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Toes in the Water: Nonprofit Community Development Real-Estate and Mortgage Brokerage Programs

Identifying State Regulatory Obstacles and Assessing the Future of a New Direction in Promoting Homeownership

A Report for the National Housing Institute

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Executive Summary

Over the past several decades, nonprofit community-based organizations have developed a range of strategies to help underserved consumers gain access to homeownership. Nonprofits have promoted homeownership primarily through education and counseling services, as well as financial assistance for consumer needs such as down payments and closing costs, and the construction or improvement of affordable homes.

In the last decade nonprofit community development organizations have begun to enter two lines of business currently dominated by the private sector: brokering first mortgages for home purchase, and brokering real-estate sales. These two lines of business—mortgage brokering and real-estate brokering—seem to be natural fits for nonprofits engaged in assisting underserved potential homebuyers for three reasons:

1. Mission: The opportunity to provide products and services appropriate to the unique needs of underserved families and neighborhoods.

2. Specialized Services: The ability to work with potential buyers who need assistance in rebuilding credit and learning about homeownership, and to promote credit enhancements by lending directly to marginally qualified borrowers.

3. Cost Recovery: The opportunity to earn recurring, fee-based income in order to support these services and to cross-subsidize other services or programs.

Project Goals

The National Housing Institute (NHI) commissioned this research to:
- Examine the trend of nonprofits entering the fields of mortgage and real-estate brokering
- Identify regulatory and other barriers to this work, and
- Recommend policy reforms and programmatic strategies to improve the ability of nonprofits to provide real-estate and financial services.

Methodology

The study was conducted by PolicyLab Consulting Group, LLC, from November 2007 to June 2008. The findings in this study are based on an analysis of mortgage and real-estate brokerage regulations in all 50 states; interviews with community development organizations involved in real-estate and mortgage brokerage activities; interviews with other industry experts; and a survey of community development practitioners regarding their perceptions of these business activities.

Findings

1. **The legal barriers to a nonprofit organization becoming a mortgage or real-estate brokerage are real but not insurmountable.**
   - Nonprofits report that they require legal guidance in starting either a mortgage or a real-estate brokerage program—it is the second-most requested service after grant funding.
   - While state laws are highly variable, nonprofits can (and have) successfully entered brokerage businesses.

- State licensure regulations for mortgage brokerages are more variable than for real estate brokerages, with some states having minimal requirements and others more rigorous institutional and staff requirements.
- State licensure regulations for real-estate brokerages are relatively standardized, with all 50 states requiring exams, initial and continuing education, and annual fees.
- Twenty states and the District of Columbia offer exemptions from minimum asset or other requirements for nonprofit mortgage brokers.
- One state and the District of Columbia offer similar exemptions from minimum standards requirements for nonprofit real-estate agents.
- Most established nonprofits with a professional staff will nevertheless be able to meet brokerage requirements even in states without exemptions.
- Leaders of nonprofits with operating mortgage brokerage programs who were interviewed for this project caution organizations beginning new programs not to underestimate the challenge of meeting demands of "compliance issues" with local, state, and federal regulations.

2. **Tax-exempt 501(c)(3) status issues are not minor but are often overestimated.**
    - Nonprofits can generate fee-based revenue which is related to their mission. Any organization entering a brokerage business must obtain appropriate legal advice, but as long as the brokerage activity is related to the mission of the organization, generally there will not be legal problems with 501(c)(3) charitable tax-exempt status.
    - Following a model used in housing development, some nonprofits have established subsidiaries to operate mortgage or real-estate brokerage programs. This may be prudent for financial or liability reasons, depending on the structure of the organization, but is not a requirement under most state or federal laws.
    - Nonprofits may need to be prepared to pay unrelated business tax on some of their activities in this arena, and consultation with a tax professional is recommended

3. **State oversight of mortgage-brokerage operations is tightening.**
    - The recent surge in mortgage defaults has led to closer scrutiny of all mortgage brokers and to a movement by state attorney's general and financial regulators to standardize state regulations for minimum assets and qualifications of brokers. This is a positive step, and most credible nonprofits should not view these changes as an impediment to their service delivery.
    - Key informants identified by an advisory group as leaders in the field who were interviewed for this project suggested that there may be more demand from Fannie Mae, Freddie Mac, and other institutions for brokered loans that come through "reliable" channels, such as proven nonprofit mortgage brokers.

4. **Of a national sample of established nonprofit community development agencies, the majority indicated they are currently involved in or planning to engage in mortgage brokerage activities, and more than a third are considering real-estate brokerage. (Figure 1)**
    - Twenty-three percent reported brokering at least one loan in the past year.
    - Fourteen percent reported brokering at least one home sale.
    - Twenty percent have never considered mortgage brokerage.
    - Forty percent have never considered real-estate brokerage.
    - Less than 10 percent have considered and rejected mortgage brokerage.
    - Twenty-three percent have considered and rejected real-estate brokerage.

5. **The challenges to starting and operating a nonprofit brokerage program are often underestimated.**

    Interviews and survey results suggest that nonprofits launching mortgage or real-estate brokerage programs should be carefully consider the following before starting a brokerage program:

- Competing with existing organizational supporters, funders, and partners, including financial institutions and real-estate professionals;
- Tension between board and staff members over engaging in a new “market-based” line of business to serve a different, relatively more affluent client base;
- Unrealistic optimism about the number of deals that will be closed and underestimation of operating costs, as most programs report not being able to achieve the planned volume of activity, fail to generate as much revenue as expected, and/or have operating costs greater than planned;
- Finding and retaining staff with skills in delivering mortgage-brokerage or real-estate services efficiently can take more time and resources than might be expected; and
- Programs often attempt to start operations without sufficient working capital to sustain the program through a lengthy developmental stage.

6. **Nonprofits should consider mortgage-brokerage operations primarily as a resource for clients, facilitating their access to mortgage capital, not as a way to generate revenue.**
   - Significant subsidies and technical support are needed for at least two years to start a brokerage operation. Even after two years, most programs require some level of ongoing subsidy, although at reduced levels. No program reported developing enough revenue to significantly cross-subsidize non-brokerage services.
   - Mortgage brokers take on risk that must be managed, even if lending is at a low volume.
   - Brokers must be trained, pass minimum requirements, and require a supportive administrative system to best serve customers.
   - Nonprofit mortgage brokers generally do not operate at the scale required to offset the expenses of their operation. In a survey of 101 organizations, of those operating a mortgage brokerage, the average annual loan volume was 14 loans. This is well below estimated break-even levels, given typical fees and the costs of staff and overhead.

7. **Real-estate brokerages are easier for nonprofits to start up than mortgage brokerages, but the benefits are less clear.**
   - Nonprofit real-estate broker programs are a good match for nonprofits involved in the development and sale of a significant volume of their own properties, as well as for agencies operating in neighborhoods where most market-based brokers resist selling or showing houses.
   - In the long run, operating outside the mainstream home sales market may not complement an organization’s neighborhood-revitalization goals.
   - There is also the potential for a backlash from those local real-estate professionals who directly or indirectly support the nonprofit.
   - Programs entering this market should work over an extended period to make clear the goals of the new real-estate services, and to engage the local real-estate community in a dialogue about how these services complement, rather than compete with, the work of private real-estate agents.

8. **The current environment of a weak housing market, tighter credit and soft labor markets presents enormous challenges for starting or expanding nonprofit brokerage.**
   - Given the dynamic business environment in the lending and real-estate industries, nonprofits operating brokerages must monitor market conditions closely and make adjustments rapidly.
   - Depending on their governance structures and institutional cultures, some nonprofits are not prepared or able to make rapid adjustments in their business activities.

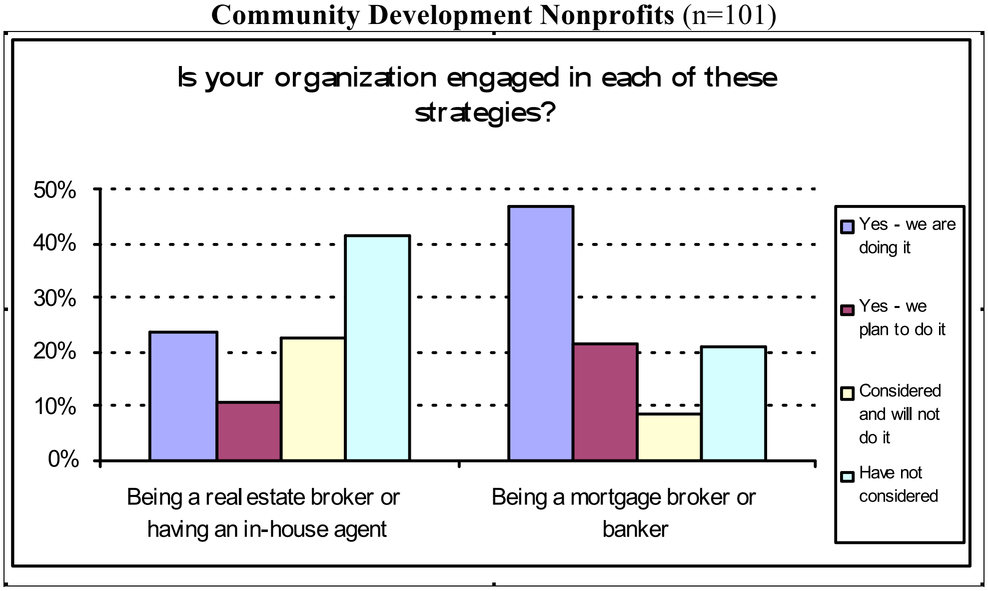
9. **Given that mortgage brokerages depend on volume to break even financially, nonprofits may need to form city or regional collaboratives or networks.**
   For example, one nonprofit could build the lending capacity to do loan originations for a network of nonprofits in a region or an entire state in order to achieve the necessary scale of operations. Such regional lending collaboratives are operating in a few locations and appear to be sustainable.

10. **Nonprofit intermediaries, foundations, and other interested funders should be cautious and strategic about providing support for nonprofit brokerage programs.**
    - Without planning assistance, few nonprofits will be able to consider business operations successfully.
    - For many organizations, a decision to forego these businesses may be the best choice.

Programs starting a new real-estate or mortgage brokerage are advised by existing programs to:
- Make a serious commitment to brokering as a major line of business;
- Hire staff with private-sector experience to get started and be willing to extend existing compensation programs in order to acquire the technical skills needed;
- Conduct consumer research to understand who will best be served;
- Work with a select group of management staff and board members to launch and foster the effort over several years;
- Make sure the board and executive leadership are comfortable with private-sector entrepreneurship and business practices, such as investing in marketing and technology systems; and
- Divide the customer base into low-cost to serve clients and higher cost to serve clients. Even though the organization's mission may compel serving the more expensive customer, consider broadening the customer base to include more low-cost customers as a way to increase volume and facilitate subsidizing mission-oriented but higher-cost customers.

Ultimately, the decision about whether to develop a nonprofit mortgage-brokerage or real-estate business is less a technical legal issue than a core governance issue.
- The decision needs to balance the opportunity of revenue generation against the risks and costs, as well as balance the organization's potentially expanded role as a broker against its core mission.

Figure 1: NHI Nonprofit Broker Survey of Established Community Development Nonprofits (n=101)



1. Introduction

This report was commission by The National Housing Institute (NHI) to explore the trend of nonprofits entering the fields of mortgage and real-estate brokerage, with a focus on state regulatory and other barriers which prevent nonprofit organizations from entering these market. This report also makes general policy and programmatic recommendations to improve the ability of nonprofits to provide real-estate and financial services.

The research for this study was conducted by PolicyLab Consulting Group, LLC. During the first half of 2008, the research team conducted more than 25 interviews with 'key informants', who are leaders in the field identified by an advisory committee and through a review of the literature. During this period the research team also conducted a survey with 101 established nonprofit organizations. A state-by-state legal/regulatory review was also conducted to create a summary of mortgage and real-estate brokerage regulations from all 50 states (available as a separate document).

This report has six sections and an appendix. The first section provides some general background and context for the emergence of nonprofits as mortgage and real-estate brokers. The next section, (Section 2) summarizes findings regarding nonprofit mortgage-brokerage strategies. Section 3 summarizes findings related to nonprofit real-estate brokerage. Section 4 examines cross-cutting legal issues that affect both types of strategies. Section 5 provides recommendations for agencies considering brokerage operations, as well as for policy-makers and funders. Section 6 includes a brief conclusion, followed by six appendices with more detailed information.

Background

Community-based nonprofit organizations have long assumed a major role in connecting underserved consumer and communities to competitive market services. Since the early 1990s, the community development field has made particularly dramatic strides in helping low-income and minority households, who have been traditionally underserved by the mortgage and housing market, to become first-time homeowners. For the most part, nonprofits have done this through prepurchase homebuyer education and counseling, financial assistance such as down-payment and closing-cost grants and loans, development of homes that are affordable by lower-income families, and delivery of mortgage-ready borrowers to private-sector partners in the real-estate and lending industries.

A small but growing number of nonprofit organizations are beginning to move from being a partner with real-estate brokers and mortgage lenders, to entering the market on their own. The concept is simple: Many nonprofit agencies already support hundreds of families in buying homes each year. Why hand off these customers to private entities just when the financial transaction is about to be consummated? By brokering first mortgage loans for home purchase, a nonprofit potentially can capture the broker fee while making sure that the client receives the best possible loan. By brokering real-estate sales for clients, the nonprofit can again collect the real-estate commission while ensuring that the buyer is well served through the settlement of the transaction.

Nonprofits mobilized during the 1990s to help renters in underserved and emerging markets—many of whom were first-generation homebuyers—to achieve homeownership by training and counseling them in the home-purchase process, and helping them to repair credit and save for a down payment. The nonprofit industry grew as the housing market boomed in the late 1990s and into the 2000s. This growth evolved through three distinct market periods:

1990 to 2002: "Stable Growth"

This was a period of low interest rates and increasingly flexible but generally traditionally based mortgage underwriting (documentation of income required, minimum credit scores and down payment required). While the financial industry became more concentrated through mergers and acquisitions, demand for Community Reinvestment Act (CRA) loans was strong, which resulted in many partnerships between nonprofits and lending institutions. This period also was marked by a strong public policy focus on homeownership and efforts by lenders and financial regulators to promote easier access to home mortgages for low-income families with lowered downpayments and other features.

2003 to 2006: "Housing Market Bubble"

Lending to borrowers with subprime credit grew dramatically as home prices increased at historic annual rates. Home purchases broke records nearly every year and extremely low mortgage interest rates fueled frequent mortgage refinancing. The number of mortgage brokers proliferated; in many markets, brokers were the source of the majority of loans made. While the housing market was strong overall, there were signs of weakness in areas with heavy manufacturing employment as foreclosures rose and home prices weakened.

2007 to the Present: "Bubble Burst"

In late 2006, the boom in home sales began to slow down, as interest rates continued to increase. The financial industry continued to promote high-risk loans aggressively, including adjustable-rate mortgages with initial teaser rates and loans requiring little to no documentation. As housing values began to stagnate, and borrowers could no longer refinance as adjustable-rate mortgage rates ratcheted upward, defaults rose. Investor sentiment toward mortgages rapidly turned pessimistic, and the availability of mortgage credit tightened dramatically. Many nonprofits shifted from pre-purchase homeownership services to default and delinquency counseling. The volume of clients seeking to buy homes declined, with the remaining clients tending to have more troubled credit histories and fewer loan options, despite home prices becoming relatively more affordable.

During the 1990s "Stable Growth" period, some nonprofits ventured into the home-purchase lending arena through subordinated amortizing and non-amortizing mortgages. These second-lien loans could reduce the buyer's down payment and other entry costs or be used to perform needed upgrades or repairs to the property. In many cases, second-lien loans were used as "piggyback" loans to reduce the first mortgage amount to below the threshold requiring private mortgage insurance.

Nonprofits could generally enter this market quite easily. Many already had loan pools funded by federal Community Development Block Grants or other sources, and with the development of Community Development Financial Institutions (CDFI) more nonprofits became involved in direct mortgage lending. The process of making second mortgage loans involved relatively small capital requirements (5 percent to 20 percent of the deal) and was governed by few regulations because of the small volume of mostly subordinated loans. Meanwhile, there were few for-profit lenders providing these loans, but many that were willing to finance the first mortgage in front of the nonprofit's second mortgage (of course, later many of these lenders would develop their own "80-20" piggyback loan programs).

As this period drew to a close and the "Housing Market Bubble" period began, automated underwriting and risk-based pricing paved the way for high-volume lending to borrowers across a very broad range of credit quality standards. During this period, loans to borrowers with subprime credit grew to more than one in every five mortgage loans made in 2005 and 2006. Nonprofit lenders experienced substantial competition from private lenders. Mortgage brokers and lenders offered customers a large variety of products designed to get them in a house immediately without attending homeownership education classes, resolving credit problems, or saving for a down payment. Most well-known prime lenders offered the same kinds of low- or no-down payment mortgages for borrowers with poor credit histories. First-time homeownership was being achieved using increasingly more exotic and risky loan products, and fewer borrowers sought the services of nonprofit programs.

By 2006, the mortgage-lending industry had shifted from one in which first-mortgage originations happened primarily at a mortgage bank to one in which originations happened primarily through a mortgage broker. Brokers are the interface with the client: They take an application, match the borrower to available loan products, and prepare the loan documents for the closing. The broker does not capitalize any loan, but collects a fee from the ultimate lender for performing the front-end services (Jacobides, 2004).

Most nonprofits encouraged clients to use local or national banks rather than brokers. Yet many clients, especially low-income and minority clients with little experience with or trust in banks, preferred to use a mortgage broker (LaCour-Little, 2007). In general, many staff of nonprofits felt they accomplished much of the work involved in developing a mortgage-ready borrower, only to deliver that borrower to a mortgage broker who collected a fee and did not necessarily have the client's best interests at heart. Nonprofits began to look longingly at the fees collected by mortgage brokers as a potential source of self-generated income to support their homeownership education, counseling and other services.

These events set the stage for nonprofits to explore the possibilities of becoming mortgage brokers. In 2007, as the housing market stagnated, adjustable-rate mortgages reset to higher rates, and foreclosures accelerated, nonprofits rallied their resources to counsel homeowners in crisis. But even as nonprofits struggle to respond to this unprecedented need, they will have one eye on the near future when they will have to stabilize neighborhoods devastated by foreclosure, and once again build a bridge to affordable and appropriate mortgage credit for traditionally underserved markets. Importantly, the overall market conditions are causing major changes in real estate markets. One recent report estimates in 2008 the number of mortgage brokerages is likely to fall to about 30,000 from a peak of 53,000 in early 2007 (Hagerty, 2008). In this environment nonprofits will be able to hire staff with experience in the field, but also will face reduced demand for real estate programs overall. .

Nonprofits and Real-Estate Brokering

During the 2002 to 2006 "bubble" period, nonprofits took increasing notice of the fees collected by real-estate brokers. As home values increased and millions of homes were bought and sold, real-estate agents incrementally increased commissions from 5 to 6 to even 7 or more percent of the sales price. Homes were selling quickly and the payoff from brokering a home sale was becoming significant. As thousands of part-time real-estate agents became attracted to this industry, nonprofits began to reevaluate their relationship with real-estate brokers.

To many observers, this was clearly a part of the homebuying process that generated significant revenue and had relatively few perceived barriers to entry. Many nonprofits felt their core customer base of buyers and neighborhoods was inadequately served by the for-profit real-estate broker industry. Brokers failed to understand the unique needs of more marginal buyers and had weaker incentives to serve them because of the lower commissions lower-income buyers represent. Nonprofits were also alarmed by the trend of real-estate brokers partnering and co-locating with a mortgage broker, which they saw as potentially further reducing the likelihood that a client would prepare adequately for homeownership by saving a down payment, building credit, and shopping for the best financing before making a home purchase.

Despite Perceived Benefits, Few Nonprofits Have Entered These Markets

These two lines of business—mortgage brokering and real-estate brokering—seemed like natural fits for nonprofits engaged in assisting underserved buyer markets with other homeownership services for two primary reasons: the opportunity to provide value-added services to underserved markets at an affordable price and the opportunity to earn fee-based income.

> "We spent all this money creating homebuyers – and when it was time to *make* money, we were sending them down the street to a for-profit real estate agent or banker." – Executive Director

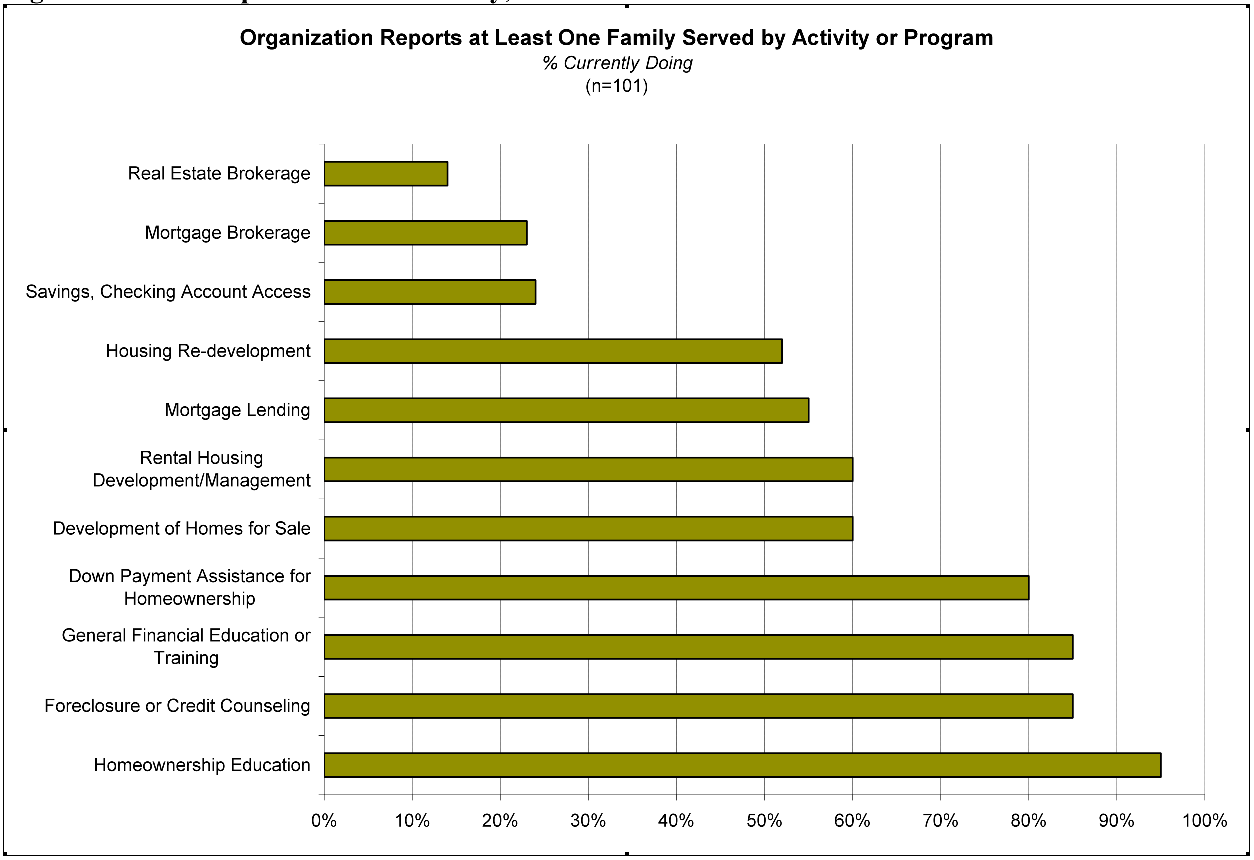
Figure 2 presents an estimate of the prevalence of brokerage programs among community development nonprofits. The survey is based on the responses of the directors of 101 established nonprofits. The median respondent has worked in the field for 15 years, and the average organization served more than 1,500 people annually (see appendix for more detail on the sample, methodology, and findings). More than three out of four organizations are engaged in homeownership promotion through counseling, education or down-payment assistance, or the preservation of homeownership through counseling and education. About two out of three are involved in home construction or development. About half are involved in making mortgage loans.

According to the estimates from this survey, just under 25 percent have an active mortgage brokerage and only 14 percent have an operating real-estate brokerage. This suggests that there are few organizations involved in brokerage programs relative to other homeownership-related strategies. Although no benchmarks are available, the survey is representative of community-based homeownership programs. It is also encouraging that the results are consistent with the findings from interviews conducted for this research.

There is a strong correlation between real-estate development and real-estate brokerage. Over 90 percent of organizations with an active real-estate brokerage also report an active housing development program. Similarly, more than 88 percent of organizations performing mortgage brokerage also have direct mortgage-lending programs and all also offer homebuyer education and counseling. In general, brokerage activity represents a small portion of total clients/families served each year—less than 10 percent of all clients served even among the highest-volume mortgage brokerage programs. It appears brokerage is still in the relatively early stages of development.

> "Our business model focuses on increasing stability and security through homeownership, so we help customers buy a home in the best way possible. It makes no sense to provide education and counseling and then turn them out to others." – Executive Director

Figure 2: NHI Nonprofit Broker Survey, 2008



These findings for mortgage brokers are generally consistent with those by Hornburg (2004) in a study for the Local Initiatives Support Corporation (LISC). In a survey of 109 nonprofits that were identified as being high-volume mortgage-production programs, Hornburg found 34 organizations, or 32 percent, with active brokerage programs in the early 2000s.

There are few nonprofit real-estate brokerages that perform buyer and seller representation. One study of seven NeighborWorks organizations that offered community-based realty services is informative (Ebenhoh, 2003). Three of the seven organizations studied had real-estate agents on staff only because California law required the licenses; only four of the seven performed buyer and seller representation. Nonprofits that are licensed real-estate brokers often only sell properties built or otherwise developed by the nonprofit, primarily a mechanism to avoid paying the commission to a listing agent.

The director of real estate brokerage subsidiary of a nonprofit housing developer mentioned in an interview, "We wanted to represent our own properties and not have to hire a Realtor to list newly developed or rehabilitated properties for sale. Also, many of our customers would leave homebuyer counseling ready to buy and would have a hard time finding an agent to represent them because they were lower-income and the agent didn't believe they were qualified. These buyers were not being treated fairly."

Based on the survey conducted for this project, Table 1 shows that only a small portion of the total households served by CDCs avail themselves of the organizations' mortgage and real-estate brokerages. The total numbers of clients served shows that agencies with higher overall client volumes tend to engage in brokerage more often. Real-estate broker operations appear to be focused on smaller organizations (with the exception of a large number of rental activities for one agency). Nevertheless, both programs remain part of the mix of services provided by CDCs.

Table 1: Number of Families Served Annually by Type of Program, from Survey of 101 CDCs Nationally

	Average Number of Families Served Annually by Type of Program				
	No Brokerage Program	Mortgage Brokerage Program	Real-Estate Brokerage Program	Both Brokerage Programs	All Programs Combined
Development of Homes for Sale	15	26	6	19	18
Down-payment Assistance	51	63	23	71	53
Foreclosure or Credit Counseling	93	134	90	71	99
General Financial Education	185	271	182	165	197
Homeownership Education	267	1,143	260	464	430
Housing Redevelopment	18	30	95	12	28
Mortgage Brokerage	0	13	0	16	14
Mortgage Lending	39	99	16	47	52
Real-Estate Brokerage	0	0	22	57	39
Savings, Checking-Account Access	75	92	18	0	72
Total	**743**	**1,871**	**712**	**922**	**1,002**

2. Nonprofit Mortgage Brokers

For more than 25 years, community development corporations (CDCs) have played an integral role in homeownership by extending the reach of the housing finance industry into underserved populations and communities. Among other activities, this work has included grass-roots outreach and marketing strategies, housing counseling activities, housing development or rehabilitation work, and, in some cases, direct lending assistance, most commonly for housing rehabilitation, down-payment assistance, closing-costs loans, and housing subsidies to enhance affordability.

Increasingly over the past decade, nonprofit organizations have started to expand their lending role by providing first mortgages to low- and moderate-income borrowers for purchase-assistance loans.

The typical reasons that nonprofits pursue this mortgage-broker role include:

- Creating consistent and reliable access to lending services for their clients;
- Being able to compete with unscrupulous mortgage brokers and predatory lenders;
- Providing more control over the lending process;
- Being able to offer clients more or better loan options;
- Creating a source of revenue and financial sustainability for the organization; and
- Fulfilling unmet needs in their communities.

Mortgage Lenders vs. Mortgage Brokers

Mortgage lenders lend money. The borrower signs a mortgage contract with the lender and agrees to a lien on the subject property.

Mortgage brokers do not lend money. They are independent contractors who offer loan products, usually from multiple lenders. Brokers find potential customers and inform them about loan products available from different lenders. Brokers provide advice on making an application for a loan and any potential problems involved in qualifying for a loan.

Brokers take the borrower's application and process the loan. Processing includes compiling a file of documents, including credit reports; property appraisals; verification of income, employment and assets; bank statements; and other required information. The broker does not evaluate the loan; the lender who funds the loan takes the information from the broker and decides to accept or deny the loan application.

Lenders who perform all the loan origination functions themselves are called "retail lenders." Lenders who have certain functions performed for them by mortgage brokers are called "wholesale lenders."

Lenders are further distinguished as "mortgage bankers" or "portfolio lenders." Mortgage bankers sell all the loans they make in the secondary market and generally do not hold mortgages permanently. Portfolio lenders hold loans permanently as an asset, although these lenders may sell servicing or other functions to other firms.

(Guttentag, December 22, 2000)

According to Wholesale Access, a research firm that collects data on for-profit mortgage brokerages, a 2006 survey of more than 50,000 firms shows that the average brokerage produced 151 loans per year totaling $32.4 million (214,000 per loan) ("Mortgage Brokers 2006," 2007). Compare this to Hornburg's estimates for nonprofit brokers, showing the typical program had brokered 64 loans over its entire existence (2004). Nonprofit programs tend to be relatively small in scale and the model for delivering brokered loans by nonprofits is still in its infancy.

2.1 Why Nonprofits Become Mortgage Brokerages

Hornburg (2004) observed two types of nonprofit mortgage brokers. First were full-service brokers providing applicants with disclosures, pulling credit reports and property appraisals, and preparing all documents for the lender. About half of the programs identified provided such services. The other half of the programs were what Hornburg called a hybrid model, where the nonprofit performed some services, but did not deliver disclosures or prepare final documents. Regardless of the model, Hornburg estimated that programs employed three full-time staff for brokerage work, costing the agency $150,000 per year.

This is a significant investment of resources, suggesting that organizations highly value the benefits of these services for clients.

Nonprofit mortgage brokers make life easier for the customer.
Nonprofits have a strong mission-related interest in making sure their customers get the most appropriate loan products. In theory, working with a nonprofit broker ensures that the customer will get the best deal, whether or not through a product that the nonprofit itself offers. If the best product is offered by the nonprofit, it is more convenient for the customer; especially one who was already a client of the program's counseling services. Some nonprofits, such as Homewise in Santa Fe, New Mexico, offer customers of the homeownership services they need to buy a home—from counseling services to selecting a mortgage to purchasing an affordable home built by the nonprofit. This vertically integrated approach is not only more convenient and less confusing for consumers, but also has led to significant long-term savings for customers. According to the survey conducted for this project, this is a leading reason nonprofits with operating brokerages entered this market, as shown in Figure 3.

Nonprofit mortgage brokers can compete with unscrupulous mortgage brokers and predatory lenders.
One study shows minorities pay up to $500 more for the equivalent loan provided by a broker to an equivalent white borrower (Woodward, 2003). A recent paper by Apgar and colleagues at the Joint Center for Housing Studies of Harvard University convincingly argues a "dual mortgage market" has developed in which minorities and low-income people enter the market through a separate "market channel," which is not defined by traditional banking relationships (Apgar & Calder, 2005). This environment is rife with real or perceived discrimination in mortgage pricing, fees, and terms (LaCour-Little, 2007; Longhofer & Calem, 1999). (Woodward, 2003).

For more than a decade, nonprofits have been aggressively combating the unscrupulous and abusive lending practices that occur in low- and moderate-income communities. Many engaged in direct lending to address problems head on. The mission of nonprofit mortgage brokers is to keep their clients' best interest in mind by helping them find the most affordable loan for their needs. According to Figure 3, this is again a leading reason nonprofits with mortgage-brokerage programs entered this market.

Because there are so many problems in the mortgage market with borrowers being deceived or just confused (Lacko & Pappalardo, 2004), a nonprofit broker might offer a better alternative from a consumer-protection perspective. One concept is that of the "Upfront broker" (Guttentag, 2000, 2004). These brokers, which nonprofits generally would embrace, work on behalf of the borrower. Their fees are transparent, and the broker is not working to maximize his or her compensation at the expense of an affordable, sustainable loan for their client. The

Case Study: Mortgage Banking

Indianapolis Neighborhood Housing Partnership (INHP)

INHP started in 1988 with a focus on home-repair lending in a market in which appraisal gaps were a barrier to conventional lending. Since that time INHP has become a high-volume (300 loans per year) nonprofit homeownership agency focusing on financial and home-purchase counseling and home-purchase and home-repair lending, with three locations in Indianapolis.

For most of its history, INHP worked only with "unbankable" borrowers, referring everyone else to its conventional lender partners. Loan funds have been replenished through microsecuritization (minimum $10 million) of the organization's loans for sale to private investors. In terms of risk — and, therefore, in terms of what price the loans can be sold for — INHP thinks of their loans in two categories, "mission" and "deep-mission." Because INHP has only been able to sell its "deep-mission" loans at a discount (less than their face value), its leaders have decided to begin lending to bankable borrowers in order to collect fees that can cross-subsidize their higher-risk lending.

Vice President of Mortgage Lending Joe Huntzinger describes the organization as technology- and leadership-driven, with a strong commitment to mission.

INHP is an approved Fannie Mae seller-servicer, an FHA Title I and Title II lender, and a correspondent lender for U.S. Bank and Self Help. See www.inhp.org for more information.

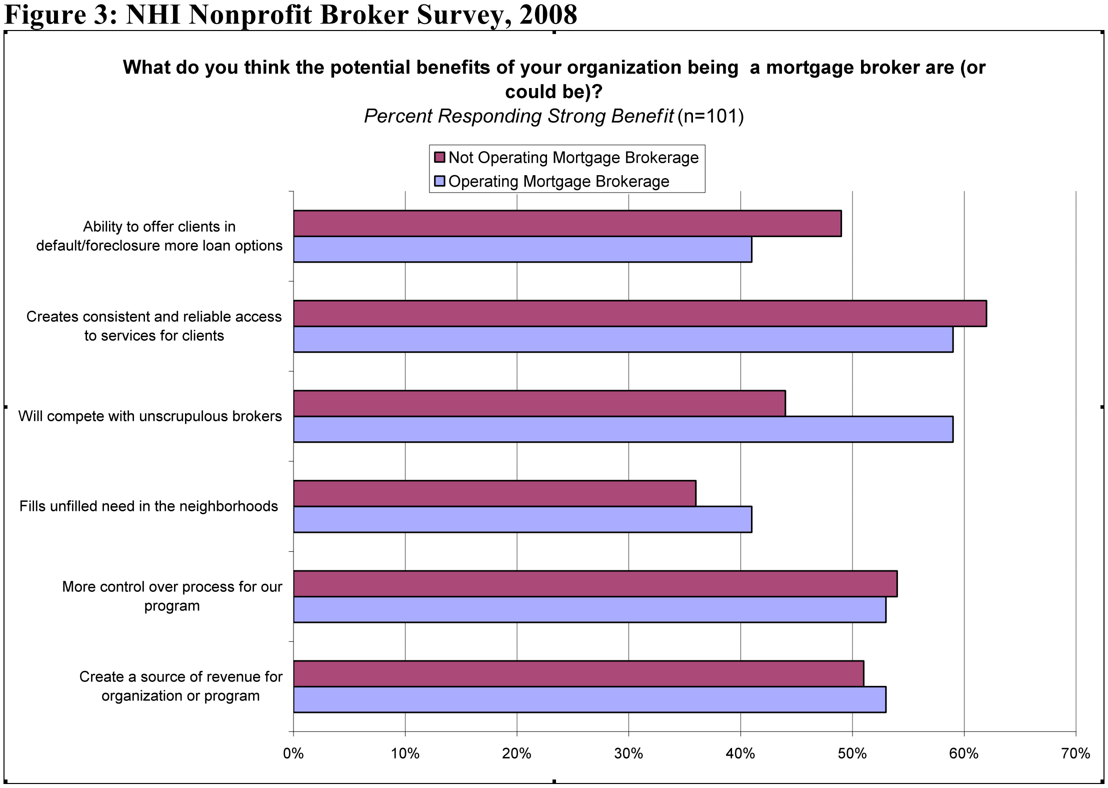
concept has remained on the sidelines of the overall mortgage market, but is attractive for consumer protection and to address current problems with mortgage default and fraud.

Brokerage may provide a source of financial sustainability for homeownership services.
While many industry partners promote the value of pre- and postpurchase education and counseling for consumers and homeowners, few of these partners provide ongoing financial support for these services. Nonprofit organizations spend significant portions of their time raising funds and seeking government grants and other resources to underwrite the cost of these counseling services. Many nonprofits view originating and brokering mortgage loans as an opportunity to obtain a reasonable fee for services to help cover the cost of their counseling services (Turner, 2006). . As one nonprofit broker put it, "Our business model focuses on increasing stability and security through homeownership, so we help customers buy a home in the best way possible. It makes no sense to provide education and counseling and then turn them out to others."

Nonprofit mortgage brokers may be better able to serve underserved markets.
The tightening credit market may make nonprofit mortgage brokers more competitive. As access to mortgage credit tightens, with requirements for higher credit scores and larger down payments, nonprofits can play a key role in finding and preparing borrowers for homeownership. The pace of transactions is now slower than it was during the housing boom, so homebuyers have more opportunity to take the time to improve their credit and seek better loan options.

Nonprofits might be able not only to find borrowers, but also to follow brokered first-mortgage loans with low-interest amortizing or non-amortizing second mortgages. Particularly in high-cost markets, the use of subordinate, below-market rate mortgages (both amortizing and non-amortizing) is critical to making homeownership affordable to low- and moderate-income buyers by helping reduce their monthly housing payments. Some nonprofit brokers report that lenders lack systems to underwrite complex loan packages that include a first mortgage along with several subordinate mortgages. Thus, some nonprofits have set up their own mortgage brokerages to handle these complex but routine transactions.

Figure 3: NHI Nonprofit Broker Survey, 2008



2.2 Challenges to Starting Mortgage Brokerages

Becoming a nonprofit mortgage brokerage is not appropriate for every nonprofit agency. It requires a significant investment in time and resources; and, in some markets, there may be no significant added value in terms of new loan products or services. The challenges often cited in starting up a nonprofit mortgage brokerage by this project's key informants, however, were somewhat different from those cited in maintaining and growing a sustainable mortgage brokerage.

Nonprofit tax status

Concerns about 501(c)(3) nonprofit legal status issues are not minor but are often overestimated. Nonprofits can generate fee-based revenue that is directly related to their charitable mission, and even unrelated income, as long as it remains less than 20 to 50 percent of all revenues (Hornburg, 2004). In furtherance of the nonprofit's charitable mission, the nonprofit should be able to engage in these activities without jeopardizing its tax-exempt status. A nonprofit may need to be prepared to pay unrelated business income tax on some of its activities in this arena, and consultation with a tax professional is recommended. Some nonprofits, following a model used in development, have established subsidiaries to operate mortgage brokerage programs. This may be appropriate, depending on the structure of the organization, but is not a requirement under most state or federal laws.

Start-up time and costs

Significant subsidies and technical support are needed to start a brokerage operation, often for two years or longer. Even after the start-up period, most nonprofit programs require some level of ongoing subsidy, although generally at reduced levels. As a result of these start-up and ongoing costs, conducting a thorough cost-benefit analysis is an important initial step for any nonprofit considering entering this line of business. The availability of significant working capital is also critically important.

A nonprofit mortgage broker in the northeast says, "Like any other new business, the biggest challenge is the need for upfront investment. You can't open a brokerage and achieve the volume that is needed to break even on day one or even day sixty. Funding is needed to cover operations for the first 1-2 years."

Assuming a nonprofit has to hire one new full-time staff with lending experience, provide space, administrative support, and overhead, the annual costs of operating a brokerage operation at a minimum $100,000 (the use of existing staff may not lower the actual costs unless that person has nothing else to do and will be paid anyway). Assuming an average $2,000 broker fee, it would require 50 closed loans per year to break even, or about one per week. Broker operations should easily manage more than one loan closing per week without requiring additional investments. If 75 or 100 loans could be closed, there is legitimate revenue potential. Recall, however, the typical organization surveyed for this report does not close half of the estimated break-even volume.

High-volume loan production goals may conflict with organizational goals.

Most nonprofit organizations considering entering the mortgage brokerage business hope to break even and even to generate excess revenue to help cross-subsidize their other services. However, nonprofit mortgage brokers generally have not been able to achieve break-even production goals when they only serve their core customers—that is, buyers with lower incomes who need intensive, time-consuming, and expensive services. Nor have nonprofits been successful in relying only on their prepurchase education and counseling programs to generate all of their mortgage customers. This means that nonprofit mortgage brokers must get to successful scale by effectively marketing mortgages to stronger buyers who may not qualify for government-subsidized mortgages and grants. This need for greater scale of production may cause conflicts among nonprofit staff and board members, some of whom may see it as mission creep. Higher production goals may also require additional resources to expand and adapt marketing efforts to reach a wider range of customers.

Fear of competing with existing partners.
This was rarely an issue with nonprofits interviewed that were already mortgage brokers, but this concern is often cited as a reason by other nonprofits for deciding not to pursue brokerage activities. National experts and nonprofit brokers interviewed said that nonprofit production will never be significant enough to offer any real competition to the private sector. Moreover, many nonprofit brokers described the benefits of a "business relationship" with lender partners (by working through their wholesale channel rather than the retail channel) to be more lucrative to everyone involved. Nonetheless, this fear persists among many nonprofits that are considering development of a nonprofit brokerage service and that depend on grants from lenders to support their operations.

Many of the nonprofit brokers we interviewed reported they had to confront this issue and adapt to survive. One reported, "We expanded our definition of our market. We serve first-time buyers no matter what income – we have to do that or we can't make it work. We cannot rely on all our customers coming from our homebuyer education and counseling program." Others, meanwhile, adjusted their expectations of revenue downward even while they expanded their customer base, "At first, the partners and brokerage expected and hoped that the program would generate revenue that could support other programs. It quickly became apparent that this was not realistic. The nonprofit's financial goal then shifted to self-sufficiency and breaking even. The focus is not on pumping out numbers but rather on the quality of the transaction. Staff are proud of this change."

2.3 Challenges to Maintaining and Growing Mortgage Brokerages

Providing diverse and competitive loan products to customers
Compared to the typical mortgage broker, few nonprofit organizations have access to a wide variety of loan products. Some have had competitive products, but were overly dependent on one or two key products or sources. If something happened to that source or product, their production suffered while they searched for other competitive products. Negotiating broker relationships with multiple lenders takes more time and a stronger lending track record than most nonprofits have. Special products such as those available from state housing finance agencies or NHSA (a secondary market for the NeighborWorks network) have generally been seen as too conservative, or too complicated or too inflexible to compete effectively with products available in the larger market for longer lengths of time.

Lack of access to capital markets.
Access to FHA-insured products as a direct endorsement lender and to Fannie Mae or Freddie Mac as direct seller-servicers were perceived as important steps to increasing loan production. But nonprofits generally have come to view access to these relationships as a significant hurdle, finding

Case Study:

FAHE/Just Choice Lending

FAHE (Federation of Appalachian Housing Enterprises) is a hub-and-spoke model of mortgage brokering and lending. It is a member-driven collaborative of more than 40 nonprofit organizations that provide affordable housing options in Appalachia. For 20 years FAHE has offered a broad range of mortgage products through its members.

Now FAHE is about to launch a new identity and a retail-lending focus — Just Choice Lending. With federal grant dollars for housing dwindling, FAHE is launching this new model in order to access more capital for its customers, to use the disparate lending capacities and interests of its member agencies, and to achieve greater scale and diversity of loan customers in order to subsidize lower-income customers.

Before Just Choice Lending, FAHE was a wholesale lender, relying on its members to be the only retail face of the operation. In the future, FAHE anticipates that about 50 percent of its business will be retail. To prepare for this change, FAHE has made significant staff changes and invested heavily in marketing (website, advertising, retail business relationships, and a new storefront office).

FAHE has closed about $10 million in loans in its current fiscal year, and intends to close $25 million next fiscal year. Members are compensated for each of the services they provide in preparing borrowers, and can provide as little or as much as they choose. See www.fahe.org for more information.

that the application processes are burdensome and time-consuming. Having access to these secondary markets would increase the array of loan products available to nonprofits as well as provide greater liquidity.

Information management is time-consuming and difficult.
Operating as a mortgage broker requires a significant investment in information management systems and their ongoing maintenance, in order to monitor and update information about loan products, federal regulations and evolving relationships between lenders. In addition, there is the issue of data sharing between loan-origination systems, customer contact systems, automated underwriting systems, and other software systems. Managing these information systems can be challenging to many nonprofits.

Case Study:

Community Equity Mortgage

Community Equity Mortgage (CEM) is a standalone mortgage broker in Tucson with a strong focus on preparing good mortgage customers so that banks will compete for their business. CEM began in 1998, and has been self-sufficient since an initial start-up grant. CEM has broker agreements with major banks and helps its customers shop for the best mortgage they can get.

President Frank Martinez believes in a business model of bundling mortgage brokering with counseling in order to cover the costs of counseling. He says nonprofits must also be able to adjust to the market: in its top year (2005), the organization closed 379 loans and employed 26 staff. In the current market, CEM employs seven staff and hopes to achieve 240 loans for the current year, the program's break-even volume.

Nonprofits are not used to making large investments in technology. Given their limited resources, nonprofits tend to invest in staff before technology. Generally, nonprofits do not invest in the typically expensive origination software packages, nor do they provide adequate training for staff to be competent in the use of these products. Nonprofits rarely have access to or use automated underwriting systems, which is standard practice in the mortgage business. NHSA (a secondary market for the NeighborWorks network) has developed a web-based system that uses alternative loan underwriting criteria and that can work with up to seven layers of financing, but it is in the early stages of marketing to nonprofit customers.

The current environment of a weakening housing market, tightening credit, and general economic turmoil presents immense challenges for nonprofit brokerages.
Nonprofit mortgage brokers are, by design, tied more closely to the private market and the larger economy. Nonprofits are not used to dealing with such dramatic fluctuations in the economy and may struggle to adapt to the current dynamic environment. It is ironic that nonprofits are encouraged to become brokers in part to insulate themselves from the vagaries of philanthropy; however, if they are successful, they become much more dependent on the vagaries of the market. That may be preferable in a stable market, but market conditions since 2006 have meant that nonprofit brokers have faced significant decreases in production and revenue. One nonprofit broker reports a 90-percent reduction in income during the past year, and several of the highest producers report laying off staff during the recent downturn. Given the dynamic business environment in the lending and real-estate industries, nonprofits operating brokerages must monitor market conditions closely and make adjustments quickly. As a result of to their governance structure and overall culture, not all nonprofits are prepared or able to make quick adjustments in their business activities.

"Another group that can benefit from nonprofit brokerages are those who need to refinance high cost loans. The need for this service has grown dramatically over the last few years with the onset of subprime boom and foreclosure crisis. Many are not the strongest borrowers, but at least half have sound credit records. By offering refinance options, nonprofit brokers are offering an important service and can also gain revenue." – Executive Director

Developing and Maintaining Appropriate Staff
In order for a nonprofit to enter the brokerage arena, technical capacity is required. While this could be developed in-house, typically this means hiring an experienced professional from the mortgage-lending field.

These types of professionals tend to be well compensated and are comfortable with incentive or performance-based employment contracts. Additional staff may also be required to process loans and manage brokerage operations. These staff may be recruited from the private sector but also require some additional training.

Many of the experts we interviewed described the staff changes needed to be a successful broker as "cultural barriers" that needed to be overcome. One stated, "There is a culture problem. Nonprofits want to spend as much time as possible with the client and they're not good at marketing. These are big impediments to scalable solutions. The nonprofit culture of not being able to proactively market loans, and not being able to say 'no' hurts volume."

Another high-volume mortgage director said, "You need to hire technically skilled people. We shifted a lot of our people, hired replacements with lending expertise, and doubled our pipeline. We are technology-driven and professional-driven. We are run like a corporation here – we just sell a social product." Yet another mortgage lending director described a deliberate and necessary reorganization in anticipation of moving the organization to high-volume lending capacity, "Almost none of our staff are the same as they were three years ago. Our President had a vision and changed staff to accommodate that. It was terribly difficult for him and a big cultural change for the organization."

Oversight and management of brokerage operations is another important issue to consider. Management staff needs to understand the risks of brokers misrepresenting a borrower or a loan application, or of mishandling loan documents. To the extent that a mortgage could be questioned or a transaction ruined, the agency could face ramifications. An additional issue is how compliance with lending regulations—state and federal laws as well as lender guidelines—is handled. The new business requires maintaining appropriate staffing and oversight guidelines from inception and as the program grows. One program director simply said, "Make sure the staff person doing this stuff is very customer- oriented."

2.4 Legal Issues for Nonprofit Mortgage Brokers

The legal barriers to becoming a nonprofit mortgage broker are not insurmountable.
Note: Nonprofits entering mortgage brokerage must research and obtain locally based legal advice, as there are significant variations in state laws. The following is a general discussion.

While many nonprofits that are exploring the development of mortgage brokerage operations are concerned about legal and regulatory issues as barriers to entry, state licensing requirements were not seen as obstacles by nonprofits that are currently operating as mortgage brokers. Even established mortgage broker programs caution, however, that the demands of compliance issues are a major challenge.

State licensure requirements for mortgage brokers are complex in some respects and highly variable (except the state of Alaska, which has no mortgage-broker licensing requirements). For example, 20 states and the District of Columbia offer exemptions for nonprofit mortgage brokers. While only 17 states require exams for mortgage brokers, 34 states require background checks. Thirty-four states also have educational requirements, which range from no hours of training to more than 115 hours; the average requirement was 33 hours of education as well as 10 hours of continuing education each year. Eleven states require annual fees. The average fee was determined to be $889; the range of fees was $343 to $2,540. Nineteen states had net-worth requirements, with the average requirement totaling $50,278. Forty-five states required surety bonds, with the average surety bond requirement totaling $37,340.

Most established nonprofits with a professional staff will be able to meet these requirements, however, even in states without exemptions. See Appendix F for a state-by-state summary of mortgage-brokerage requirements.

State oversight of mortgage-brokerage operations is tightening.
The current subprime mortgage crisis is triggering closer scrutiny of all mortgage brokers and increasing standards for assets, licensing, and qualifications. This is a positive step, and most credible nonprofits will not be penalized.

Potential conflict of interest between nonprofit counseling and lending roles
Nonprofits that are HUD-approved counseling agencies must walk a careful line between their counseling services and their lending services to avoid a potential or real conflict of interest where clients may be channeled to the in-house mortgage brokerage rather than offered choices of various products in the market. To avoid this conflict, many nonprofits develop firewalls between their counseling and lending functions as well as provide dual-agency disclosures to all customers to be clear about their roles.

Ultimately the decision to develop a nonprofit mortgage-brokerage business is less a technical legal issue than a core governance issue. The decision needs to balance the opportunity of revenue generation against the risks and costs, as well as their potentially expanded roles as brokers against their core mission.

Selected Nonprofit Mortgage-Broker Programs

Organization	**Year Started**	**Staffing for Broker Program***	**Activity #**
Federation of Appalachian Housing Enterprises / Just Choice Lending	2005	8	Goal of $25 million in loans
NHS of Chicago (mortgage banking)	1987	14	685 loans in 2007
Indianapolis Neighborhood Housing Partnership (mortgage banking)	1988	11	266 loans in FY 2008
Neighborhood Housing Services of South Florida	2000	2	Goal of 65 mortgage loans per year
CDC of Long Island	2005	1	8 mortgage loans in 2007 (goal of 50)
NHS Mortgage Company (NHS) of NYC	2007	3	22 loans in 2007 (goal of 88 in 2008)
Homewise, Santa Fe, N.M.	1998	3	167 loans originated in 2007
HomeSight, Seattle	2003	7	Goal of 200 mortgage loans per year
NHS Silicon Valley, Calif.	2000	3	140 in 2007 (goal of 240)
Community Equity Mortgage, Tucson, Ariz.	1998	7	150 per year (goal of 240) in 2007
Ventura County CDC (Cabrillo EDC), Calif.	2002	3	Goal of 60 mortgage loans per year
Manna Mortgage Co., Washington, D.C.	2003	4	66 mortgage loans in 2007 (goal of 70)

* FTEs. These statistics are not consistent across organizations. Some count only positions which would not exist in absence of the mortgage broker program. Others count any position that supports the broker program.

2007 estimates or goals for 2008, except as noted. Sites may follow different fiscal years which account for some variation.

3. Nonprofit Real-Estate Brokers

3.1 Why Nonprofits Become Real-Estate Brokers

Nonprofit real-estate brokers can provide more integrated services for customers.
As shown in Figure 4, nonprofits offering real-estate brokerage services are in part motivated to provide better quality services. Nonprofits often develop long-term relationships with customers who attend their financial and homeownership education and counseling programs. Once these clients have graduated, they are typically asked to find their own real-estate agent to purchase a home. This hand-off can be confusing to customers. And at times, real-estate agents may encourage consumers to purchase more expensive homes than buyers can conservatively afford, since the agent's fee is based on a percentage of the home sale price. To address these issues, some nonprofits have brought real-estate services in-house to enable a seamless transition for their customers to obtain real-estate services, and to ensure that the home they choose is in an acceptably affordable range.

Real Estate Brokers and Agents

A real estate broker has been licensed by his or her state to own and operate a real estate agency, or brokerage. A real estate agent is also licensed by the state and works for a real estate broker. Agents earn their living matching buyers and sellers and are usually paid a commission by the seller of a home.

Realtist is a designation given to an agent or broker who is a member of the National Association of Real Estate Brokers. A Realtor is a member of The National Association of Realtors. Not all brokers are members of either association.

A typical commission is between 5 and 7% of the sale price, and may be split between a selling agent and a buyer's agent. All agents are able to represent both sellers and buyers, but some specialize.

(Source: NeighborWorks® America, 2004)

Nonprofit real-estate brokers can reduce costs on their own housing development activities.
Some nonprofits engaged in affordable housing development activities can reduce the cost of real-estate sales by having an in-house real-estate broker.

Nonprofits can earn revenue through real-estate sales.
When the market is good, a nonprofit can earn a significant amount of income from a real-estate brokerage. One nonprofit reported earning $1.2 million in brokerage income in 2006. The downside is that when the market reverses, the fortunes of the nonprofit can also reverse very quickly. As this director described it, "Our financial health as an organization is now tied to production, which is very dependent on the psychology of the homebuyer – so market fluctuations have a big impact on us."

For-profit real-estate agents are often blamed for steering lower-income families into poor housing and lending choices.
As shown in Figure 4, a leading reason nonprofits enter into real-estate brokerage operations is to compete with unscrupulous brokers targeting their communities. Nonprofit real-estate brokers potentially can protect their existing homeownership customers and help them make better housing choices. Similarly, they can help customers from the neighborhood buy and sell homes and even facilitate consumers to search for and find reasonable and affordable mortgage products.

Frequently, both lower-income potential buyers and lower-income communities are poorly served by for-profit real-estate agents.
Since compensation is based on a commission—a percentage of the home sale price—many for-profit real-estate agents focus their work on higher-income families and higher-end communities to maximize their fees. This means that there are fewer real-estate agents working in the affordable-housing range. Nonprofit real-estate brokers can provide services to these underserved customers and to underserved

communities. Nonprofit brokers can also help to market these neighborhoods and stimulate demand in these historically low-demand areas.

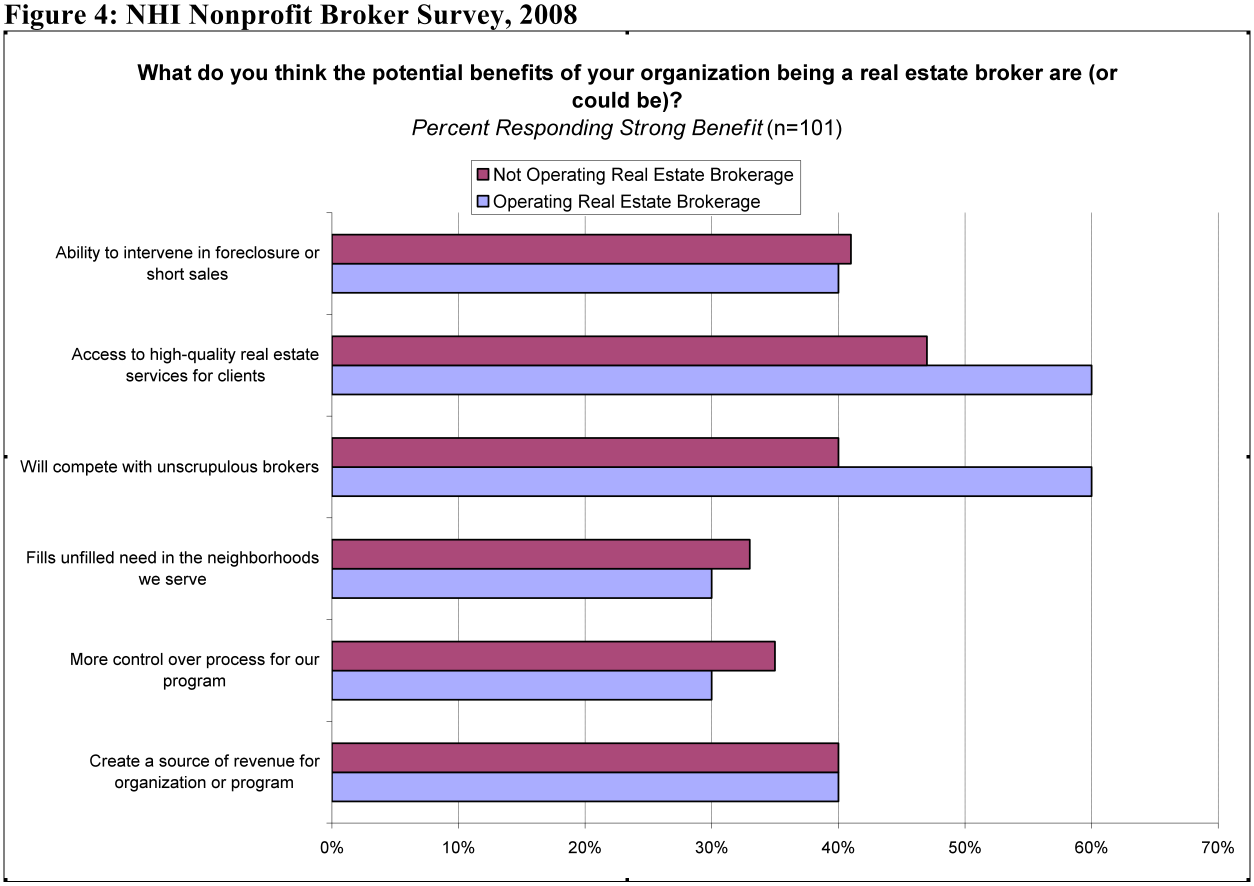
Access to MLS data

Several key informants cited access to Multiple Listing Service (MLS) data as an important benefit of having real-estate agents on staff. The access to this online database can assist in finding properties for potential buyers, for listing properties for sale, and for doing general research about local real-estate markets. The MLS database is searchable in a variety of ways so, for example, users can see what is available in selected price ranges and in selected locations.

In addition to helping customers find properties, the MLS data are useful in helping customers compare prices of similar homes in the various neighborhoods or can be helpful in pricing homes that nonprofits have purchased and/or revitalized for sale.

MLS data have generally been restricted to licensed real-estate agents, but in some areas are available to affiliate members for an annual fee. A recent settlement (in May 2008) between the U.S. Justice Department and the National Association of Realtors may also mean that the MLS listings may be more broadly available on the Internet (Hagerty & Wilkes, 2008).

Figure 4: NHI Nonprofit Broker Survey, 2008



3.2 Challenges to Starting Real-Estate Brokerages

Fear of competing with partners

This fear was often cited as a reason for deciding not to pursue a real-estate brokerage by nonprofits, but it was not an issue with any nonprofit interviewed that is already a real-estate broker. National experts and nonprofit brokers interviewed said that nonprofit production will never be significant enough to offer substantial competition to the private sector. There remains a general concern about the potential for backlash from local real-estate professionals who may provide funding to the nonprofit directly or support the organization indirectly as a volunteer, although again this was not typically raised as an issue by practitioners with experience starting a nonprofit broker program,.

Case Study:

Homewise, Santa Fe, NM

Homewise is a full-service homeownership agency in Santa Fe, and is widely regarded as having pioneered the "vertical integration" model of a nonprofit homeownership provider. Homewise's mission is centered on helping people become more financially secure through homeownership. The organization decided that providing affordable, responsible services for every phase of the homeownership process was critical to achieving this mission. Homewise has grown steadily over the years, creating a new identity for itself and moving into a new retail-focused office. Customers can now receive financial and homeownership counseling at Homewise, and buy an affordable home developed by Homewise, with a Homewise mortgage with the assistance of a Homewise real estate agent. The fees Homewise earns from brokerage services subsidize its counseling and education programs.

See www.homewise.org for more information.

Concerns about attracting and retaining qualified real-estate agents

Some nonprofits were worried about recruiting and retaining qualified real-estate agents on staff. Various strategies were being used by nonprofits to successfully recruit and retain real-estate staff, including competitive salaries and benefits as well as some bonuses for reaching sales quotas. The current downturn in the housing market has made this somewhat of a moot issue, however.

3.3 Challenges to Maintaining a Nonprofit Real-Estate Brokerage

Real-estate brokerages are easier for nonprofits to start up than mortgage brokerages, but the benefits are less clear.

There may be circumstances in which it makes sense for a nonprofit to establish a real-estate brokerage, such as when it is building and selling a significant volume of its own properties or if market-based brokers resist selling or showing houses in a community-development target area.

Nonprofits need to judge if supplanting private-sector agents is a valid goal.

Operating outside the mainstream home sales market may not complement an organization's neighborhood revitalization goals. If a nonprofit seeks a well-functioning real-estate market in a targeted neighborhood, it cannot be the sole source of listings and buyers. In a healthy neighborhood, demand is robust across both subsidized and non-subsidized market segments. To the extent that a nonprofit real-estate broker supplants an active market of listings and showings, the nonprofit may regret its role.

"Nonprofits that are starting up real estate brokerages will need to consider whether or not they will represent sellers. We began our real estate brokerage to help buyers, not to sell homes. Nonprofits need to be careful with this or others will think you are in it for the wrong reasons."

Building a real-estate brokerage is not a simple task.

Creating a real-estate brokerage should not be undertaken by organizations unwilling or unprepared for the responsibilities and time necessary to initiate and sustain the business. It takes time to research and monitor the appropriate licensing requirements, hire and train qualified staff, provide competitive compensation structures, and perform the necessary community outreach. As an alternative, it is also possible to work toward a closer partnership with outside real-estate agents, rather than to bring the full array of realty services in-house.

3.4 Legal Issues for Real-Estate Brokerage

The legal barriers to becoming a nonprofit real-estate broker are minimal. State licensing requirements for real-estate brokers were generally not seen as obstacles by nonprofits that are currently operating as real-estate brokers. There are significant variations in state laws, however. For example, one state and the District of Columbia offer exemptions for nonprofit real-estate agents. State licensure requirements for real-estate brokers are relatively simple, with all states requiring exams, 48 states having educational requirements (the average requirement is 96 hours of education, as well as continuing education), and all states requiring annual fees (the average fee is $264; the range of fees is $50 to $869). Only three states required surety bonds.

Most established nonprofits with a professional staff will be able to meet these requirements readily, even in states without exemptions. See Appendix E for a state-by-state summary of real-estate brokerage requirements.

Case Study:

Community Realty, Albany Region, New York State

Community Realty is a real estate brokerage with a social revitalization mission that specializes in first-time homebuyer representation in four counties in the Albany, New York, region. Community Realty was formed by a collaborative of seven nonprofit community development organizations, collectively known as the Affordable Housing Partnership of the Capital Region, to promote affordable homeownership and strengthen city neighborhoods.

Although it was hoped that the brokerage would earn enough revenue to support some of the other programs of the organizations, this proved to be incompatible with the labor-intensive needs of the "mission" customers the collaborative wants to continue including as a large part of its base. Community Realty does cover its own expenses, and measures success by the quality of the transaction for the buyer. Staff members are proud that 98 percent of their buyers were able to get prime financing.

Community Realty tracks customer data closely in order to manage the balance of mission and revenue. On average, Community Realty works with three clients for each one who buys a home. Typically, each client looks at an average of twelve homes at one hour each. Therefore, for each closed sale, Community Realty invests 50 hours of staff time. The average commission in 2007 was $2,900, and Community Realty closed on 40 homes and worked with 156 clients.

See www.yourownhome.org for more information.

Selected Nonprofit Real-Estate Brokerage Programs

Location/Agency	Model	Volume	Year Started	Staffing
Community Realty (Albany)	Real estate brokerage formed by a collaborative of 7 nonprofits.	In 2007, closed 40 homes and worked with 156 buyers. Total transaction volume of $5,167,000.	2003/ 2004	1 managing broker 1.75 agents .5 licensed assistant
Neighborhood Housing Services of South Florida	Adding real estate services to full-service homeownership agency (development, counseling, real estate, lending).	New brokerage - project less than 20 closings in year one.	2008	2 part time agents
Delta Real Estate **(New Jersey)**	Subsidiary of Affordable Homes Group (umbrella organization for 5 nonprofit housing groups). Created to sell their development and represent their counseling customers. Officed with parent.	In 2007, closed 12 homes.	2000	1 broker 2 agents
Homewise (Santa Fe)	Full-service homeownership agency (development, counseling, real estate, lending).	In 2008, closed 115 purchase contracts. Goal in next fiscal year is 168.	2004	4 agents
NHS Silicon Valley	Full-service homeownership agency (development, counseling, real estate, lending).	Goal is to close 10 homes *per month* or 120 per year, but with market downturn more likely to average 6 per month.	2000	3 agents

4. Legal and Regulatory Issues Facing Nonprofits Considering Brokerage Programs

4.1 Common Themes in State Licensure Requirements for Real-Estate and Mortgage Brokerages

Appendix E and F provide a summary of state laws, and a separate document "Summary of State Laws Regarding Mortgage Brokerage and Real Estate Brokerage for Nonprofit Organizations" includes state-by-state statutes. Based on a coding of these regulations, several themes emerge. The regulation that seems to remain the most consistent across all states, and for both real-estate and mortgage brokers, is a fitness requirement. Honesty, truthfulness, and "generally good moral character" are listed in the majority of state regulations for both types of brokers. This is a generic legal requirement, however, with no real enforcement provisions. One common component is a requirement that the licensee applicant has not had a license revoked, suspended, or denied, and has not been convicted of a felony or crime involving "moral turpitude." This provision covers a range of personal and property crimes, fraud, tax evasion, perjury, mail fraud, and conspiracy to commit such crimes.

Fitness requirements are closely related to the requirement of a background check. This is consistently included across states and often accompanied by a fingerprinting requirement. About half of states require this for both real-estate and mortgage brokers, with other states typically imposing the requirement only on mortgage brokers.

Also fairly consistent across states and both categories of brokerage are the exemptions from licensing for attorneys, accountants, and regulated financial institutions. In some cases the exemption only applies to attorneys licensed in the exempting state, but not always. Eleven states offer exemption from certain provisions of mortgage-brokering regulations if a person has been brokering less than a set number of loans, between one and 10, per year. This exemption is always applicable only to mortgage brokers.

While some states focus on individual real-estate and mortgage brokers, other states include provisions for a firm or corporation to operate as a group of brokers. States that allowed for corporate licensure consistently require background checks of all involved partners and officers, individual licensure for each person participating in brokerage activities, and a designated principal broker in whose name the corporate license is held. Rarely is the principal broker required to have extra education or experience. States that provided corporate licensure are split on whether to license corporate real-estate brokering or corporate mortgage brokering, with only Oregon appearing to license neither. However, several state codes do not explicitly address the issue of corporations.

Requirements for nonresident licensees seem fairly consistent as well. Most states are involved in reciprocity agreements with at least a few other jurisdictions, requiring only filing of a certificate of good standing and a copy of the broker's original license. Where states did not have reciprocity, the applicant was usually required to meet the same requirements as non-licensed applicants.

4.2 Variations in State Licensure Requirements for Brokerages

The three brokerage-licensure requirements that vary most among states were examinations, experience, and education. Most states require examination only for real-estate brokers but not for mortgage brokers, although some require both.

Experience requirements were more commonly imposed on real-estate brokers than on mortgage brokers. The majority of states impose experience requirements for real-estate brokers; slightly less than half of

the states impose experience requirements for both mortgage brokers and real-estate brokers, and only one state imposes experience requirements for mortgage brokers and not for real-estate brokers. The content of experience requirements varies, from one to five years for real-estate brokers and zero to 10 years for mortgage brokers.
Education requirements vary similarly. A substantial majority of the states impose education requirements only on real-estate brokers and not on mortgage brokers. A few states impose education requirements on both, and one state imposes education requirements only on mortgage brokers. The specific requirements are very different. Real-estate brokers are required to have completed a minimum of 20 hours and a maximum of 1,000 hours of training. Mortgage brokers need to have completed between zero and 90 hours of training.

4.3 Provisions for Nonprofit Brokerages

Twenty-two states offer special provisions for nonprofit brokerages. The exemption is for "nonprofit companies acting to increase home ownership for the economically disadvantaged or low income." South Dakota is the only state that exempts nonprofits from some of the financial burdens of becoming licensed, without generally exempting nonprofits from licensing requirements. Nonprofits are exempt from initial license fee requirements, renewal fee requirements, and surety bond requirements.

In general, licensing requirements for mortgage and real-estate brokerage providers should be viewed in a positive light. The past several years have certainly demonstrated the dangers of having a large number of marginally qualified professionals providing mortgages or selling homes. The most beneficial regimen for nonprofits seeking to start a brokerage service might be a blanket exemption for nonprofits from licensing. To the extent that training or education and experience requirements are important protections for the public, these provisions may go too far, however. Rather than risk uninformed or poorly trained people from becoming brokers, the best approach may be the South Dakota model, in which nonprofits are relieved of the financial burdens of licensing but still must meet fitness, experience, and training requirements.

4.4 Real Estate Settlement and Procedures Act (RESPA) Issues

Many nonprofits are concerned about receiving fees for referrals to mortgage brokers and real-estate agents. These concerns derive from the provisions of Section 8 of the Real Estate Settlement and Procedures Act (RESPA), which prohibit fees for referrals in connection with the very broad range of services considered to be "settlement services." The prohibition in RESPA (26 U.S.C. § 2607) prohibits kickbacks and unearned fees. These include:

(a) Business Referrals
No person shall give and no person shall accept any fee, kickback, or thing of value pursuant to any agreement or understanding, oral or otherwise, that business incident to or a part of a real estate settlement service involving a federally related mortgage loan shall be referred to any person.

(b) Splitting Charges
No person shall give and no person shall accept any portion, split, or percentage of any charge made or received for the rendering of a real estate settlement service in connection with a transaction involving a federally related mortgage loan other than for services actually performed.

The definition of a "settlement service" in the regulations is extremely broad (see 24 CFR §3500.2) and pertains to any service provided in connection with a prospective or actual real-estate settlement. The definition includes “provision of any other services for which a settlement service provider requires a borrower or seller to pay,” specifically including taking a loan application, loan processing, acting as a mortgage broker, including counseling services, the rendering of credit reports, and real-estate broker services, among other services.

Therefore, nonprofits engaged in mortgage brokerage or real-estate brokerage, in addition to other homeownership services, will need to design the structure of services and fees carefully. Although rare, violations of RESPA can happen and bring on enforcement actions that include not being able to operate in this market.

In general, the organizations interviewed for this report did not find RESPA to be a major impediment. For full-service mortgage brokers it simply means having systems in place to deliver documents in a timely manner. There are several systems developed in the private sector which can help manage RESPA requirements using computer programs or online tools.[1]

4.5 Caution: Potential Conflict of Interest

Nonprofits that are HUD-approved counseling agencies must walk a careful line between their counseling services and their lending services to avoid a potential or real conflict of interest, in which clients may be channeled to the in-house mortgage brokerage rather than offered choices of various products in the market. To avoid this conflict, many nonprofits develop firewalls between their counseling and lending functions, as well as providing dual-agency disclosures to all customers to be clear about the roles within the agency.

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[1] For example, Blackacre's RESPA, see west.thomson.com.

5. Recommendations for Nonprofits, Intermediaries, and Funders

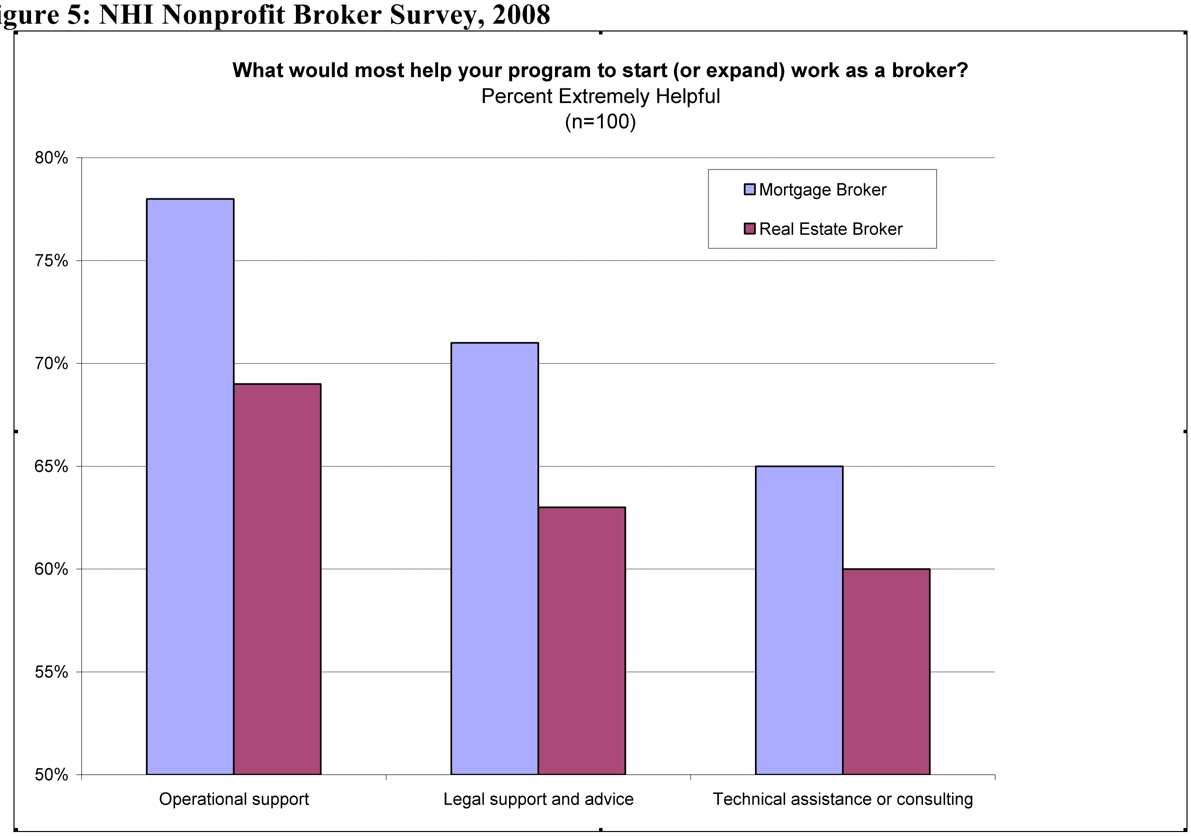
The perceived needs and obstacles for the start-up of a nonprofit brokerage are often different from the challenges of maintaining a sustainable brokerage operation.

Survey results in Figure 5 suggest what support program staff perceive as being important for becoming a nonprofit brokerage. After funding, legal advice and technical assistance were all top concerns. In general, more support was suggested for mortgage brokerage than real-estate brokerage in all three categories, but not by a wide margin.

There are different needs as programs evolve, however. While nonprofits interviewed for this report were often concerned about issues such as competition with the private sector, operational funding, board or staff resistance, and legal or regulatory barriers at the start-up stage, brokerages in operation were much more concerned about sufficient operating capital, access to competitive and affordable loan products, achieving sufficient volume of lending to cover expenses, and adapting to the volatility of the economic environment.

These responses suggest that intermediaries providing support and guidance to nonprofits developing or expanding brokerages need to provide customized technical assistance and long-term operating support for these organizations to be successful.

Figure 5: NHI Nonprofit Broker Survey, 2008



The start-up time and costs for nonprofit brokerages are significant and should not be taken lightly.
Becoming a nonprofit broker is a long-term strategy and requires significant commitment from local nonprofit leadership as well as the support of an institutional partner. The start-up time typically runs over a two-year period and requires significant operating subsidies, customized technical support, and organizational development assistance. Thorough business planning and detailed cost-benefit analyses are important steps for any nonprofit considering entering these lines of business. Even after two years, in order to be successful most programs require some level of ongoing subsidy, although at reduced levels. As one nonprofit leader suggested, “Go slow and take your time to get into it.” Another added, “Create what you think would be a realistic schedule for getting the broker operations up and running...and then double it.”

Even with broad support, becoming a nonprofit broker is not for every nonprofit organization. For example, in a well-designed nonprofit broker pilot program operated by the Housing Partnership Network starting in 2003 (with the support of the Ford Foundation), only three of the eight programs in the pilot decided to move forward with becoming brokers at the end of the pilot period.

Organizations that may be best positioned to become nonprofit brokers exhibit these characteristics: highly entrepreneurial leadership, highly skilled technical staff, willingness to tolerate risks, and commitment to serve broad markets of consumers. One nonprofit executive recommended the leader of the organization “ideally must study for and obtain the broker's license him/herself.” Another commonly voiced sentiment focused on staff recruitment and training. One program director said “Make sure that anyone whom you hire is committed to the mission of the organization and not just [committed] to ‘closing the next deal.”

Organizations also have to be realistic about the revenue potential of real-estate or mortgage brokerage program. Almost every program interviewed echoed a common response in the surveys—that programs starting brokerage operations overestimated the number of clients they would serve. As one leader said, “Do not expect it to be a way to increase profit. Expenses exceed revenue unless volume is very high.”

Mortgage Broker Training Programs

NeighborWorks Training Institute (NTI) www.nw.org.
Course # HO316: The Nonprofit Mortgage Broker (3 days)
This course is designed to reinforce understanding of the current lending environment and the expanded role of the nonprofit lender. Special emphasis is placed on examining brokerage benefits and drawbacks. Participants will learn what is involved in establishing a brokerage operation, as well as examine daily operations and sustainability.

The NTI also offers many other useful courses on lending, compliance issues and marketing.

Mortgage Bankers Association (MBA) www.campusmba.org/default.htm
The MBA offers many training courses, including classroom-based, web-based and live online courses, such as:

- FHA Fundamentals
- Pricing Strategies
- Understanding Loan Products
- Essentials of Residential Underwriting
- Fair Lending Essentials

National Association of Mortgage Brokers (NAMB) www.trainingpro.com/namb/
The NAMB offers extensive classes on mortgage broker issues, including state accreditation courses for mortgage brokers.

Real Estate Broker Training Programs

National Association of Realtors (NAR) www.realtor.org/education/index
NAR also offers classroom-based and online course on many real estate topics including state accreditation courses for real estate brokers. Their courses include:

- Advanced Studies in Market Analysis
- Business Planning and Marketing for the Residential Specialist
- Effective Buyer Sales Strategies
- Ethics for the Real Estate Manager
- Fair Housing for Residential Management
- Innovative Marketing Techniques for Buyer's Representatives

Getting to appropriate scale may require regional collaborative approaches.
Nonprofits pursue brokerage operations both for reasons related to mission and as a way of obtaining fees for their services, but the revenue potential is far more limited than is often assumed. Most nonprofit brokers do not operate at the scale required to offset the expenses of the brokerage and be self-sustaining. In this project's survey, the average annual loan volume was 14 loans among programs operating a mortgage brokerage. This production is well below the estimated volume necessary to break even.

One strategy to address the production scale issue is to develop a hub-and-spoke lending system, whereby nonprofit brokers with sufficient capacity serve a larger network of regional nonprofits. For example, one nonprofit could build the lending capacity to do loan originations for a network of nonprofits in a region or an entire state in order to achieve the necessary scale of operations and volume of loans. These regional nonprofit lending collaboratives are operating in a few locations, such as the Montana Homeownership Network and FAHE. Intermediaries could help support the development of these regional collaboratives by thinking more strategically at the network level rather than supporting the development of individual nonprofit brokers in markets in close proximity.

For example, intermediaries should look for business-to-business strategies that they can use to assist nonprofit brokerages by developing a platform with shared technology tools such as automated underwriting systems, access to competitive and affordable loan products, access to low-cost capital, and high-quality training and networking opportunities for brokerage staff.

The Next Wave? Network Lending Collaboratives

Opportunity Finance Network's "Opportunity Mortgage Network Mortgage Platform"

This system will support finding borrowers, product searches, origination processing, and other services for Community Development Financial Institutions. More than a dozen organizations are part of the system, including several leading nonprofit mortgage brokerages

The mortgage platform uses mortgage products for home purchase or refinancing from its partners, Just Price Systems and Fannie Mae.

For more information:
www.savvysoundandsafe.org .

Opportunity Finance Network
www.opportunityfinance.net

The Ford Foundation has provided support for a new effort called the Fair Mortgage Collaborative—a national collaboration of nonprofit loan brokerages. The goal of this project is to increase the volume of fairly priced mortgages made under a unified mortgage brand to directly compete and displace high-cost and/or predatory mortgage brokers. The collaborative supports the development of nonprofit mortgage brokerages, including new models such as land trusts or cooperative ownership, with the goal of increasing financial resources for lower-income households.

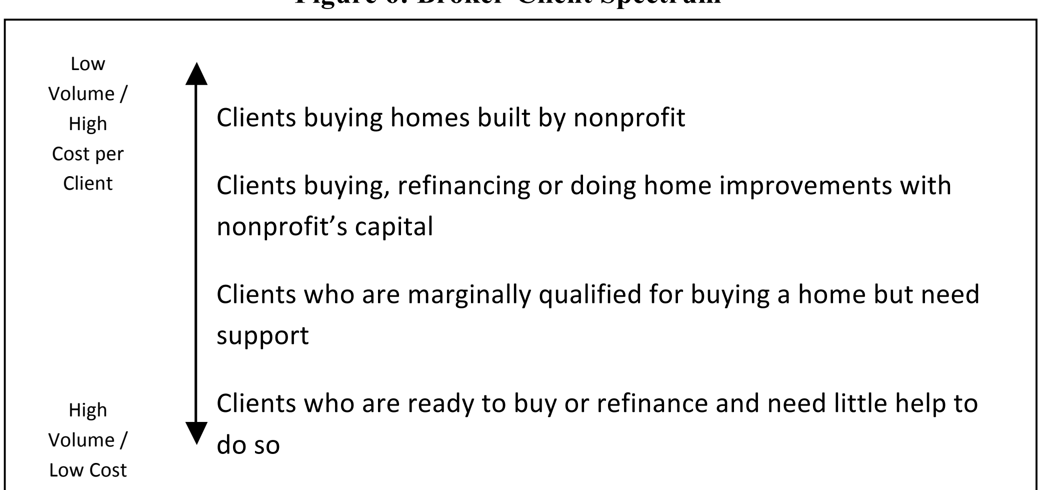
One aspect of the collaborative's work is a nationally scalable web-based information directory connecting homebuyers and homeowners seeking to refinance to real-estate settlement services providers through Mortgage Grader (www.mortgagegrader.com). Through this system, borrowers will also be able to anonymously price-shop for nine essential real-estate settlement services online (www.fairclosingcosts.com).

More detailed research is needed on starting and maintaining brokerage services.
This report focused primarily on the licensure obstacles to start-up nonprofit mortgage and real-estate brokerages. Future research might:

- Compare the demographics of customers of high-volume and low-volume mortgage brokers;
- Identify the costs and production benchmarks for nonprofit brokerages;
- Document the use of technology and other "best practices" in nonprofit brokerages;
- Conduct feasibility analyses of regionalized models; and
- Analyze the replicability of vertically integrated business models.

Nonprofit brokerages should recognize the different typologies of their customer markets and the implications of serving these markets.
One lens for viewing the market for nonprofit brokerage services is to delineate the spectrum of potential clients that may be served. As illustrated in Figure 6 below, this spectrum could be defined as beginning with a level of clients who require highly intensive services (for instance, those clients requiring services such as housing development work, homeownership education and counseling services, deep financial subsidies, or a combination of these services), and as a result are relatively the most costly to serve, on a per-client basis. The next level might be those clients who need high levels of financial assistance from a nonprofit broker's capital for purposes such as purchasing, refinancing, or performing home improvements, but only require modest amounts of ancillary services. A third level might include clients who only need a modest amount of nonprofit financial or counseling services to qualify to buy a home. A fourth level of clients are those who are mortgage-ready or ready to refinance and need little assistance to do so. Given the limited needs of these clients, they would be the least costly to serve on a per-client basis. This spectrum of clients suggests that if increased scale of production is a goal, then nonprofit brokerages on a limited budget need to serve more low-intensity, low-cost customers than high-intensity, high-cost customers. If the goal is to generate fee income to cross-subsidize other nonprofit services, then the approach means serving low-cost clients at scale to offset costs of low-volume, high-cost clients.

Figure 6: Broker-Client Spectrum



6. Conclusion

The barriers—legal and otherwise—to becoming a mortgage or real-estate broker for nonprofits are not insurmountable. While state laws are complex, nonprofits can—and have—successfully entered these businesses.

The mortgage-brokering business is seen as complex and challenging, especially to nonprofits without lending experience. Even nonprofits who are comfortable with multimillion-dollar real-estate development deals can be very apprehensive about lending, viewing it as complicated and risky. There is a clear need to demystify this business and help develop better risk-mitigation strategies in order to encourage more nonprofits to explore entering it.

> "One significant barrier to expanding into this service for most nonprofits is the necessary technical expertise. Running a mortgage brokerage is a business. There are systems to manage and requirements to fulfill. Training is needed to integrate these services into a nonprofit culture."
>
> For funders: "Just putting money out there will not generate a greater number of successful nonprofit brokerages. It's going to require coaching and monitoring – make sure there is an actual plan and monitor success against the plan regularly."

Nonetheless, the start-up time and costs for nonprofit brokerages are significant and should not be taken lightly. Significant subsidies and technical support are needed to start a brokerage operation for at least two years. Even afterward, most programs require some level of ongoing subsidy, although generally at reduced levels. Conducting a thorough cost-benefit analysis is an important initial step for any nonprofit considering entering these lines of business.

Nonprofits pursue brokerage operations both for mission reasons and as a way of obtaining fees for their services, but the revenue potential is far more limited than is often assumed. Most nonprofit brokers generally do not operate at the scale required to offset the expenses of the brokerage and be self-sustaining. In a survey of 101 nonprofit organizations, among programs operating a mortgage brokerage, the average annual loan volume was 14 loans. Among programs operating a real-estate brokerage, the annual sales volume was 39 homes. This production is below the volume necessary to break even. But even if production is at a low volume, brokers take on risk that must be managed and overhead costs that must be covered.

Mortgage brokerages depend on high volume for sustainability, so for organizations that want only to serve mission clients, it may make sense to participate in a larger network of regional nonprofit brokerages in order to achieve that volume. For example, one nonprofit could build the lending capacity to do loan originations for a regional network of nonprofits in order to achieve the necessary scale of operations and volume of loans. These regional lending collaboratives are operating in a few locations and appear to be sustainable.

Nonprofit brokerages who are not interested, willing, or able to make the cultural changes necessary to achieve scale in traditional mortgage lending, may operate best in distinct business or client niches where they have little or no direct competition from the private market. Nonprofits may be able to segment their market and identify underserved customers or business activities that they can effectively serve. These lending business niches could include:

- Home rehabilitation lending services;
- Purchase-rehabilitation transactions;
- Real-estate-owned (REO) or vacant properties; and
- Specialty loan products such as state housing finance loans or FHA loans.

The demands of maintaining and growing a brokerage differ from those of the start-up phase, but are just as challenging. Most nonprofit brokers reported finding that the business is more complicated and challenging than they expected it to be, especially given the current turmoil in the housing market and the overall economy.

Based on key informant interviews, the characteristics of highly productive brokerages include:

- A serious commitment to brokering as a major line of business;
- Highly entrepreneurial board and executive leadership who are comfortable with private-sector business practices such as effective use of marketing and technology;
- The willingness to hire and reward skilled technical staff;
- The willingness to broaden the customer base to include more mortgage-ready customers as a way to increase volume and thus subsidize mission customers; and
- Favorable market conditions.

The tensions between production of loans or closings and the organization's mission should not be underestimated. "Breaking even" can dominate the process and cause major conflicts among staff, board and clients. It is also true that that brokerage programs in some organizations can be aligned within already existing programs so the marginal or incremental costs are less than starting *de novo.* The situation will vary with the organization and its chosen approach.

Legal issues are perceived as a major barrier to starting brokerage services among nonprofit practitioners. As long as programs remain relatively small, mission focused and seek appropriate legal advice, legal issues are not major barriers. In 2008, policymakers at the federal level appeared to be supportive of many changes in real estate and lending laws. Proposed changes to the laws regulating loan and home closings (RESPA and TILA) could create new issues programs need to consider. In the end such efforts are not likely to have a major impact on nonprofit brokerage programs. The primary regulatory mechanism will continue to be precedents set by correspondence or letters drafted by HUD or other agencies to set legal standards, which unfortunately requires continual monitoring and legal interpretation.

Ultimately, the decision of whether to develop a nonprofit real-estate or mortgage brokerage business is less a technical legal issue than a core governance issue. The decision needs to balance the opportunity of revenue-generation against the risks and costs, as well as their potentially expanded roles as brokers against the responsibilities of their core mission.

CAUTIONS FROM THE FIELD:

"This is a risky business and is highly competitive. Nonprofits need to act like for-profits, but they'll have to do even more because they have to make money *and* serve the mission. It's a challenge that shouldn't be taken lightly."

'Nonprofit' needs to be seen as a tax status rather than a method of operating.

"Nonprofits need to realize that adding a brokerage is not like adding a whole new program. If it fits into the overall business model and serves a complementary function, then do it. If it doesn't, then don't."

"It's only for exceptional nonprofits. It's a scale game, and not the way most nonprofits like to work."

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Appendix A: Advisory Committee Members

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Tommy FitzGibbon, President
MB Financial Bank Community Development Corporation
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Community Realty
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Appendix C: Methodology

This study is based on interviews with key informants, a state-by-state legal review, and a survey of practitioners.

More than 25 key informants from the nonprofit community development field were interviewed, as well as funders, lenders, real-estate professionals, and regulatory experts. Interviews were conducted by telephone from November 2007 to June 2008. The interview guide is below. All calls were documented with handwritten notes. Themes from the calls were summarized and then analyzed in the aggregate by the research team.

The state-by-state review of mortgage and real-estate brokerage regulations was completed by a search of each state's statutes, including government Web sites and legal search systems. The summary of laws was reviewed by a practicing attorney and law school faculty. The regulations of each state were documented and are available in a companion document. A matrix summarizing state laws is included in Appendix E.

Finally, this study is based on a survey of 101 community development practitioners regarding their perceptions of mortgage and real-estate brokerage activities, barriers to delivering these services, and related issues. The survey was distributed via email in March and April 2008 to 450 practitioners. The email list for the sample was obtained from NeighborWorks America based on attendees at its mortgage broker and lender trainings from 2005 to 2007. Organizations attending the trainings represent a variety of regions, and more than half have no connections to NeighborWorks, Neighborhood Reinvestment, or the NHS field. This sample is intentionally biased toward homeownership activity and is not representative of all CDCs or housing organizations nationally, but likely does provide a snapshot of higher-volume homeownership-focus agencies. The response rate of 22 percent is typical for online surveys with practitioners, especially given staff turnover for email addresses from trainings several years ago. The first three questions screened out staff of for-profits or government, as well as non-management staff. A total of four duplicate responses were dropped from the data (multiple staff from one organization; the first entry was retained). This left 101 completed surveys. Appendix D summarizes the main results, including the wording of questions. Several open response questions are not included, although those responses were part of the data analyzed by the team in framing this report.

INTERVIEW GUIDE:

Goal of interviews: testing hypotheses (for interviewer only)

1. Community-based nonprofits are interested in expanding into mortgage and/or real-estate brokerage services.
2. Community-based programs have the capacity to expand into mortgage and/or real-estate brokerage services.
3. State laws and regulations present a significant barrier to groups seeking to become mortgage and/or real-estate brokers.
4. The costs, benefits and risks of becoming a mortgage broker are more substantial than for becoming a real-estate broker.
5. Developing brokerage services will not provide a significant source of revenue for most organizations, but may still be desirable based on mission-based objectives.

Introduction Script

The National Housing Institute (NHI) is sponsoring a research project being conducted by PolicyLab Consulting Group, LLC. The goal of this study is to create a report which describes the approaches that nonprofit mortgage and real-estate brokers are taking, and also any regulatory barriers that may prevent expansion into real-estate and financial brokerage services. The project is expected to conclude by June 2008 and the report will be released publicly. No statements by anyone interviewed in this project will be used without prior consent. No materials will be used without attribution.

You have been selected for this interview based on recommendations from NHI and an advisory committee of national experts that assembled to guide this study. Your participation is voluntary, and our conversation will not be recorded, although hand-written notes may be used simply to capture the major ideas discussed. The interview will take approximately 30 minutes. Are you comfortable with this? [If no, terminate interview.]

Overview

1. What has been your experience with real-estate brokerage strategies in the context of nonprofit community development programs? Mortgage brokerage (or banking)?
2. If your program has developed real-estate and/or mortgage brokerage capacity, was it driven first and foremost by a focus on neighborhood revitalization, filling a need in the neighborhood, better serving existing clients, seeking a source of revenue or another consideration? How has this focus developed over time?

Sustainability

3. Does your organization directly deliver all brokerage services you offer? What is the fee-structure like? Are there also partners involved? What does it cost to provide those services—per client? (roughly?) Does this help cover the expenses of other programs?
4. Did you set up an LLC or other entity to deal with risk and liability issues? How difficult was this process?

Outcomes

5. How else do you monitor the success/track results of your brokerage service(s)?
6. Do you define "success" differently for brokerage versus other programs?
7. Can you think of any examples of clients or groups of clients for whom brokerage would make a big difference?
8. What do you consider to be the major accomplishments of your program(s)? What innovations are you most proud of? Do you think these are replicable?

Challenges

9. What are the most significant barriers to expanding into brokerage services? How has your organization attempted to address these barriers?
10. How did the board react? Did you have resistance from the board, or support?
11. How have you managed legal/regulator issues?
12. How about issues of competing with your partners?
13. What recommendations would you have for other organizations?

Capacity

14. What is your assessment of the field's capacity to brokerage services? How does it compare with the demand from potential consumers?
15. How do you staff the program? Number of brokers on staff? What are staff responsibilities?
16. How is the broker paid? Commission? Salary?

17. How would you characterize the level/quality of training available for your staff to deliver brokerage services?
18. What were/are the most significant <u>programmatic</u> (operational) challenges for expanding into brokerage services for your organization?

Marketing/outreach

19. How do you market the program?

Looking Ahead

20. What specific strategies are your highest priorities for the next two years in regards to brokerage services? What advice would you give a major grant maker interested in supporting community-based programs as a platform to launch new brokerage efforts?
21. What would you do differently if you could start again?
22. Can you suggest any relevant reports or publications that we should review?
23. What other organizations/institutions are doing similar work that we should be talking to?

Appendix D: Summary Results of NHI Brokerage Survey

Background of survey respondents:

- Total of 101 responses
- 96% of responding community development organizations were in operation for more than 5 years
- Median organization had 15 years of experience in community development field

Where is your organization located by region?	
	Response Percent
New England	26.5%
Mid-Atlantic	20.5%
Midwest	19.3%
Southeast	15.7%
Pacific	15.7%
Southwest	7.2%
Mountain	4.8%

Q3. Is your organization engaged in each of these strategies?				
	Yes - we are doing it	Yes - we plan to do it	Considered and will not do it	Have not considered
Building new homes for sale	64%	10%	10%	16%
Rehabbing homes for resale	62%	20%	7%	11%
Making market-rate mortgage loans	40%	21%	14%	26%
Making below-market-rate mortgage loans	64%	12%	13%	11%
Being a real-estate broker or having an in-house agent	**24%**	**11%**	**23%**	**42%**
Being a mortgage broker or banker	**47%**	**22%**	**9%**	**21%**
Down-payment assistance for homeownership	84%	9%	3%	3%
Foreclosure or credit counseling	88%	7%	4%	1%
General financial education	83%	11%	3%	2%
Homeownership education	97%	0%	3%	0%
Rental housing development/management	62%	11%	10%	16%
Offer access to savings or checking accounts	24%	8%	19%	49%

Q4. What do you think the potential benefits of your organization being a real-estate broker are (or could be)?				
	No Benefit	Slight Benefit	Somewhat of a Benefit	Strong Benefit
Create a source of revenue for organization or program	7%	19%	34%	40%
More control over process for our program	11%	22%	32%	34%
Fills unfilled need in the neighborhoods we serve	28%	16%	24%	32%
Will compete with unscrupulous brokers	18%	20%	20%	42%
Access to high-quality real-estate services for clients	**17%**	**17%**	**18%**	**49%**
Ability to intervene in foreclosure or short sales	10%	19%	30%	41%

Q5. How much do you think each of the following factors may prevent nonprofits from becoming real-estate brokers?			
	Major Challenge	Minor Challenge	Not a Challenge
Takes too much time	44%	46%	10%
Not produce enough revenue	41%	41%	17%
Risk to reputation	31%	45%	24%
Lack of capacity (staff, technology, know-how)	**60%**	**32%**	**8%**
Poor customer service	15%	42%	43%
Finding funding for start-up	**68%**	**27%**	**6%**
Availability of training	18%	52%	30%
Competition with private sector	53%	34%	12%
Board resistance	30%	49%	20%
Staff resistance	15%	51%	35%
Funder resistance	29%	46%	25%
Legal issues	39%	49%	11%
Lack of technology	17%	53%	30%
Insufficient operating capital	**67%**	**25%**	**8%**

Q6. What would most help your program to start (or expand) work as a real-estate broker?				
	Extremely Helpful	Very Helpful	Somewhat Helpful	Not Helpful
Quality training	52%	25%	18%	5%
Quality materials	49%	29%	18%	4%
Opportunity to network with other specialists	46%	29%	20%	5%
Technical assistance or consulting	**60%**	**26%**	**6%**	**8%**
Operational support	**69%**	**23%**	**4%**	**5%**
Legal support and advice	**63%**	**26%**	**5%**	**6%**

Q8. What do you think the potential benefits of your organization being a mortgage broker are (or could be)?				
	No Benefit	Slight Benefit	Somewhat of a Benefit	Strong Benefit
Create a source of revenue for organization or program	3%	20%	26%	51%
More control over process for our program	**5%**	**19%**	**23%**	**53%**
Fills unfilled need in the neighborhoods	13%	20%	30%	37%
Will compete with unscrupulous brokers	7%	20%	25%	47%
Creates consistent and reliable access to services for clients	**2%**	**15%**	**21%**	**62%**
Ability to offer clients in default/foreclosure more loan options	3%	27%	22%	48%

Q9. How much do you think each of the following factors may prevent nonprofits from becoming mortgage brokers?			
	Major Challenge	Minor Challenge	Not a Challenge
Takes too much time	48%	44%	8%
Not produce enough revenue	42%	46%	12%
Risk to reputation	29%	46%	25%
Lack of capacity (staff, technology, know-how)	**59%**	**36%**	**5%**
Poor customer service	11%	38%	51%
Finding funding for start-up	**69%**	**26%**	**5%**
Availability of training	35%	48%	17%
Competition with private sector	52%	37%	11%
Board resistance	31%	49%	20%
Staff resistance	19%	48%	33%
Funder resistance	29%	47%	24%
Legal issues	38%	54%	8%
Lack of technology	36%	48%	16%
Insufficient operating capital	**73%**	**24%**	**4%**

Q10. What would most help your program to start (or expand) work as a mortgage broker?			
	Extremely Helpful	Very Helpful	Somewhat Helpful
Quality training	60%	27%	13%
Quality materials	55%	30%	14%
Opportunity to network with other specialists	57%	26%	17%
Technical assistance or consulting	**65%**	**25%**	**10%**
Operational support	**78%**	**18%**	**4%**
Legal support and advice	**71%**	**17%**	**12%**