

## **Addressing mortgage default and delinquency before it occurs: An evaluation framework for the homeownership counseling industry**

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### **Abstract**

The decade of the 1990s helped usher in a renewed effort to increase the U.S. homeownership rate. This was achieved largely through the elimination of barriers to previously underserved populations that had traditionally not experienced home ownership. The rise of the housing counseling industry, particularly pre-purchase counseling, coincided with the rise in homeownership opportunities. This new emphasis on pre-purchase homeownership counseling served two purposes: to educate clients about the responsibilities of homeownership and to mitigate risk of delinquency and foreclosure. Still, there is much ambiguity over the proper role that housing counselors should fill in evaluating clients after the housing counseling intervention. A framework for evaluation of homeownership counseling clients is provided, and specifically makes the case for more emphasis by counselors on providing follow-up during the first few years of vulnerability after the home has been purchased, in a more active attempt to prevent mortgage default and foreclosure.

***Keywords:** home ownership, housing counseling, evaluation, first-time home buyers*

### **Introduction**

During the 1990s and much of the early 21st century, a determined effort has been made to increase homeownership opportunities. Several state and local governments have supported the growth of homeownership through programs aimed at low- and moderate-income populations (Basolo 2007). Meanwhile, research has been conducted that openly questions the wisdom of such programs for the low-income population (Shlay 2006). From the governmental stand point, while it may be good public policy to encourage low- and moderate-income homeownership, it

also seems desirable that consumers be well-informed when making a home buying decision (Feins, Bain, and Kirilin 1980). Because of the many risks and uncertainties involved in the home buying process, the housing counseling industry has gained increasing importance. There has also been an increasing need for analysis on the overall effectiveness of housing counseling as it relates to behavior change on the part of the housing counseling client after the counseling sessions have been completed. An example is provided for an accountability-based model for the housing counseling industry that helps assure long-term stability in one's homeownership situation.

### **History, development, and evaluation of the housing counseling industry**

The American housing counseling industry came into existence through the passage of the 1968 Housing and Urban Development ("HUD") Act, which proposed that proper counseling in budget and credit matters would aid lower-income families in becoming successful homeowners (U.S. Department of Housing and Urban Development 1983). One significant change within the industry during the late 1980s and early 1990s was the shift in the industry's overall orientation from primarily post-purchase default prevention to pre-purchase homeownership education (McCarthy and Quercia 2000). Today, there are literally thousands of organizations and entities providing this type of housing counseling services to low- and moderate-income borrowers. Table 1 shows the trend for the amount of HUD grant dollars devoted to housing counseling operations. Still, despite this increase in funding, there remains some ambiguity as to whether housing counseling efforts are creating the type of long-term homeownership stability that benefits communities.

#### **[INSERT TABLE 1]**

During housing counseling, counselors help clients acquire the skills and confidence to navigate the mortgage lending process (Quercia and Wachter 1996). Counseling is especially important for the lower income, minority, young, and elderly households, who often lack experience dealing with traditional financial institutions (Jacob, Hudson, and Bush 2000). Counseling is of greater importance for poor households because on average these groups possess more credit cards with high balances than ever before (Bird, Hagstrom, and Wild 1999). By intervening in the lives of potential first-time homebuyers, housing counseling providers also help clients avoid "predatory" and sub-prime lenders, who are not as heavily monitored as traditional bankers (Jacob et al. 2000). For those who are counseled, the knowledge gained can make dealing with otherwise intimidating lenders a more comfortable experience. Pre-purchase homeownership counseling also teaches potential homebuyers about wealth accumulation and asset-building programs (Vitt et al. 2000). This particular aspect of the counseling experience allows many new homeowners to build the foundation to withstand some of the circumstances that contribute to delinquency, default, and foreclosure.

There are three broad types of homeownership counseling and education services offered to the public: (1) general pre-purchase education and counseling sessions, (2) post-purchase counseling; and (3) delinquency intervention. The rationale behind the existence of pre-purchase housing counseling is straightforward. If low- and moderate-income homebuyers can gain an understanding of the requirements and responsibilities of homeownership **before** the home purchase is made, their chances for having a successful homeownership experience improve considerably. The basic menu of pre-purchase counseling is extensive and can vary considerably between agencies, but it usually includes modules devoted to establishing and improving creditworthiness, setting and achieving income goals, saving to cover down payment and closing costs, budget and credit counseling, and maintaining the home. Initial research has shown that housing counseling programs can be a catalyst for change by improving a household's family budgeting behavior, among other things (Shelton and Hill 1995).

Post-purchase counseling is defined as counseling that is performed after the home purchase event has occurred, and it includes such topics as home maintenance skills and advanced budgeting (McCarthy and Quercia 2000). The goal of post-purchase counseling is to increase the chances that the owner will have a sustained and positive homeownership experience and avoid future default. In essence, it serves as the reinforcement for home "owning," rather than the more immediate concept of home "buying" facilitated by the traditional pre-purchase counselor. Indeed, many low-income borrowers are more susceptible to approaching sub-prime lenders after their initial home buying experience for refinancing purposes (Schloemer et al. 2006), which considerably increases their susceptibility for future delinquency and foreclosure. This type of counseling is usually delivered during the six-month period after the purchase is made. Ideally, low-income borrowers would undergo a regimen of receiving both pre- and post-purchase counseling services. However, even though these "homeowner maintenance" programs help reinforce pre-purchase lessons learned, attendance at post-purchase sessions is often sparse at best. Recently, there has been a renewed interest in post-purchase counseling, as many established housing counseling service providers try to encourage full-cycle homeownership sustainability (McCarthy and Quercia 2000).

Default counseling is usually afforded the highest priority among all other types of housing counseling because of the individual and household financial risks involved with each unique circumstance, but also due to the legal and technical complexities of the default and foreclosure processes (Heintz, Schnare, and Turner 1984). Default counseling differs from post-purchase programs in that default counseling occurs primarily when borrowers start displaying signs that they will be unable to make routine payments on their mortgages. By contrast, post-purchase counseling simply refers to systematic visits that the borrower will make with a counseling agency after the purchase has been made, without any signs that the borrower has come into financial crisis.

### **The case for a long-term client-centered assessment model**

Today's pre-purchase housing counseling experience usually ends when the housing counselor makes a determination of a borrower's fitness to purchase a home. Currently, there is no oversight agency or standard-setting body for the housing counseling industry. As a result, the industry's practices and methods are non-uniform across the nation. Previous research has stated that "[a]ttention needs to be paid to what happens to home buyers after purchase, especially from a preventive...perspective" (Quercia, Gorham, and Rohe 2006, 337). Currently, counseling agencies have a very limited benchmark by which they judge their performances and interactions with clients. Much of the evidence that counseling agencies have on their effectiveness is reflected either in program outputs or through exit surveys, which do not provide enough evidence that counseled borrowers have retained the knowledge given to them during the counseling intervention. Program outputs, such as number of people attended and number of programs offered, differ dramatically from actual outcomes related to human behavior change effected by such service delivery programs. Yet, still there is evidence that a large number of nonprofit agencies evaluate themselves based on this metric (Henderson, Whitaker, and Altman-Sauer 2003; Rivenbark and Menter 2006). Many sponsors of nonprofit services like homeownership counseling and educational services want hard evidence as a return on their invested capital, rather than soft evidence expressed through appreciation and good will on the part of those counseled borrowers (Vitt et al. 2000). More effective follow-up procedures can be put in place by the counseling agencies, in order to accurately track the progress of the borrowers on a longitudinal basis. The efficacy of counseling programs is made more important because low- to moderate-income buyers have more income volatility than their higher-income counterparts (Gosselin 2004). Perhaps as a result, Stone (2006) estimates that nearly one-quarter of homeowner households are "shelter poor," in that they do not have enough funds left over after their housing obligation to meet non-shelter needs at a minimally adequate level. Most models of housing counseling success are rooted in the mindset of reducing long-term default and foreclosure (Hirad and Zorn 2002, Quercia and Wachter 1996), thus ignoring some of the finer points of financial budgeting behavior that could eventually portend delinquency and foreclosure, but which for now remain hidden to evaluators and stakeholders. Rather than focusing simply on the rather dry measure of foreclosure and delinquency, a more long-term client-centered evaluation attempts to understand outcomes from the perspectives of the end user (Guba and Lincoln 1989; Stake 1970). Focusing on the client also helps to determine whether the objective indicators of nonprofit organizations' effectiveness are in line with that of the clients and the organizations that fund housing counseling operations, relationships that do not always produce a high correlation in evaluative research (Link and Oldendick 2000; Ott 2001). Because funding is so often tied to outcomes of the program itself, housing counseling evaluation is thus a logical extension of program evaluation typically used to justify federal expenditures (Rossi, Freeman, and Wright 1979). Future efforts to enhance the evaluative component of homeownership counseling could be strengthened through the implementation of a strong post-

purchase counseling program. These sessions are routinely poorly attended, however, because there is little incentive for a counseled home buyer to continue receiving counseling services once the house has been purchased. Thus, some organizations resort to incentive programs for counseled borrowers that focus on rewards such as coupons for home improvement stores (such as Home Depot) for attending post-purchase counseling programs (Krecji 2007). Still, it appears that this type of incentive program is more often the exception, rather than the norm.

### **Proposed model for housing counseling assessment**

Because evaluation has been identified as a key element in foreclosure prevention strategies (Quercia et al. 2006), a proper pre-test and post-test evaluation should be put in place for a respectable evaluation effort of housing counseling programs. Such a process is currently not commonplace within the industry (Quercia et al. 2006). The housing counseling community could benefit from implementing such an assessment measure in two important ways. First, it would theoretically help to alleviate some of the capacity issues that mortgage delinquency counselors are currently experiencing (Fahim 2008). Second, it ensures potential funding agencies that a system is put in place that helps to ensure the maintenance of homeownership, a much loftier public policy goal than simply becoming a homeowner in the first place. A proposed evaluation model is shown below in Table 2.

### **[INSERT TABLE 2]**

The first step in the long-range evaluative process is for academic researchers to meet with the counseling practitioners before the initial counseling cohort group arrives for the start of the housing counseling process. This phase aids in doing two things. First, it allows for the representatives from the counseling agency to realize their involvement as stakeholders, which usually enhances the usefulness of the evaluation results (Greene 2005) and increases the legitimacy of the research effort to them. Second, this involvement increases the probability of obtaining background information of the counseled population received at intake and subsequent data related to the ongoing counseling sessions. This method of including counseling practitioners at the outset of the evaluation process has also helped define successful outcome measures for examination (Housing Assistance Council 1997), despite the fact that nonprofit organizations outside the housing arena have difficulty quantifying measurable outcomes of “success” (Morino and Jonas 2001, Rivenbark and Menter 2006, Speckbacher 2003).

Testing the first-time homebuyer population on its knowledge of basic homeowner issues would also be helpful to academic researchers to better understand individual counseling recipients on a case-by-case basis. This stage would likely occur during the initial group educational session, which many housing counseling agencies hold at the very beginning of the counseling process. The personal financial literacy industry has already created several template programs that

measure many areas of consumer financial knowledge (in areas outside of homeownership), which help increase knowledge retention (Jacob et al. 2000; Lyons 2005). The housing counseling model could also incorporate methods used from research in the financial literacy field, which help determine whether a counseled person's *perceived* knowledge and skill in handling certain homeowner situations, whether financial or otherwise, is in concert with the subject's *actual* knowledge (Goldsmith and Goldsmith 1997; Lyons 2005).

At the conclusion of the counseling experience, a similar type test could be administered to determine how much information has been retained by this counseled cohort group. To be thorough, yet another final test could be administered to the counseled population six or more months after the borrower has moved into the home, which should be enough time for homeowners to provide valuable information about the quality of their homeownership experiences. Similar to the above recommendation, there exists the further possibility that this tracking of the counselee cohort group would extend over a period of a few *years*. This level of tracking may be necessary, in that many defaults and foreclosures do not occur until almost four years have elapsed since the home purchase (Hakim and Haddid 1999), thus strengthening the argument for more evaluative follow-up after pre-purchase counseling. Such long-term tracking is also consistent with previous efforts within the financial literacy arena (Shockey and Seiling 2004; Staten, Elliehausen, and Lundquist 2002; Xiao et al. 2004). As a whole, this type of evaluation of housing counseling organizations would simply follow an evaluative model implemented within some nonprofit organizations, which assesses both the level of client satisfaction with the service and the degree of change engendered by the program (Ott 2001), further legitimizing both the individual agencies involved and the housing counseling industry as a whole. In addition, it creates a transparency to the process that improves citizens' perceptions of government (Aristigueta 1999). Meanwhile, housing counseling agencies are usually dealing with a client in a stationary location, given the recent home purchase. This situation is superior to that of financial literacy advocates, who are concerned about the accurate tracking of clients due to privacy and mobility concerns (Lyons 2005; Lyons et al. 2006). Because of the rapport built through weeks, if not months, of face-to-face contact, the response rate to evaluation efforts should be fairly high.

### **Conclusion and discussion**

This particular model for evaluation of housing counseling is purely exploratory in nature. Previous evaluative models have also addressed some measures of competence and accountability within the housing counseling organization, but have been limited primarily to the practitioners and the competence they display (Shelton and Moss 2002). There is clearly a need for a process that provides meaningful evaluation to housing counseling clientele. Further evaluative efforts need to be developed to determine the next and ultimate step in the housing

counseling process – whether the counseling interventions being offered by these housing professionals are actually achieving long-term success in the form of homeownership stability.

Adhering to an evaluative component may not necessarily be universally embraced from within the housing counseling agencies. It is realistic to assume that individual agencies will have neither the funding nor the capacity to engage in wholesale evaluation efforts to meet the demands of their various stakeholders (Sawhill and Williamson 2001). Research has shown that nonprofit evaluation efforts are indeed expensive, ranging into hundreds of thousands of dollars for state program evaluations (Aristigueta 1999). Housing counseling efforts are nearly always under the auspices of local authorities, however, which should drastically reduce evaluation expenses.

Meanwhile, the proper education of first-time home buyers may produce benefits that far outstrip the costs of implementing an evaluation component. Research has shown that foreclosures not only produce real costs to individual homeowners, but also to communities through increased crime and direct municipal costs (Apgar and Duda 2005; Immergluck and Smith 2006). On top of that, there are indirect costs to municipalities in the form of reduced property tax revenues (Immergluck and Smith 2005). The need for reinforcement of education on sustaining homeownership has perhaps never been more in demand, given the rapid rise in foreclosures since 2006 (Christie 2007).

The development of stated outcomes consistent among all housing counseling agencies is perhaps unlikely, but would certainly be an improvement beyond the current system of limited follow-up procedures. Regarding outcome measurement, variables such as priority of bill payment and timeliness of payment have served as proxy variables for financial stability during the vulnerable period after one becomes a first-time home buyer (Carswell 2005). No matter what performance variables are chosen, however, the biggest challenge may be in getting organizations to actually use them, a problem that other evaluators have also noted (Kamensky 1995). Still, there is evidence from the nonprofit community that evaluation of housing counseling service delivery can become a reality. State and local governments have been moving toward a more results-based management form of governance for the past several years. This trend is no doubt aided by the ascendancy of the Government Accounting Standards Board and the passage of the Government Performance and Results Act during the 1990s in an effort to make government more accountable to its constituents (de Lancer Julnes and Holzer 2001; de Lancer Julnes 2006; Hatry 1997). There are some encouraging signs that this type of evaluation can be implemented by the housing counseling community. When given specific directions on what the goals of the organization or agency are, service delivery professionals have shown clear signs of embracing performance-based results (Poister and Streib 1999; Rivenbark and Menter 2006; Wilkins 1996).

The housing counseling industry is currently at a crucial juncture in its short history as a service delivery organization. For almost a decade, the business of providing mortgage loans to low- and moderate-income families was embraced as a public policy directive, and concerns about the safety and soundness of such business practices were tempered somewhat through the risk mitigation efforts of housing counselors and educators. With the current housing recession weighing on the minds of lenders, mortgage lending practices will likely become more prudent over time. For housing counseling agencies, evaluation efforts of their service delivery outcomes should provide a necessary observation of the critical experiences of first-time home buyers during the period after they first move into a home and before their first mortgage delinquency occurs. These early interventions may forestall a number of delinquencies from occurring in the first place. Thus, a shift in focus from crisis management to one involving preventive measures through active evaluation can help communities remain stable through the intervening variable of homeownership *stability*, rather than simply home *acquisition*.

**Table 1: HUD appropriations for Housing Counseling Act**

Fiscal year	Statutory authorizations (\$000)
1988	6,000
1993	15,000
1998	20,000
2003	40,000
<b>Source:</b> Office of the Assistant Secretary for Housing, HUD	

Table 1 Summary: Table 1 shows the trend for the amount of U.S. Department of Housing and Urban Development grant dollars devoted to housing counseling operations as follows: 1988, \$6,000; 1993, \$15,000; 1998, \$20,000; 2003, \$40,000. Source: Office of the Assistant Secretary for Housing, HUD.

**Table 2: Proposed longitudinal framework for future researchers of homeownership counseling**

Step	Timeframe	Event
1	One month before intake	Meet with counseling community before intake of counseling cohort group.
2	At or immediately before intake	Attend first group educational session. Give exam to test potential borrowers on homeownership and financial knowledge.



3	At or immediately after intake	Collect intake data on borrower background from counselor.
4	Within first month after intake	Meet with counselor to obtain file data on individual counseling experiences within cohort group.
5	Immediately after conclusion or counseling experience	Administer follow-up survey/questionnaire to determine homeownership and financial knowledge.
6	Roughly 6 months after conclusion of counseling experience	Periodic follow-up with both counseling agency and borrower.
7	One to two years after conclusion of counseling experience	Final survey/questionnaire on homeownership and financial knowledge to borrowers.

Summary: Table 2 proposes a longitudinal framework for future researchers of homeownership counseling. The framework is as follows: (1) one month before intake, meet with counseling community before intake of counseling cohort group; (2) at or immediately before intake, attend first group educational session and give exam to test potential borrowers on homeownership and financial knowledge; (3) at or immediately after intake, collect intake data on borrower background from counselor; (4) within first month after intake, meet with counselor to obtain file data on individual counseling experiences within cohort group; (5) immediately after conclusion or counseling experience, administer follow-up survey/questionnaire to determine homeownership and financial knowledge; (6) roughly 6 months after conclusion of counseling experience, periodic follow-up with both counseling agency and borrower; and (7) one to two years after conclusion of counseling experience, final survey/questionnaire on homeownership and financial knowledge to borrowers.

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