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The Reckoning

Building Flawed American Dreams

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SAN ANTONIO — A grandson of Mexican immigrants and a former mayor of this town, [Henry G. Cisneros](#) has spent years trying to make the dream of homeownership come true for low-income families.

As the Clinton administration's top housing official in the mid-1990s, Mr. Cisneros loosened mortgage restrictions so first-time buyers could qualify for loans they could never get before.

Then, capitalizing on a housing expansion he helped unleash, he joined the boards of a major builder, [KB Home](#), and the largest mortgage lender in the nation, [Countrywide Financial](#) — two companies that rode the housing boom, drawing criticism along the way for abusive business practices.

And Mr. Cisneros became a developer himself. The Lago Vista development here in his hometown once stood as a testament to his life's work.

Joining with KB, he built 428 homes for low-income buyers in what was a neglected, industrial neighborhood. He often made the trip from downtown to ask residents if they were happy.

“People bought here because of Cisneros,” says Celia Morales, a Lago Vista resident. “There was a feeling of, ‘He’s got our back.’ ”

But Mr. Cisneros rarely comes around anymore. Lago Vista, like many communities born in the housing boom, is now under stress. Scores of homes have been foreclosed, including one in five over the last six years on the community's longest street, Sunbend Falls, according to property records.

While Mr. Cisneros says he remains proud of his work, he has misgivings over what his passion has wrought. He insists that the worst problems developed only after “bad actors” hijacked his good intentions but acknowledges that “people came to homeownership who should not have been homeowners.”

They were lured by “unscrupulous participants — bankers, brokers, secondary market people,” he says. “The country is paying for that, and families are hurt because we as a society did not draw a line.”

The causes of the housing implosion are many: lax regulation, financial innovation gone awry, excessive debt, raw greed. The players are also varied: bankers, borrowers, developers, politicians and bureaucrats.

Mr. Cisneros, 61, had a foot in a number of those worlds. Despite his qualms, he encouraged the unprepared to buy homes — part of a broad national trend with dire economic consequences.

He reflects often on his role in the debacle, he says, which has changed homeownership from something that secured a place in the middle class to something that is ejecting people from it. “I’ve been waiting for someone to put all the blame at my doorstep,” he says lightly, but with a bit of worry, too.

The Paydays During the Boom

After a sex scandal destroyed his promising political career and he left Washington, he eventually reinvented himself as a well-regarded advocate and builder of urban, working-class homes. He has financed the construction of more than 7,000 houses.

For the three years he was a director at KB Home, Mr. Cisneros received at least \$70,000 in pay and more than \$100,000 worth of stock. He also received \$1.14 million in directors’ fees and stock grants during the six years he was a director at Countrywide. He made more than \$5 million from Countrywide stock options, money he says he plowed into his company.

He says his development work provides an annual income of “several hundred thousand” dollars. All told, his paydays are modest relative to the windfalls some executives netted in the boom. Indeed, Mr. Cisneros says his mistake was not the greed that afflicted many of his counterparts in banking and housing; it was unwavering belief.

It was, he argues, impossible to know in the beginning that the federal push to increase homeownership would end so badly. Once the housing boom got going, he suggests, laws and regulations barely had a chance.

“You think you have a finely tuned instrument that you can use to say: ‘Stop! We’re at 69 percent homeownership. We should not go further. There are people who should remain renters,’ ” he says. “But you really are just given a sledgehammer and an ax. They are blunt tools.”

From people dizzily drawing home equity loans out of increasingly valuable houses to banks racking up huge fees, few wanted the party to end.

“I’m not sure you can regulate when we’re talking about an entire nation of 300 million people and this

behavior becomes viral,” Mr. Cisneros says.

Homeownership has deep roots in the American soul. But until recently getting a mortgage was a challenge for low-income families. Many of these families were minorities, which naturally made the subject of special interest to Mr. Cisneros, who, in 1993, became the first Hispanic head of the [Department of Housing and Urban Development](#).

He had President Clinton’s ear, an easy charisma and a determination to increase a homeownership rate that had been stagnant for nearly three decades.

Thus was born the National Homeownership Strategy, which promoted ownership as patriotic and an easy win for all. “We were trying to be creative,” Mr. Cisneros recalls.

Under Mr. Cisneros, there were small and big changes at HUD, an agency that greased the mortgage wheel for first-time buyers by insuring billions of dollars in loans. Families no longer had to prove they had five years of stable income; three years sufficed.

And in another change championed by the mortgage industry, lenders were allowed to hire their own appraisers rather than rely on a government-selected panel. This saved borrowers money but opened the door for inflated appraisals. (A later HUD inquiry uncovered appraisal fraud that imperiled the federal mortgage insurance fund.)

“Henry did everything he could for home builders while he was at HUD,” says Janet Ahmad, president of Homeowners for Better Building, an advocacy group in San Antonio, who has known Mr. Cisneros since he was a city councilor. “That laid the groundwork for where we are now.”

Mr. Cisneros, who says he has no recollection that appraisal rules were relaxed when he ran HUD, disputes that notion. “I look back at HUD and feel my hands were clean,” he says.

Lenders applauded two more changes HUD made on Mr. Cisneros’s watch: they no longer had to interview most government-insured borrowers face to face or maintain physical branch offices. The industry changed, too. Lenders sprang up to serve those whose poor credit history made them ineligible for lower-interest “prime” loans. Countrywide, which [Angelo R. Mozilo](#) co-founded in 1969, set up a subprime unit in 1996.

Mr. Cisneros met Mr. Mozilo while he was HUD secretary, when Countrywide signed a government pledge to use “proactive creative efforts” to extend homeownership to minorities and low-income Americans.

He met Bruce E. Karatz, the chief executive of KB Home, when both were helping Los Angeles rebuild after the Northridge earthquake in 1994.

There were real gains during the Clinton years, as homeownership rose to 67.4 percent in 2000 from 64 percent in 1994. Hispanics and African-Americans were the biggest beneficiaries. But as the boom later gathered steam, and as the Bush administration continued the Clinton administration's push to amplify homeownership, some of those gains turned out to be built on sand.

Mr. Cisneros left government in 1997 after revelations that he had lied to federal investigators about payments to a former mistress. In the following years, HUD continued to draw attention in the news media and among consumer advocates for an overly lenient posture toward the housing industry.

In 2000, Mr. Cisneros returned to San Antonio, where he formed American CityVista, a developer, in partnership with KB, and became a KB director. KB's board also included [James A. Johnson](#), a prominent Democrat and the former chief executive of [Fannie Mae](#), the mortgage giant now being run by the government. Mr. Johnson did not return a phone call seeking comment.

It made for a cozy network. Fannie bought or backed many mortgages received by home buyers in the KB Home/American CityVista partnership. And Fannie's biggest mortgage client was Countrywide, whose board Mr. Cisneros had joined in 2001.

Because American CityVista was privately held, Mr. Cisneros's earnings are not disclosed. He held a 65 percent stake, and KB had the rest. In 2002, KB paid \$1.24 million to American CityVista for "services rendered."

'A Little Too Ambitious'

One of American CityVista's first projects, unveiled in late 2000, was Lago Vista — Spanish for "Lake View." The location was unusual: San Antonio's proud and insular South Side, a Hispanic area home to secondhand car dealers, light industry and pawnshops.

Mr. Cisneros and KB pledged to transform an overgrown patch of land into a showcase. Homes were initially priced from \$70,000 to about \$95,000, and Mr. Cisneros promised that Lago Vista would be ringed with jogging paths and maple trees.

The paths were never built, and few trees provide shade from the Texas sun. The adjoining "lake" — at one point a run-off pit for an asphalt plant — is fenced off, a hazard to neighborhood children. The houses are gaily painted in pink, blue, yellow or tan, and most owners keep their yards green and tidy.

KB considers Lago Vista a "model community," a spokeswoman said.

To get things rolling in Lago Vista, traditional bars to homeownership were lowered to the ground. Fannie Mae, CityVista and KB promoted a program allowing police officers, firefighters, teachers and others to get loans with nothing down and no closing costs.

KB marketed its developments in videos. In one from 2003, Mr. Karatz declared: “One of the greatest misconceptions today is people who sit back and think, ‘I can’t afford to buy.’ ” Mr. Cisneros appeared — identified as a former HUD director — saying the time was ripe to buy a home. Many agreed.

Victor Ramirez and Lorraine Pulido-Ramirez bought a house in Lago Vista in 2002. “This was our first home. I had nothing to compare it to,” Mr. Ramirez says. “I was a student making \$17,000 a year, my wife was between jobs. In retrospect, how in hell did we qualify?”

The majority of buyers in Lago Vista “were duped into believing it was easier than it was,” Mr. Ramirez says. “The attitude was, ‘Sign here, sign here, don’t read the fine print.’ ” He added that some fault lay with buyers: “We were definitely willing victims.” (The Ramirez family veered close to foreclosure, but the couple now have good jobs and can make their payments.)

KB and Mr. Cisneros eventually built more than a dozen developments, primarily in Texas. But the shine slowly came off Lago Vista.

“It started off fabulously,” Mr. Karatz recalled. Then sales slowed considerably. “It was probably, looking back, a little too ambitious to think that there would be sufficient local demand.”

And then the foreclosures started. “A lot of people got approved for big amounts,” says Patricia Flores, another Lago Vista homeowner. “They bit off more than they could chew.” Families split up under the strain of mortgage payments. One residence had so much marital turmoil that neighbors nicknamed it “The House of Broken Love.”

Some homes were taken over and sold at a loss by HUD, which had insured them. KB was also a mortgage lender, a business many home builders pursued because it was so profitable. At times, it was also problematic.

Officials at HUD uncovered problems with KB’s lending. In 2005, about two years after Mr. Cisneros left the KB board, the agency filed an administrative action against KB for approving loans based on overstated or improperly documented borrower income, and for charging excessive fees. Because HUD does not specify where improprieties take place, it is not clear if this occurred at Lago Vista.

KB Home paid \$3.2 million to settle the HUD action without admitting liability or fault, one of the largest settlements collected by the agency’s mortgagee review board. Shortly afterward, KB sold its lending unit to Countrywide. Then they set up a joint venture: KB installed Countrywide sales representatives in its developments.

By 2007, almost three-quarters of the loans to KB buyers were made by the joint venture. In Lago Vista, residents secured loans from a spectrum of federal agencies and lenders.

During years of heady growth, and then during a deep financial slide, Countrywide became a lightning rod for criticism about excesses and abuses leading to the housing bust — which Countrywide routinely brushed off.

Mr. Cisneros says he was never aware of improprieties at KB or Countrywide, and worked with them because he was impressed by Mr. Karatz and Mr. Mozilo. Mr. Mozilo could not be reached for comment.

Still, Countrywide expanded subprime lending aggressively while Mr. Cisneros served on its board. In September 2004, according to documents provided by a former employee, lending audits in six of Countrywide's largest regions showed about one in eight loans was "severely unsatisfactory" because of shoddy underwriting.

HUD required such audits and lenders were expected to address problems. Mr. Cisneros was a member of the Countrywide committee that oversaw compliance with legal and regulatory requirements. But he says he did not recall seeing or receiving the reports.

Nor, he says, was there ever a board vote about the wisdom of subprime lending.

"The irresistible temptation to engage in subprime was Countrywide's fatal error," he says. "I fault myself for not having seen it and, since it was not something I could change, having left."

Mr. Cisneros left Countrywide's board last year. At the time, he expressed "enormous confidence in the leadership." In 2003, Mr. Cisneros ended his partnership with KB because, he says, he felt constrained working with just one builder. He formed a new company with the same mission, CityView, that has raised \$725 million.

Mr. Karatz has a different recollection of why the partnership ended.

"It didn't become an important part of KB's business," he says. "It was profitable but I don't think as profitable in those initial years as Henry's group wanted it to be."

Troubles in Lago Vista

Today in Lago Vista, many are just trying to get by. Residents say crime has risen, and with association dues unpaid, they cannot hire security. Salvador Gutierrez, a truck driver, woke up recently to see four men stealing the tires off his pickup. Seventeen houses are for sale, but there are few buyers.

Hugo Martinez, who got a pair of Countrywide loans to buy a two-bedroom house with no down payment, recently lost his job with a car dealership. He has a lower-paying job as a mechanic and can't refinance or sell his house.

“They make it easy when you buy,” Mr. Martinez says. “But after a while, the interest rate goes up. KB Home says they cannot help us at all.”

Five years ago, Carlo Lee and Patricia Reyes bought their first home, a three-bedroom house in Lago Vista.

After Mrs. Reyes became ill last year and lost her job, they fell behind on their payments. Last month, Mr. Reyes was laid off from one of his jobs, assembling cabinets. He still works part time at a hospital, but unless the couple come up with missed payments and fees, they will lose their home.

“Everyone isn’t happy here in Lago Vista,” Mr. Reyes says. “Everyone has a lot of problems.”

Countrywide was bought recently at a fire-sale price by [Bank of America](#). Mr. Cisneros describes Mr. Mozilo as “sick with stress — the final chapter of his life is the infamy that’s been brought on him, or that he brought on himself.”

Mr. Karatz was forced out of KB two years ago amid a compensation scandal. Last month, without admitting or denying the allegations, he settled government charges that he illegally backdated stock options worth \$6 million.

For his part, Mr. Cisneros says he is proud of Lago Vista. “It is inaccurate to say that we put people into homes that they couldn’t afford,” he says. “No one was forcing people into homes.”

He also remains bullish on home building, despite the current carnage.

“We’re not selling cigarettes,” he says. “We’re not drawing people into casino gambling. We’re building the homes they’re going to raise their families in.”

David Streitfeld reported from San Antonio, and Gretchen Morgenson from New York.

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