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What's it worth?

January 2005

What's it worth?

Murky pricing hurts consumers in the manufactured housing industry

Executive Summary:

Murky pricing in the manufactured housing industry hurts consumers, lenders and communities. In this report we document these problems, and suggest solutions to the pricing problem that have been adopted in the real estate and automotive markets.

Our survey of recent purchasers of manufactured homes found a high degree of variation in the prices paid for the same homes. Almost a quarter of respondents paid more than 5% above the average price paid for their model of home. With a 5% down-payment, this starts them underwater on the loan.

We also found:

■ **It's worth shopping around:** Consumers who shopped at more than 3 dealerships paid 9.1% less than consumers who shopped at 3 or fewer.

■ **Independent financing pays:** Consumers who financed their homes through the dealer paid 10.9% more for their home than consumers who bought the same model for cash or used an outside lender. On an average home (\$47,037 in our survey), that is a \$5,144 higher price.

■ **Knowledge is power:** First time homebuyers paid 8.2% more on average than experienced homebuyers, while consumers who felt they knew "a lot" about manufactured homes paid 4.1% less than other homebuyers.



We recommend:

■ **Invoice based – sticker prices.** Sticker prices make it easier to shop – and shopping around saves consumers' money. Seventy-two percent of survey respondents thought that sticker prices would make the purchase process easier, but only 26% saw prices posted when they shopped for a home.

■ **Independent financing – Corporate consolidation of sales and financing lead to higher prices.** We recommend consumers shop for their loan separate from their home, and home ownership programs should require the use of independent lending companies.

■ **Appraisals – The conventional real estate housing market has realized for years that independent checks are needed on what is often a family's largest investment, the home.** We recommend policies to encourage the use of appraisals in the manufactured housing market.

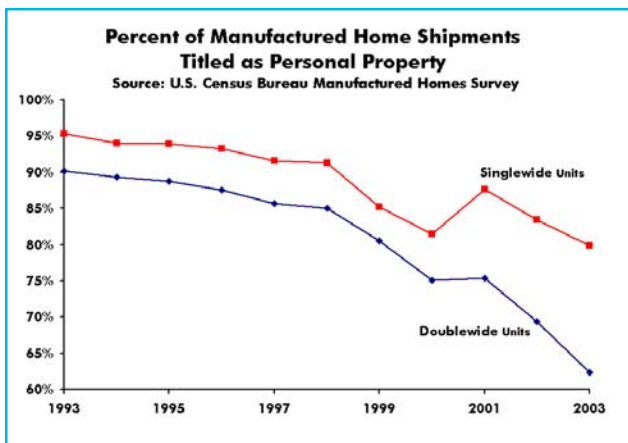


The problem of murky pricing

When Sammy J. Huey of Monohans, TX went to buy a manufactured home in the spring of 2003, he quickly learned how difficult it is to get a clear price for a home. The dealerships he visited didn't have posted prices, making it difficult to assess which homes among the dealer's offerings fit his price range. He was forced to rely on the sales staff's advice about which homes he should consider. One dealership refused to give him a price on their inventory until they'd had a chance to run his credit to see what he could afford!

Even the dealership from which Mr. Huey finally bought his home was somewhat ambiguous about the final price. Mr. Huey described negotiations for the price of his home with the sales staff to Consumers Union: "They'd say 'It's about this' and it was about 'that', but 'about' was a couple of thousands of dollars higher." The final closing price was 28% higher than the teaser prices they had discussed earlier in the purchase process. Mr. Huey had the feeling the sales staff "talk you into a higher priced home," and without posted prices, shoppers can't easily assess which homes they want to consider.¹

Stories like this one are all too common in the manufactured housing industry, where much of the traditional dealer sales process is based on the uncertainty surrounding the value of each home. We detailed in our 2002 report *In Over Our Heads* how this sales and financing process leads to problems for the consumers, lenders and communities touched by the manufactured housing industry. Consumers who pay too much for a home or end up in overpriced financing often end up with negative equity in the purchase, owing more on the loan than the



See footnotes for chart p. 8.

THEN:

"The consumer is led into the showroom by wild and strident advertising of huge discounts, over-allowances, or even paid trips to Paris."

Senator Monroney, testifying before the Subcommittee on Automobile Marketing Practices. Circa 1958.²

& NOW:

"...The consumers noted a number of problems with the original loan document including an amount for \$1,496 for Package B—which consisted of a free satellite dish, a \$1,000 gift certificate from Sams and a trip package to Orlando Florida or Las Vegas."

In *Over Our Heads*, 2002, p. 8.³

home is worth. In the last decade alone, this led to repossession and financial failure for hundreds of thousands of families, and contributed to a widespread downturn in the industry.

In this report, we look at how the market has changed since 2002, and examine closely how the lack of transparent pricing is a major barrier to this industry's ability to serve consumers.

Manufactured housing: The recent shakeout

Today only a handful of the major lenders active in the recent industry boom remain in the manufactured housing market. Consec, the largest lender during the boom years, entered a high profile bankruptcy.⁴ Chase Manhattan, one of the largest personal property lenders in the post-Consec world for home-only loans, has recently announced its exit from the industry.⁵ The CIT Group, bought by Champion homes to act as a captive lender, closed down in 2003.⁶

These lenders all financed homes using personal-property rather than real-property loans. Lenders who made real-property mortgages tended to be less specialized in manufactured homes and were more likely to demand better underwriting practices, including independent appraisals, and so better survived the market downturn. Nevertheless, the mortgage market has suffered as the resale values of manufactured homes, even those legally attached to land, collapsed from the oversupply of repossessed units. This reduces the value of the collateral of the loan portfolio. These changes caused Fannie Mae to severely restructure its guidelines on manufactured homes, and the FHA title I program has reduced its volume to a negligible fraction of the market.⁷ Freddie Mac has also quietly wound down its program for park-placed manufactured homes.⁸

The tightening of personal-property lending has pushed the financing mix slowly towards mortgage loans (see chart.) More homes are now titled as real estate, although personal property loans still dominate the marketplace. Nationwide, 80% of single section homes, which are those most accessible to low-income individuals, are titled as personal property.⁹ This varies by region – in 2004, fewer than 8% of singlewide manufactured homes titled in Texas were mortgage financed.¹⁰

A hybrid lending product has developed that still uses personal property loans even as fewer homes are being placed in rental communities. In a typical “land/home” deal, the home remains personal property, but a related transaction creates a separate note for real estate. This allows the seller to avoid conducting a formal appraisal on the home sale or providing the disclosures required by the federal Real Estate Settlement Procedures Act. It also gives the lender the ability to repossess the home like a car, rather than go through a more formal foreclosure if the buyer misses payments. (For more details on difference between foreclosure and repossession, see our upcoming report “Manufactured Housing, a Home the Law Still Treats like a Car”)

The industry trade group, the Manufactured Housing Institute, has been working to implement a voluntary “Lender Best Practices” project to better document the underwriting standards used by lenders on manufactured home loans. Participating companies must have procedures to verify loan characteristics such as borrower’s employment and credit history.¹¹ This program was developed in reaction to the loss of the sector’s credibility in the financial markets after the drop in underwriting standards as companies fought for market share in the late 90s. Six companies have joined the program as of the end of 2004, but the true test of their commitment to this program will come when the market re-enters a boom. Previous attempts to tighten the underwriting in the sector failed to survive the boom years. See sidebar “Deja-vu all over again,” (right).

Deja-vu all over again

The late 90’s boom in the manufactured housing business in the United States wasn’t the first of its kind. The early 70’s and mid 80’s saw a similar run up followed by bust in manufactured housing. And like the 2000 bust, it wasn’t just the financial markets that suffered, it was also the families who lost their homes in the financial fallout.

The early 70’s boom and bust cycle had many of the same characteristics of the late 90’s. In 1979, an op-ed in the American Banker reported

Up through 1973, the mobile home industry was going great guns.... One reason for this boom was that lenders were willing to make high-interest loans to less than credit-worthy customers. But in 1974, economic recession led to a depression in the housing industry, particularly mobile homes.... Financing dried up, and mobile home sales slumped so low some thought they would never recover.

but the op-ed reported that industry had learned from its mistakes and straightened itself out.

The recession also forced manufacturers, dealers, and lending institutions to make wholesale reassessments of the way things were previously done. Belts were tightened, credit was controlled, operations were upgraded. The manufactured housing industry pulled out of its doldrums.¹

Just as in the 70’s, the industry now claims to have fixed itself thru better sales practices. But in the late nineties, when the marketplace was in full boom, lenders and dealers who wanted to get the best deal for their customers couldn’t compete with competitors offering easy-in deals (which had hidden terms structured to strip equity from consumers), and had to drop to the lowest common denominator to compete.

Without fundamental enforceable reform, we will likely see history repeat itself when the next economic cycle increases competition for market share.

¹ Leichey, David “Backward Attitudes Towards Mobile Home Financing Persist,” American Banker, 10/16/1976.



Fifty years of auto sticker pricing

Sticker prices have often been discussed as a solution for the manufactured housing market – A 2003 consumer protection bill in North Carolina would have required sticker prices on all manufactured homes, but after opposition by the industry, was watered down before it passed to only apply to some homes.¹ Despite the simplicity of sticker prices, they are not voluntarily prevalent today – only 26% of our Texas survey respondents said that prices had been posted when they shopped for their home.

Sticker prices have been required in the automobile marketplace since the 1950s. At that time, problems with sales practices in the automobile market were threatening the health of what was one of the U.S.'s largest post-war industries. In response, the U.S. Senate Committee on Interstate and Foreign Commerce formed the Subcommittee on Automobile Marketing Practices to investigate and document the problems in the industry.

The committee found dealers using various tactics to inflate the price of cars and prevent valid price comparison by consumers. Dealers packed on extra charges and manipulated trade-in values, among other things. The problems confronting the auto industry at the time led to the introduction of the “Automobile Information Disclosure Act,” (AIDA) requiring sticker prices on new automobiles.

The house report on the AIDA found these questionable practices were so prevalent that all dealers felt they were forced to use them to stay in business.² The same report found that, as result of the confusion and suspicion of the auto industry caused by these tactics, the industry suffered from a decrease in the demand for new cars.

Although the bill was supported by the American Automobile Association, not everyone supported the final sticker price bill. The Department of Justice's comments on the Automobile Information Disclosure Act when it was filed foreshadowed the limitations of a non-binding price.

“...[I]f the purpose of this bill is to protect the consumer, it would seem that most helpful information to the consumer would be either the price actually paid by the dealer or the excise tax from which the purchaser could easily calculate the price paid by the dealer.”

June 5th, 1958
Lawrence E. Walsh
Deputy Attorney General
Department of Justice³

In today's auto market, it is standard advice to consumers to negotiate up from the invoice price



Murky pricing – part of the problem

In order to better understand the variation in the sales prices of new manufactured homes, Consumers Union surveyed Texas consumers who bought manufactured homes in the last two years and compared the prices paid by those who bought the *exact same new home*.¹² We found differences in prices across consumers that made conventional 5% down-payment requirement look small in comparison. Twenty-four percent of the respondents to our survey paid a

price that was more than 5% higher than the average pricing, washing out the equity provided by this 5% buffer.

Some of this variation seems to be related to the bargaining position of the purchaser. We found first time homebuyers paid 8.2% more on average than experienced homebuyers. Consumers who felt they knew “a lot” about manufactured homes paid 4.1% less than other homebuyers.

Consumers who find their own financing or pay cash have more bargaining power in the price negotiations. We found that consumers who

rather than down from the sticker prices, which are often inflated to give dealers negotiation room. These invoice prices can be obtained through private pricing service, (such as Consumers Union's own Consumer Reports New Car Price Service), but such consumer services have not yet developed in the marketplace for manufactured homes. The limited size and regional variation of models in the manufactured housing market, as well as the difficulty of obtaining transaction prices, makes it more difficult for such market intermediaries to develop.

It can perhaps be said that sticker prices didn't solve all the problems in the auto industry, but it did open up the market to some transparency, allowing consumers to easily compare the upper range of prices as well as the included options and specifications such as mileage.

¹ Stradling, Richard, "Mobile home bill passes," *The News & Observer*, July 17th, 2003.

² Automobile Information Disclosure Act. House Report No. 1958, June 24th, 1958.

³ *ibid*

financed their homes through the dealer paid 10.9% more for their home than consumers who bought the same model for cash or used an outside lender. For a consumer who buys an average home (\$47,037 in our survey), that translates into \$5,144 in additional costs.

Consumers who compared the offerings of different dealerships are more likely to get a better deal. Consumers who shopped at more than 3 dealerships paid 9.1% less than consumers who shopped at 3 or fewer. For a consumer who buys an average home, that translates into \$4,261 in savings.



This variation in price hurts both consumers and the industry. Many consumers overpay for their purchase. The lenders are hurt when the consumers realize they owe more on the loan than the home is worth and give the home back to the bank via default. In the long run, the manufacturers and dealers are hurt when consumers interpret this large discrepancy in prices as a sign of a rip-off or "first day off the lot" depreciation and avoid buying manufactured homes all together.

Long-term solutions

To curb fraud, stabilize the related lending market, and increase trust among buyers, the automobile industry developed the sticker price (see story, p. 4), and the real estate market adopted independent appraisals (see story, p. 6) to help certify the fairness of transactions. Both of these practices could improve the manufactured housing marketplace.

Sticker prices

The current system is designed to make it hard for consumers to shop around, but our research

shows that shopping around can save money. Consumers need to know which homes fit their price range, as well as the cost of options and available upgrades. Seventy-two percent of the recent purchasers who responded to our survey indicated that sticker prices would help make the purchase process easier, but only 26% indicated that prices were posted when they shopped for a home.

Half a century of experience with sticker prices on automobiles indicate that a sticker price should include both MRSP and the wholesale invoice price to prevent the listed MRSP from becoming an inflated part of the bargaining game. Invoice pricing allows consumers to determine the cost of the home itself.

Independent lenders already demand invoice information from dealers to establish the value of the collateral. Fannie Mae has proposed creating a central database of invoices that will allow lenders to access the original invoice at sale and for the life of a home. Any information available to lenders, including the invoice price, should be available to the consumer buying the home. This will allow the dealer's mark-up for their services to be transparent, giving the dealer, the consumer, and the lender the same information in the negotiation for the final transaction price.¹³

Real estate: Appraisals are the norm

The conventional housing market has developed mechanisms to stabilize its prices. Tight underwriting standards, independent appraisals, and transparent transaction prices all contribute to relatively consistent prices by region. Residential real estate prices do go through cycles that reflect the strength and weakness of the market, however, extreme busts and booms are relatively localized and frequently result from the underwriting and appraisal process becoming less transparent and independent (see chart.)

One of the largest real estate swings in recent history was a result of the failure of the Savings and Loans industry to use appropriate underwriting and appraisal standards. One policy response to this was the development of consistent appraisal standards for many of the large real estate transactions involving federally regulated banks and financial institutions.¹

The GSEs (Fannie Mae, Freddie Mac, etc) have recognized the importance of independent appraisals and create de-facto appraisal standards for residential purchases through the underwriting standards they require for the loans they package for the secondary market.

The more transparent nature of real estate transactions also assists the marketplace. Information about real estate transactions is filed with local governments, allowing the governments to monitor values and ownership for tax purposes. This information also allows both appraisers and other consumers to develop an understanding of current market prices. Consumers can quickly narrow their search for a home to one in their price range without undergoing a credit check first or entering a discussion with a particular seller. Independent realtors can check the Multiple Listing Service (MLS) at any given moment and review up-to-date information on the price of houses currently on the market. The manufactured housing market has not widely adopted the MLS sales process, although some internet-based MLS style systems have appeared in recent years that focus exclusively on used manufactured homes.

¹ Committee on Government Operations, House of Representatives. Implementation of Title XI, The Appraisal Reform Amendments of the Financial Institutions Reform, Recovery, and Enforcement Act of 1989. p 1-3. Opening statement by Chairman Barnard. May 17th 1990.

Appraisals

Today, real-estate mortgages commonly undergo an independent appraisal. But because many manufactured home transactions are still classified as personal property purchases, this independent oversight is rare. This is a direct result of the evolution of the manufactured housing sales process from its travel trailer roots – the homes are still sold like a car off a lot. Like auto dealers, manufactured housing dealers retain close ties to specific lenders.

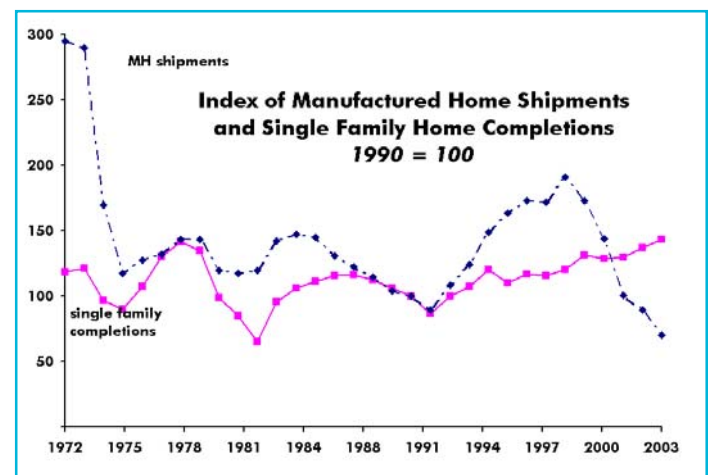
When the lender's financial interest is completely independent from the dealer, the lender's interest in the sales price of the home is aligned with the consumers. Both the lender and the consumer want the best price for the home and expect

that the home will be adequate collateral for the loan.

But when the dealer acts as the primary sales channel for the lender's loans, the lender must maintain an ongoing relationship with the dealer in order to access that dealer's consumer business. This need

“Appraisals provide vital market information, helping to ensure that underwriting practices are safe and sound and that adequate collateral stands behind each loan”

Letter to Alan Greenspan from members of congress Carroll Hubbard, Bill McCullum, James P. Moran, and Paul E. Gillmor.
July 8th 1991¹⁴



THEN:

“...[T]here were literally no rejects in mobile home financing.”

Lender representative in 1975 regarding 1972 lending standards¹⁵

& NOW:

“If you could make an X you could get a loan”

Louisiana manufactured housing dealer on mid-1990s lending standards¹⁶

nanced by Vanderbilt or 21st Century.¹⁹ In a case like this, the company has even less incentive to appraise the transaction because it may benefit directly from inflated sales prices.



for access to consumers creates a conflict. Lenders fight for market share by offering dealers larger profit margins in exchange for loan volume. Those profits come from higher home prices. In this market, competition among lenders actually increases home prices, as lenders compete for dealers by allowing higher loans for lower collateral rather than competing for consumers by offering lower interest rates.¹⁷

In some cases, the lender and the dealer may even be separate parts of the same company. For example, both 21st Century Mortgage and Vanderbilt Mortgage Finance Inc. are owned by the same holding company that owns both Clayton and Oakwood homes.¹⁸ Examination of the liens recorded with the state of Texas show that 83% of the homes sold by Clayton that are financed are fi-

Despite calls for appraised real-property lending as a solution to the problems in the manufactured housing industry since the 1970s,²⁰ they have not been adopted by the industry. The state of Texas briefly required all manufactured homes constructed on non-rental land to be considered real property, a change which was intended to encourage real property conventions such as appraisals and third party closings. This requirement was rolled back after opposition by the industry.²¹ Today, few manufactured home purchases undergo independent appraisals.

\$42,000, \$34,000, or \$25,000?

In May 2003, a Texas couple finished buying their manufactured home in Dallas County after shopping at half a dozen dealerships over the preceding four months. They closed on their newly constructed basic “Alamo by Clayton” 16 X 76 single-wide home, paying about \$42,000.¹

About a two hour drive east, in Franklin County, another consumer was settling into his new home. This home was also a basic “Alamo by Clayton” 16 X 76 unit, purchased a few months before from a dealership in nearby Sulphur Springs. The Franklin consumer paid only 33,800 for the exact same home.²

Did the Franklin consumer get a great deal? When the Franklin County tax appraiser came to value his home, he assigned it (excluding land) an appraised value of \$25,300. This lower appraised price likely reflects some dealer markup and installation costs which would not be captured on resale by the consumer.

The Franklin consumer’s \$8,500 markup over appraised value looks like a good deal compared to the details of purchase by the Dallas County couple. Their tax appraisal (for the same model home) came in slightly lower than the Franklin County home, \$22,920 for the home only. This makes the un-recoverable markup on their home an astonishing \$19,080, lost equity that will cause them to owe more on the home loan than the home is worth for years to come.

¹ Response to Consumers Union Survey of Manufactured Home Purchasers, phone interview. Survey ID: 1120. Dallas County Appraisal Rolls.

² Response to Consumers Union October 2004 Survey of Manufactured Home Purchasers. Email 10/18/04. Survey ID: 1150. Franklin County Appraisal Rolls.

Recommendations:

Sticker prices simplify the sales process and make shopping for a home easier. All homes should be required to have a posted price that includes the invoice price as well as the recommended dealer markup and the specifications and options included and/or available with the home. Consumers can then easily compare the value offered by different retailers. This information is already prepared by most manufacturers, because many lenders demand invoice information before financing a purchase. Any information a manufacturer or retailer provides a lender should be provided to the consumer before the sale.

Independent financing puts the bank on the same side of the price negotiations as the buyer. In an industry that is ever more vertically integrated, dealers, manufacturer, and lender can often be the same company, and only independent lenders have the incentive to make sure the transaction occurs at a fair price. We recommend consumers shop for their loan separate from their home, and home ownership programs should require the use of independent lenders.

Appraisals are the fundamental solution to stabilizing this industry. Consumers need a safeguard in the system, and an independent appraisal is an option that is available for both new and used homes. Several specific policies can be implemented to encourage the use of appraisals in this marketplace.

■ **The sales price of homes should be publicly recorded upon sale.** The current state of this procedure varies by state law, but is common in the conventional real estate market. The easy availability of this data makes appraisal and monitoring of market prices much easier for market participants.



■ **Appraisals and documented independent financing should be used with all homebuyer assistance programs that have a goal of building equity for homebuyers.**

■ **The GSEs and community lending programs should develop and expand the use of products that use appraisals in both the Chattel and mortgage market. Existing commercial products increase interest rates to price the higher risk of not having appraisals, placing the cost of the risk on the consumer.**

(Footnotes)

¹ Survey response and follow up phone interview. Survey ID: 0603.

² Automotive Information Disclosure Act, House Report No. 1958, June 24th, 1958.

³ Complaint to the Office of the Attorney General, 8/23/1999, El Paso, Texas.

⁴ Morse, Neil J. "Manufacturing the Dream," Mortgage Banking, 8/1/04.

⁵ "US Manufactured Housing ABS Continues to Struggle," Standard and Poor's, 8/2/04.

⁶ "Champion Enterprises, Inc. Exits Consumer Lending Business," PR Newswire, 7/31/03.

⁷ Comments of the Coalition to Advance Manufactured housing to HUD, Docket FR-4790-p-01, July 15th, 2004.

⁸ Leasehold mortgages are listed as ineligible for sale to Freddie Mac at <http://www.freddiemac.com/sell/expmkt/mhle.html>, Accessed 1/3/04.

⁹ "Selected Characteristics of New Manufactured Homes Placed by Region," US Census Bureau, Internet Source: <http://www.census.gov/const/mhs/Char03.xls>, accessed 1/17/05.

¹⁰ Texas Department of Housing and Community Affairs Home Ownership Records, accessed 1/13/05. 7.6% of single section homes were titled as real estate, a necessary step for obtaining a real-property loan on the combined land-home property.

¹¹ "Lender Best Practices Program Certifies First Applicants," Manufactured Housing Institute Press Release, June 17, 2002.

¹² We received 100 responses to the survey. Consumer responses were compared to other consumers who bought homes that were the same model, width, length, number of sections, square footage, wind-zone, and approximate weight. Significant upgrades were controlled for, and respondents who indicated there were "exceptional factors" affecting the price of their home were excluded from the analysis.

¹³ Annual Meeting Report, Manufactured Housing Institute, October 17-19th, 2004.

¹⁴ Committee on Banking, Finance, and Urban Affairs, House of Representatives, *Implementation of Appraisal Reform Sections of FIRREA* p. 708, 9/12/1992.

¹⁵ Charles A. Lockett "Mobile Home Demand and Sources of Financing," 1979 Working paper No. 27, Credit Research Center, Purdue University. p. 6.

¹⁶ John D. Grissim, "The Complete Buyer's Guide to Manufactured Homes and Land," 2003 p. 24.

¹⁷ "US Manufactured Housing ABS Continues to Struggle," Standard and Poor's, 8/2/04.

¹⁸ "Clayton Homes subsidiary buying \$4 billion Chase portfolio," Associated Press State and Local Wire, 12/8/04.

¹⁹ Texas Department of Housing and Community Affairs Home Ownership Records, accessed 1/13/05.

²⁰ Leichey, David, "Backward Attitudes Towards Mobile Home Financing Persist," American Banker, 10/16/1976.

²¹ Slater, Wayne, "Bill causes rift between mobile home sellers, consumer groups," Dallas Morning News, 4/28/2003.

Chart p. 2:

¹ U.S. Census Bureau Manufactured Homes Survey Series.

² US Census C-25 report series, Table 1 "New housing units completed by ownership, type of structure and location."

³ Lichenstein, Grace, New York Times, Page 30, Column 1, October 25th, 1975.

⁴ Forbes "Return Of The Founding Father," March 1st, 1976.