter repayment period or may elect to repay the loan ahead of schedule with no prepayment penalty.

To learn more about how to develop a program like this in your region, please contact:

Dede Myers  
Vice President and Community Affairs Officer  
Federal Reserve Bank of Philadelphia  
10 Independence Mall  
Philadelphia, PA 19106  
(215) 574-6482  
Dede.Myers@phil.frb.org

See program specifications on next page.

Use of Proceeds	Correcting code violations and improving energy conservation. If these deficiencies are corrected, the loan may, in some cases, be used for general property improvements. The loan may not be used to refinance existing debt.
Loan Size	\$15,000 for single-family home and \$20,000 for two-unit structure where one unit is owner-occupied.
Product Type	Home-improvement loan. City of Johnstown's portion is a 0 percent interest-deferred loan with maximum seven-year term. Loan forgiven if borrower owns and occupies the home as his/her principal residence for term of the loan and keeps the property free of code violations. U.S. Bank portion is fixed-rate loan at 1 percent below the bank's normal market rate with maximum term of 10 years.
Risk Sharing and Collateral	There are two separate loans, but only one application is completed, which is done at the city's office. The bank's loan is 50 percent of the proceeds, and the lien on the borrower's residence is in first position. The city's deferred loan is 50 percent of the proceeds and the lien is in second position.
Underwriting	U.S. Bank conducts a credit investigation according to normal procedures. If credit is approved, a property appraisal is conducted containing pre-rehabilitation and post-rehabilitation values. If appraisal is approved by U.S. Bank guidelines, the city will proceed with loan application.
Construction Specifications	A city inspector conducts a full inspection of the property and prepares a detailed cost estimate that the borrower reviews and approves. The city assists the borrower with the choice of contractors to whom bid proposals are sent. At least three bids must be made, and the city awards the contract to the lowest responsible (within 15 percent of the estimate) bidder.
Documentation	Borrower provides standard documentation normally requested for collateralized loan, including proof that city, county, and school property taxes have been paid for the previous two years. Borrower must provide property insurance in an amount equal to the loan amount and list U.S. Bank as loss payee on the insurance policy. The city is not listed as loss payee.
Applicant Requirements	Must be home owner within the city limits of Johnstown. Income eligibility is based on most recent HUD Section 8 income guidelines for the city of Johnstown, with adjustments for the number of people in the household. Applicant must also meet U.S. Bank's underwriting requirements.
CRA Test	Loans should earn lending test credit, and the program may receive credit as an innovative or flexible lending practice. However, lenders should contact their regulatory agencies.
Program Performance	From inception in March 1999 through September 15, 2000, 21 loans, totaling \$141,191 of city funds and \$153,373 of bank funds, were closed. There have been no defaults. More loans would have been made, but the city expended all of its allotted state and federal HOME funds in 1999 and 2000.
Lenders	City of Johnstown, U.S. Bank, and Northwest Bank, which signed participation agreement in November 2000.
Program Information	To learn more about this program, contact Kelly Barger, Residential Development Officer, city of Johnstown, (814) 533-2046, or Michael Roth, Assistant Secretary and Loan Officer, U.S. Bank, (814) 255-9633.

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FEDERAL RESERVE BANK OF PHILADELPHIA