

## Conventional Financing for Manufactured Homes

### Consider the Future of Housing Finance

Submitted to  
U.S. House Financial Services Committee

Submitted by  
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For the past 30 years, CFED has fostered innovations that build wealth for low-income individuals and families. We recognize the important role government and private industry play in promoting and sustaining economic opportunities for all families. We applaud the Committee's call for this hearing to consider the future of housing finance. We appreciate the opportunity to provide you with written testimony on an oft-overlooked segment of the housing finance industry that is critical to many low-income homeowners, particularly those in rural areas: financing for manufactured homes. For more than five-years, CFED, through its Innovations in Manufactured Homes (I'M HOME) initiative, has worked to address challenges in the manufactured housing marketplace and help ensure that all homeowners – regardless of whether their home is manufactured or site-built – have equal access to the asset-building opportunities of homeownership, which includes access to fair, affordable, and responsible home financing.

### Background

Assets are the foundation for promoting long-term economic opportunity for Americans. For the past few generations, homeownership has been the bedrock of household financial assets. The value of a home is the most significant source of wealth for most low- and middle-income households. For 17 million Americans, the path to the American Dream includes a manufactured home. Today's manufactured-housing market offers a high-quality and affordable entry into asset building for many families at a cost of less than half the average square-foot cost of a site-built home.

Manufactured housing represents 66% of new affordable housing produced in the United States. In fact, 26% of low-income homeowners in rural areas and 12% of low-income homeowners nationwide own a manufactured home.

However, obstacles in obtaining conventional mortgage financing for owners of manufactured homes create a roadblock for many because these homes – though as permanent as homes built on site – are often financed more like automobiles than homes. This type of personal property financing is called chattel lending.

Prior to 1995, owners of manufactured housing had few lender options and most of these lenders engaged in chattel lending. As the popularity of manufactured housing increased and the market grew, the number of chattel lenders increased and real property mortgage lenders entered the market more aggressively. During the second half of the 1990s, the number of securities backed by manufactured home loans (primarily chattel loans) doubled in the secondary market. The drive to increase manufactured home sales and lending led to poor underwriting practices, resulting in high default rates and declining profits which led to a market crash not dissimilar to the one facing the overall housing market today.

When reviewing the possibility of expansion of Federal Housing Agency (FHA) financing for manufactured housing in 2007, the Government Accounting Office concluded that very little was known about the causes of loan losses in manufactured housing due to a lack of adequate tracking of risk factors by the agency. This lack of understanding of losses and market risk factors prevented adequate adjustments to underwriting and hinders future efforts at risk pricing. This history has devastated lending in the manufactured housing sector long before the current crisis.

## CHALLENGES FACING THE MANUFACTURED HOUSING FINANCE SECTOR

### I. Single Family Financing

We have much to learn from this earlier housing bust. CFED recommends that this Committee not ignore the finance market for manufactured homes for two reasons: first, revival of lending on manufactured housing is key to this industry that produces low-cost, and increasingly energy efficient, housing, and second, this lending is key to helping many low-income homeowners acquire, maintain and re-sell their biggest wealth building asset. When working on comprehensive solutions for the future of manufactured housing finance, which comprises a significant share of the affordable homeownership sector, there are unique challenges that must be taken into consideration: 1) homeownership title, 2) types of financing options 3) the depreciation myth and 4) lack of understanding of the risk factors.

- 1) Ownership is represented by a title. How a home is titled affects the homeowner's financing options. Manufactured homes are titled either as personal property (chattel) or real property (real estate). Options for titling vary by state, but most begin with a personal property title that in some states and under specific circumstances may be converted to a real property title, and then usually only if the home is sited on land owned by the homeowner. In 2008, approximately 79,000 new manufactured homes were placed and 50,000 of these were titled as personal

property, even though 75% were placed on private land (not in a land-lease community). Homes titled as personal property are generally not listed on multiple listing services (MLS) by real estate agents. In comparison to site-built homes, they are subject to different procedures if the homeowner defaults. For these reasons, conventional mortgage lenders generally do not engage in chattel lending.

- 2) For manufactured homes titled as personal property, chattel lending is their only financing option. Even for homes titled as real property, many owners of manufactured homes are steered into chattel financing by unscrupulous captive lenders or due to lack of other options. Chattel mortgages differ from conventional mortgages in many ways and are more akin to auto loans. The disadvantages of financing a home with a chattel mortgage compared to a conventional mortgage are:
  - Shorter loans terms,
  - Higher interest rates,
  - Fewer rights when in default,
  - Lack of private and government mortgage insurance, and
  - More limited pool of lenders, including steering to in-house financing.
- 3) A third unique challenge facing this industry is the assumption of depreciation of manufactured homes. From a financier's perspective, the collateral of a loan should outlive the loan term and maintain sufficient value to enable the lender to recoup its outstanding loan in the event of default. The history of manufactured housing, including its origins in the travel-trailer industry and lack of national standards until the mid-1970s, resulted in justifiable concerns over the quality and long-term durability of manufactured homes as collateral. Today's manufactured housing, however, is built to a national standard and with materials comparable to those of site-built homes, but with the added efficiencies and quality controls of the factory process. Experience shows that well-built manufactured homes that are properly installed on a permanent foundation and with long-term security in the land beneath the home will appreciate in value comparable to site-built homes. Unfortunately, while the production of manufactured homes has evolved, the financing market for these homes has not.

For homes on leased land there are numerous other factors that affect a home's value and financing options. A primary driver of this is land-tenure security. Not surprisingly, if a home's land-tenure is not secure, that adversely affects its value and the ability to resell. One study by the University of New Hampshire's Carsey Institute found that homes in resident-owned communities are more likely to appreciate in value than homes in investor-owned communities. The study found that, controlling for other factors, such as construction quality and foundation systems, differences in appreciation were largely due to two factors: land tenure security and access to reasonably-priced financing.

- 4) A fourth challenge is the lack of understanding by lenders of the risks leading to loan losses. Many of the risks associated with the manufactured housing sector are not understood, including the inter-relation of manufacturing and distribution of homes, financing, the land-lease community owner model and the titling of homes as chattel. For example, Origen, one of

the largest lenders on manufactured homes, speaking at an international roundtable two years ago stated that they developed a captive loan program together with park owners because their research showed that park owners control over 80% of the factors that lead to losses in lending on manufactured homes. The challenge is to understand why and underwrite accordingly.

## **II. Multi-Family Financing for Communities**

There are approximately 50,000 lease-hold communities (mobile home parks) in the United States which provide a home site for 3.5 million homes, primarily owned by low-income homeowners such as the elderly, the disabled, single parent households and young families.

Unfortunately for these homeowners, they suffer not only from a lack of single family financing, as discussed above, but other risks, such as the loss of home value due to increasing speculation and complete loss of home through community closure and redevelopment. One option for homeowners is to join together, buy the community and operate it as a cooperative.

Many land-lease communities are financed with Commercial Mortgage Backed Securities (CMBS) and placed in Real-Estate Investment Trusts (REITs). There is pressure in this market leading to foreclosures, bankruptcies, refinancing and sales. Unfortunately, homeowners have few options. Most state foreclosure laws do not require that notice be given the homeowners when their land-lease community is being foreclosed on. The federal Protecting Tenants at Foreclosure Act does not protect these tenants either because land-lease communities are considered commercial, not residential, properties.

## **CFED'S RECOMMENDATIONS**

A lender's primary concern is repayment of a loan and, in the event of default, whether the resale price of the home will cover the outstanding loan balance. In fact, lender and homeowner interests coincide because a homeowner also seeks security and stability in a home's value. The following recommendations will promote the availability of responsible, conventional mortgage lending for owners of manufactured homes. They will also support a more sustainable and robust manufactured housing finance industry.

- Underwriting requirements that the manufactured home financed be classified as real property;
- Strengthen the resale market for manufactured homes;
- Encourage small, community lenders, such as community development financial institutions (CDFIs);
- Reconsider approaches to valuation and improve dealer price transparency;
- Promote use of conventional mortgages over chattel loans;
- Renew GSE efforts to purchase conventional mortgage loans backed by manufactured housing to meet their statutory duty to serve requirements and chattel loans on homes in communities if they meet certain "Safe Chattel" requirements; and

- Improve the efficiency of federal programs to support this sector, including improving the accessibility of government-insured mortgage loans for manufactured housing, such as FHA and USDA's Rural Development 502 loan programs

Classify manufactured homes as real property: A manufactured home classified as personal property will not have access to conventional mortgage lending – regardless of the home's value as security or the borrower's creditworthiness. Classification as real property opens the door for conventional mortgage lending but does not guarantee it. Many states allow the conversion of a manufacture home's title from personal to real property; however, the process is often onerous and overly complicated and expensive. Moreover, many state laws do not allow for the conversion of homes on leased land. In order to support the conventional financing of manufactured homes, a state's conversion process should be simple, voluntary or automatically, easy to verify through public records and not be tied to ownership of the land. The Uniform Law Commission has begun a manufactured housing project to draft and promulgate a uniform code for converting manufactured homes from personal to real property. While a long-term process, this would dramatically alter the manufactured housing finance sector by bringing consistency and efficiencies to the market and would appeal to the secondary mortgage market.

Strengthen the resale market for manufactured homes: Current underwriting favors new manufactured homes. Moreover, many lenders have close ties to manufactured home dealers through their captive lending programs. The resale market for manufactured homes has few financing options. Strengthening the resale market for manufactured housing through Government-Sponsored Enterprises (GSEs) and other interventions would benefit homeowners, lenders and the marketplace in many ways by allowing homeowners the flexibility to sell their home when needed or desired, allowing home values to rise where demand and quality are sufficient, and providing lenders with a viable resale market in the event of default. One way to strengthen the resale market of manufactured homes is to modernize the appraisal process, discussed below.

Encourage small, community lenders: Community-based non-profit and small private lenders are most in-tune with their local market and are at the forefront of developing innovative, safe and sound conventional mortgage products for manufactured homes. These innovations, many led by CDFIs, have a greater likelihood of replication and going to scale if they are supported by GSEs that allow their participation in the secondary mortgage market.

Reconsider approaches to valuation and improve dealer price transparency: For too long the lending industry has relied heavily on manufactured home design as the primary method of valuation. There are many, more important, factors related to a home's value, including land tenure security and access to reasonably priced mortgage financing. As with all real estate, other factors include construction quality, proper installation, foundation type and location. Moreover, manufactured housing finance lacks price transparency, which could be addressed by requiring independent appraisals for new and used homes. The resale market for manufactured homes relies on the N.A.D.A. guidelines, which is the bluebook for manufactured homes and assumes depreciation. Appraisal standards need to be modernized and not presume depreciation, but instead should be based on home quality and factors such as location and comparable home prices. This factor would change dramatically with real estate titling and the inclusion of Multi-State Listing

Service (MLS) and real estate appraisers in the process and would require developing new methodologies by the organizations that accredit and train appraisers.

Promote the use of real estate mortgages over chattel loans: Every manufactured home titled as real property should be financed with a real estate mortgage loan, rather than a chattel mortgage. The prevalence of chattel lenders in this industry is restricting the vibrancy and sustainability of this sector, even where homes are or may easily be titled as real property and the homeowner owns the real estate. Promoting conventional mortgages over chattel mortgages can be achieved through regulation, legislation or pressure from the secondary market. In cases where chattel lending is the only option, such as in states that lack a real estate title conversion statute, borrowers should have an option of “Safe Chattel” loans that meet the following criteria:

- An APR lower than the rate for higher-priced mortgage loans as defined by the Federal Reserve Board’s Regulation Z, § 226.35<sup>1</sup> regardless of whether the loan is subject to the Truth in Lending Act.
- No prepayment penalties.
- No loans with yield spread premiums or other incentives that encourage the party arranging the loan (such as a retail seller, broker or community owner) to act against the borrower’s best interest.
- Chattel loan origination must comply with the Real Estate Settlement Procedures Act’s requirements, such as disclosure of all costs and fees and the prohibition on kickbacks.
- Loans should never exceed 100% of the value established by appraisal
- Fair lease terms should be required for homes on leased sites which assure right to long-term land tenure, rent predictability, rights upon sale of the community, rights to organize a tenant group and a right to sell the home in-place to a buyer of your choice.

Renew GSE efforts to purchase conventional mortgage loans backed by manufactured housing to meet their statutory duty to serve requirements: GSE involvement is vital to the reestablishment of a secondary market for manufactured housing mortgages. Because manufactured housing is one of the nation’s most widely used, unsubsidized forms of affordable housing, the GSEs should promote the extension of conventional mortgage loans for new and existing manufactured housing on fee-simple or land-lease sites based on sound, but not overly restrictive, underwriting criteria. Doing so will encourage conventional mortgage lenders to enter the market. Irresponsible chattel lending (not meeting the Safe Chattel terms, above) should not count toward meeting the GSEs’ duty to serve requirements.

Improve the efficiency of federal programs to support the manufactured housing sector:

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<sup>1</sup> 12 C.F.R. § 226.35(a) as amended by 73 Fed. Reg. 44603 (July 30, 2008) (effective Oct. 1, 2009). The definition is: “(a) Higher-priced mortgage loans —(1) For purposes of this section, a higher-priced mortgage loan is a consumer credit transaction secured by the consumer’s principal dwelling with an annual percentage rate that exceeds the average prime offer rate for a comparable transaction as of the date the interest rate is set by 1.5 or more percentage points for loans secured by a first lien on a dwelling, or by 3.5 or more percentage points for loans secured by a subordinate lien on a dwelling.”

- *Improve the accessibility of government-insured mortgage loans for manufactured housing, such as FHA and USDA's Rural Development 502 loan programs.* The I'M HOME Network includes local, state and national partners across 40 states. These partners are at the forefront of providing responsible mortgage lending to low-income owners of manufactured homes. The two most common loan products within the I'M HOME Network are USDA Rural Development 502 loans (both direct and guaranteed) and FHA Title I loans. Despite their prevalence within the network, however, the RD 502 products only financed a total of 525 manufactured homes nationwide in 2007, while the FHA Title I program financed 50,366 in 2007, making it the single most common affordable financing product for fee-simple manufactured homes. Based on Home Mortgage Disclosure Act (HMDA) data, FHA guaranteed more manufactured home mortgages than Fannie and Freddie put together. However, this represents a small portion of the market need.
- *Allow eligibility of manufactured homes in resident-owned communities for FHA and USDA loan products.* In addition, extend FHA Title II lending to manufactured homes in land-lease communities where the homes are titled as real property and there is assurance of long-term land tenure.
- *Create streamlined and consistent standards and requirements for manufactured home financing across government agencies, especially FHA and USDA.*
- *Establish a temporary source of mortgage insurance for manufactured home loans until such time as adequate data can be maintained, analyzed and distributed by the agencies and GSEs to address the data gap on loan losses.*
- *Allow weatherization funds and other housing rehabilitation funds to subsidize replacement for substandard mobile homes to energy-efficient manufactured homes.*

Special recommendations for promoting conventional financing of manufactured homes located in land-lease communities: Homes on rented land face additional barriers and challenges to accessing conventional mortgage loans. Factors that would promote conventional lending for homes in land-lease communities include permitting the sale of homes to a new owner on its current site; ensuring that homeowners may remain in their community through measures such as protections from unjust rent increases, opportunity to purchase legislation and limits on no-cause evictions; and protecting lender interests, such as allowing the lender to sell the home in place in the event of foreclosure.

Special recommendations for improving multi-family lending to benefit homeowners in land-lease communities: We recommend that the Protecting Tenants at Foreclosure law be revised to apply to manufactured home community residents so homeowners have at least 90-days to prepare and possibly bid at sale, or negotiate with the owner and lender. We further recommend that sources of financing at the GSEs, USDA and HUD be made available to homeowner groups to purchase their communities and preserve them as affordable housing in the long term. This will provide the land tenure security and control homeowners need in order to access reasonably priced mortgage products, improve their communities and build assets.

## CONCLUSION

CFED is dedicated to promoting the use of good quality manufactured housing as one of many mechanisms to cost-effectively increase the supply of affordable housing and promote asset building. We welcome the opportunity to aid the Committee as it considers the future of housing finance.