

A Guide to Homeownership for Family Child Care Providers



A California Statewide Collaborative

Project Background

Building Child Care (BCC) is a collaboration of organizations working together to provide a centralized clearinghouse of information and services that improve child care providers' access to financial resources for facilities development projects in California. BCC is funded by the California Department of Education, and is comprised of the following four collaborative partners: the National Economic Development and Law Center, the California Child Care Resource and Referral Network, the Child Development Policy Institute Education Fund, and the Child Care Facilities Fund of the Low Income Investment Fund.

All too often, people interested in starting a child care business or current providers who need help expanding their services have been forced to find their way through a confusing maze of codes, regulations, financing requirements, building requirements, and construction challenges. In California, there has never been a central place to turn for technical assistance, support, training, referrals, publications, information, and materials specifically designed to help providers with child care financing and facilities development issues. This Collaborative takes the first step in establishing such a place.

Specifically, BCC provides technical assistance and information about facilities development and financing strategies to the child care community in California. We have a project web site (www.buildingchildcare.org) that contains information on community resources, publications, and financial resources, and we have a toll-free line (888-411-3535) that people can call to ask questions related to child care facilities development, and to learn more about the resources available to them.

Additionally, the BCC collaborative partners provide financial development trainings for local child care advocates such as Resource and Referral Agency and Regional Resource Center staff, who often provide the first level of contact to existing and potential providers looking for help in purchasing, expanding, building or renovating a center or home-based facility. As part of this effort to collaborate with existing advocates we also work to pull together the resources and expertise of other technical assistance entities across the state to create stronger networks of assistance for California's child care providers.

In recognition of the fact that the lack of available funding for child care facilities remains a major obstacle to creating sufficient child care capacity, BCC has begun to address the need for expanded financing options by working to identify the barriers to current financing and recommending concrete actions that will improve access to available funding for facilities development projects.

Finally, in addition to helping child care providers access the technical assistance, funding sources, and publications that are currently available, BCC also works to ensure that those resources expand and new ones are created to meet the enormous demand for child care facilities development and financing assistance throughout the state.

Acknowledgements

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Introduction

Family child care homes provide essential child care services for California’s families. They are frequently long-term, stable businesses that are integrally woven into the fabric of their neighborhoods. Many family child providers rent their homes, however, and therefore face the challenges of uncertain tenure. Providers who rent may not have the housing security or good relationships with their landlords that foster a quality environment for the children in their care. Housing instability may threaten the businesses that are the source of providers’ livelihoods. As a result, family child care providers are often interested in becoming homeowners. Homeownership enables providers to be more in control of their destinies.

The process of purchasing a home can be daunting for first time buyers. The hurdles appear even greater for low-income families, particularly in California’s more expensive markets. This guide will provide an overview of steps to take if you are a family child care provider considering buying a home in which to operate your business. It will review some of the preparation needed before you begin the home buying process. It will then cover mortgage basics, working with a lender, and finding a property. Last, it will discuss financing assistance options available to low income and first time homebuyers in California.

Preparation for Homeownership

Initial Steps

Buying a property almost always requires assuming a mortgage loan for the majority of the purchase price. Before embarking on the home buying process, it is useful to assess your capacity to acquire a mortgage from a lender. There are several basic pieces of information any lending institution will review to determine how much you can borrow and to assess whether you are a good risk for meeting your mortgage obligation. Lenders will always have some flexibility, but in general they will look closely at the following factors:

- Job History

Even if your salary is not high, a stable employment history will be attractive to a lender. If you have interruptions in employment, be prepared to give a reasonable explanation. Employment showing a salary progression is favorable.

- Credit history

Credit reports are comprehensive documents that include information from credit card companies, banks, student loan agencies and other lending entities. Past foreclosures and bankruptcies will also be recorded. Lenders will review your credit report to see your track record in paying bills and repaying debts. If you have a poor past credit history, be prepared to explain the reasons and demonstrate that you have worked to better manage your finances. If your credit history is spotty, you may want to seek guidance from a nonprofit credit-counseling organization. Avoid “credit-repair” companies that offer to fix your credit for a fee. You can check whether a credit counselor is reputable through the Better Business Bureau.

- Down payment capacity

Although there are programs that offer down payment assistance, it is generally necessary to have saved money for at least a small portion of the purchase price of your home, as well as closing costs. We will review down payment assistance programs later. Typically, you will need to have a minimum of 3-20% of the house’s cost for a cash payment toward purchase. The more you have saved, the better positioned you are to buy a property.

- How much you can borrow

A lender will calculate the maximum amount of money you are able to borrow. Your actual monthly payments will vary depending upon the amount you borrow, the term of the loan and the interest rate. If you want to make a rough calculation, your monthly housing costs, including mortgage payments, insurance and property taxes should not

exceed 29% of your gross household income. Your monthly housing costs plus other long-term debts (debt with more than 10 months outstanding) should be no more than 38% of your gross household income. A lender will also typically expect you to have a cash reserve at closing sufficient to cover at least two months' mortgage payments

Several useful basic guides to homeownership readiness and credit history are available through the Fannie Mae Foundation website at www.fanniemae.org.

Homeowner Education Programs

If you think you meet the criteria for homeownership, or believe you might qualify but have questions, it is highly advisable to take advantage of a local homebuyer education program. These programs are tailored to first time homebuyers, and offer invaluable guidance from counselors. A typical counselor will set up an appointment to meet with you individually. They will ask you to provide documentation of your income, debt, expenses and savings. They will help you understand the basics of establishing good credit, and will refer you to a consumer credit counseling agency if your credit needs repair. A homeownership educator will help you assess your readiness to assume a mortgage. They will often then help you choose a broker and/or lender and assist in deciding which mortgage is best for you. Counselors will be familiar with local programs offering financing assistance or homes designated for low-income or first time buyers. Other services may include help with contracts, inspections, closings and post-purchase counseling.

Homeownership education programs are located in a variety of institutions, including community service organizations, community colleges, and government housing or development agencies. Community based organizations frequently offer programs and materials in languages other than English. An initial resource for locating homeownership counseling programs throughout California by zip code may be found on the Fannie Mae Foundation website at www.fanniemae.org. You can also find California listings on the HUD website at <http://www.hud.gov/offices/hsg/sfh/hcc/states/california.txt>, or by calling (800) 569-4287. In addition, HUD offers an on-line homebuyer education program at <http://mirage.towerauction.net/homebuyer/coursehud.html>

Mortgage Basics

Mortgage loans are available through a variety of lenders, including thrift institutions, mortgage companies, savings and loan associations, commercial banks, federal credit unions and other financial institutions. You will want to shop around for a lender, comparing the terms of the mortgages they offer.

You may also find a loan through a **mortgage broker**. Brokers act as an intermediary that finds a lender for you. They often have access to a greater range of lenders than you will on your own. Brokers may charge an additional fee, however. It is important to discuss a broker's services at the outset to determine costs, and sign a contract specifying whether you want them to find the best mortgage available, or simply provide you with options.

To be an educated consumer in selecting a mortgage lender or broker, it is essential that you understand mortgage basics. There are many different types of mortgages and a range of mortgage terms, and the more familiar you are with them, the better choices you can make. This section will provide a brief overview of mortgages. It is important that you also consult with a homeownership counselor as you refine your decisions, or do further research to fully understand the process.

A mortgage loan is comprised of both **principal**, the sum you borrow, and **interest**, which is the additional cost of borrowing. The larger the **down payment**, the less principal you will need to borrow. The other key features that determine your monthly loan obligation are the repayment **term** (number of years), and the **interest rate**. Mortgages are generally offered in terms of 15, 20 and 30 years. Shorter terms are associated with lower interest rates, but the quicker repayment schedule leads to higher monthly costs. More of each payment will be principal, however, and less will be interest. One option is to choose a longer term loan but to make additional payments to accelerate repayment when you are able.

Interest rates may be **fixed** or **adjustable**. A fixed rate is constant for the entire term of the loan, while an adjustable rate varies within a cap that is set for both a given period and the life of the loan. Adjustable rates are often initially lower than fixed ones, but may end up being more costly in the long run if they fluctuate upward. Some adjustable mortgages may be converted to fixed ones within a given time period. You may also want to consider a **balloon** mortgage under certain conditions. Balloon mortgages have shorter terms, usually 5-10 years, and lower interest rates, with a monthly payment calculated on a longer amortization, or repayment, period than the actual loan term. This results in low monthly payments with an outstanding "balloon" or balance due when the loan term ends. You will then need to pay off the balance, refinance your loan, or sell your home. A balloon mortgage may make sense if you are certain you will move by the time the loan reaches maturity, or if you are sure you will be able to refinance, or even pay off the balance. The risk of foreclosure is greater, however, if you are unable to meet one of these conditions

Interest rates change frequently, sometimes daily. As you near the point when you are ready to purchase a home, you may want to **lock in** a given rate with your lender. This process ensures that you can borrow at a specified rate if you close your loan within a set time period. Locking in makes sense if interest rates appear to be rising, but may set your interest rate high than necessary if rates are falling. When to lock in is a judgment call best made by carefully tracking the market or with the help of an advisor.

There are additional costs associated with obtaining a mortgage. If you make less than a 20% down payment, you will usually be required to assume **mortgage insurance**. This insurance protects your lender if you miss a monthly payment. The cost of mortgage insurance is folded into your total loan amount. You will also need to budget for **closing costs**. These vary, but are often 3-7 % of the total sale price. Closing costs may include charges for recording the deed and mortgage, title and mortgage insurance, mortgage taxes, escrow costs, bank fees, site survey fees, attorney fees, document preparation fees and **discount points**. A point is a sum equaling one percent of your total loan amount. You will be given the option of paying up to several points at closing. While this makes your up-front costs higher, it in turn lowers your interest rate by a fraction of a percentage. The points calculation is a cost-benefit tradeoff that will depend on your cash in hand vs. your ability to assume more long-term debt.

The **annual percentage rate (APR)** is the annual credit cost, including interest rate, points, broker charges and other fees. The APR is a useful tool for comparing different mortgage options

Once you have roughly calculated the mortgage amount you can manage, and have familiarized yourself with the types of mortgages available, it is a good idea to begin contacting several local lenders to see what terms they will offer and to get **pre-qualified** for a loan. **Prequalification** is a formal or informal assessment of your borrowing capacity by a lender. The assessment is subject to change pending verification of your financial documents. This process will enable you to compare mortgage options between institutions, learning what size loan on what terms each will make available. You can see which mortgages and which lender feel most comfortable to you. Pre-qualification will also enable you to explore the real estate market knowing the housing price that will fit your budget. It will enable you to quickly make a credible offer if you find a property that you want to purchase.

A useful beginning tool to determine the mortgage amount you can afford is at http://www.ginniemae.gov/vpth/2_prequal/intro_questions.htm You will also find a good guide to comparative mortgage shopping as well as an excellent **mortgage comparison worksheet** at <http://www.ftc.gov/bcp/online/pubs/homes/bestmorg.htm> The same document is available in Spanish at <http://www.ftc.gov/bcp/online/spanish/homes/s-bestmort.htm> HUD also offers a guide to mortgage shopping and negotiation at <http://www.hud.gov/buying/booklet.pdf>

Special Loan and Assistance Programs

There are many special loan and assistance programs earmarked for first-time homebuyers and low-income households. These vary by region, but fall into several general categories. One common type of program offers **down payment assistance**. Some of these provide a down payment grant to qualified borrowers. Others allow you to borrow a percentage of the down payment and/or closing costs from a government agency or non-profit institution. These programs will be described in more detail below.

Another popular option is a **government insured loan**, which is typically offered through the Federal Housing Administration (FHA). These loans generally require down payments of under 5%. If you live in a rural area, the Rural Housing Service (RHA) offers government insured loans requiring no down payment to people within specified income limits. Veterans may be eligible for Veterans Administration (VA) fixed rate mortgage loans that offer 100% financing.

In California, the California Housing Finance Agency (CalHFA) is a primary source of homeownership programs that offer **below-market interest rate loans** to low-to-moderate income first time homebuyers. Additional special loan programs are offered through local housing agencies as well as private lenders. Most mortgage lenders will be familiar with these types of loan program. If they are not, find another lender who can better help you.

An excellent starting resource for researching local homebuyer programs sorted by city is <http://www.hud.gov/local/ca/buying/prgmscity.cfm> You can find a similar guide broken out by county at <http://www.hud.gov/local/ca/buying/prgmscounty.cfm> It is useful to look through some of these program guidelines just to familiarize yourself with the range of assistance available. Some of the larger programs and agencies will be reviewed in more detail below.

California Housing Finance Agency (CalHFA) programs

CalHFA is California's chartered affordable housing bank. Its mission includes making below-market rate loans to low-to-moderate income first time homebuyers. CalHFA loans may be secured through many approved lenders. To locate one in your community, you may call CalHFA at 916-322-3991 or review their approved lender list at <http://www.calhfa.ca.gov/homeownership/qualifications/lenders/index.htm> You may also directly inquire whether a local lending institution offers CalHFA loan products.

CalHFA's primary program is the **Homeownership Mortgage Loan Program**, which offers below-market rate fixed loans in all 58 California counties. The Homeownership Mortgage Loan Program and most of CalHFA's other homeownership programs have certain requirements. They include:

- Have an annual household/family income that does not exceed income limits for the family size and county in which the home is located.
- Property must be owner-occupied for the term of the loan or until sold.
- Meet credit, income and loan requirements of the CalHFA lender and the mortgage insurer.
- Be a first-time homebuyer, which is defined as a person(s) who has not had an ownership interest in their primary residence during the previous three years. This requirement is waived if property is located in a federally designated Target Area.
- Have sufficient funds available to meet the required down payment - 3-5% plus closing costs. Some restrictions apply to gift funds.
- Have the legal right to permanently reside in the United States.

CHFA loans are subject to a Federal recapture tax. Recapture is a Federal income tax that borrowers may have to pay if they sell or transfer their CHFA-financed home within 9 years. The property must fall within CalHFA-defined sales price limits, and be a single-family, one-unit residence, including condominiums. Manufactured housing is permitted if it is permanently attached to the foundation.

The Homeownership Mortgage Loan program can be combined with a number of other programs, including the CalHFA Housing Assistance Program, the High Cost Area Home Purchase Program, and the Extra Credit Teacher Program. To find out more about these as well as additional CalHFA Homeownership assistance programs, go to CalHFA's website at <http://www.calhfa.ca.gov/homeownership/index.htm>

CalHFA also partners with cities, counties, redevelopment agencies and housing authorities to provide down payment and closing cost assistance. This service will be discussed below in the "Down Payment Assistance" section.

Federal Housing Administration (FHA) programs

The Federal Department of Housing and Urban Development (HUD) offers mortgage insurance programs through the Federal Housing Administration (FHA). HUD mortgage loan insurance helps people buy or refinance their current homes with a low down payment. HUD does not make direct loans. You need to go to a local HUD-approved lender, who will help you find out if a HUD program is appropriate for you. There are over 3,000 HUD-approved lenders in California. You may find those in your area using the search form on HUD's website at <http://www.hud.gov/ll/code/llplcrit.html>

FHA-insured loans have many benefits. They are not available just to first-time homebuyers. FHA loans typically have easier credit qualifying and job history guidelines than conventional loans. FHA loans require smaller down payments, often as low as 3% of sales price. They permit gifts to be applied toward down payments and closing costs, and also regulate closing costs. FHA loans may be used toward the purchase of single-family homes, condominiums, or 2-4 unit buildings. Limits on sales price will vary by location. You can find the FHA mortgage limit for your area through this website: <https://entp.hud.gov/idapp/html/hicostlook.cfm>

Down Payment Assistance programs

For many prospective homebuyers, the biggest hurdle is saving for down payment and closing costs. A variety of programs exist that help reduce this burden. Down payment assistance can be structured as gifts, recoverable grants, or no- or low-interest loans. These programs will often be subject to income and sales price restrictions. It is always worth asking your lender, homeownership counselor and/or local government or non-profit agencies about the availability of such programs.

- I. As noted above, CalHFA offers several down payment assistance programs. The **Affordable Housing Partnership Program (AHPP)** is a joint effort by CalHFA and cities, counties, redevelopment agencies and housing authorities whereby a deferred payment subordinate loan from a locality is utilized by the first-time homebuyer to assist with down payment and/or closing costs.

You can find a valuable directory of participating local government agencies, programs and contacts at <http://www.calhfa.ca.gov/homeownership/programs/ahpp-approved.pdf>. These contacts are also useful for learning about other local homebuyer assistance programs.

- II. CalHFA also offers the **California Homebuyer's Down Payment Assistance Program (CHDAP)**. This program provides a deferred-payment subordinate loan of an amount up to the lesser of three percent (3%) of the purchase price or appraised value. Homebuyers are able to use these funds to help with down payment and closing costs without needing to make monthly payments on the loan. Interest will be calculated at 3% simple interest. The assistance may be combined with any CalHFA or non-CalHFA conventional or government first mortgage loan.
- III. In conjunction with **FHA**, CalHFA offers the **CalHFA Housing Assistance Program (CHAP)**, which provides up to 100% of home loan financing to eligible first-time homebuyers. It generally consists of a standard 97% CalHFA fixed-rate 30- year mortgage (at CalHFA's published below-market interest rate at the time the loan is reserved) and a 3% CalHFA down payment assistance second mortgage, which is also called a "sleeping" second. The second mortgage is offered for 30 years at 5% simple interest. All payments are deferred on this second mortgage until one of the following happens: the CHAFA first mortgage becomes due and payable; the first mortgage is paid in full or refinanced; or, the property is sold. The CalHFA 100% Home Loan Program is available to all low-income homebuyers in all 58 counties in California. Moderate-income homebuyers are eligible only in certain counties.

Non-profit agencies also offer down payment assistance programs. Three major ones are described below. These programs require the participation of the seller. Prospective buyers should ask their lenders, housing counselors or realtors about the availability of these or similar programs.

IV. The Nehemiah Down Payment Assistance Program

Nehemiah is a private California non-profit housing corporation. The Nehemiah Program makes gifts to qualified buyers to purchase Nehemiah properties throughout the United States. Nehemiah will gift up to 1-6% of the final sales price to a qualified Nehemiah buyer for the down payment. This allows a home purchase with no down payment when combined with a FHA loan. This program requires the assistance of the home seller.

Before a Nehemiah transaction is scheduled to record, Nehemiah delivers the participating buyer's 1-6% gift money taken from a pre-existing pool of funds and delivers it to the closing company. Using the Nehemiah program to buy a home can be broken into two simple steps: 1) Get pre-approved for a FHA Loan or conventional loan that permits gifts for down payment assistance; 2) once approved, find a home and have your Realtor write up the offer using the Nehemiah program. The seller must agree to participate in the program and make a contribution back to Nehemiah.

V. Housing Action Resource Trust (HART)

HART is a California 501(c)(3) non-profit housing and community development corporation. HART provides down payment assistance to low and moderate income homebuyers in the form of a "gift" of up to \$15,000 for down payment & closing costs. Properties must be purchased with FHA eligible loans. The buyer must provide 1% of the sales price from her own funds. The HART program can be used to purchase 1-4 units homes. Buyers are required to complete pre-purchase counseling. As with the Nehemiah program, HART requires the participation of the seller in the transaction. HART applicants must first get pre-qualified; they will then be referred to an approved Real Estate agent in the area to find a home that qualifies under the program guidelines.

VI. The Neighborhood Gold Down Payment Assistance Program

Neighborhood Gold is a nonprofit program that provides from 3-10% towards down payment and closing costs, depending on the amount of participation by the seller. This program is not limited to first time homebuyers, and may be used by any homebuyer who qualifies for an FHA loan. The program issues cash grants at loan closing. Since the program requires the participation of the seller, it must be negotiated before finalizing a purchase offer. There is 1% fee (not to exceed \$1,000) for the use of this program. This fee maybe paid by the seller or deducted from the cash grant and again, must be negotiated in the initial transaction.

HUD Homeownership Vouchers (Section 8 Homeownership)

In some California counties, homeownership vouchers (such as Section 8) are available to assist first-time homeowners with their monthly expenses. HUD may administer a homeownership program through your local Public Housing Authority (PHA), although it is not required to do so. The PHA may impose limits on the size of the program, or limit the program for only certain uses. However, a PHA must provide homeownership assistance as a reasonable accommodation to a person with a disability.

To be eligible, families must meet the following requirements:

- Be a first-time homeowner;
- Not have owned or had an ownership interest in the past three years;
- Meet a minimum income requirement; The qualified annual income of adult family members that will own the home must not be less than the federal minimum hour wage multiplied by 2,000 hours (currently \$10,300). For disabled families, the qualified annual income of adult family members who will own the home must not be less than the monthly Supplemental Security Income (SSI) benefit for an individual, multiplied by 12 (currently \$6,624). The PHA may also create higher income requirements.
- Meet an employment requirement; One or more of the adult family members who will own the home is currently employed on a full time basis and has been continuously employed on a full time basis for at least one year before commencement of homeownership assistance.
- Meet any other eligibility requirements set by the local PHA; and
- Attend and satisfactorily complete the PHA's pre-assistance homeownership and counseling program.

The PHA uses its normal voucher payment schedule to determine the amount of the subsidy. The subsidy can be used for monthly homeownership expenses, which includes such expenses as mortgage principal and interest, real estate taxes and homeownership insurance, and PHA allowances for utilities, routine maintenance, and major repairs. The PHA may make the payments to the homeowner, or directly to the lender. Families may purchase homes in a district outside the district where the initial voucher was issued, as long as the PHA in the new jurisdiction where the home is purchased administers a homeownership program for which the family is eligible.

Homeownership vouchers discontinue after 15 years if the initial mortgage incurred to finance purchase of the home has a term that is 20 years or longer. For all other cases, the maximum term of homeownership assistance is 10 years. There is no time limit for an elderly household or family with a disabled person.

For more information in your community, contact your local Public Housing Authority office.

Selecting a Real Estate Broker

You will want to start looking at houses early in the home buying process. Sometimes this can be accomplished simply by scouting for “for sale” signs in your neighborhood, or looking through the local newspaper. It is advisable to also work with a real estate broker. Choosing a broker with whom you feel comfortable is crucial. You may be able to get references from family or friends, or use the Yellow Pages or similar directories. Your housing counselor or lender may also make broker recommendations.

It is important that you clearly communicate your target price range as well as the type of house for which you are looking. Family child care providers may have specific design requirements, which you should think through beforehand. What kind of outdoor yard space will you need? What kind of interior layout? Do you want a primary large room for child care? Sightlines to the kitchen? Extra bathrooms and/or storage? How busy or quiet a street would you prefer, for marketing purposes and/or safe drop-off of children? Remember that you are looking for both a home and a site in which to run a successful business. You may want to research the siting of other family child care homes in a given neighborhood, since these will provide both a potential network and potential competition. Your real estate agent should be able to respond to your concerns and show you appropriate properties.

Finally, remember that real estate professionals may have a wide range of formal training and experience. Look for one who has been in business for a while, and who works full time. Approximately 15-20% of brokers are accredited by the National Association of REALTORS. These individuals will be certified as Graduates of the REALTORS® Institute. While this designation is not necessary, it will provide an extra assurance of competence.

The most important step is to interview several brokers and select one in whom you feel confident. You will then be ready to use the information above and begin taking the first steps toward homeownership.