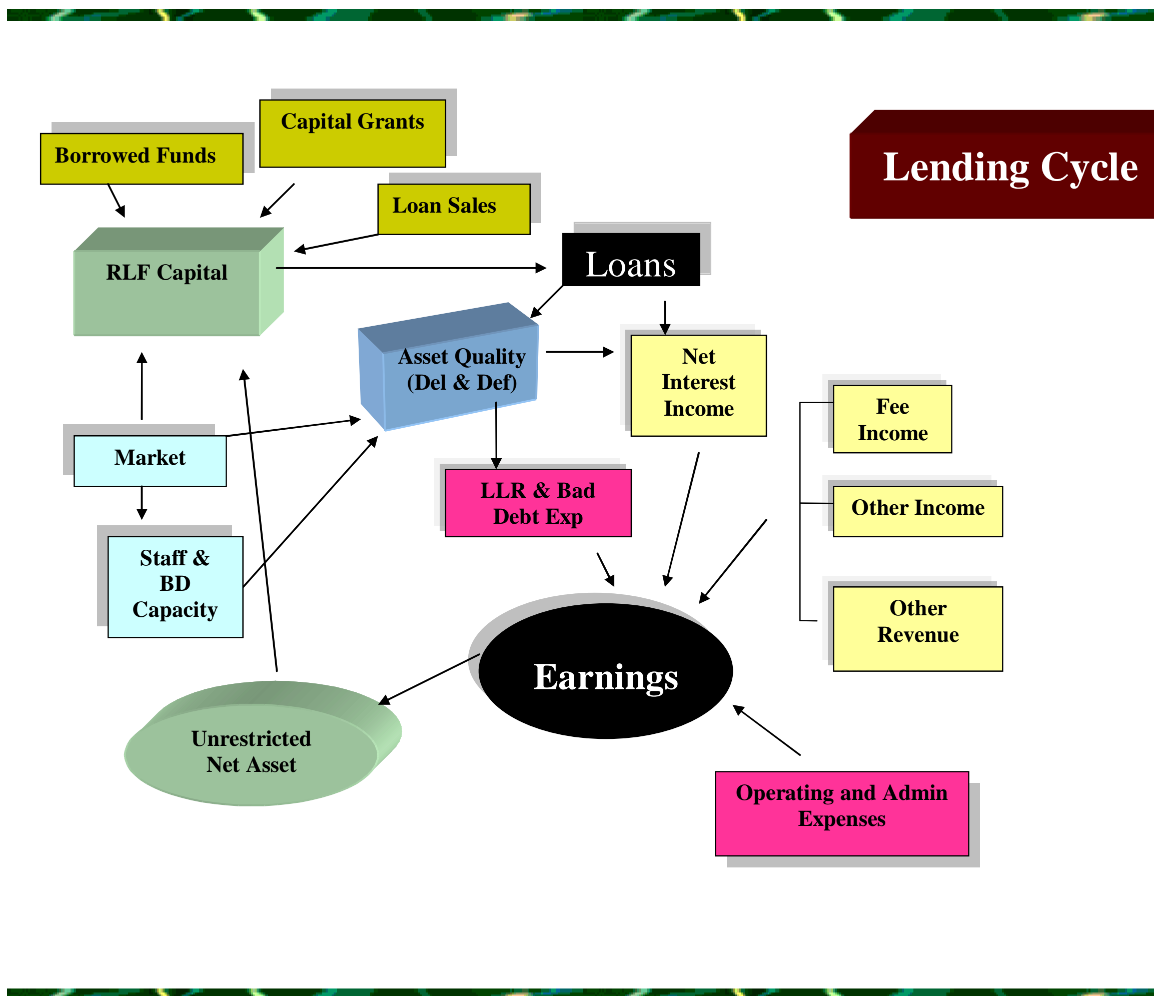
RESIDENTIAL LENDING ASSESSMENT REPORT

JULY 2008 THROUGH JANUARY 2009



REBECCA SEIB
NATIONAL INITIATIVES AND APPLIED RESEARCH

NEIGHBORWORKS® AMERICA

ACKNOWLEDGMENTS

I would like to thank the ten participating NeighborWorks® organizations for allowing me to dive into their organizational records to prepare this Residential Lending Assessment report. A special acknowledgement goes to the leaders of those ten participating organizations Ludy Biddle, NW Western Vermont; Al Gold, Colorado Rural Housing; Kim Bumber, NW Rochester; Debe Mahoney, NW Anchorage; Ron Miller, Reading, NHS; Tim Bolding, United Housing, Inc; Lauren Anderson, NHS New Orleans; Rodney Fernandez, Cabrillo EDC; Michael Loftin, Homewise; and Holly Olsen, Neighborhood Finance Corporation for their continued support and guidance throughout this process. Special thanks to Lauren Anderson for hosting a beautiful convening venue in her home community of New Orleans and enlightening us on the post-Katrina progress in the community. In addition, the staff of these remarkable organizations were very helpful, friendly and cooperative when I or the consultants would interrupt their daily routines and request additional information. I really appreciated the efforts you put forth for the successful completion of this project.

In addition, I would like to thank Michael Schaaf, Andrew Loubert, and Robert Stearns for their professionalism and who, as consultants, conducted many of the assessments while working with me to standardize the reports for the final analysis.

There are a host of others within NeighborWorks® that have been very helpful in the assessment process. Special thanks to Leon Gray, Michael Williams, and Enayat Oliver for their assistance at the NWO convening in New Orleans. In addition, thank you to the members of the NeighborWorks Affordable Financing Products Development Committee that provided assistance in identifying the NWOS and other critical components of the study methodology.

Last but not least, I would like to thank David Dangler, Director of the Rural Initiative and Community Economic Development, for his mentorship and his great support throughout this endeavor, and for serving as a peer reviewer during the final stages of report preparation. In addition, David stepped up to the plate at the NWO convening when I was called away on personal affairs. As always thank you David for your support and assistance.

REBECCA SEIB
NEIGHBORWORKS® AMERICA
APRIL 2009

TABLE OF CONTENTS

INTRODUCTION 4
EXECUTIVE SUMMARY 4
METHODOLOGY 8
LENDING CYCLE 9
RLF BUSINESS MODELS 10
RLF LOAN PRODUCTS 11
PRODUCTION ANALYSIS 12
PERFORMANCE ANALYSIS 13
CAPITAL (CAPACITY MEASURE) 14
ASSET QUALITY (PERFORMANCE MEASURE) 16
MANAGEMENT AND MARKETING (CAPACITY MEASUREMENT) 18
EARNINGS (PERFORMANCE MEASURE) 20
LIQUIDITY (CAPACITY MEASURE) 23
ADDENDUM "A" 26
ADDENDUM "B" 27
ADDENDUM "C" 29
ADDENDUM "D" 30

NEIGHBORWORKS® AMERICA
RESIDENTIAL LENDING ASSESSMENT
REPORT

INTRODUCTION

NeighborWorks® America, a government sponsored enterprise, grew out of the anti-redlining movement in the 1970s. Created as a nonprofit organization by Congress in 1978, NeighborWorks® America supported local community-based organizations in their neighborhood revitalization strategies involving public-private partnerships with strong resident involvement. Core programs in the Network's first decade were owner-occupied rehab affordably financed by local revolving loan funds.

Today, NeighborWorks® HomeOwnership Centers and full cycle lending, inclusive of homebuyer education and residential loans, are the foundation of NeighborWorks® America and its approximately 248 chartered organizations. In the 2007 annual survey 159 NeighborWorks® organizations (NWO) reported some level of direct residential lending, totaling an outstanding loan balance of $648,702,000. Little information is known, however, about *how* the residential lending line of business operates across the Network at the organization level.

The purpose of the Residential Lending Assessment was to assess a cross-section of NeighborWorks® organizations and perform a "deep-dive" into the residential lending line of business. The "deep-dive" was also to include a greater understanding of how a variety of home purchase and improvement products are being financed using first and second mortgages. The study's objectives were as follows:

- Understand more fully how these residential lending lines of business operate and perform.
- Assess the financial strength and operational performance of the residential loan fund (RLF) line of business.
- Test proposed lending standards.

EXECUTIVE SUMMARY

The following report contains a production and performance deep-dive assessment of residential lending line of business of ten NeighborWorks® organizations (NWO). Since the sample organizations were carefully selected and not randomly chosen, the study findings can not be generalized to the entire network. However, the findings reveal certain capacity and performance indicators that warrant further discussion in relation to organizational underwriting, data point collection for the quarterly and annual surveys, and the organizational assessment performance objectives that are now employed. It is hoped that through these discussions that standardized lending indicators will be developed and used interdepartmentally throughout the NeighborWorks® system.

Two socio-economic goals drive the residential loan fund (RLF) line of business –

(1) Access to residential capital for low-income, underserved and disadvantaged communities to access affordable housing and home preservation, and

(2) Generation of unrestricted income to lessen the organization's dependency on outside funding.

These two intertwined and co-dependent goals are essential if the lending line of business is to support the organization's mission over time.

From 159 NWOs claiming residential lending as a line of business, ten NWOs were recommended by the NeighborWorks® Affordable Financing Products Development Committee (Loan Products Committee) to participate in the assessment. These ten NWOs represent eight districts, various geographies and market types (rural and urban), and have a current OHTS rating of strong or exemplary,

The NWOs participating in the assessment were -

NWO	District	Geographic Distribution
1- United Housing, Inc.	Great Lakes	Mixed Rural
2- NHS of Reading	Mid-Atlantic	Mixed Urban
3- NW of Western Vermont	New England	Rural
4- Neighborhood Finance Corp	North Central	Urban
5- NW Rochester	North East	Urban
6- Cabrillo EDC	Pacific	Mixed Markets
7- NW Anchorage	Pacific	Mixed Urban
8- Colorado Rural Housing	Rocky Mt.	Rural
9- Homewise	Rocky Mt.	Mixed Urban
10- NHS of New Orleans	Southern	Urban

During the assessment process three distinct lending business models surfaced – ***Just Lending, Lending Plus**, and **Loan Sales***. As will be seen, these business models become important when analyzing the relative performance of the various RLFs. Two primary loan categories surfaced – Home Buyer Assistance and Home Improvement Loans. Within these categories a variety of loan products were identified including - home mortgages, down payment and closing costs, purchase/rehab, owner/rehab and minor repair loans. Insufficient and inconsistent loan product data limited the depth and scope of the analysis.

PRODUCTION ANALYSIS

An annual production analysis was conducted utilizing nine NWOs borrower databases for calendar years 2005 through 2007. The analysis was conducted in three sections – RLF loan pool aggregate totals, RLF mortgage instrument analysis, and RLF loan payment structure analysis.

During a three-year period (2005-2007), an aggregate total of 2,998 individual loans comprised over $375.4 million in total project values from all sources, of which $114.3 million were RLF loans. When looking at the entire RLF loan pool for the three-year span the following statistics revealed that

- 88% were amortized
- 9% were deferred and
- 3% were forgivable

The aggregate RLF loan pools demonstrated the following stats on mortgage instruments types

- 67% first mortgages
- 27% second mortgages
- 4% other mortgages
- 2% unsecured loans

The mortgage instrument analysis indicated that 94 percent of all RLF loans were secured by first or second mortgages.

The loan payment structure analysis revealed that

- First mortgages -- 99% amortized, 1% deferred,
- Second mortgages --70% amortized, 26% deferred, and 3% forgivable
- Other mortgages -- 24% amortized, 43% deferred, and 33% forgivable
- Unsecured loans -- 82% amortized, and 18% forgivable.

The loan payment structure analysis indicated that the majority of deferred and forgivable loans were secured by second and other mortgage instruments and 99 percent of first mortgages and 70 percent of second mortgages were amortized.

These statistics reveal that only 12% of all RLF loans for this sample were either deferred or forgivable which is less than previously suspected. In addition, 94 percent of all RLF loans, whether housing assistance or home improvement, were secured by a first or a second mortgage position, whereby reducing the RLF investment risk.

PERFORMANCE ANALYSIS

The deep-dive performance analysis was based in CAMEL – ***C****apitalization,* ***A****sset Quality,* ***M****anagement/Marketing,* ***E****arnings, and* ***L****iquidity.* The following is a glance at the deep-dive findings.

Capitalization:

NWOs leveraged NeighborWorks® America capital by attracting borrowed funds from traditional lenders and/or receipt of other capital grants as well as through loan sales to secondary markets (NHSA, banks, and Fannie Mae). In addition the RLF leveraged outside resources through loan deal participation with lending partners

1) NWA capital leveraged at a 2:1 ratio to capitalize the RLF loan pool
2) NWA capital leveraged loan sales to secondary markets to capitalize RLF, and
3) RLF leveraged loan participation with other lenders to make loan deals happen at a 2:1 ratio (one dollar of RLF funds with two dollars of other lenders funds).

Asset Quality

The aggregate total RLF loan pool asset quality was better than the CDFI standard of seven percent. [1] The RLF loan pool demonstrated a three percent 90+ day delinquency ratio and a net loss ratio of below one percent. However, three out of six *Lending Plus* models individually showed an average delinquency ratio greater than the national CDFI delinquency standard while the other business models fell below the national delinquency standard. Further research concerning relationship of asset quality to portfolio management and homeownership counseling should be explored.

Management/Marketing

The NWOs retained qualified staff to originate, service, and foreclose on residential loans. Staff tended to have either mortgage lending, banking or mortgage origination experience prior to being employed by the NWO. All the RLFs had Loan Fund Policies and Procedures in some form to guide the lending process. However, many policies did not address write-offs, portfolio quality control, risk rating, the role of the loan committee, and/or other aspects of loan processing, management, and oversight.

Annual production projections were not uniform among the RLFs analyzed. For example, *Just Lending* and *Loan Sales* business models tended to project RLF annual revenue and expenses, and FTEs dedicated to lending functions. However, the *Lending Plus* business model tended to

[1] The CDFI Fund's MPS governing delinquencies exceeding 90 days (a.k.a. "portfolio at risk") is 7% for CDFIs providing first mortgage loans.

project the number of loans only and not the annual revenue and expenses associated with the lending LOB.

In addition, *Just Lending and Loan Sales* tracked their lending FTEs time and expenses separately from Homeownership Counseling and therefore, could demonstrate 26 loans per FTE per loan and between $4,000 and $7,000 operating expense per loan. *Lending Plus,* on the other hand, did not track lending FTEs and operating expenses separate from the Housing Counseling function and could not calculate FTE per loan or the operating expense per loan.

All lending models prepared an annual budget and reported a budget to actual, loan fund activity and loan fund performance to management and boards, but few reported cash available for lending, and none reported deployment information.

In relation to the lending business models these findings -- annual production projections, FTE per loan, and capitalization requirements -- raise issues around asking the right questions during the organizational underwriting process, quarterly report and annual survey data collection, and the organizational assessment performance measures. It also raises a concern on how to determine the cost of doing business for the *Lending Plus* model if the lending expenses are not segregated from other programmatic activities.

Earnings

The Earnings section was examined by two primary performance analyses – the relationship between cost of funds and price of loans, and whether the loan fund earned sufficient revenues to meet operation expenses.

The relationship between the cost of funds (interest expense) and the price of RLF loans (interest earned) varied between the business' models employed.

- *Loan Sales* demonstrated a 7:1 ratio.
- *Lending* Plus demonstrated a 2:1 ratio
- *Loans Sales and Just Lending* hybrid model demonstrated a 3:1 ratio (for every dollar owed three were earned).

RLF earnings were calculated on revenue minus expenses model. The analysis looked at the operational ratio and the sustainability ratio.

Operational Ratio

An *operational ratio (*earned income/operation expense) determines whether there is sufficient earned income to cover operation expenses. The hybrid *Loan Sales and Just Lending* business model had an operational ratio over 100 percent. *Lending Plus* and *Loan Sales* models did not generate sufficient net interest income, fees and investment fees to cover operational expense.

Sustainability Ratio

A *sustainability ratio* (revenue/operation expense) determines whether there is sufficient revenue to cover operation expenses. *Lending Plus* models were able to generate sufficient revenue to cover all operational expenses. This indicates that other revenue sources such as administrative grants and fundraising activities were generated to cover the costs of doing business. However, *Loan Sales* did not generate sufficient revenue, through grants and donations, to cover operation expenses but had to rely on internal subsidies to cover some of the operation expenses.

In summary, *Loan Sales and Just Lending* hybrid business model showed a 3:1 ratio between cost of funds and the price of RLF loans as well as a greater than 100 percent Operational Ratio. While these figures can not be generalized throughout the network, they indicate that the price of

the RLF loan may exceed the cost of funds by 3-4% to fully cover the operation expenses. The exception to this would be the *Loan Sales* model with a 7:1 ratio between the cost of funds and the price of the RLF loan. The *Loan Sales* model as seen in the body of the report did not reach interest earnings scale and had low interest expense therefore would not be able to cover its operation expenses without subsidies from the parent organization.

Liquidity
Liquidity measure, in this study, refers to the deployment of cash available for lending in relation to outstanding loan balance. The deployment ratio is generally a management tool used to determine whether to seek additional funds to capitalize the loan pool. It must be noted that a good business practice is not to deploy all available funds but retain approximately 25 percent for liquidity purposes. The benchmarks used in this study were 65% and 75% -- if the deployment ratio was 75% or higher the RLF needed to secure more capital for lending; if the deployment ratio was below 65% the RLF had sufficient capital for lending. The study found that the deployment ratio was not dependent on the type of business model employed but was unique to each RLF.

The following Residential Lending Assessment report is divided into 6 sections - methodology, lending cycle, RLF business models, RLF loan products, production analysis, and performance analysis with recommended RLF capacity and performance standards. The performance analysis is sub-divided into capitalization, asset quality, management and market, earnings, and liquidity (the so-called CAMEL).

METHODOLOGY

To assess the capacity and performance of NWOs' residential lending line of business, a formative residential loan fund (RLF) assessment study, a qualitative research methodology, was conducted in three phases -initial research, data collection and analysis, and reporting.

1. ***Initial Research***—the Loan Products Committee approved the recommended NWOs and coordinated with Field Operations, Organizational Assessment Division, and NHSA to secure requested discovery and other NeighborWorks® in-house documentation.

Through this process, ten NWOs were recruited to participate in the study. The NWO selection criteria included:

a. Representation of all eight districts;
b. Geographic distribution among rural and urban organizations;
c. Representation of low to high RLF loan volume as reported on the 2007 annual survey;
d. OHTS rating of Exemplary or Strong as of April 2008; and
e. Agreements with District Directors and the NWOs to participate in study.

Upon obtaining participation agreements with the District Directors and the NWO Executive Directors, RLF discovery and site-visit phases were initiated. The discovery phase utilized existing sources of information, such as three-year audits and management prepared documents, to:

- Conduct a preliminary assessment of the financial strength and organizational capacity;
- Identify residential loan products and the magnitude of use; and
- Identify sources of capital and leveraged resources.

Three experienced lending research consultants were retained to conduct three RLF assessments each. The principal researcher conducted one RLF assessment. The research consultants, in turn,

were trained by the principal researcher on how to conduct the RLF assessment according to a pre-designed CAMEL methodology and the development of a structured report.

2. ***Data Collection and Analysis*** — Data was collected in three venues – structured RLF assessments, borrower databases, and NWO convening.

Upon completion of the initial research phase, research consultants conducted site visits and interviewed key personnel. Each NWO's RLF was assessed independently from the over-all organization's performance and capacity concerns, based on the proposed lending standards found in Addendum "A". The proposed lending standards were integrated into a CAMEL methodology comprising a standardized set of thirty questions to be used during the assessments (Addendum "B"). CAMEL stands for -

a. *Capital*
b. *Asset Quality*
c. *Management*
d. *Earnings*
e. *Liquidity*

The ten individual NWO standardized assessment report findings were aggregated and analyzed.

In addition, the NWOs were asked to submit annual lending production data for the period of January 1, 2005 through December 31, 2007. Utilizing pre-described data points and in cooperation with NeighborWorks® IM Department, an NStep crystal report template was prepared and distributed to the individual NWOs. Nine NWOs provided borrower databases for the proscribed time frame (see Addendum "C" for data points). The borrower databases were exported into an excel spreadsheet and submitted to the principal researcher. The principal researcher subsequently "scrubbed" and sorted the data according to year of loan origination, fund source, source of funds, and type of loans.

An NWO convening was held in January 2009 in New Orleans, LA. Executive staff from nine NWOs attended the two-day convening culminating in recommended CAMEL standards including key indicators, measurements and benchmarks (Addendum "D").

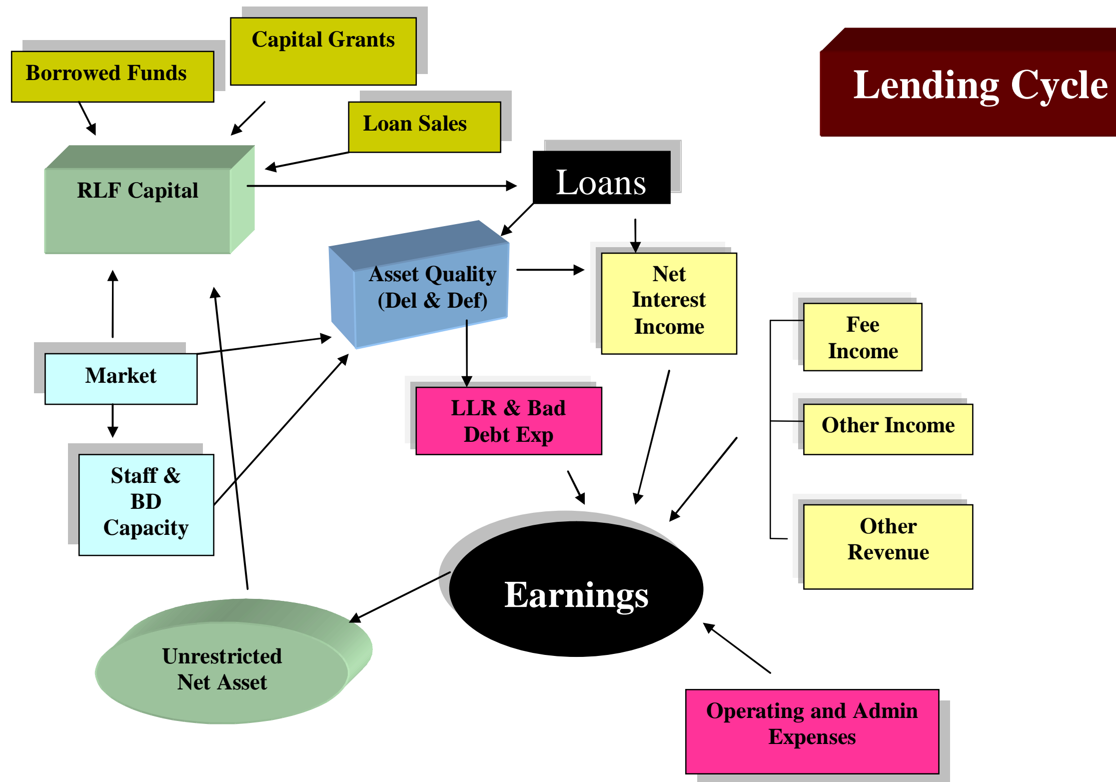
3. ***Reporting*** — Research consultants were required to prepare, in cooperation with their respective NWO Executive Directors and the principal researcher, individual NWO RLF Assessment Reports. The reports were distributed to the NWO Executive Directors and the principal researcher for comments and edits. At this time each NWO was able to submit additional data to clarify capacity and performance information in the draft assessment report. Subsequently, ten NWO RLF Assessment Reports were finalized and distributed to the NWOs and the appropriate NeighborWorks® district personnel.

In addition, this report contains the analysis of the aggregated borrower databases (annual production), an analysis of the standardized RLF questions (performance analysis), and other key observations derived from the RLF assessment. The report was prepared and distributed by the principal researcher to the 10 NWOs and the Loan Products Committee for comments and edits, prior to finalization.

LENDING CYCLE

The RLF line of business is driven by two socio-economic goals – 1) access to residential capital to low and moderate-income individuals, underserved and disadvantaged communities and individuals, and 2) organizational income generation to lessen dependency on outside funding. These two goals intertwine and are dependent upon one another to achieve sustainable community revitalization. The lending cycle provides an illustration of the relationship between

various components of the lending line of business – capitalization, asset quality, management & market, earnings, and liquidity -- and how they inter-relate.



As seen in the diagram above, capitalization of the RLF loan pool can be obtained in four primary areas – borrowed funds, capital grants, loan sales and unrestricted net assets. However, loan pool **capitalization** is influenced by the prevailing **market** conditions. Once capitalization and organizational capacity is addressed, the RLF can provide residential loans to the community. The amount of funds available for lending in relation to the outstanding loans (**liquidity**) determines how much capital is needed to be secured for lending purposes. The performance of the loan pool, or **asset quality**, is dependent on the capacity of **management,** staff and the oversight of the loan pool through the board of directors and/or loan committee. Sound performing loan pools can generate income and other revenue to cover the costs of borrowed funds, programmatic, and operating expenses. The ultimate goal is to have positive **earnings** (net income or net assets) that can be transferred to the parent organization or revolved back into RLF. Positive earnings ensure that the social mission of providing access to mortgage capital for low-income individuals and communities will continue.

RLF BUSINESS MODELS

Three primary Residential Lending Business Models surfaced as the RLF assessment reports were developed.

1) ***Just Lending*** – This business model pertains to just the RLF lending line of business. It is usually found in a subsidiary organization (such as a CDFI) or is segregated as a separate program free from other programmatic components such as Homeownership technical assistance and training. It tends to have multi-layered loan pool capitalization including borrowed funds, capital grants, and loan sales. This model allows for financial transparency of all revenues and expenses associated with the RLF.

2) ***Lending Plus*** – This business model integrates RLF lending with Homeownership Promotion and Homeowner Preservation programs. The model integrates programmatic and lending revenues and expenses and therefore does not allow for financial transparency for the lending component alone. The model primarily tends to capitalize the RLF loan pool with equity funds, such as grants and contributions.

3) ***Loan Sales*** – This business model capitalizes the RLF loan pool primarily with loan sales to outside concerns, such as Fannie Mae, NHSA and/or banks. These loan sales can be with recourse or without recourse. When sold with recourse, a high restricted cash loan loss reserve can appear on the financial statement. This model may allow for financial transparency for the lending component alone and leverages the RLF through the sale of loans with 1st and 2nd mortgages.

These are "pure" RLF business models. NWOs have a tendency to incorporate a hybrid of *Just Lending* and *Lending Plus* with *Loan Sales* to fit their mission and programmatic structure. *Loan Sales* tends to be a capitalization strategy but it can stand alone as a business model as well.

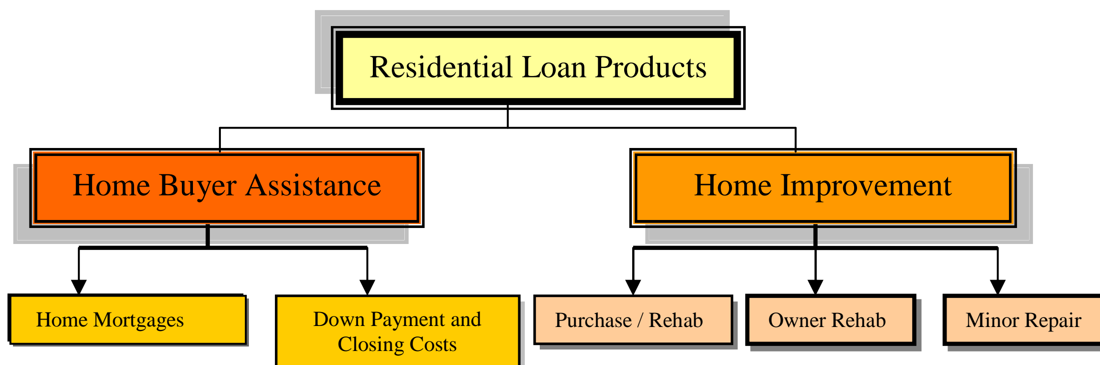
The ten RLFs in the study represented the following business models:

- Six were *Lending Plus;*
- One *Lending Plus & Loan Sales;*
- Two *Just Lending & Loan Sales;* and
- One *Loan Sales*

The business models will be further explored and become important when looking at the loan fund capacity and performance indicators throughout CAMEL.

RLF LOAN PRODUCTS

As evidenced in the RLF assessment there were two primary loan product categories – **home buyer assistance** and **home improvement**. Key personnel interviews revealed a variety of loan products in each category, but between the review of the RLF assessments and scrutiny of the borrower databases, it was impossible to consistently discern these loan products for analysis.



The **Home Buyer Assistance** loan product has two basic loan products – Home Mortgages, and Down Payment/Closing Costs loans.

- Home Mortgage loans are amortized and can be leveraged with other loan providers that offer the 1st mortgage. NWOs also offer Home Mortgages with no outside lender participation that is amortized with 1st mortgage.

- Down Payment/Closing Cost loans are provided by the NWO or leveraged with other loan providers. These loans can be secured through a first, second or other mortgage, and are amortized, deferred, forgivable, or grants.

Home Improvement loan product has three loan products – Purchase/Rehab, Owner/Rehab and Minor Repairs ($2,000 or less).

- Purchase/Rehab loans can be combined with Home Buyer Assistance loans whereas the 1st mortgage can be captured by a lending partner. A lending partner or the NWO can provide the rehab and down payment/closing loan costs which can be an amortized loan, a deferred loan, a forgivable loan or a grant. These loans tend to be secured by a second or other mortgage.
- Owner/Rehab loans can be amortized, deferred, forgivable, or grants. They also can be secured by a second or other mortgage.
- Minor Repair loans are less than $2,000. These loans are not usually secured. They are provided as loans only and can be amortized, deferred or forgivable.

In addition to the above described loan products, the assessments also discovered that some of the NWOs are providing Foreclosure Prevention Loans with no discernable pattern in amortizing vs. non-amortizing loans**.**

PRODUCTION ANALYSIS

Nine of the ten NWOs provided borrower databases from January 1, 2005 through December 31, 2007 representing annual loan production incorporating any loans that may have been sold at a later time (see Addendum "C" for loan production data points). During the three-year period analyzed there were **2,998 individual loans in the aggregate database comprising over $375.4 million in total project value** including RLF funds, leveraged funds and owner's contributions.

Aggregate Annual Production Volume
RLF Funds, Leveraged Funds and Owner's Contributions
2005-2007

9 NWOs	2005	2006	2007	3-yr Totals
Total Annual Principal Amt	***104,510,841***	***128,927,238***	***142,010,706***	***375,448,785***
# of Annual Loans	879	987	1,132	2,998
RLF Funds	**31,418,294**	**40,512,880**	**42,329,138**	**114,260,313**
%RLF to Loan Principal	30.06%	31.42%	29.81%	30.43%
Leveraged	**67,212,161**	**80,975,081**	**91,992,545**	**240,179,787**
%Leveraged to Loan Principal	64.31%	62.81%	64.78%	63.97%
Owner's Contribution	**5,880,386**	**7,439,277**	**7,689,024**	**21,008,686**
% Owner's Contribtuion to Loan Principal	5.63%	5.77%	5.41%	5.60%

RLF funds comprised over 30 percent of the total principal amount[2] in the 3-year totals realizing almost a 2:1 ratio – for every RLF dollar and additional two dollars were leveraged to make the deal flow.

Part of the production analysis was to look at two key questions:

1) Of the total RLF loan volume what percentage are 1st, 2nd, other mortgages, and unsecured loans?

[2] Total principal amount is the total cost of the loan deal. It includes all contributions to make the loan deal happen.

3- Year RLF Loan Production & Mortgage Analysis 2005-2007

	RLF Loan Amt	% of RLF
1st Mortgage	76,055,630	67%
2nd Mortgage	30,839,876	27%
Other Mortgage	4,555,990	4%
Loans	2,808,816	2%
Total RLF Loans	**114,260,312**	

Of the total RLF loan volume 67% were 1st mortgages, 27% were second mortgages and 4% were other mortgages. In addition, only 2% of the total RLF loans were unsecured loans.

2) Of all RLF mortgages and unsecured loans what percentage are amortized, deferred, or forgivable?

3-Year Total RLF Loan Amt, Terms and Mortgage Analysis 2005-2007

	Total RLF Loan Amt	RLF Amortized Loans	% of RLF Amortized Loans	RLF Deferred Loans	% of RLF Deferred Loans	RLF Forgivable Loans	% of RLF Forgivable Loans
1st Mortgage	76,055,630	75,537,292	99%	442,800	1%	75,538	0%
2nd Mortgage	30,839,876	21,695,076	70%	8,104,168	26%	1,040,633	3%
Other Mortgage	4,555,990	1,079,485	24%	1,971,954	43%	1,504,551	33%
Loans	2,808,816	2,304,244	82%	-		504,572	18%
All RLF Loans	**114,260,312**	**100,616,096**	**88%**	**10,518,922**	**9%**	**3,125,294**	**3%**

As illustrated in the chart above, 99% of all RLF 1st mortgages were amortized, and 70% of RLF second mortgages were amortized. Of RLF *other mortgages* 43% were deferred and 33% were forgivable. As for the unsecured loans 82% were amortized.

In summary, one area of concern has been *the degree to which NWOs utilize deferred loans and other non-amortizing loan structures, thus possibly weakening the overall RLF performance.* The annual loan production analysis revealed that non-amortizing loan structures were not a large component of residential loans with first and second mortgages, and when used as an other mortgage type tended to strengthen first and second mortgage lending types. The production analysis demonstrated that the RLF–

- Grew over the 3 years analyzed
- Contained 88% amortized, 9% deferred, and 2% forgivable loans
- Could be further broken out as 67% in 1st mortgages, 27% in 2nd mortgages
- Showed better than a 2:1 leverage ratio of RLF capital to external sources of funding to make the loan deal happen

PERFORMANCE ANALYSIS

The following segment is an in-depth analysis of ten NeighborWorks® organizations' residential lending line of business. This segment divides into five sections presenting each component of CAMEL – ***C****apital,* ***A****sset quality,* ***M****anagement and* ***M****arketing,* ***E****arnings, and* ***L****iquidity*. Within each section there are a series of questions focusing on the aggregate analysis of key capacity and performance indicators of the ten NWOs (see Addendum "C" for a list of the questions).

Following each section, observations are noted along with a recommended CAMEL standard. The CAMEL standards were devised and recommended by the nine NWOs attending a convening held January 28-30, 2008 in New Orleans, LA. During this first and only meeting, NWO executive staff were understandably reluctant to indicate benchmarks for some of the standards. These are noted throughout this section.

Capital (Capacity Measure)
Capital refers to capitalization of the loan fund. The individual NWO assessments reviewed three years of audits, other internal financial documents and conducted key personnel interviews. The audits revealed that each organization had multiple sources of secured funding for re-lending activities. Some of these funds were borrowed from public and private sources such as CDFI and banks. In addition to borrowed funds, the NWOs also capitalized their RLFs with equity funds such as capital grants and contributions, as well as sold loans to a secondary market. The following analysis explores the three avenues of loan pool capitalization and the leveraging of RLF funds.

<u>1) RLF Capitalization</u>
Audits between 2005 and 2007 and other internal financial documents revealed that NeighborWorks® America capital comprised approximately 31percent of total funds in the RLF for re-lending, for slightly better than a 2:1 capitalization leveraging ratio.

The following table shows the aggregated fund sources, notes payable as borrowed funds, and capital grants awarded at the end of fiscal year 2007. Capital grants function as revolving funds and are considered equity[3].

[3] For the purposes of this analysis only, it must be noted that NWA capital in practice functions more like "near equity" due to restrictions in our grant agreement language.

Aggregated Fund Sources to Capitalize RLF 2007

	Fund Source	Notes Payable Outstanding 2007
Borrowed	City	8,209,873
	Banks	4,300,927
	Other Sources	3,250,000
	CDFI	2,088,000
	NHSA	653,044
	Borrowed Total	**18,501,844**
		Grant Amt
Capital Grants	NWA	13,357,520
	City	3,803,386
	Donations	3,000,000
	CDFI	2,023,029
	State	1,221,486
	Other Sources	489,906
	HUD	268,603
	CDBG	258,237
	USDA	250,000
	Corporations	166,658
	Foundations	75,000
	Other Non-Profits	17,242
	Equity Total	**24,931,067**
	Total Funds	**43,432,911**

2) RLF Loan Sales

In addition to the fund sources listed above, some NWOs reported loan sales to secondary markets as a source of funds to capitalize the RLF.

The following chart illustrates to whom loans were sold and the outstanding loan balance at the end of fiscal year 2007.

Sold RLF Loans 2007

Sold Loans	Balance Outstanding 2007
NHSA	4,006,338
Bank Investors	29,584,065
Fannie Mae	11,225,997
Total	**44,816,400**

Four NWOs were able to use their RLF resources to leverage additional funds totaling $44.8 million through loan sales to various secondary market entities to capitalize the loan pool.

3) Funds Attracted to loan deals from outside the RLF

Public and private lending partnerships are a key ingredient to the success of the RLF. The RLFs demonstrated loan deal leveraging partnerships with federal agencies, local banks, municipalities, counties, state, regional development organizations and other like non-profits. These various

partners provided direct loans, deferred loans, forgivable loans and/or grants to the borrower. All of these loan types were considered as leveraged sources. In addition, the borrower and sometimes the seller would contribute to make the loan deal happen.

The best source of data for this leveraging ratio appears in the production data as discussed in the previous report section. As discussed previously, the production data illustrated an RLF 2:1 capitalization leveraging ratio; for every RLF dollar, there were $2 of leveraged funds to make the loan deal happen.

In summary, the NWOs demonstrated that the RLF was comprised of 31 percent of NeighborWorks capital and was able to leverage the RLF in three fundamental ways: 1) loan pool capitalization with a NeighborWorks® capital 2:1 ratio, 2) selling loans to outside secondary markets, and 3) partnering with outside entities to make a loan deals happen which also showed a RLF 2:1 ratio.

Another important aspect of capitalization is minimization of the loan pool risk. This is accomplished through the development of a loan loss reserve (LLR). Some RLF loan pool investors, including buyers of loans, require a certain amount of restricted cash reserves to be set aside to protect their principal investments. On the whole, investor's LLR requirements were met by all NWOs; however, only four NWOs had a written LLR policy. Five had no written LLR policy which caused auditors and management to calculate the LLR and adjust the loan receivables at the time of the annual audit.

As an outcome of the New Orleans convening held in January 2008, participating NWOs recommended the following capital standard, key capacity indicators, measurements and benchmarks.

Capital Standard

The NWO has a credible capitalization plan to support its lending activities.

Key Capacity Indictors :

Indicator	Measurement	Benchmark
Sources of Funds	NWO has adequate sources of funds (public and/or private) to allow continuity of lending.	Projected cash available = projected loan volume
Leverage	NWO leverages resources consistent with operating plans.	
Loan Loss Reserve	NWO has a Loan Loss Reserve policy to determine the LLR amount for all loan products offered.	

Asset Quality (Performance Measure)

Loan fund managers are concerned about the quality of their loans (assets) since loan interest income provides earnings to the RLF. Two indicators are examined in this area - 90+ day delinquency ratio and the net loan loss ratio.

Management tracks 30, 60, and 90+ day delinquencies, however, 90+ day delinquent loans serve as a better indicator to inform the risk of the entire RLF portfolio. The chart below illustrates the aggregate 3-year total outstanding loan balances and the aggregate 3-year total 90+ day

delinquency loan balances for 9 NWOs.[4] The *Loan Sales* model does not hold loans on a long-term basis and therefore no delinquencies were reported in 2005, 2006 and 2007.

Aggregate and Business Models 90+ Days Delinquency Ratio 2005-2007

	3-Yr Aggregate Totals		
	Outstanding Loan Balance	90+ Day Del	Avg Del Ratio
Lending Plus	5,290,056	24,111	0.46%
Lending Plus	15,165,254	278,909	1.84%
Lending Plus	29,382,144	831,101	2.83%
Lending Plus	5,813,491	436,000	7.50%
Lending Plus	6,272,458	1,238,988	19.75%
Lending Plus	7,398,465	3,516,428	47.53%
Lending Plus & Loan Sales	6,317,914	183,076	2.90%
Just Lending & Loan Sales	118,814,211	375,593	0.32%
Just Lending & Loan Sales	27,057,883	250,389	0.93%
Aggregate 3-year Totals	**221,511,876**	**7,134,595**	**3.22%**

According to CDFI Fund the national average delinquency ratio for loan funds providing first mortgages is 7percent. The nine RLF demonstrated an aggregate 3-year average delinquency ratio at 3.22% , well below the CDFI average delinquency ratio. However, three out of six *Lending Plus* models showed an average delinquency ratio greater than the national standard, while the other hybrid models were below. This raises a question concerning the correlation of the asset quality to homeownership counseling and portfolio management.

Delinquent and defaulted loans do not create income for the RLF and therefore are non-performing loans. Loans in default are also called bad debt, bad loans, or “toxic” assets. When writing-off bad debt, adjustments can be made to either the LLR or expensed on the Statement of Activities. But in all cases the outstanding loan balance is adjusted. Some bad debt values are recovered either through foreclosure and asset liquidation or borrower repayment. Therefore, this analysis looks at the net loan loss (bad debt write-offs minus bad debt recovery) as opposed to just bad debt write-offs.

Several of the NWOs have a policy to foreclose and liquidate the asset prior to write-offs. This practice allows for a low or zero net loan loss ratio and lessens the risk of the portfolio. Five of the RLFs reported zero bad debt write-offs or bad debt recovery between 2005 and 2007. The following chart illustrates the remaining five RLFs 3-year aggregate outstanding loan balances and write-offs in relation to the business model.

[4] One NWO, (*Loan Sales)* did not demonstrate any delinquency or loan loss information since they sell their loans upon closing.

Aggregate Business Models Net Loan Loss Ratio 2005-2007

	3-Yr Aggregate Totals		
	Outstanding Loan Balance	**Net Write Offs**	**Avg Loan Loss Ratio**
Lending Plus	5,290,056	(8,373)	-0.16%
Lending Plus	15,165,254	9,694	0.06%
Lending Plus	6,272,458	173,067	2.76%
Lending Plus & Loan Sales	6,317,914	45,300	0.72%
Just Lending & Loan Sales	27,057,883	94,897	0.35%
3-yr Totals	**60,103,565**	**314,585**	**0.52%**

As can be seen, the 3-yr total net loan loss ratio averaged below one percent. This net loan loss ratio is low in comparison to national standards of greater than 2%.

As an outcome of the New Orleans convening, the participating 9 NWOs recommended the following asset quality standard, key capacity indicators, measurements and benchmarks.

Asset Quality Standard

The NWO originates and manages sound performing loans consistent with the mission.

Key Performance Indicators:

Indicator	Measurement	Benchmark
		3 year trend analysis
90+ days Delinquency Delinquencies are determined by 90+days delinquent of outstanding loan balance minus non-amortized loans.	Homebuyer assistance	Tied to local private sector mortgage performance (i.e. market specific) or, <5%.
	Home Improvement	< 10% of outstanding loan balance
	Home Purchase- First Mortgage Lien	
and		*3 year trend analysis*
Net Loan Loss (Write Offs minus bad debt recovery) Net Loan Loss is determined by loans expensed as a bad debt or credited to the restricted LLR cash reserve plus any bad debt recovered as revenue.	Homebuyer assistance	Default rate < 2%
	Home Improvement	
	Home Purchase- First Mortgage Lien	

Management and Marketing (Capacity Measurement)

All of the NWOs in the assessment have qualified staff in place to manage and operate the loan fund, and sometimes make loan decisions. Staff have mortgage origination or loan experience, and/or portfolio management and loan origination training. The Executive Directors felt having staff experienced in the mortgage field was essential to operating and maintaining a sound

residential loan fund. In addition, when a loan committee was utilized to make loan decisions, the assessment found that the committee and/or board members were highly qualified.

All NWOs were in compliance with current mortgage origination state and federal licensing requirements. One NWO, a mortgage banker, had a Nationwide Mortgage License System (NMLS) license as required by federal and state governments. In August 2009, all mortgage originators will be required to have an NMLS license. This includes all non-profits nation-wide. Prior to August of 2009, the NWOs will have to obtain the NMLS license to originate mortgage loans. Upon a random review of the loan files, all NWOs were in compliance with all required legal documents for mortgage loans.

All the NWOs had loan fund policies and procedures in some form. However, four of the ten did not address loan loss reserve in their policies. Also, many of the policies did not address write-offs, portfolio quality control, risk rating, the role of the loan committee or other aspects of loan processing, management, and oversight. Loan fund policies on the whole were not board approved within the last year.

NWOs varied in the planning aspects of the RLF. The *Just Lending* and *Loan Sales* business models tended to project RLF annual loan volume, revenue and expenses (proforma), track FTE dedicated to lending functions and provided a budget to actual. They demonstrated around 26 loans to FTE and between $4,000 and $7,000 operating expenses per loan.

The *Lending Plus* business model tended not to project lending volume, revenue and expenses but rather projected the number of annual loans. Also the number of annual loans to FTE and operating expenses to loan were difficult to calculate since this function is so integrally tied to the homeownership training and technical assistance components of the program. However, these organizations prepare annual budgets and report budget to actual to management and boards.

The NWO Board of Directors provided oversight to the RLF. Management prepared and presented loan fund information to the board of directors and/or the loan committee on a pre-described schedule. All NWOs reported loan fund activity and loan fund performance, but few reported cash available for lending and none report deployment information.

As an outcome of the New Orleans convening, nine NWOs executive staff recommended the following management and marketing standard, key capacity indicators, measurements and benchmarks.

Management and Marketing Standard

The NWO has the staff and board capacity, partnerships developed, and the policies and financial systems in place to operate the RLF in a defined market and be in compliance with all applicable requirements.

Key Capacity Indicators:

Indicator	Measurement	Benchmark
Loan Policies and Procedures	Defined processes for loan approval, underwriting, collateralization, licensing, monitoring and quality control, portfolio mgmt, loan loss reserve, write-offs, and borrower eligibility.	Ratified by Board every year.
Staff and Board Capacity	Dedicated staff and board members have the professional experience and/or education and licensing in related field(s).	Dedicated staff are qualified to originate, underwrite, monitor, and service loan products offered by the NWO (i.e. quality control plan in place).
Market	The NWO operates with a clear understanding of the market trends and has developed loan products to meet the market demand.	A market study or market analysis has been developed and is described in organization's underwriting proposal.
Performance Measures	NWO projects next year's lending activity, including the number and amount of loans, earned income and associated expenses.	Has a cost accounting system for the lending line of business and prepares a report comparing the projected lending activities with actual.
Loan Performance Data	NWO has financial systems in place to report loan fund performance to board and management	Write-offs and delinquency reports per loan fund, individual loan fund outstanding loan balances, new loans approved and loan closure reports, principal repayments, available cash for lending in each loan fund, and interest earned.

Earnings (Performance Measure)

Earnings are calculated on the revenue minus expenses model. One of the questions guiding this section of the report relates to the cost of funds and the price of RLF loans.

What is the relationship between the cost of funds and the price of RLF loans?

Interest income is dependent upon having performing loans on the books, and interest expense is derived from cost of funds borrowed. These two indicators represent the cost of funds and the price of loans.

Depending on the RLF business model employed, interest income and interest expense varies between organizations. The *Loans Sales* business model is based on selling loans to recapitalize the loan pool. This may not allow for a high volume of interest income or interest expense. *Lending Plus* relies heavily on capital grants to capitalize the loan pool and therefore may not demonstrate a significant interest expense. However, *Just Lending* business model can show interest income and interest expense in the financial documents.

The following chart calculates the three-year sum of interest income and interest expense to illustrate the spread between interest income and interest expense for the various RLF business models. As illustrated, only 5 of the NWOs are represented in the chart; 4 NWOs (*Lending Plus*

models) did not borrow funds, and the *Loan Sales & Lending Plus* model could not discern loan interest income from other interest income in their audits and financial documents. Therefore, these five RLFs were omitted from this analysis.

Interest Expense to Interest Income 2005-2007

Business Model	3-yr Interest Income	3-yr Interest Expense	Ratio
Lending Plus (2)	1,026,747	425,646	2:01
Just Lending & Loan Sales (2)	2,290,662	828,525	3:01
Loan Sales (1)	57,604	7,881	7:01
Totals	**2,348,266**	**836,406**	**3:01**

As seen above, the *Loans Sales* model's interest income and interest expense values were low in comparison to the other business models. This model, however, earns some interest while waiting 30-45 days for the loan sale transaction to take place. The ratio shows that for every dollar owed, this RLF business model earned almost $7 to every dollar owed. The risk associated with this approach is that if the RLF were unable to sell their mortgages shortly after funding, then they would sustain a negative arbitrage on interest expense as well as potential higher cost of capital due to the need to convert the borrowed capital form short-term to longer-term notes.

The *Just Lending & Loan Sales* business models earned between three dollars for every dollar owed while *Lending Plus* earned two dollars. It must be noted that the five NWOs analyzed above is a very small number and can not be generalized to the whole population. However, it may indicate that the ***business model type employed may influence the potential spread between price of loans and cost of funds.*** This is an area for further research.

Another question surfaces when analyzing earnings.

Do certain RLF business models generate sufficient earned income to cover all expenses?

Earned Income comprises Net Interest Income, Fee Income, and Investment Income. The question above is directly related to the loan fund's ability to sustain its operations through earned income. The following chart looks at the operational ratio – Earned Income to Total Expenses – of the various RLF business models.

3-Year Total Operational Ratio 2005-2007[5]

	Earned Income	Oper & Admin Exp	Net Income	Opr Ratio
Lending Plus (5)	2,675,814	5,499,794	(2,823,980)	48.65%
Loan Sales & Lending Plus (1)	359,689	1,063,182	(703,493)	33.83%
Loan Sales & Just Lending (2)	4,616,958	3,452,759	1,164,199	133.72%
Loan Sales (1)	435,465	2,215,326	(1,779,861)	19.66%
Totals	**8,087,926**	**12,231,061**	**(4,143,135)**	**66.13%**

[5] Nine NWOs were included in this analysis. One NWO's earned income, except for interest income, and all expenses were attributed to the organization's general fund.

As illustrated, the *Loan Sales & Just Lending* hybrid model earned sufficient income, during the 3-years analyzed, to cover expenses while the other models did not. This suggests that *Lending Plus* and *Loan Sales* may require other types of revenues to sustain lending and programmatic expenses.

The chart below looks at the sustainability ratio – total Revenue to Expenses - of the various RLF business models.

3-Year Sustainability Ratio 2005-2007

	Total Revenue	Oper & Admin Exp	Net Income	Sustainability Ratio
Lending Plus (5)	7,119,672	5,499,794	1,619,878	129%
Loan Sales & Lending Plus (1)	1,158,123	1,063,182	94,941	109%
Loan Sales & Just Lending (2)	4,805,419	3,452,759	1,352,660	139%
Loan Sales (1)	1,922,333	2,215,326	(292,993)	87%
Total	**15,005,547**	**12,231,061**	**2,774,486**	**123%**

Nine RLFs were included in this analysis. One RLF's total Earned Income and Expenses were attributed to the organization's general fund, therefore omitted from the analysis.

As shown above, *Lending Plus* models were sustainable over 100 percent with additional Revenue. Other Revenue may include administrative grants, and donations & contributions. It must be noted that the *Loan Sales* business model above has been in operation for three years and its dependency on the parent organization's subsidies has been declining throughout the time frame analyzed.

In summary, *Loan Sales and Just Lending* hybrid business model showed a 3:1 ratio between cost of funds and the price of RLF loans as well as a greater than 100 percent Operational Ratio. While these figures can not be generalized throughout the network, it indicates that the price of the RLF loan may exceed the cost of funds by 3-4% to cover the operation expenses. The exception to this would be the *Loan Sales* model with a 7:1 ratio between the cost of funds and the price of the RLF loan. The *Loan Sales* model as seen above did not reach scale of interest earnings and had low interest expense nor did it secure additional revenues to cover its operation expenses without subsidies from the parent organization.

As an outcome of the New Orleans convening, 9 NWOs executive staff recommended the following earnings standard, key performance indicators, measurements and benchmarks.

Earnings Standard

The RLF contributes to the NWO's unrestricted income on a continuous basis by earning fees for service, and a positive net income. The NWO has financial strength in the line of business in a way that is appropriate to its mission, risk, sources of funds and market conditions.

Key Performance Indicators:

Indicator	Measurement	Benchmark
	3-year trend analysis -- Income minus Expense formula:	
Loan Fund Sustainability Ratio	**Revenue:** Interest Income (Interest Expense) Investment Income Fee Income Bad Debt Recovery External source contributions (grants, fundraising, etc) **Total Revenue** **Expenses:** Bad Debt Expenses Loan Loss Reserve Expenses Operating Expenses **Total Expenses** **Net Operating Income** **Loan Fund Sustainability Ratio** ________ (Total Revenue/Total Expenses)	Loan Fund Sustainability Ratio should remain the same or increase during the three-year trend.
Net Interest Income Ratio	Interest expense/interest income	Should exceed 1:1

Liquidity (Capacity Measure)

Liquidity ratios usually refer to Current Ratio, Quick Ratio, and Days Cash Available. However, most RLFs do not create a balance sheet but are consolidated with the over-all organization's Financial Position Statement. Therefore, the standard liquidity ratios could not be calculated.

RLF liquidity measures, in this study, refer to the deployment of cash available for lending. The deployment ratio is a management tool that can be used to determine whether to secure additional loan pool funds. It must be noted that a good business practice is to retain approximately 25 percent of cash for re-lending thereby providing a liquidity cushion. The benchmark in the industry for seeking additional cash for lending is equal to or greater than 75 percent. As well, the benchmark that determines whether a loan fund has sufficient cash for relending is below 65 percent.

The deployment formula used in this analysis was

Outstanding Loan Balance/ (Outstanding Loan Balance + Cash Available for Lending)

The following chart shows the aggregate total of outstanding loan balances, cash available for lending, and the deployment ratio for eight RLFs in the study. One RLF (*Loan Sales)* utilized a short-term line of credit for relending along with loan sales to capitalize the loan fund, and therefore had no cash for relending. Once the loans were sold, the capital was immediately turned over into new loans, or the line of credit was repaid. Another RLF's cash available for lending

was held in the parent organization's general fund and could not be discerned from other forms of cash. Those two RLFs were omitted from the following analysis.

3-Year Average Deployment Ratio 2005-2007

Aggregate Deployment Ratio	**2005**	**2006**	**2007**	**3-YR Average**
Total Loan Balances	20,345,304	22,982,035	27,978,352	23,768,564
Total Cash Available	16,862,710	18,833,378	19,294,193	18,330,094
Cash and Balances Total	37,208,014	41,815,413	47,272,545	42,098,657
Deployment Ratio	54.68%	54.96%	59.19%	56.46%

As shown in the aggregate, the RLF loan pool had below 65 percent deployment ratio which indicates sufficient cash for relending. But when looking deeper into the individual RLF business models a clearer picture surfaces.

RLF Business Models 3-Year Average Deployment Ratio 2005-2007

	2005	**2006**	**2007**	**3-YR Average**
Lending Plus	59.29%	55.37%	59.03%	58.02%
Lending Plus	70.98%	75.75%	80.58%	75.77%
Lending Plus	91.91%	89.39%	83.62%	87.90%
Lending Plus	44.80%	76.19%	69.75%	60.42%
Lending Plus	67.95%	31.08%	48.78%	45.77%
Loan Sales & Lending Plus		77.97%	83.41%	80.76%
Loan Sales & Just Lending	41.40%	51.63%	56.65%	50.23%
Loan Sales & Just Lending	43.91%	46.09%	46.60%	45.54%

As shown *Loan Sales & Just Lending* business models had sufficient cash for lending throughout the three year period. The *Lending Plus* business model varied throughout the time frame. However, two *Lending Plus* models and the *Loan Sales & Lending Plus* model suggested the need for additional capital for lending.

In summary, liquidity measures such as deployment ratios are most useful as management tools to determine whether to seek additional funds to capitalize the loan pool. This varies among the RLF business models, suggesting that, the deployment ratio may be a useful tool to determine the amount of capital grant awards as well as a reliable indicator in determining the financial strength of the RFL.

As an outcome of the New Orleans convening, 9 NWOs executive staff recommended the following liquidity standard, key performance indicators, measurements and benchmarks.

Liquidity Standard

The NWO's lending line of business has sufficient liquid assets to fund operations, short-term liabilities and unexpected short-falls. The NWO's lending line of business has sufficient cash available for lending or a plan to secure the funds to meet the annual lending projections.

Key Capacity Indicators:

Indicator	Measurement	Benchmark
Cash Management Plan	Cash management plan inclusive of cash flow projections for all loan products.	projection for 90 days or a clear plan to address any anticipated cash short-fall.
Deployment Ratio	NWO generates internal documents indicating the available cash for re-lending and outstanding loan balance for each funding source.	

ADDENDUM "A"

Proposed Lending Standards For the NWO Residential Lenders	
Indicators	**Lending Standards**
Production	3 year trend Annual Loan volume including annual principal recaptured per loan fund
	Loan Volume Projection to Actual
	Creates an annual lending proforma projecting earned revenues and Operating Expenses
	Comparison of 3 yr trend average to future volume projection
Operating	Annual Direct Loan, Participation, and Equity investment 3-yr trend analysis
	#of loans/FTE
	Cost/ # of loans
	Lending Policy and procedures
	operating expenses/ # loans
	total days loan intake to closing/ # Loans
	Staff and board capacity
	Appropriate lender or broker licenses
	All necessary documents in loan files
	Periodic financial and loan performance reporting to board and management
Leveraging	Annual Direct Loan, Participation, and Equity investment 3-yr trend analysis
Managed Loans	# of loans managed/ # of FTE managing loans
	Loan management operating expenses/ # of managed loans
	Managed Portfolio Earnings/ # of Managed loans
Mission	# & % of loans to underserved individuals
	# & % of loans to underserved communities
Financial	3- yr trend Operating Ratio (Earned Income/Operating Expenses)
	3 -yr trend Sustainability Ratio (Total Revenue/Operating Expenses)
	Lending Net Income/Org Net Income
	InterestExpense/ Interest Income
	Lending Net Cash Flow/Org Net Cash Flow
Liquidity	Lending Net Asset Change/Org Net Asset Change
	Each Loan Fund Deployment Ratio (Outstanding Loan Bal/Cash Available for Lending plus outstanding loan bal)
Risk	Loan Loss Reserve meets investors requirements or Org's Policy and Procedures
	Amount of Loan Loss Reserve/ Amount of Loan Portfolio
Asset Quality	90+days loan bal delinquent/Outstanding Loan Balance per loan fund
	Write off amount/outstanding loan balance per loan fund

ADDENDUM "B"

CAMEL Questions

CAPITAL:

1) What are the sources of funds to capitalize the loan fund? List borrowed funds, Pmt term, and maturity date in a three year trend. List capitalization grants, funder and award date for the last three years?

2) What is the annual direct loan volume, participation and equity investment 3-year trend analysis?

3) Is the Loan Loss Reserve adequate to meet investor's requirements or Organization's Policies and Procedures?

4) What is the ratio of each loan fund's loan loss reserve to the outstanding loan fund portfolio?

ASSET QUALITY:

5) What are the 90+ day delinquency ratios for each loan fund/product and the entire loan portfolio (do not include managed funds)?

6) What is the write-off ration for each loan fund and the entire loan portfolio (do not include managed funds)?

7) What are the 90+ day delinquency ratios for each managed fund?

8) What are the write-off ratios for each managed fund?

MANGEMENT/MARKETING:

9) Does the NWO compare a 3-year average production to future volume Projection?

10) Does the NWO create an annual lending proforma projecting earned revenues and operating expenses associated with the residential lending line of business?

11) Does the NWO project loan volume annually and provide a projection to actual report?

12) What is the number of annual loans to FTE?

13) What is the annual operating expense to the number of loans produced annually?

14) Does the NWO have a current Lending Policy and Procedure that depicts borrower eligibility, underwriting, criteria, loan products, loan loss reserve, write-offs, rewrites/restructured, loan approval process and authority, portfolio risk rating, portfolio management, loan fund committee/board, and other aspects of the lending process?

15) Does NWO staff have the capacity to originate and underwrite loans?

16) Do NWO Board members have the capacity to make loan action decisions?

17) In a random selection of 4 loan files are all required legal documents contained in the files?

18) Does the residential landing line of business periodically report financial and loan performance to the board and management, inclusive of delinquencies, defaults, cash available for lending and deployment ratios?

19) Does the NWO have the required and necessary state lender and broker licenses to conduct a residential lending line of business?

EARNINGS:

20) Does the NWO sell package or service loans? If so, provide descriptions, inclusive of loan owners, dollar volume, number of loans and fees earned in a three-year trend.

21) In a three-year trend what are the operating expenses to sell packaged or services loans outside of the direct lending operations?

22) In a three-year trend what is the net income per managed loan? (Ratio = net income/#of loans)?

23) For the direct lending line of business, what is the operating ratio in a three-year trend (Earned Income/operating Expenses)?

24) What is the sustainability ratio in a 3-year trend (Total Revenue/Operating Expenses)?

25) How much net income is the residential lending line of business contributing to the over-all organization's net income (Lending net income/org net income)

26) What is the contribution of the lending net asset change to the over-all organization's net asset change?

27) What is the ratio of interest expense to interest income in a three-year trend? (Interest expense/interest income)

28) In a three-year trend what is the annual loan volume and annual principal recaptured per loan fund?

LIQUIDITY:

29) What is the deployment ratio of each loan fund and the aggregate loan pool? (Outstanding loan bal/cash available for lending plus outstanding loan balance)

SOCIAL IMPACT:

30) In a three-year trend what is the total # and % of loans going to underserved individuals and underserved communities?

ADDENDUM "C"

Borrower Data Points
Collected Using
NStep Crystal Reports
2005-2007

- Client ID
- Client name
- Zip Code
- Census Tract
- Closing Date
- Purchase Price
- Amount
- Rate
- Term
- Fund Source
- Fund Type
- Source of Funds

ADDENDUM "D"

Recommended RLF Capacity and Performance Standards

The RLF assessment was based on in-house proposed performance standards and a CAMEL methodology (Addendum "A" and Addendum "B"). Upon completion of the individual RLF assessments, each participating NWO received an individual RLF Assessment Report. NWOs recommended RLF capacity and performance standards at a convening held January 28, 2008 in New Orleans, Louisiana. Nine of the ten NWOs attended along with key NeighborWorks® staff. At the culmination of the convening, the NWOs firmly suggested that this process be the beginning of the lending project and not the end. In addition, it must be noted that the NWOs at the convening and during their deliberations engaged in limited discussions on benchmarks for some of the performance standards.

The following are the recommended capacity and performance standards as the nine NWO executive staff recommended.

Capital Standard

The NWO has a credible capitalization plan to support its lending activities.

Key Capacity Indictors :

Indicator	Measurement	Benchmark
Sources of Funds	NWO has adequate sources of funds (public and/or private) to allow continuity of lending.	Projected cash available = projected loan volume
Leverage	NWO leverages resources consistent with operating plans.	
Loan Loss Reserve	NWO has a Loan Loss Reserve policy to determine the LLR amount for all loan products offered.	

Asset Quality Standard

The NWO originates and manages sound performing loans consistent with the mission.

Key Performance Indicators:

Indicator	Measurement	Benchmark
		3 year trend analysis
90+ days Delinquency Delinquencies are determined by 90+days delinquent of outstanding loan balance minus non-amortized loans.	Homebuyer assistance	Tied to local private sector mortgage performance (i.e. market specific) or, <5%.
	Home Improvement	< 10% of outstanding loan balance
	Home Purchase- First Mortgage Lien	
and		*3 year trend analysis*
Net Loan Loss (Write Offs minus bad debt recovery) Net Loan Loss is determined by loans expensed as a bad debt or credited to the restricted LLR cash reserve plus any bad debt recovered as revenue.	Homebuyer assistance	Default rate < 2%
	Home Improvement	
	Home Purchase- First Mortgage Lien	

Management and Marketing Standard

The NWO has the staff and board capacity, partnerships developed, and the policies and financial systems in place to operate the RLF in a defined market and be in compliance with all applicable requirements.

Key Capacity Indicators:

Indicator	Measurement	Benchmark
Loan Policies and Procedures	Defined processes for loan approval, underwriting, collateralization, licensing, monitoring and quality control, portfolio mgmt, loan loss reserve, write-offs, and borrower eligibility.	Ratified by Board every year.
Staff and Board Capacity	Dedicated staff and board members have the professional experience and/or education and licensing in related field(s).	Dedicated staff are qualified to originate, underwrite, monitor, and service loan products offered by the NWO (i.e. quality control plan in place).
Market	The NWO operates with a clear understanding of the market trends and has developed loan products to meet the market demand.	A market study or market analysis has been developed and is described in organization's underwriting proposal.
Performance Measures	NWO projects next year's lending activity, including the number and amount of loans, earned income and associated expenses.	Has a cost accounting system for the lending line of business and prepares a report comparing the projected lending activities with actual.
Loan Performance Data	NWO has financial systems in place to report loan fund performance to board and management	Write-offs and delinquency reports per loan fund, individual loan fund outstanding loan balances, new loans approved and loan closure reports, principal repayments, available cash for lending in each loan fund, and interest earned.

Earnings Standard

The RLF contributes to the NWO's unrestricted income on a continuous basis by earning fees for service, and a positive net income. The NWO has financial strength in the line of business in a way that is appropriate to its mission, risk, sources of funds and market conditions.

Key Performance Indicators:

Indicator	Measurement	Benchmark
	3-year trend analysis -- Income minus Expense formula:	
Loan Fund Sustainability Ratio	**Revenue:** Interest Income (Interest Expense) Investment Income Fee Income Bad Debt Recovery External source contributions (grants, fundraising, etc) **Total Revenue** **Expenses:** Bad Debt Expenses Loan Loss Reserve Expenses Operating Expenses **Total Expenses** **Net Operating Income** **Loan Fund Sustainability Ratio** ________ (Total Revenue/Total Expenses)	Loan Fund Sustainability Ratio should remain the same or increase during the three-year trend.
Net Interest Income Ratio	Interest expense/interest income	Should exceed 1:1

Liquidity Standard

The NWO's lending line of business has sufficient liquid assets to fund operations, short-term liabilities and unexpected short-falls. The NWO's lending line of business has sufficient cash available for lending or a plan to secure the funds to meet the annual lending projections.

Key Capacity Indicators:

Indicator	Measurement	Benchmark
Cash Management Plan	Cash management plan inclusive of cash flow projections for all loan products.	projection for 90 days or a clear plan to address any anticipated cash short-fall.
Deployment Ratio	NWO generates internal documents indicating the available cash for re-lending and outstanding loan balance for each funding source.	