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State housing agency forecloses on borrowers even as they remain current on payments, report finds

SACRAMENTO—The California Housing Finance Agency – known as the state's "affordable housing bank" – is forcing some of its borrowers into foreclosure even though they remain current on their payments, a new report by the Senate Office of Oversight and Outcomes has found.

Other borrowers are living in cramped quarters with growing families as a result of the agency's strict policy preventing them from temporarily renting out their CalHFA-financed residences and moving into more suitable homes, according to the report. Not only is the policy at odds with the practice in other state housing agencies – it's costing CalHFA money.

The report, "Good Deeds Punished: California's State-Run Mortgage Lender Forecloses on Californians Current on Their Loans," is available here.

Borrowers are being squeezed because of CalHFA's interpretation of federal law governing tax-exempt bonds, which traditionally have funded the mortgages offered by the housing finance agency. On the advice of its bond counsel, CalHFA only allows its borrowers to rent out their residences in the event of unforeseen economic hardship, such as losing a job. Otherwise, borrowers are expected to stay put for the duration of their mortgages.

The bond counsel opinion did not anticipate the collapse of the housing market, which put many borrowers underwater: They owe more on their loans than their residences are worth. Under current conditions, borrowers forced to sell face severe losses. Instead, several hundred CalHFA borrowers who have gotten married, had children, started a home-based business or had another change in life circumstances have rented out their former homes.

CalHFA gives them an ultimatum: pay off the loan balance, move back in, or face foreclosure. So far, 348 CalHFA borrowers have rented out their residences without permission from the agency. Twenty-one of these loans have ended in foreclosure. Another 49 are delinquent, at high risk for foreclosure. An even bigger number, 186, are current on their payments but in violation of CalHFA's policy, faced with the prospect of selling in the depressed market, returning to their CalHFA-financed homes or foreclosure.

Each foreclosure currently costs CalHFA more than $50,000 in uninsured losses.

Established in 1975, CalHFA offers low-interest loans to first-time homebuyers and promotes the development of affordable rental housing. Its policy on rentals is at odds with the practice in most of the other states surveyed by the oversight office, covering most of the U.S. population. All but two of them do not foreclose on borrowers who have rented out their properties and remain current on their payments.

Most interpret the federal law to mean that a borrower intended to move into the property and occupied it for a reasonable time – a safeguard against speculators setting themselves up as landlords. In the current real estate market, these state housing agencies have decided not to foreclose on borrowers who took out loans in good faith and later moved because of a change in life circumstances.

“We’re not going to be foreclosing on homes if they’re making their mortgage payments in this market,” a Washington state official told the oversight office. As a Minnesota housing official put it, “Life happens down the road.”

Among those who have run afoul of CalHFA’s policy are Andrea and Joshua Bernard. They got an unexpected letter in September from the California Housing Finance Agency, which in 2007 provided the money for the purchase of their San Jacinto home.

The Bernards lived in the 880-square-foot house for three years, then bought a bigger house for less money to accommodate their third child and Andrea’s photography business. With the CalHFA-financed house now worth $175,000 less than they paid, they rented it to another family. Even though the Bernards had never been late on a payment and were losing more than $600 a month to cover the note, CalHFA told them to move back in, pay up or face foreclosure.

The Bernards worked extra hours, put off home repairs, cut short vacations and got by with ten-year old vehicles so they could continue to honor their commitment.

“I definitely feel like we’re punished for trying to do the right thing,” Andrea Bernard told the oversight office. The Bernards may seek a rental waiver, but even if they get one, would likely find themselves in the same situation when the waiver expired in a year.

The non-partisan Senate Office of Oversight and Outcomes was created in 2008 by Senate President pro Tempore Darrell Steinberg (D-Sacramento) to bolster the Senate’s ability to gauge government performance.

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