Predatory Mortgage Lending

What is it?

Predatory mortgage lending, whether undertaken by creditors, brokers, or even home improvement contractors, involves engaging in deception or fraud, manipulating the borrower through aggressive sales tactics, or taking unfair advantage of a borrower's lack of understanding about loan terms.

Predatory lenders will target homeowners who have equity in their homes and may also have credit problems or need cash. They will advertise their services to people in financial need - people who may have fallen behind paying in their bills, or need money for medical bills, cars or costly home repairs. Often targeted are the elderly, low-wage earners and minority homeowners.

Warning Signs:

- **Large future costs**: Typically known as "end-of-loan features," they are high-risk adjustable rate mortgages with payments that rise substantially after a short introductory period. They are seldom appropriate for families who already have had problems repaying other loans. You should also avoid a large, single "balloon" payment (a lump sum due at the end of the loan's term).
- **Excessive fees**: Make sure fees are typical of those in your market. Because these costs can be financed as part of the loan, they are easy to disguise or downplay. On competitive loans, fees are negotiable. It is common for you to pay only one percent of the loan amount for prime loans. By contrast, a typical predatory loan may cost five percent or more.
- **Over-valued property**: Inflated appraisals can allow for excessive fees to be included in the loan, resulting in you owing more to the bank than the home is worth.
- **False or misleading promises**: Be wary of claims that sound too good to be true, such as, "easy credit," "we say yes to anybody," "no out of pocket expenses," "easy payment terms," "no payment for 60, 90, 120 days, or more," and other ploys.
- **High or adjustable interest rates**: Find out what type of interest rate will be applied to the loan and if the rate is adjustable. If the loan interest rate is adjustable, find out how much the rate can increase over the life of the loan. While a loan with an adjustable rate often starts out with reasonable monthly payments, the loan rate can increase over time, making it unaffordable. Also,

check to see if you've been offered a teaser rate. A teaser rate is a low introductory interest rate that can increase during the loan term.

- **Repeated refinancing**: Be wary of any lender who tries to get you to refinance repeatedly. This practice, called "loan flipping" or "churning," can vastly increase your overall debt and will get you a relatively small amount of cash compared to the refinanced amount.
- **Abusive Prepayment Penalties**: A prepayment penalty is a fee for paying off a loan early. I you have a higher-interest subprime loan you have a strong incentive to refinance as soon as your credit improves. However, up to 80% of all subprime mortgages carry a prepayment penalty. An abusive prepayment penalty typically is effective more than three years and/or costs more than six months' interest.
- **Steering and Targeting**: Even when you can qualify for a mainstream loan, predatory lenders may steer you into subprime mortgages. This can include aggressive sales tactics and sometimes outright fraud. Fannie Mae has estimated that up to half of borrowers with subprime mortgages could qualify for loans with better terms.

What You Can Do:

- **Compare loan terms**: If you have a relationship with a bank or credit union, consult it first regarding the best mortgage and loan rates. Then check with at least three lenders and compare their rates. Look at the annual percentage rate (APR), fees, points and closing costs associated with the loan. Examine the terms of the loan and the monthly payment. Look for prepayment penalties. Interest rates and fees vary widely. Don't assume you will not qualify for a loan from a traditional lender. Those loans are less expensive than predatory loans.
- **Study the paperwork**: There are several important papers that are key to understanding your loan. Three days before your loan closing, your lender must give you a written "Good Faith Estimate." Study that document carefully. It explains how much your loan officer thinks you will pay for the loan, and where he/she thinks all of the money you borrow will go. At your closing, compare it to the document referred to as a "Settlement Statement" or "HUD-1." It tells you where all of the money you borrow will actually go. If there are major changes between that document and your Good Faith Estimate, be sure you understand and agree with them.
- **Get a copy of your credit report**: Make sure it is accurate before applying for a loan or mortgage. Lenders use your credit report to decide if you are a good credit risk. If the report is wrong, ask the agency to change its records.
- **Get references**: Check with the local Better Business Bureau before doing business with a lender or mortgage broker. Make sure the lender and broker you

are dealing with are licensed by the State Banking Department.

- **Do not borrow more money than you can pay back**: If you get a loan, make sure you see in writing how much your monthly payments will be every month of the loan, and carefully consider if you can make the payments. Borrow only the amount you need and can afford to repay.
- **Take your time**: Don't let anyone rush you.
- **Do not be pressured by lenders**: If the lender calls you or comes to your door uninvited, don't agree to anything. Don't sign anything or give out your Social Security number. Watch out for lenders who say they can give you next day approval or low interest rates as long as you apply over the telephone or pay them money today. Do not be pressured into signing for a loan you can't afford. Ask about the cancellation period and what you have to do if you change your mind about the loan. Be wary of high pressure sales pitches, such as claims that an offer is good only for a limited time.
- **If you're thinking about consolidating your debts into a home equity loan**: Talk to a local non-profit housing or consumer credit counseling agency first. Think very carefully before rolling unsecured debt like credit card balances into a secured debt with your home collateral. If you can't make the payments, you may lose your home.
- **No life or disability insurance is required as a condition of a loan**: If it is, and a charge is included for it, ask that it be removed. The lender may not require that you buy insurance from a particular company. Stay away from premiums that you have to pay all at once.
- **Get advice**: Predatory lenders are ready to take your money and even your home. You need someone on your side. Talk to a HUD-certified loan counseling agency, and accountant, your banker, an attorney or a trusted friend. Talk to a non-profit credit counseling agency for help in deciding if you can afford your loan.
- **Call several home repair contractors**: Rather than buying a service from a door-to-door contractor who offers to arrange financing for you, call several contractors. There is usually a high built in fee. Also, beware of home improvements suggested by an unsolicited contractor who offers to arrange financing for you through a home equity loan or second mortgage. If you do need home repairs, find the contractor yourself after checking the references of several.
- **Fill in the blank spaces**: Read the entire loan application carefully before signing. Do not sign a document until you have completed every space.
- **Find out if you may cancel**: Under certain conditions you may be able to cancel a loan. Under the Truth in Lending Act, borrowers may have until midnight of the third business day to cancel the credit transaction. To see if you qualify for cancellation, view the Federal Trade Commission web site.

I you are in trouble you may want to consider other alternatives as well:

- **Call the servicer**: If you are worried you can't make your payments, industry experts say, call the company that takes your loan payments, called the mortgage servicer, to try to improve your situation. Servicers are often allowed by the agreements governing loans to renegotiate terms, a process known as a "work out" or "loss mitigation."
- **Talk to a housing counselor**: Counselors communicate with servicers on your behalf and can give advice on how to delay foreclosure. They are available in many cities, and their services often are free.
    - **Downside**: I you are in foreclosure you are short on time and many counseling agencies are already swamped.
- **File for bankruptcy**: If talking to the servicer doesn't work, consider Chapter 13 bankruptcy, which can at least delay foreclosure and can force the lender and other creditors to negotiate a payment plan approved by the court.
    - **Downsides**: Your credit score will take a big hit, but making timely payments can gradually raise it. Also, hiring a lawyer can be expensive, but can help ensure an accurate filing.
- **Sue**: A growing number of private lawyers, with help from consumer rights groups and legal aid lawyers, are pursuing legal relief for you who get loans you had little chance of repaying and, the lawyers argue, shouldn't have been granted. Taking cases on a contingency fee basis, these lawyers are giving you the chance not only to stop foreclosure and rescind the loan, but also to seek damages for abuses in some cases. The aim is to prove that lenders granted fraudulent or "unconscionable" loans with terms skewed heavily in their favor, or to fight abuses by servicers such as phony fees that cause you to default.
    - **Downside**: In extremely rare instances, if you lose a suit you may get saddled with attorneys' fees for the lender.
- **Beware of "foreclosure rescue" scams**: Federal and state prosecutors are investigating companies that offer temporary refinancing schemes in which you get to stay in the home but go deeper into debt because the payments to the "rescuer" are higher than your mortgage payments.