

## Office of Affordable Housing Research

The Office of Affordable Housing Research is dedicated to using research-based data to drive the Ohio Housing Finance Agency's (OHFA) mission "We open the doors to an affordable place to call home" for Ohio families. OHFA helps homebuyers, renters, senior citizens and others obtain quality, affordable housing that meets their needs while supporting developers and property managers financially and through maintaining compliance with guidelines and regulations. Staffed by OHFA, the office works in partnership with The John Glenn School of Public Affairs at The Ohio State University and collaborates with other colleges, universities and partners to engage research to guide affordable housing policies.

## The Truth about Homebuyer Education and Counseling

*While face-to-face homebuyer education and counseling have the most standardized formats, telephone and online education and counseling are the most common formats, particularly for borrowers who are required to receive homebuyer education as part of their mortgage prior to a home purchase and for borrowers who are in foreclosure seeking assistance.*

Some suggest that one of the primary causes of the mortgage crisis was the purchase of homes by borrowers who lacked the financial knowledge needed to appropriately evaluate mortgage alternatives or the skills to manage their finances and meet mortgage obligations. In a recent speech before the National Association of Realtors, the U.S. Secretary of Housing and Urban Development (HUD) Shaun Donovan commented: "The housing crisis has illustrated that many families need help with the complex homebuying process and need a trusted place to turn when they face foreclosure." Accordingly, the proposed FY2010 budget for HUD requests an additional \$35 million for housing counseling, a more than 50 percent increase from FY2009's total budget of \$65 million.

But what do we know about homebuyer education and counseling? There are many different types and strategies. Are all types of homebuyer education and counseling equally effective?

### The State of the Industry

There are two primary types of homebuyer education and counseling. The first includes interventions provided prior to the purchase of a home to increase homeownership opportunities and prevent future default. This is typically referred to as "pre-purchase homebuyer education and counseling." The second type takes place after a home purchase, typically when a borrower is in default on their mortgage payment, to prevent foreclosure. This is often referred to as "post-purchase foreclosure intervention counseling."

Both types of homebuyer education and counseling are provided by a variety of different organizations, in a variety of different

formats. Homebuyer education and counseling may be provided by nonprofit or public organizations through face-to-face workshops and one-on-one counseling sessions. Homebuyer education and counseling may also be provided over the telephone or online, by a variety of different organizations including nonprofit and public organizations, lenders, mortgage insurance companies and state housing finance agencies.

While face-to-face homebuyer education and counseling have the most standardized formats, telephone and online education and counseling are the most common formats, particularly for borrowers who are required to receive homebuyer education as part of their mortgage prior to a home purchase and for borrowers who are in foreclosure seeking assistance. A study of Freddie Mac "Affordable Gold" mortgages in 2002 found that 95 percent of borrowers receiving homebuyer education and counseling as a requirement of their mortgage received the counseling through the lender or mortgage insurance company, most frequently over the telephone. Another study found that among borrowers receiving pre-purchase homebuyer education and counseling, 80 percent received the services after signing a purchase agreement.

A recent report prepared for HUD, "The State of the Housing Counseling Industry," highlights the scope and presence of HUD-certified housing counseling organizations. For example, in 2007, approximately 1.7 million individuals nationwide received counseling and education from HUD-certified counseling

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agencies, up from 244,000 receiving counseling from such agencies in 1994. The largest increase recently has been due to increasing demand for foreclosure intervention counseling, with nearly 500,000 borrowers receiving this type of counseling in 2007, up from just over 200,000 in 2004.

## **Effectiveness of Homebuyer Education and Counseling**

The targeted outcome of homebuyer education and counseling, both pre-purchase and foreclosure intervention, is homeownership sustainability. That is, homebuyers are less likely to become delinquent or default on their mortgages payments, and/or are better able to recover from a delinquency or default and avoid foreclosure. Further, homeowners receiving counseling and education will be better equipped to make financially sound decisions to refinance or sell their homes (referred to as “prepayment”). While there is much anecdotal evidence to support the effectiveness of homebuyer education and counseling, there are only a few empirical evaluations of its effectiveness. This is due in part to the diversity of approaches available and difficulty isolating the effects of homebuyer education and counseling with so many other influences that can potentially account for observed outcomes.

A few studies lend evidence to the effectiveness of pre-purchase face-to-face education and counseling compared with other types of education and counseling. A study of Freddie Mac’s “Affordable Gold” mortgage program in 2001 for low-income homebuyers found that only individual counseling and face-to-face classroom education were effective at reducing mortgage delinquency, whereas there was

no reduction in delinquency for borrowers receiving telephone or book education and counseling. Similarly, a recent study (2008) of an affordable mortgage program found that borrowers receiving pre-purchase face-to-face education (classroom or individual) were more likely to prepay their mortgages under financially optimal conditions compared with borrowers receiving home study or telephone counseling. However, the study did not find a relationship between any form of education or counseling and reduced mortgage delinquency or default.

While these studies, and others like them, are often referenced to lend evidence to the effectiveness of education and counseling, there is an important caveat to keep in mind. There are potentially significant issues of “self-selection” with these studies. Borrowers who select to go to face to face education and counseling, or who seek help when they are in foreclosure, may inherently make better financial decisions than borrowers who do not seek out education and counseling. Thus, it may not be the education and counseling causing the observed outcomes, as much as it is the type of borrower who seeks out education and counseling. Further, more information is needed about why these interventions may be effective. Is it the education and knowledge provided or the counseling and coaching the relationships that make these interventions effective? Understanding the “mechanism,” the knowledge or the relationship- is critical to designing effective interventions.