



**Indiana  
Mortgage Bankers  
Association**

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## **INDIANA MORTGAGE FORECLOSURE RATE**

Much attention has been directed during the last several months to the high rate of mortgage foreclosures in Indiana. The foreclosure rates usually cited are those prepared by the Mortgage Bankers Association of America (MBA). As of June 30, 2002, Indiana's foreclosure rate was 2.22% as compared with the national average of 1.24%.<sup>1</sup> Many news reports attribute Indiana's high foreclosure rate to predatory lending without supporting evidence other than anecdotal statements by individuals. An analysis of the empiric evidence clearly establishes that predatory lending is not the cause of Indiana's high mortgage foreclosure rate.

It has been well accepted that predatory lending occurs primarily in subprime lending.<sup>2</sup> However, the MBA has indicated that less than one-half of one percent of all of the loans covered by its report were sub-prime loans.<sup>3</sup> With such a small number of sub-prime loans in the MBA report, it is not possible for predatory lending to be the cause of Indiana's higher foreclosure rate. This is confirmed by independent evidence that predatory lending is not as prevalent in Indiana as in other states. In 2000, the Mortgage Area Research Institute (MARI) found that Indiana ranked in MARI's lowest level in the category of predatory lending.<sup>4</sup>

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<sup>1</sup> Mortgage Bankers Association, *National Delinquency Survey for 2<sup>nd</sup> Quarter* (June 30, 2002).

<sup>2</sup> "Predatory Lending generally occurs in the subprime mortgage market where most borrowers use the collateral in their homes for debt consolidation or other consumer credit purchases." DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT AND DEPARTMENT OF TREASURY, JOINT REPORT FROM TASK FORCE CONVENED BY SECRETARY CUOMO AND SECRETARY SUMMERS (April 2000). "We continued to see problems in the subprime industry, in particular, the home equity loan business..." Statement of the Federal Trade Commission on Predatory Lending in the Subprime Industry before the House Committee on Banking and Financial Services (May 24, 2000).

<sup>3</sup> On September 18, 2002, Phil Colling reported to the Indiana Mortgage Bankers Association the following: "We estimate that less than one half of one percent of the loans in our sample are subprimes. That is basically negligible."

<sup>4</sup> MORTGAGE AREA RESEARCH INSTITUTE (August 22, 2000).

There are several primary reasons and a number of secondary reasons for Indiana's high foreclosure rate that are unrelated to predatory lending. First, there is a high concentration of Federal Housing Administration (FHA) and Veteran's Administration (VA) loans in the total number of loans made in Indiana. Twenty percent (20%) of all mortgage loans in Indiana are FHA-insured and five percent (5%) are VA-guaranteed. Only nine states have a larger percentage of FHA-insured loans and only fourteen states have a greater percentage of FHA insured and VA-guaranteed loans combined than Indiana. This is relevant because the national rate of foreclosure on FHA-insured loans is more than three times that of conventional loans (loans that are not insured by FHA or guaranteed by VA), and the national rate of foreclosure on VA-guaranteed loans is almost twice as high as the rate of foreclosure on conventional loans.<sup>5</sup>

Another primary reason for Indiana's high foreclosure rate is that Indiana homebuyers use significantly more down payment assistance programs than homebuyers in other states. Down payment assistance programs allow homebuyers to avoid or reduce their cash down payment. In its audit of down payment assistance programs in 2000, the HUD Inspector General reported that Indianapolis was among the top four cities with the highest number of down payment assistance loans. More recently, during the Fourth Annual FHA Mortgage Conference in October 2002, the metropolitan Indianapolis area was again singled out as one of four cities utilizing a significant number of down payment assistance programs. FHA also noted in its October 2002 report that the rate of default for loans with down payment assistance programs had risen to 19.42% which is significantly higher than the default rate of loans not utilizing down payment assistance.<sup>6</sup>

An analysis of the available data indicates that loans made to purchase newly constructed homes also play an important role in Indiana's foreclosure rate. As identified in FHA's Neighborhood Watch data, the national rate of serious defaults and foreclosures on FHA-insured loans to acquire newly constructed homes is higher than that of other FHA-insured loans. Further, the percentage of new

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<sup>5</sup> Mortgage Bankers Association, *National Delinquency Survey for 2<sup>nd</sup> Quarter*

<sup>6</sup> Department of Housing and Urban Development, Office of Inspector General Audit Report, Audit report No.: 2002-SE-0001, Follow up of Down Payment Assistance Programs (September 25, 2002).

construction FHA insured loans in Indiana as well as the percentage of defaults on new construction FHA insured loans in the state are both disproportionately higher than other states. Although Indiana has originated only 2.62% of all FHA insured loans nationally during the last two years, it has originated 5.39% of all FHA new construction loans nationally. Stated in another way, of the 59,252 FHA loans originated in the state of Indiana during the last two years, 18.76% were new construction loans which is significantly higher than that of other states.<sup>7</sup> These FHA new construction loans in Indiana have a combined serious default and foreclosure rate of 4.29% and this is much higher than the overall FHA combined serious default and foreclosure rate of 2.57% for all loans. Additionally, of the 1,858 loans that FHA has identified as being in serious default or foreclosed in the state of Indiana during the last two years, 25.67% of those loans were made for new construction financing.<sup>8</sup> The higher new construction default and foreclosure rate likely is linked to the higher default and foreclosure rate associated with down payment assistance programs for the reason that down payment assistance programs are most often used to purchase new construction homes. Clearly, the higher foreclosure rates for new construction loans and down payment assistance programs are not linked to predatory lending, because neither down payment assistance programs nor new construction loans are associated with predatory lending.<sup>9</sup>

There are a number of secondary factors that contribute to Indiana's high foreclosure rate. Difficult economic times and a low rate of appreciation for residential real estate are two such factors. Between 2000 and 2002, Indiana lost more jobs than any other state in the country.<sup>10</sup> Specifically, Indiana lost 4.1% of its jobs while the nation lost only .9%.<sup>11</sup> At the same time, the average wage in Indiana relative to the nation declined from relative parity (100.6) to the comparatively low level of

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<sup>7</sup> Department of Housing and Urban Development Neighborhood Watch Early Warning System.

<sup>8</sup> *See id.*

<sup>9</sup> *Supra* note 3.

<sup>10</sup> Morton Marcus, *Indiana*, in *INDIANA BUSINESS REVIEW* (Volume 77, Number 4).

<sup>11</sup> *See id.*

86.7.<sup>12</sup> In addition, the rate of appreciation of Indiana residential real estate is less than other states. For example, the rate of appreciation in Indianapolis is 3.71%, approximately half the national average.<sup>13</sup> While this low rate of appreciation has allowed Indiana traditionally to avoid the bust cycle that generally follows the boom of rapidly appreciating home values, the low rate of inflation means a borrower with little or no down payment will need more time to establish an equity cushion if and when financial difficulties arise.

An analysis of the factors behind Indiana's mortgage foreclosure rate points to a far more complicated scenario than predatory lending. Instead of predatory lending, the statistics establish that borrowers and lenders in Indiana utilize programs available to assist low and moderate-income borrowers more often than borrowers and lenders in other states. One consequence of this practice is a higher rate of mortgage foreclosures, but a significant benefit is a higher rate of home ownership. In 2001, Indiana ranked seventh nationally in home ownership with a rate of 75.3%.<sup>14</sup> This represents a significant increase from Indiana's 1984 ranking of fifteenth.<sup>15</sup> Indiana's 75.3% compares favorably with the overall national average homeownership rate of 67.6%.

The advantages and disadvantages of making home ownership available to more marginally qualified borrowers can be legitimately debated. However, there is no debate that the high rate of foreclosure in Indiana is not a result of predatory lending practices.

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<sup>12</sup> Morton Marcus, *Indiana*, in INDIANA BUSINESS REVIEW (Volume 77, No. 1).

<sup>13</sup> Gargi Chakrabarty, *Area Home Values See Small Gains*, INDIANAPOLIS STAR, December 4, 2002 at C1.

<sup>14</sup> United States Census Bureau, Annual Statistics 2001/2002.

<sup>15</sup> United States Census Bureau, Housing Vacancies and Homeownership Annual Statistics 2001.