

## The Role of Housing Counseling in Reducing Mortgage Delinquency and Foreclosure

By Laura Williams<sup>1</sup>

The following is a brief summary of the research evidence<sup>2</sup> on the role of housing counseling in reducing mortgage delinquency and foreclosure.

### **1. There is strong evidence that housing counseling can be an effective intervention in helping distressed homeowners avoid foreclosure. Specifically:**

- A nationwide study of the foreclosure mitigation counseling program found that borrowers who had missed a payment on their mortgage were 45 to 50 percent more likely to get up-to-date on payments if they received counseling.<sup>3</sup>
- Homeowners in default who received counseling were twice as likely to avoid foreclosure as those who did not in a study of the Mortgage Foreclosure Prevention Program in Minneapolis.<sup>4</sup>

**2. Early intervention is important.** One study found that borrowers who received counseling in the early stages of default were far more likely to receive a loan modification and/or keep their homes than those who received counseling when they were seriously delinquent.<sup>5</sup>

**3. Families who participated in the national foreclosure mitigation counseling program were also able to negotiate lower monthly costs.** An evaluation found that the monthly payments of households that received counseling were, on average, \$267 less than those who did not participate in counseling. Counseling also made it 45 percent more likely that the homeowner would sustain those payments after modification.<sup>6</sup>

**4. There is also evidence that counseling provided before a household purchases a home can reduce the likelihood of mortgage delinquency.** Most studies have found that pre-purchase counseling leads to positive results, reducing delinquency anywhere from 19 to 50 percent, although one study reported no impact.<sup>7</sup> Research in 2001 found that face-to-face counseling was most effective, resulting in a 34 percent reduction in delinquency for participating homeowners.<sup>8</sup>

**5. Pre-purchase counseling can help reduce the likelihood of default and foreclosure by helping individuals determine if they are ready for homeownership, and by connecting them with safer and more affordable mortgage products.** One study has estimated that 30 to 50 percent of subprime borrowers prior to the housing crisis could have qualified for prime loans.<sup>9</sup> Well-underwritten, prime loans to low- and moderate-income borrowers have much lower default rates than subprime loans made to comparable borrowers.<sup>10</sup> Pre-purchase housing counseling from a HUD-certified housing counselor can improve homeowners' access to appropriate mortgage products.

**6. Additional research is needed to better understand the impact of homeownership education and counseling.** Researchers have employed a variety of methods to examine the effects of homeownership education and counseling but to date have not conducted an experimental trial. Research comparing outcomes for households randomly selected to receive pre-purchase homeownership counseling against control groups of households that do not receive counseling would make a significant contribution to the field.

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Endnotes:

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<sup>2</sup> A number of recent literature reviews explore the research base in greater depth. See generally: University of Wisconsin-Madison. 2010. "Weighing the Evidence of the Effectiveness of Counseling and Education for Home Owners." *CFS Issue Brief*, 2010-7.1; Collins, Michael J. and Collin O'Rourke. 2011. *Homeownership Education and Counseling: Do we know what works?* Research Institute for Housing America Special Report. Mortgage Bankers Association.

<sup>3</sup> Mayer, Neil et al. 2010. *National Foreclosure Mitigation Counseling Program Evaluation: Preliminary Analysis of Program Effects*. Washington, DC: The Urban Institute; Ding, Lei, Robert G. Quercia, and Janneke Ratcliffe. 2007. "Post-purchase Counseling and Default Resolutions among Low- and Moderate-Income Borrowers." *Journal of Real Estate Research*, 30(3): 315-344.

<sup>4</sup> Quercia, Roberto and Spencer M. Cowan. 2008 "The Impacts of Community-based Foreclosure Prevention Programs." *Housing Studies*, 23(3): 461-483.

<sup>5</sup> Collins, J. Michael and Maximilian Schmeiser. 2010. *Estimating the Effects of Foreclosure Counseling for Troubled Borrowers*. Federal Deposit Insurance Corporation Center for Financial Research Working Paper; Mayer et al. 2010.

<sup>6</sup> Mayer et al. 2010.

<sup>7</sup> In contrast to the several studies that have found a correlation between pre-purchase counseling and lower delinquency rates, Quercia and Spader (2008) found no evidence of an impact on default rates. One possible explanation for this finding is that interest rates were very low during the study period, while housing values were increasing, allowing borrowers who ran into trouble to refinance into a new loan and avoid default. The study did find evidence that classroom education improved homeowners' ability to make good judgments about refinance options – an important benefit given the recent history of predatory lending in the refinance sector.

<sup>8</sup> Hirad, Abdighani and Peter M. Zorn. 2001. "A Little Knowledge is a Good Thing: Empirical Evidence of the Effectiveness of Pre-Purchase Homeownership Counseling." In *Low-income Homeownership: Examining the Unexamined Goal*, Nicolas Retsinas and Eric Belsky (eds.), 146-174. Cambridge, MA; Washington, DC: Joint Center for Housing Studies; Brookings Institution Press; Brown, Thalia. 2002. *Homeownership Counseling: Effectiveness, Trends and Research*. Neighborhood Reinvestment Corporation; Agarwal, Sumit et al. 2009. *Do Financial Counseling Mandates Improve Mortgage Choice and Performance? Evidence from a Legislative Experiment*." Working Paper No. 2009-04, Federal Deposit Insurance Corporation Center for Financial Research.

<sup>9</sup> Reid, Carolina. 2006. "Preventing Foreclosure: Initiatives to Sustain Homeownership." *Community Investments*. Federal Reserve Bank of San Francisco.

<sup>10</sup> Ding, Quercia, and Ratcliffe. 2007.