

Shared Equity Ownership Initiative

Homeownership remains a major goal for low and moderate income households seeking to increase housing stability, independence and wealth. Affordable home ownership remains a major goal for state and local governments to promote vibrant, stable neighborhoods; reduce poverty; and secure their tax base. Creating affordable homeownership, however, has grown more difficult. Median home prices increased by over 60% between 1996 and 2006 while median income increased by just 35%.

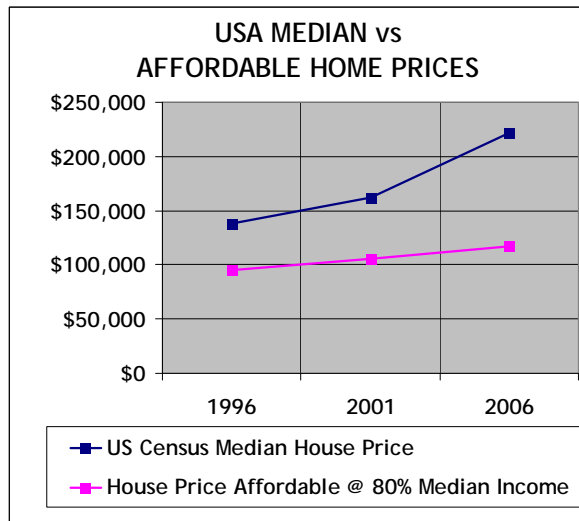


CHART 1

The graph in Chart 1 shows two important, distinct points. First, focusing on the blue line, our current foreclosure crisis notwithstanding, there is a longer running trend over the last several years that the price of a single family house is going up faster than in the past and much faster than incomes. These rapid price increases mean that it is taking more subsidy money every year to fill the gap between what people can afford and what housing costs.

Second, focusing on the pink line, when the increase in the prices of some housing is limited, so that certain housing remains affordable to families at 80% of the median income, not only does the house remain affordable, but also, the gradual price increases that do occur create an opportunity for the owners to build real wealth over time.

State and local governments have stepped up efforts during the last few years in the creation of affordable homeownership programs, in part to let more Americans in on the opportunity to use their housing to build wealth. The number of reduced rate mortgages provided through state housing finance agencies has been slowly increasing to over one hundred thousand nationally. Additionally, 40% of Federal block granted HOME funds are used to subsidize homeownership opportunities for low-income families, representing a substantial increase from the nominal 3% of 1992. The average amount of HOME assistance per unit has also grown to over \$25,000 in 2005.

Despite these efforts, the homeownership rate has been declining since 2004, particularly among African American families. That rate is likely to continue to decline as foreclosures increase and credit standards tighten in reaction to the mortgage crisis. Private sector efforts to meet the demand for affordable homeownership led to the growth of sub-prime loans (from 8.6% of mortgages in 2001 to over 20% of mortgages in 2005) and adjustable rate mortgages (from 13% of mortgages in 2003 to 35% in 2005), have clearly backfired. The resulting backlash has made affordable homeownership increasingly difficult. In light of the growing public cost of affordable ownership and the time, land and other resources required to create affordable ownership units, we believe the current models in which a city merely either forgives or recaptures subsidy no longer make sense.

Chart 2 shows that the amount of subsidy required to develop affordable ownership more than doubled from 1996 to 2006, increasing from \$42,880 to \$104,736 per unit.

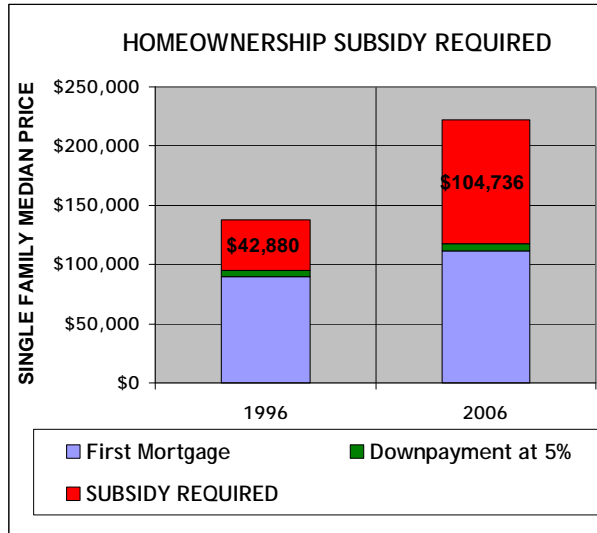


CHART 2

A Growing Alternative

In reaction to these trends, state and local government agencies are increasingly looking at Shared Equity homeownership. Shared Equity Ownership - community land trusts, deed restricted housing, and limited equity cooperatives - is a model where the increase in property value is shared between the homeowner and the general public; the home is priced to be permanently affordable.

Shared Equity Ownership housing creates a balance between homeowner wealth accumulation and the public interest in permanent affordability. The resale price of Shared Equity Ownership homes is restricted - to permit increases either based on an index (median income or wage rates, for example) or as a percent of the market value appreciation.

Over 800,000 Shared Equity Ownership homes have been developed during the last 25 years - and the numbers are growing rapidly. The number of community land trusts has increased from approximately 150 in 2000 to close to 200 today. Over 100 cities have adopted some form of deed restricted housing. Several large cities including San Francisco, Chicago, Irvine and Denver have recently begun large scale Shared Equity Ownership programs, often in conjunction with inclusionary housing or large subsidy programs.

Why Shared Equity?

Shared Equity homeownership provides several advantages to both the local government and to low and moderate income homeowners that have made it an appealing option. For a city or state government the advantages include:

- ❑ **Maximizes Subsidy:** The subsidy provided under a Shared Equity Ownership program maintains the house as permanently affordable - for the first and future home buyers. Under most existing homeowner programs a new subsidy - often at an ever increasing amount as home prices increase - is required for every subsequent buyer.
- ❑ **Promotes Stable Market:** During periods of upswing, large numbers of affordable homes are lost - during downswings lower income neighborhoods often experience a high number of foreclosures, typically resulting in decreased investment and property values. For example, a 2006 Georgia Tech study found that within an eighth of a mile radius, property values of single family homes declined by between 0.9% and 1.44% per foreclosed home. In Shared Equity Ownership programs, speculation is reduced and property value increases are stable, thus moderating the artificial price spikes and inevitable bursting bubble associated with the real estate market;

- **Lowers foreclosure and delinquency rates:** Several studies have found foreclosure rates to be far lower for Shared Equity Ownership than the general market. A recent survey of 2,500 low and moderate income community land trust homeownership transactions showed that only 17 out of 2,500 went to foreclosure in the last decade, including only 2 last year for a 2007 foreclosure rate of .06%. By comparison, in the 4th quarter of '07, the annual foreclosure rate for all U.S. mortgages was 2.0%, with some areas running as high as 3.4%. In recent stable years foreclosure rates for all U.S. mortgages have run a little over 1%. Shared Equity Ownership reduces both the substantial costs associated with foreclosures and the negative community impacts discussed above;
- **Promotes economic integration:** In a Shared Equity Ownership program, a home is kept permanently affordable, even if it is in a neighborhood that is otherwise facing escalating property values. In recent years many Shared Equity Ownership programs have developed in conjunction with inclusionary housing, further promoting economic integration;
- **Prevents the “preservation challenge” of the future:** Increasingly cities and states are struggling with preserving affordable housing - expiring HUD mortgages, expiring tax credit, and other subsidized properties are either being lost to the affordable housing stock or require substantial additional subsidy to maintain as affordable. Through Shared Equity Ownership the homes are preserved as affordable in perpetuity.

The benefits of Shared Equity Ownership to the *homeowner* include:

- **Increased stock of affordable homeownership opportunities:** A Shared Equity Ownership home will remain affordable in perpetuity. Thus each new home developed will become part of an ever increasing affordable housing stock available to aspiring homeowners;
- **Safe, level monthly mortgage payments:** The initial and future home buyers of a Shared Equity Ownership home make monthly payments that are underwritten to be affordable. Even though purchasers are lower income, in Shared Equity Ownership, mortgages are on standard terms and at market rates, rather than exotic terms and sub-prime rates. The below market price for the home usually eliminates the cost of private mortgage insurance. Many localities also ensure property tax assessments are based on restricted, rather than market price, lowering property taxes. At market prices, many would be tempted to succumb to gimmicks that leave them at greater risk of default;
- **Equity appreciation and wealth creation:** Shared Equity Ownership is designed to build wealth for residents, both through home value appreciation and through mortgage pay-down. While the loan pay-down is usually more gradual than the market appreciation, programs are designed to ensure residents receive sufficient equity appreciation to enable real wealth accumulation.

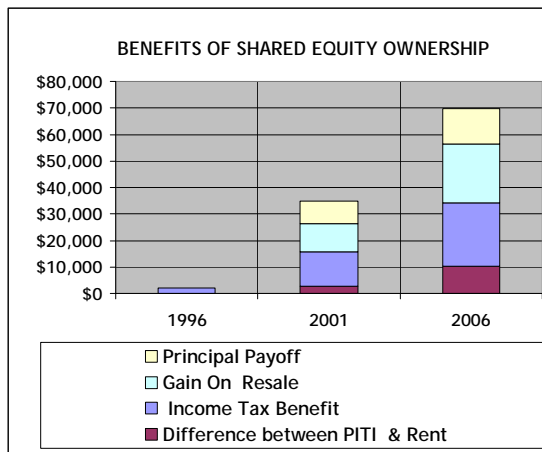


Chart 3 shows the wealth accumulation possible over ten years on a home purchased in 1996 by a family earning 80% of the U.S. median income at that time, \$33,120. That family could afford a house costing \$94,766. Totaling all of the benefits, including only 25% of the gain on resale, this family would have increased their wealth by over \$35,000 after 5 years and by almost \$70,000 after 10 years;

- **Shared responsibility:** Many Shared Equity Ownership programs include post-purchase assistance to homeowners. This can range from providing reduced rate loans for home improvements, to bulk purchase of fuel or insurance, to homeowner association rules for neighborhood improvement.

Shared Equity: Key Elements of Success

One of the keys to achieving scale is to have more standardization of the development and lending processes and documents. While local choice remains important, there should be enough standardization in the model to ensure that all of the key functions are expertly performed in each community. Further, localities across the country should have a shared understanding of the key functions, sufficient to allow them to exchange best practices and benchmark their performance against one another.

A comprehensive Shared Equity Ownership model will produce more units than current models and unlike most traditional models for serving new homeowners, the Shared Equity Ownership units will remain permanently affordable. Further, by creating a critical mass of ownership units, other local community development efforts will be bolstered, such as commercial development that meets the needs of a neighborhood. Based on the experience of existing Shared Equity Ownership, we believe every strong, long-term sustainable Shared Equity Ownership program must have four essential components:

- **Affordability Steward:** A local Affordability Steward is a combination of nonprofit, for-profit and government partners who collaborate to ensure the community has all four requisite elements of a successful Shared Equity Ownership strategy. The Affordability Steward should be substantially funded through monthly homeowner fees, financial packaging fees, home sales and resale fees. In most cases, the Affordability Steward will require on-going subsidy to supplement its revenue. There are three crucial functions that a local Affordability Steward must provide:
 - **On going enforcement of resale restrictions and any equity recapture:** Permanent affordability requires active enforcement. Self-enforcement is not sufficient. Resale price or equity appreciation formulas often require precise calculations. Permanent affordability requires the incomes of prospective purchasers to be verified. Some programs provide an option for the Affordability Steward to have a right of first refusal to purchase the property and then resell as a further protection of permanent affordability.
 - **Asset Management:** Ensuring Shared Equity Ownership housing stock remains in good repair and is a community asset is crucial. Homeowners often need support to better understand maintenance and budgeting. Homeowners must have access to reduced rate capital, particularly in Shared Equity Ownership models that do not permit resale formula adjustments for home improvements. Several models, in particular the community land trust and limited equity cooperative models, incorporate structures that facilitate active resident involvement in asset management of the housing/land. Alternatively, if owners do not properly maintain their units even with incentives, the affordability steward can retain the right to claw back more of the capital gain to cover maintenance that was not done.
 - **Local Leadership and Public Policy:** A critical role of the Affordability Steward is to be the local champion for Shared Equity Ownership. Local developers, lenders, realtors, and policy makers need to understand the product and be involved. Eligible home owners need to understand the program and its advantages, as well as responsibilities. The Affordability Steward needs to devise policy and program parameters, including the equity recapture formula and the legal method for enforcing it. The Affordability Steward provides the on-going leadership and enlists the various partners to ensure the success of the Shared Equity Ownership housing program.

The local Affordability Steward also monitors how the community is doing at maintaining the other three essential functions that are performed primarily by the private market, but that may also require some government subsidy or other role:

- ❑ **Production capacity**: In most communities, Shared Equity Ownership will be a new concept. Since it is targeted to low and/or moderate income households, lower developer profits than market rate homes are likely. Developers need to be educated about Shared Equity Ownership and recruited to build. Communicating with developers early in devising a program assists in creating a model more easily adopted by the market;
- ❑ **Financing and underwriting expertise**: Similar to other affordable housing, Shared Equity Ownership housing requires complex combinations of private and government subsidy financing. Local lenders need to understand how Shared Equity Ownership works and understand how the loans can meet their underwriting requirements. Programs work best where government and private financing are able to be jointly underwritten and easily combined both for the developer and the home buyers;
- ❑ **Homebuyer identification and preparation**: Preparing low and moderate income households to understand the process and obligations of homeownership generally, and Shared Equity Ownership in particular, is a key component for success. Credit repair and education is often required. Many Shared Equity Ownership programs include homeowner involvement or shared responsibilities, which need to be explained and fostered. Having a pipeline of ready and interested buyers assists in both initial sale and re-sale. Most cities and regions already have active homeowner training and counseling programs whose curriculum can be supplemented for Shared Equity Ownership buyers.

The Role of NCB Capital Impact

NCB Capital Impact believes that Shared Equity Ownership will be a significant part of the affordable housing solution and is the most sensible public policy for promoting homeownership for low and moderate-income households. As a national nonprofit organization with a mission and history of creating new systems to reduce poverty, including extensive technical assistance and financing for limited equity cooperatives, we intend to work with local and national partners to foster Shared Equity Ownership strategies.

Specifically, NCB Capital Impact will provide technical assistance, facilitate local and national planning, and invest financing in programs designed to create scalable Shared Equity Ownership housing. We intend to work in markets where there is public and private support for Shared Equity Ownership to assist in the formation of Affordability Stewards, develop strategic and business plans, enlist the involvement of development partners, create financing systems, develop required documents and curriculums, start-up community land trusts, deed restricted housing, and limited equity cooperatives.

As we all look for strategies to avoid repeating the market disruptions we are currently experiencing, NCB Capital Impact submits that it will be far better for everyone in the long run - consumers, the real estate industry, and the public interest -- if affordability gaps for marginal first-time homebuyers are closed with Shared Equity Ownership tools, such as a soft second mortgage, instead of exotic and risky loan products, such as those that led to the current foreclosure crisis.

For more information on Shared Equity Ownership, please contact: Jim Gray, jgray@ncbcapitalimpact.org; Jay Marcus, jmarcus@ncbcapitalimpact.org or Jon Kelly, jkelly@ncbcapitalimpact.org