SEPARATE AND UNEQUAL

Predatory Lending in America

November 2002

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ACORN, the Association of Community Organizations for Reform Now, is the nation's largest community organization of low- and moderate-income families, with over 120,000 member families organized into 600 neighborhood chapters in 45 cities across the country. Since 1970 ACORN has taken action and won victories on issues of concern to our members. Our priorities include: better housing for first time homebuyers and tenants, living wages for low-wage workers, more investment in our communities from banks and governments, and better public schools. We achieve these goals by building community organizations that have the power to win changes -- through direct action, negotiation, legislation, and voter participation. ACORN's website is at http://www.acorn.org.

ACORN HOUSING CORPORATION

In 1986, ACORN Housing originated from neighborhood-based campaigns conducted by ACORN, a national organization formed by low-income members to improve neglected, impoverished communities. ACORN Housing creates affordable housing opportunities by acquiring and rehabilitating affordable housing units, developing single-family homes, providing homeownership counseling, coordinating sweat-equity programs, creating groundbreaking mortgage financing programs, and securing homebuyer subsidies. Since its inception, ACORN Housing's homeownership and counseling program has grown to 29 cities and provides free mortgage counseling to more individuals than any other organization in the country. ACORN Housing is also the national leader in assisting victims of predatory lending by providing refinancing at improved terms, through loan modification, and by providing outreach that teaches individuals to identify and avoid predatory loans.

ACORN Fair Housing Organization

ACORN Fair Housing fights housing discrimination by conducting research, providing training for community organizations, and conducing outreach and education efforts on the Federal Fair Housing Act. ACORN Fair Housing has worked against insurance and mortgage redlining and is currently working to identify victims of discrimination who have obtained predatory mortgage loans. ACORN Fair Housing is a project of the American Institute for Social Justice.

SEPARATE AND UNEQUAL
Predatory Lending in America

INTRODUCTION

Jonathan and Darlene and their two children had lived in their home since 1995, which had risen in value since then; Jonathan works as a carman for the railroad. They had bought the house with a 7% interest rate mortgage and later took out a 12% second mortgage. After another few years, they started receiving phone calls and solicitations in the mail from Beneficial, a part of Household Finance. In August 2001, Beneficial pressured them to consolidate debts into a third lien for $23,000 at a 21.9% interest rate. The mailings and phone calls kept coming, and three months later Beneficial convinced them to consolidate their three mortgages and pay off some other debts.

Beneficial never told Jonathan and Darlene that it had financed nearly $18,000 in 7.0 discount points into their loan, increasing the principal to over $248,000. The loan amount was also inflated by a single-premium credit life insurance policy for almost $8,000, despite Jonathan's telling the loan officer to not include it because he has a much less expensive term life insurance policy. And despite all the discount points, their history of never missing a home or car payment, and the fact that nearly two-thirds of the loan amount went toward the 7% first lien, fees, and credit insurance, the new loan contained an interest rate of 10.4%. Beneficial never told them that the new payments would not cover taxes and insurance, and the loan did not pay off all the debts Beneficial had promised. They were told the loan had a three-year prepayment penalty but not that the amount was over $6,000. The high monthly payments forced them to cut back on other expenses, and the high loan-to-value ratio plus the prepayment penalty prevented them from refinancing to a more reasonable rate. In the end, they had little choice but to sell their house and buy a less expensive one; they'll never get back the $26,000 of equity Beneficial stripped away, but their new mortgage with another lender will have an interest rate of 7.5%.

Mason and Josie are an elderly African-American couple who have excellent credit and whose primary source of income is Mason's veteran's benefits. Their mortgage was at a 7% interest rate when a broker convinced them to consolidate some credit cards into the mortgage. While the new mortgage for $99,000 had a reasonable interest rate of 8.4%, the broker also slipped in a second mortgage for $17,000 at an interest rate of 13.0%. The first loan for $99,000 also financed in nearly $6,000 in broker and third-party fees, and both loans contained prepayment penalties – lasting for three and five years, respectively. The broker used a series of payment schedules to confuse them, and they didn't realize that both loans had balloon payments after 15 years. After making monthly payments of nearly $950 over the next fifteen years, Mason and Josie will face a balloon payment for $93,000.[1]

[1] All of the examples of predatory lending abuses on subprime loans cited in this study were made in 2001 or 2002. The one exception is the balloon payment example, which was originated in 1996 with the balloon coming due in 2001 (the second story in the introduction also provides an example of a balloon payment loan originated in 2001).

The above families are just two of the millions of unsuspecting homeowners and homebuyers who have been robbed by predatory lenders – mortgage and finance companies that make loans with high interest rates, exorbitant fees, and harmful terms, often through fraudulent and deceptive methods. Elderly homeowners, communities of color, and low-income neighborhoods are the most severely impacted by these practices.

Despite increased awareness of the issue and some progress over the last year in combating the problem, predatory lending has continued, as these modern day loan sharks sink their teeth into new prey every day. In 2001, for the eighth consecutive year, home prices nationally rose at a greater rate than general inflation, exacerbating the problem by making more homeowners targets for predatory lenders intent on stripping their equity.[2]

Nationally, the number of subprime loans has skyrocketed since the early 1990s. In 1993, just over 100,000 subprime refinance and home purchase loans were originated, compared to over a million subprime loans in 2001. The proportion of subprime loans compared to all home loans fell somewhat from 2000 to 2001, but this was primarily a reflection of the growth in prime refinances due to historically-low interest rates. Even then, however, the growth in prime refinances for African-Americans (131%) and Latinos (231%) substantially trailed the increase for whites (294%). The subprime industry's tremendous growth has continued through the first half of 2002, as the volume of subprime originations rose to $106 billion, an increase of 19% compared to the first half of 2001 and the highest figure since the data started being collected a decade ago.[3]

The rise in subprime and predatory lending has been most dramatic in minority communities. Subprime lenders account for half, 51 percent, of all refinance loans made in predominantly black neighborhoods, compared to just 9 percent of the refinance loans made in predominantly white neighborhoods.[4] Subprime lending, with its higher prices and attendant abuses, is becoming the dominant form of lending in minority communities. But while minority communities suffer from an extreme concentration of higher cost, harmful loans, the problem should not be viewed as one that only affects minorities, since the vast majority of borrowers in subprime loans – and thus the vast majority of predatory lending victims – are white.

While not all subprime lenders are predatory, just about all predatory loans are subprime, and the subprime industry is a fertile breeding ground for predatory practices. Subprime loans are intended for people who are unable to obtain a conventional prime loan at the standard bank rate. The loans have higher interest rates to compensate for the potentially greater risk that these borrowers represent. There is a legitimate place for flexible loan products for people whose credit or other circumstances will not permit them to get loans on 'A' terms. Predatory lending occurs when loan terms or conditions become abusive or when borrowers who should qualify for credit on better terms are targeted instead for higher cost loans.

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[2] *The State of the Nation's Housing: 2001*, Harvard University Joint Center for Housing Studies, p. 1.
[3] "Subprime Volumes Keep Rockin'", *National Mortgage News*, by Paul Muolo, September 16, 2002, p. 38.
[4] *Curbing Predatory Home Mortgage Lending: A Joint Report*, June 2000, U.S. Department of Housing and Development and U.S. Department of Treasury, p. 47.

Fannie Mae has estimated that as many as half of all borrowers in subprime loans could have instead qualified for a lower cost mortgage.[5] Freddie Mac suggested a somewhat lower, but still extremely large figure – that as many as 35 percent of borrowers who obtained mortgages in the subprime market could have qualified for a prime loan.[6] The difference this could make is enormous: borrowers can easily pay $200,000 more in payments on a subprime loan over its 30 year life.

Too often higher rate subprime loans are also loaded with abusive features – high fees, large and extended prepayment penalties, financed single premium credit insurance – which cost borrowers even more money, and can lock them into the higher rates. When a borrower with good credit in a high rate loan is also charged inflated up front fees, assessed a prepayment penalty, and/or sold financed single premium credit insurance, it often leaves them without enough equity to refinance into a loan at a more reasonable rate.

Those borrowers who are not in a position to qualify for an 'A' loan are also routinely overcharged in the subprime market, with rates and fees that reflect what a lender or broker thought they could get away with, rather than any careful assessment of the actual credit risk. These loans too are often loaded with additional abusive features like financed credit insurance, hidden balloon payments, and mandatory arbitration clauses. As a result, such borrowers also find themselves trapped in high rate loans even once they have improved their credit. Many borrowers are also repeatedly solicited, and repeatedly refinanced into high rate loans, losing equity through every transaction.

Unfortunately, these problems pervade too much of the subprime industry. Just in the past few months, two of the largest subprime mortgage lenders – Household International and The Associates, which is now owned by Citigroup – announced respective settlements of $485 million and $240 million for engaging in predatory lending practices. While these are the largest settlements in American history for any type of consumer complaints, the dollar figures are well below the financial damage these companies have inflicted on their borrowers. Abuses are also widespread among unscrupulous mortgage brokers, who convince consumers they are acting to secure the lowest-priced loan when they are actually taking kickbacks from lenders to jack up interest rates, in addition to their standard origination fees.[7]

Predatory lending practices are even more insidious because they specifically target members of our society who can least afford to be stripped of their equity or life savings, and have the fewest resources to fight back when they have been cheated. Subprime lending is disproportionately concentrated among minority, low-income, and elderly homeowners.[8] Over 1.8 million lowest-income senior citizen homeowners pay more than half their incomes for housing, leaving them with little room to make increased mortgage payments.[9]

Many in the lending industry argue that the disproportionate concentration of subprime loans among low-income and minority borrowers is only a reflection of the greater risk that these borrowers represent based on their lower credit ratings. However, Fannie Mae has stated that the racial and economic disparities in

[5] "Financial Services in Distressed Communities," Fannie Mae Foundation, August 2001.
[6] "Automated Underwriting," Freddie Mac, September 1996.
[7] See testimony of Harvard Law School Prof. Howell E. Jackson to the Senate Banking Committee hearing on "Predatory Mortgage Lending Practices: Abusive Uses of Yield Spread Premiums," January 8, 2002.
[8] "We think [predatory lending is] at epidemic proportions, particularly in low-income, elderly and minority communities." Craig Nickerson, vice president of community development lending, Freddie Mac, as quoted in "Campaign to Help Buyers Avoid Predatory Loans", *Los Angeles Times*, by Lee Romney, July 18, 2001, Business p. 1.
[9] *The State of the Nation's Housing: 2001*, Harvard University Joint Center for Housing Studies, pp. 26-27.

subprime lending cannot be justified by credit quality alone. According to Fannie, loans to lower-income customers perform at similar levels as loans to upper-income customers; indeed, some recent research suggests that mortgages to low- and moderate-income borrowers perform better than other mortgages when the lower prepayment risk is taken into account.[10] In addition, the level of disparity presented in studies which showed that black households had more credit problems than white households was not even close to the levels of disparities seen in subprime lending.[11]

Predatory lending threatens to reverse the progress that has been made in increasing homeownership rates among minority and lower income families. Many in the subprime industry like to portray their primary role as helping families realize the American dream of homeownership. But the vast majority of subprime loans are refinances and home equity loans to existing homeowners, not purchase loans; last year, more than 65% of the reported home loans made by subprime lenders were for refinances, and an additional 6% were home-improvement loans.

While it is important for homeowners to be able to use the equity in their homes to meet financial needs, predatory lenders bombard homeowners in many communities with refinance offers that lead to loans at high rates, with inflated fees, and other abusive terms. By stripping equity, increasing indebtedness, and even costing families their homes, these practices cause homeowners to lose their equity, rather than use it for their benefit.

Furthermore, when we do examine the subprime industry's role in the home purchase market, there is additional cause for concern. From 1993 to 1995 there was a substantial increase in prime home purchase loans to minorities. Since then, however, the number of prime loans has stagnated, while the number of subprime purchase loans has skyrocketed. From 1995 to 2001 the number of subprime purchase loans to African-American homebuyers rose 686%, while the number of prime conventional purchase loans to African-American homebuyers actually fell 5.7%. A huge homeownership gap remains, with over three-quarters of white households owning their own homes, compared to less than half of African-American and Latino families.

This, along with the data from Fannie Mae and Freddie Mac mentioned above, suggests that higher cost subprime loans are replacing rather than supplementing less expensive 'A' credit, with tremendous extra costs for borrowers who should be qualifying for, or previously were in, 'A' loans. When buyers who should be eligible for loans at good interest rates are instead steered towards subprime lenders, they end up paying hundreds of dollars more each month than they would with a prime loan, and the higher interest rates and added fees deprive these homeowners of a fair opportunity to build equity. In the worst cases, the high interest and fees are only the tip of a predatory lending iceberg in which the loan also contains harmful terms, and the combination of these factors greatly increase the likelihood of foreclosure. The prevalence of predatory lending abuses in the subprime market has been a major factor behind record-breaking foreclosure rates; the Mortgage Bankers Association's survey of borrowers entering foreclosure and mortgages already in foreclosure for second quarter 2002 showed the highest percentages in each category since the statistics first started being tabulated in 1972.[12]

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[10] "Performance of Low-Income and Minority Mortgages," by Robert Van Order and Peter Zorn, in *Low-Income Homeownership: Examining the Unexamined Goal*, ed. Nicolas Retsinas and Eric Belsky, 2002, p. 324.
[11] "Financial Services in Distressed Communities," Fannie Mae Foundation, August 2001.
[12] "2nd Quarter Foreclosure Rates Highest in 30 Years," *Washington Post*, by Sandra Fleishman, September 14, 2002, p. H1.

In addition, subprime purchase loans are the financing mechanism of choice for carrying out "property flipping" scams, which unfortunately have become all too common an occurrence in a number of cities. Property flipping involves the purchase of distressed properties at a negligible price, and then, after minimal cosmetic or even no repairs, the property is sold at prices far above their actual worth. The victims of property flipping are often unsuspecting low-income, minority first-time homebuyers.

The damage that predatory lending inflicts on our communities cannot be overestimated. Homeownership provides the major source of wealth for low-income and minority families, with around two-thirds of their wealth coming from home equity. Rather than strengthening neighborhoods by providing needed credit based on this accumulated wealth, predatory lenders have contributed to the further deterioration of neighborhoods by stripping homeowners of their equity and overcharging those who can least afford it, leading to foreclosures and vacant houses.[13]

The last few years have seen a growing recognition of the serious harm being caused by predatory lending, and federal and state regulators have begun to take modest yet significant steps against the abuses. The Office of Thrift Supervision moved forward in September with regulations that effectively restored consumer protection laws on late fees and prepayment penalties in about half the states. Last December, the Federal Reserve used its regulatory authority under the federal Home Ownership Equity Protection Act (HOEPA) to announce two significant changes that went into effect in October – counting single-premium credit insurance policies as a fee under the HOEPA test, and expanding HOEPA coverage to a few more first mortgages with very high rates. In May, the Federal Reserve also announced that it would require the collection of annual percentage rates on most high-cost home loans, although the data collection was disappointingly postponed until January 2004, meaning nothing will be publicly available until mid-2005.

As mentioned above, two major subprime lenders – Household and The Associates – have been forced into huge predatory lending settlements after extensive investigations by the state attorneys general[14] and the Federal Trade Commission. The Household settlement's two-year limit on prepayment penalties and the hundreds of millions of dollars in payouts coming from these subprime lending giants are clearly breakthroughs. But at the same time, many of their abusive practices remain in place, and the settlement amounts for individual borrowers will fall far short of how much wealth was stolen from families by these multi-billion dollar corporations, let alone providing any punitive damages, and will offer little solace to the countless Household and Associates borrowers who have already lost their homes.[15] And of course, a substantial number of other subprime lenders and brokers have also engaged in widespread abuses without serious investigations into their business practices ever having been conducted.

[13] "Equity Strippers," Pennsylvania ACORN, May 2000; "Preying on Neighborhoods," National Training and Information Center, September 1999; "Unequal Burden in Baltimore," HUD, May 2000; "The Expanding Role of Subprime Lending in Ohio's Burgeoning Foreclosure Problem," Ohio Community Reinvestment Project, October 2002.

[14] A group of 20 state attorneys general began their joint investigation into Household's lending practices within a year of ACORN launching a nation-wide effort in the summer of 2001 to file hundreds of consumer complaints with state AGs and state banking commissioners against the company. See http://www.naag.org/issues/20021011-multi-household.php.

[15] To put these dollar amounts in context, Citigroup CEO Sandy Weill received $523 million in compensation from 1999 through 2001. A more accurate estimate of the actual direct damage inflicted by Household and Beneficial's predatory lending abuses on home loans would range to around $8 billion. On Household's practices, see "Home Wrecker", *Forbes*, by Bernard Condon, September 2, 2002; and Washington [State] Department of Financial Institutions report on Household's predatory lending practices, April 30, 2002.

While the settlements were on-balance positive, their limitations demonstrate the need for strong legislative protections in the subprime market. State legislatures and city councils around the country continue to debate anti-predatory lending bills, with victories of varying levels being won in just over the past year in Georgia, New York City and State, California, and Oakland. On the federal level, the Senate Banking Committee in the 107th Congress, under the leadership of Chairman Paul Sarbanes (D-MD), held a number of major hearings on predatory lending. Senator Sarbanes and Rep. John LaFalce, Ranking Democrat of the House Financial Services Committee, also introduced comprehensive anti-predatory lending legislation in the 107th Congress, S. 2438 and HR 1051.

While much of the financial industry has desperately tried to hold off legislation through a combination of announcing insufficient "best practice" standards, hiring high-paid lobbyists, and making large campaign contributions, the actual experience with legislation has been that it works without reducing access to credit. North Carolina Governor Michael Easley recently announced that the state's 1999 law had saved homeowners $100 million while borrowers with incomes below $25,000 received a higher share of subprime loans than in any other state in the country.[16] Meanwhile, a huge fight looms in Congress as segments of the financial industry view the Republican takeover of the Senate as an opportunity to preempt state and local consumer protections against predatory lending without setting any new, meaningful safeguards for homeowners at the federal level.[17] The fate of our country's gains in homeownership over the last couple decades among people of color and low- and moderate-income Americans hang in the balance.

[16] *North Carolina's Subprime Home Loan Market After Predatory Lending Reform*, prepared by The Center for Responsible Lending, Durham, NC, August 13, 2002. See also "Predatory loan crackdown won't ruin the business; City, state laws raise howls of protest, but experience suggests limited impact," *Craine's New York Business*, by Heike Wipperfurth, October 21, 2002, p. 4; "Surprisingly Strong Subprime Growth," Morgan Stanley, by Kenneth Posner and Athina Meehan, July 31, 2002.
[17] "GOP Rout Means a Change in Committees," *National Mortgage News*, by Brian Collins, Nov. 11, 2002, p. 2.

SUMMARY OF FINDINGS

Subprime Refinance Loans[18]

• **Minorities are much more likely than whites to receive a subprime loan when refinancing.** In 2001, more than one out of four, 27.76% of all conventional refinance loans received by African-American homeowners were from subprime lenders, as were 13.60% of the refinance loans received by Latino homeowners, compared to 6.32% of the refinance loans received by white homeowners. In comparative terms, African-Americans were 4.4 times more likely to receive a subprime loan, and Latinos were 2.2 times more likely to do so.

• **The concentration of subprime loans is greatest among lower income minorities.** Nearly half of the refinance loans received by low and moderate income African-American homeowners were from subprime lenders. Subprime lenders accounted for 41.74% of the refinance loans made to low-income African-American homeowners and 33.95% of the refinance loans made to moderate-income African-American homeowners. More than one in six refinance loans made to low and moderate income Latinos was subprime. Subprime lenders accounted for 17.97% of the refinance loans made to low-income Latino homeowners and 17.06% of the refinance loans made to moderate income Latino homeowners.

• **The racial disparity remains if we compare minority homeowners with white homeowners of the same income, and it persists among higher income homeowners**. 18.05% of the conventional refinance loans received by upper-income African-American homeowners were from subprime lenders, as were 10.06% of the refinance loans received by upper-income Latino homeowners. In contrast, only 4.81% of the refinance loans received by upper-income white homeowners were from subprime lenders. In addition, upper-income African-American homeowners were more likely than low-income white homeowners to receive a subprime loan when refinancing.

• **Subprime lenders also target lower income white homeowners.** Subprime lenders made 11.76% of all conventional refinance loans received by low-income white homeowners and 8.98% of all refinance loan received by moderate-income white homeowners. In contrast, subprime lenders made just 4.81% of the refinance loans to upper-income white homeowners.

• **Minorities receive a larger share of subprime refinance loans than of prime refinance loans.** In 2001, African-Americans received 9.43% of all the subprime refinance loans made in the United States, a 3.3 times larger share than the 2.83% of prime refinance loans they received. Latinos received 6.65% of the subprime refinance loans, a 1.4 times greater share than the 4.88% of prime refinance loans they received. In contrast, whites received 41.70% of the subprime refinance loans, but a much greater 71.27% of prime refinance loans.

• **There is a greater concentration of subprime loans in minority neighborhoods.** Subprime lenders represent nearly one-third, 32.44%, of the refinance loans made in neighborhoods where minorities constitute 80-100% of the population. In 50-80% minority communities, one out of five refinance loans, 19.40%, were from subprime lenders. In contras, less than one in eleven refinance loans 8.51% were from subprime lenders in heavily white communities (0-20% minority population.).

[18] Throughout this report, "refinance loans" refers to conventional refinance loans and does not include government-backed refinance loans.

In comparative terms, homeowners in 80-100% minority communities were 3.8 times more likely to receive a subprime refinance loan than homeowners in heavily white communities (0-20% minority population).

Subprime Purchase Loans

• **African-American homebuyers were 3.6 times more likely than white homebuyers to receive a subprime loan, and Latinos were twice as likely to do so.** Of the conventional prime and subprime purchase loans originated in 2001, subprime loans made up 25.49% of the loans received by African-Americans and 14.55% of the loans to Latinos, but just 7.14% of the loans to whites.

• **Minorities Receive a Much Larger Share of Subprime Purchase Loans Than of Prime Conventional Loans.** In 2001, African-Americans received 12.21% of all the subprime purchase loans made in the United States, a 3.5 times larger share than the 3.51% they received of prime purchase loans. Latinos received 11.51% of the subprime loans, 1.7 times their 6.6% share of prime loans. In contrast, whites received slightly more than half, 55.80%, of the subprime purchase loans, but nearly three quarters, 71.36%, of the prime loans.

• **The rate of growth of subprime lending has been much faster than the rate of growth of prime lending, especially to African-American borrowers.** The number of subprime purchase loans to African-American homebuyers has risen 686% from 1995 to 2001, while the number of prime conventional purchase loans received by African-American homebuyers in 2001 decreased 6% from 1995. Subprime purchase loans increased 882% to Latino homebuyers during this time, while prime loans rose 65%. White homebuyers also saw a larger percentage increase in subprime loans than in prime loans during this time, a 415% increase in the number of subprime loans compared to a 7.8% increase in the number of prime loans.

PREDATORY LENDING AND REFINANCING

The vast majority of subprime loans are for refinances, rather than purchases, and a significant number of predatory practices are linked to refinances. Subprime loans are usually not the traditional refinance in which homeowners seek to lower their interest rate or lock-in at a fixed rate. Subprime refinances are most often promoted for debt consolidation or in order to provide money for home improvements or other household or personal needs.

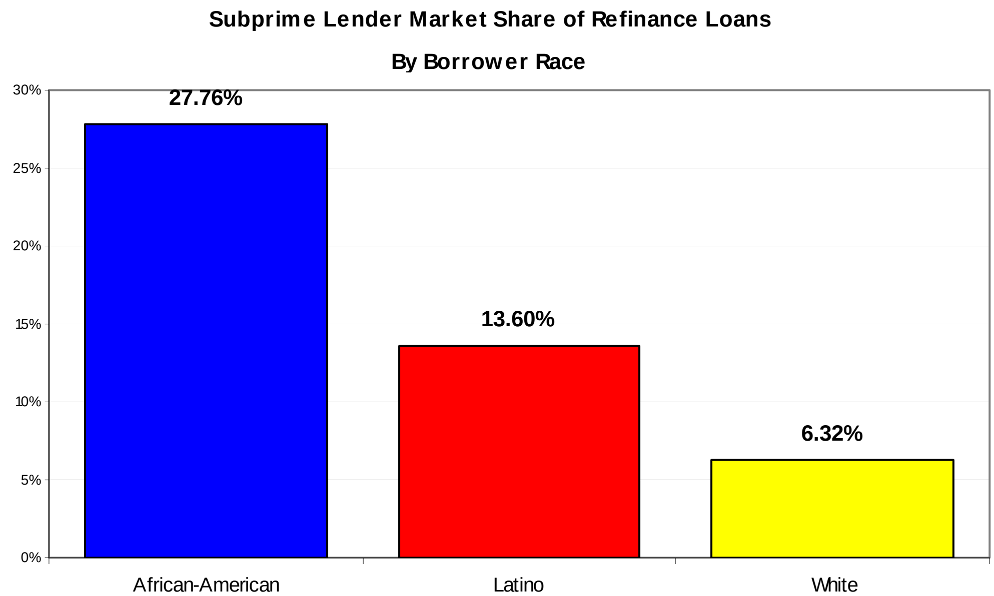
There are circumstances where refinancing to use some of the equity in one's home makes sense for the borrower, but cash-out refinances are rife with potential for abuse by predatory lenders, and too often homeowners with significant amounts of equity are convinced to refinance under conditions that are not in their best interest. In some cases, homeowners are sold refinance loans which produce just a few thousand dollars in cash-out, but which refinance their existing mortgages at higher rates and with high fees. In other cases, homeowners roll debt that is not secured by their house, such as credit cards or car loans, into a mortgage which is secured by their house. This may provide the homeowner with a short term reduction in total monthly obligations, although often it does not even accomplish this because of the high interest rates and fees. In addition, cash-out refinances increase the amount of debt tied to the borrower's house, as well as frequently extending the length of the loan and the total amount of payments. And now if a family is unable to make the payment they will lose their house.

Predatory lenders use refinancing as an opportunity to strip homeowners of their equity by financing thousands of dollars in unnecessary fees and costly credit insurance in the loan. They then add insult to injury by including harmful prepayment penalties in these high-interest refinance loans. More than two-thirds of subprime loans have prepayment penalties, compared to less than 2% of conventional prime loans.[19] It is not uncommon for subprime lenders to make loans at 12%-14% interest rates with prepayment penalties lasting from three to five years that require the borrower to pay six months interest on the loan as a penalty for refinancing with another lender to get a lower interest rate. On a $100,000 loan at 11% interest, such a penalty would cost a borrower over $5,000.

[19] HUD-Treasury report on Predatory Lending, p. 90.

Subprime Refinance Loans[20]

In 2001, 27.76% of all refinance loans received by African-American homeowners were from subprime lenders, as were 13.60% of refinance loans received by Latino homeowners, compared to 6.32% of the refinance loans received by whites. In comparative terms, African-American homeowners were 4.4 times more likely than white homeowners to receive a subprime loan while Latinos were 2.2 times more likely to do so.



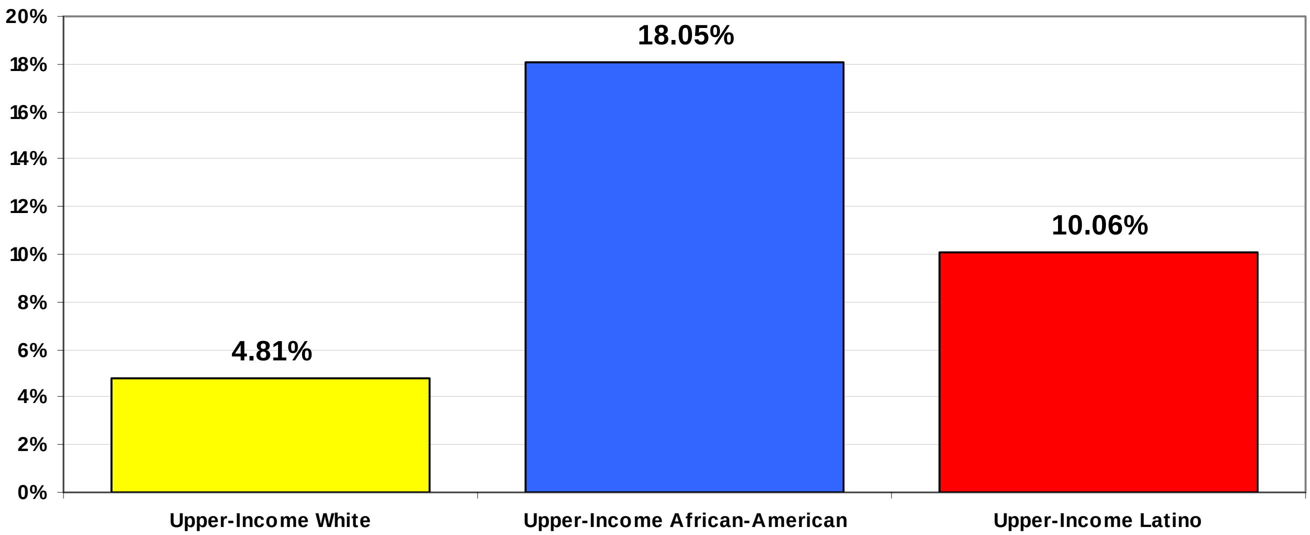
The racial disparity remains when we compare minority borrowers with white borrowers of similar income levels, and it persists among upper-income borrowers. 18.05% of the refinance loans received by upper-income African-Americans were from subprime lenders, as were 10.06% of the refinance loans received by upper-income Latinos. In contrast, only 4.81% of the refinance loans received by upper-income whites were from subprime lenders.[21]

Subprime Lender Market Share of Refinance Loans by Borrower Race and Income

	African-American	Latino	White
Low-Income	41.74%	17.97%	11.76%
Moderate-Income	33.95%	17.06%	8.98%
Middle-Income	27.35%	15.39%	6.78%
Upper-Income	18.05%	10.06%	4.81%

[20] Throughout this report "refinance loans" refers to conventional refinance loans and does not include government-backed refinance loans.
[21] Upper income is defined as earning more than 120% of the area median income. Middle income is defined as earning 80-119% of the area median income. Moderate income is defined as earning 50-79% of the area median income. Low income is defined as earning less than 50% of the area median income.

Subprime Lender Market Share of Refinance Loans



In comparative terms, upper-income African-Americans were 3.8 times more likely than upper-income whites to receive a subprime loan when refinancing, and upper-income Latinos were 2.1 times more likely. Worse yet, upper-income African-American homeowners were more likely than low-income whites to receive a subprime loan when refinancing.

The concentration of subprime loans is greatest among lower-income minority homeowners. More than two-fifths, 41.74%, of the refinance loans received by low-income African-American homeowners were from subprime lenders as were 33.95% of the refinance loans received by moderate-income African-Americans. More than one out of six, 17.97%, of the refinance loans received by low-income Latinos were from subprime lenders as were 17.06% of the subprime refinance loans received by moderate-income Latinos.

Lower-income white homeowners also receive a greater portion of subprime loans compared to upper-income white homeowners. Subprime lenders made 11.76% of all the refinance loans made to low-income white homeowners, and 8.98% of all the refinance loans made to moderate-income white homeowners. In contrast, subprime lenders made just 4.81% of the subprime loans made to upper-income white homeowners. This means that low-income owners who refinanced were 2.4 times more likely than upper-income white homeowners to receive a subprime loan and moderate-income whites were 1.9 times more likely than upper-income whites.

There is a greater concentration of subprime loans in minority neighborhoods. Subprime lenders represent nearly one-third, 32.44%, of the refinance loans made in neighborhoods where minorities constitute 80-100% of the population. In 50-80% minority communities, one out of five refinance loans, 19.40%, were from subprime lenders. In contrast, less than one in eleven refinance loans, 8.51%, were from subprime lenders in heavily white communities (0-20% minority population). In comparative terms, homeowners in 80-100% minority communities were 3.8 times more likely to receive a subprime refinance loan than homeowners in heavily white communities (0-20% minority population).

Subprime Lender Share of Refinance Loans by Census Tract % Minority

	0-20% Minority	20-50% Minority	50-80% Minority	80-100% Minority
Subprime Lender Loans	431,208	140,235	60,935	59,154
Prime Lender Loans	4,633,651	916,026	253,117	123,180
% Subprime	8.51%	13.28%	19.40%	32.44%

In comparative terms, homeowners in neighborhoods with 80-100% minority population were 3.8 times more likely than homeowners in heavily white neighborhoods (0-20% minority) to receive a subprime loan when refinancing. Homeowners in neighborhoods with 50-80% minority population were still 2.3 times more likely to receive a subprime loan when refinancing than homeowners in heavily white neighborhoods.

Subprime Refinance Lending in Specific Metropolitan Areas

Greatest and Least Concentrations of Subprime Loans[22]

Greatest Concentration of Subprime Refinance Loans to African-American Homeowners

In 41 cities of our study, at least one out of four refinance loans received by African-Americans were from subprime lenders. The cities where subprime loans were the greatest share of refinance loans to African-Americans were: Houston, Cleveland, Kansas City, San Antonio, Jacksonville, Toledo, Memphis, Miami, Pittsburgh and Detroit.

MSA		Subprime Lender Loans	Prime Lender Loans	% Subprime
Houston	TX	1295	1616	44.49%
Cleveland	OH	1651	2311	41.67%
Kansas City	MO	837	1237	40.36%
San Antonio	TX	128	200	39.02%
Jacksonville	FL	459	720	38.93%
Toledo	OH	325	532	37.92%
Memphis	TN	1086	1895	36.43%
Miami	FL	918	1617	36.21%
Pittsburgh	PA	281	526	34.82%
Detroit	MI	5564	10621	34.38%

Least Concentration of Subprime Loans to African-American Homeowners

In all the cities examined, at least one out of seven refinance loans to African-Americans were from subprime lenders. In only 11 cities did subprime lenders represent less than 20% of the refinance loans made to African-American homeowners.

MSA		Subprime Lender Loans	Prime Lender Loans	% Subprime
Baltimore	MD	668	2687	19.91%
Boston	MA	569	2295	19.87%
San Francisco	CA	215	886	19.53%
Hartford	CT	124	511	19.53%
Bergen-Passaic	NJ	132	586	18.38%
San Jose	CA	195	869	18.33%
Orange County	CA	152	761	16.65%
Lake Charles	LA	36	187	16.14%
Seattle	WA	250	1332	15.80%
Stamford-Norwalk	CT	46	248	15.65%
Washington	DC	1695	9671	14.91%

[22] All rankings exclude cities where there were fewer than 50 refinance loans made to African-Americans or Latinos. Excluded from rankings with African-American homeowners are: Sioux Falls, SD, and Las Cruces, NM. Excluded from rankings with Latino refinance loans are: Sioux FallsSD; Pine Bluff, AR; Houma, LA; and Lake Charles, LA.

Greatest Concentration of Subprime Loans to Latino Homeowners

Subprime lenders represented at least one out of five of the refinance loans made to Latinos in five cities in this report. The cities where subprime loans represented the greatest share of refinance loans to Latinos were: San Antonio, Providence, Phoenix-Mesa, Pittsburgh, Brockton, Denver, Cleveland, Houston, Waterbury, and Ft. Wayne.

MSA		Subprime Lender Loans	Prime Lender Loans	% Subprime
San Antonio	TX	966	2196	30.55%
Providence	RI	104	354	22.71%
Phoenix-Mesa	AZ	2138	7494	22.20%
Pittsburgh	PA	38	134	22.09%
Brockton	MA	29	115	20.14%
Denver	CO	1739	7243	19.36%
Cleveland	OH	152	637	19.26%
Houston	TX	1094	4685	18.93%
Waterbury	CT	14	62	18.42%
Ft. Wayne	IN	32	149	17.68%

Least Concentration of Subprime Refinance Loans to Latino Homeowners

At least one in ten refinance loans to Latinos were from subprime lenders in all but 11 cities in this report. The cities were subprime lenders were the smallest share of refinance loans to Latinos were: Atlanta, Seattle, Tampa-St. Petersburg, Las Cruces, Memphis, St. Louis, Washington (DC), Columbus, Baltimore, Milwaukee, Little Rock and Seattle.

MSA		Subprime Lender Loans	Prime Lender Loans	% Subprime
Atlanta	GA	167	1663	9.13%
Seattle	WA	133	1325	9.12%
Tampa-St. Petersburg	FL	366	3685	9.03%
Las Cruces	NM	67	704	8.69%
Memphis	TN	8	86	8.51%
St. Louis	MO	65	456	8.43%
Washington	DC	345	4072	7.81%
Columbus	OH	17	220	7.17%
Baltimore	MD	31	432	6.70%
Milwaukee	WI	67	1005	6.25%
Little Rock	AR	2	59	3.28%

Greatest Concentration of Subprime Loans to White Homeowners

Although subprime lenders represent a smaller share of the refinance loans made to white homeowners, they still represented at least one out of eleven loans in 12 of the cities in this report. The cities where subprime lenders represented the largest share of refinance loans to white homeowners were: San Antonio, Riverside-San Bernardino, St. Louis, Stockton-Lodi, Pine Bluff, San Diego, Houston, Nassau-Suffolk, Wilmington, and Ft. Worth-Arlington.

MSA		Subprime Lender Loans	Prime Lender Loans	% Subprime
San Antonio	TX	705	5384	11.58%
Riverside-San Bernardino	CA	4472	36279	10.97%
St. Louis	MO	3360	67549	10.87%
Stockton-Lodi	CA	1032	9226	10.06%
Pine Bluff	AR	31	283	9.87%
San Diego	CA	6435	59154	9.81%
Houston	TX	2470	23550	9.49%
Nassau-Suffolk	NY	3620	34598	9.47%
Wilmington	DE	747	7157	9.45%
Ft. Worth-Arlington	TX	1397	13402	9.44%

Least Concentration of Subprime Loans to White Homeowners

Subprime lenders represented fewer than one out of 20 refinance loans to white homeowners in 12 cities. The cities where subprime lenders represent the smallest share of subprime loans to white homeowners were: Hartford, Houma, Chicago, Boston, Springfield (Mass.), Stamford-Norwalk, Sioux Falls, Washington (DC), Las Cruces, and Milwaukee.

MSA		Subprime Lender Loans	Prime Lender Loans	% Subprime
Hartford	CT	858	18134	4.52%
Houma	LA	134	2945	4.35%
Chicago	IL	7838	178029	4.22%
Boston	MA	3980	92638	4.12%
Springfield	MA	325	7837	3.98%
Stamford-Norwalk	CT	330	8012	3.96%
Sioux Falls	SD	170	4243	3.85%
Washington	DC	3340	84391	3.81%
Las Cruces	NM	29	1076	2.62%
Milwaukee	WI	949	43163	2.15%

Greatest Concentration of Subprime Loans to Minority Neighborhoods (80-100% Minority Population)[23]

In 15 cities in our study, subprime lenders represented over half the refinance loans made in minority neighborhoods. In 51 cities, subprime lenders represented at least one out of every four refinance loans in minority neighborhoods. The cities where subprime lenders represented the largest share of refinance loans in minority neighborhoods were: Toledo, Kansas City, Orlando, Wilmington, Little Rock, San Antonio, Dallas, Pittsburgh, Houston, and Jacksonville.

MSA		Subprime Lender Loans	All Lender Loans	% Subprime
Toledo	OH	178	285	62.46%
Kansas City	MO	690	1114	61.94%
Orlando	FL	167	286	58.39%
Wilmington	DE	123	215	57.21%
Little Rock	AR	85	149	57.05%
San Antonio	TX	725	1287	56.33%
Dallas	TX	534	959	55.68%
Pittsburgh	PA	287	517	55.51%
Houston	TX	1234	2291	53.86%
Jacksonville	FL	332	624	53.21%

Least Concentration of Subprime Loans to Minority Neighborhoods (80-100% Minority Population)

The cities where subprime lenders represented the smallest share of refinance loans in minority neighborhoods were: Riverside-San Bernardino, Albuquerque, Stamford-Norwalk, Washington (DC), Los Angeles-Long Beach, San Jose, Las Cruces, San Francisco, Orange County and Seattle.

MSA		Subprime Lender Loans	Prime Lender Loans	% Subprime
Riverside-San Bernardino	CA	192	880	21.82%
Albuquerque	NM	114	527	21.63%
Stamford-Norwalk	CT	11	52	21.15%
Washington	DC	1017	5236	19.42%
Los Angeles-Long Beach	CA	5822	30602	19.02%
San Jose	CA	684	3604	18.98%
Las Cruces	NM	58	344	16.86%
San Francisco	CA	748	4532	16.50%
Orange County	CA	272	2030	13.40%
Seattle	WA	39	370	10.54%

[23] Excludes cities where fewer than 50 loans were made in census tracts with 80-100% minority population: Sioux Falls, SD; Brockton, MA; Houma, LA; Portland, OR; Waterbury, CT.

Greatest and Least Disparity in Subprime Refinance Lending

Most Disparate MSAs for African-American Homeowners

In every city we studied, African-Americans were at least two times more likely than whites to receive a subprime loan when refinancing. African-Americans were at least three times more likely in 51 cities. The cities with the greatest disparity between subprime lenders share of refinance loans to African-Americans compared to whites were: Milwaukee, Memphis, Springfield (Mass.), Chicago, Houma, Kansas City, Detroit, Minneapolis-St. Paul, Cleveland, and Toledo.

MSA		Subprime Share of Loans to African-Americans	Subprime Share of Loans to Whites	Disparity
Milwaukee	WI	23.63%	2.15%	11.0
Memphis	TN	36.43%	4.89%	7.4
Springfield	MA	29.38%	3.98%	7.4
Chicago	IL	30.92%	4.22%	7.3
Houma	LA	26.62%	4.35%	6.1
Kansas City	MO	40.36%	7.03%	5.7
Detroit	MI	34.38%	6.03%	5.7
Minneapolis-St. Paul	MN	30.15%	5.31%	5.7
Cleveland	OH	41.67%	7.61%	5.5
Toledo	OH	37.92%	6.94%	5.5

Least Disparate MSAs for African-American Homeowners

The cities with the least disparity between the subprime share of loans to African-Americans and share of loans to whites were: Stockton-Lodi, Nassau-Suffolk, Wilmington, San Jose, Portland, Ft. Lauderdale, San Diego, Riverside-San Bernardino, San Francisco, Pine Bluff and Orange County.

MSA		Subprime Share of Loans to African-Americans	Subprime Share of Loans to Whites	Disparity
Stockton-Lodi	CA	28.35%	10.06%	2.8
Nassau-Suffolk	NY	26.91%	9.47%	2.8
Wilmington	DE	26.06%	9.45%	2.8
San Jose	CA	18.33%	6.65%	2.8
Portland	OR	22.30%	8.11%	2.7
Ft. Lauderdale	FL	24.80%	9.40%	2.6
San Diego	CA	24.36%	9.81%	2.5
Riverside-San Bernardino	CA	26.02%	10.97%	2.4
San Francisco	CA	19.53%	8.25%	2.4
Pine Bluff	AR	23.16%	9.87%	2.3
Orange County	CA	16.65%	8.21%	2.0

Most Disparate MSAs for Latino Homeowners

In 32 of the cities examines, Latinos were at least two times more likely to receive a subprime loan than whites. The cities with the greatest disparity between the subprime share of refinance loans to Latinos and the subprime share of loans to whites were: Springfield (Mass.), Providence, Hartford, Boston, Las Cruces, Tucson, Brockton, Milwaukee, Ft. Wayne, Fresno, Stamford-Norwalk and Waterbury.

MSA		Subprime Share of Loans to Latinos	Subprime Share of Loans to Whites	Disparity
Springfield	MA	17.60%	3.98%	4.4
Providence	RI	22.71%	5.88%	3.9
Hartford	CT	15.81%	4.52%	3.5
Boston	MA	13.83%	4.12%	3.4
Las Cruces	NM	8.69%	2.62%	3.3
Tucson	AZ	15.78%	5.09%	3.1
Brockton	MA	20.14%	6.64%	3.0
Milwaukee	WI	6.25%	2.15%	2.9
Ft. Wayne	IN	17.68%	6.20%	2.9
Fresno	CA	16.34%	5.68%	2.9
Stamford-Norwalk	CT	11.60%	3.96%	2.9
Waterbury	CT	18.42%	6.35%	2.9

Least Disparate MSAs for Latino Homeowners

Subprime lenders represented a smaller portion of loans to Latinos than of the loans to whites in only two cities in this study: Little Rock and St. Louis. In nine cities, the disparity was less than 1.5 times: Jacksonville, Baltimore, Stockton-Lodi, Portland, Riverside-San Bernardino, Tampa-St. Petersburg, Ft. Lauderdale, Columbus, and Baton Rouge.

MSA		Subprime Share of Loans to Latinos	Subprime Share of Loans to Whites	Disparity
Jacksonville	FL	10.83%	7.61%	1.4
Baltimore	MD	6.70%	4.72%	1.4
Stockton-Lodi	CA	13.81%	10.06%	1.4
Portland	OR	11.13%	8.11%	1.4
Riverside-San Bernardino	CA	15.65%	10.97%	1.4
Tampa-St. Petersburg	FL	9.03%	6.77%	1.3
Ft. Lauderdale	FL	11.94%	9.40%	1.3
Columbus	OH	7.17%	5.81%	1.2
Baton Rouge	LA	10.23%	8.36%	1.2
St. Louis	MO	8.43%	10.87%	0.8
Little Rock	AR	3.28%	4.77%	0.7

Most Disparate MSAs for Homeowners in Minority Neighborhoods (80-100% Minority Population)

In 56 cities, subprime lenders made more than two times a greater share of the refinance loans in minority neighborhoods than they did in heavily white neighborhoods (0-20% white population)[24]. The cities with the greatest disparity were: Milwaukee, Springfield (Mass.), St. Louis, Minneapolis-St. Paul, Toledo, Little Rock, Detroit, Hartford, Kansas City, Chicago.

MSA		Subprime Share of Refinance Loans: 80-100% Minority Population	0-20% Minority Population	Disparity
Milwaukee	WI	43.93%	3.20%	13.7
Springfield	MA	52.86%	6.86%	7.7
St. Louis	MO	51.44%	7.25%	7.1
Minneapolis-St. Paul	MN	45.60%	6.40%	7.1
Toledo	OH	62.46%	9.11%	6.9
Little Rock	AR	57.05%	8.43%	6.8
Detroit	MI	46.99%	6.96%	6.8
Hartford	CT	47.94%	7.31%	6.6
Chicago	IL	32.77%	4.96%	6.6
Kansas City	MO	61.94%	9.57%	6.5

Least Disparate MSA for Homeowners in Minority Neighborhoods

The cities with the least disparity between the subprime lender share of refinance loans in minority neighborhoods (80-100% minority) and white neighborhoods (0-20% minority) were: Jersey City, San Diego, Stockton-Lodi, Los Angeles-Long Beach, Pine Bluff, Riverside-San Bernardino, San Francisco, Albuquerque, Orange County, and Seattle.

MSA		Subprime Share of Refinance Loans: 80-100% Minority Population	0-20% Minority Population	Disparity
Jersey City	NJ	27.27%	8.95%	3.0
San Diego	CA	25.88%	9.15%	2.8
Stockton-Lodi	CA	28.54%	10.55%	2.7
Los Angeles-Long Beach	CA	19.02%	8.32%	2.3
Pine Bluff	AR	40.38%	18.38%	2.2
Riverside-San Bernardino	CA	21.82%	11.36%	1.9
San Francisco	CA	16.50%	8.54%	1.9
Albuquerque	NM	21.63%	12.07%	1.8
Orange County	CA	13.40%	8.36%	1.6
Seattle	WA	10.54%	6.55%	1.6

[24] Excludes cities where fewer than 50 loans were made in census tracts with 80-100% population as well as cities where fewer than 50 loans were made in census tract with 0-20% minority population: Sioux Falls, SD; Brockton, MA: Houma, LA: Portland, OR: Waterbury, CT; Las Cruces, NM.

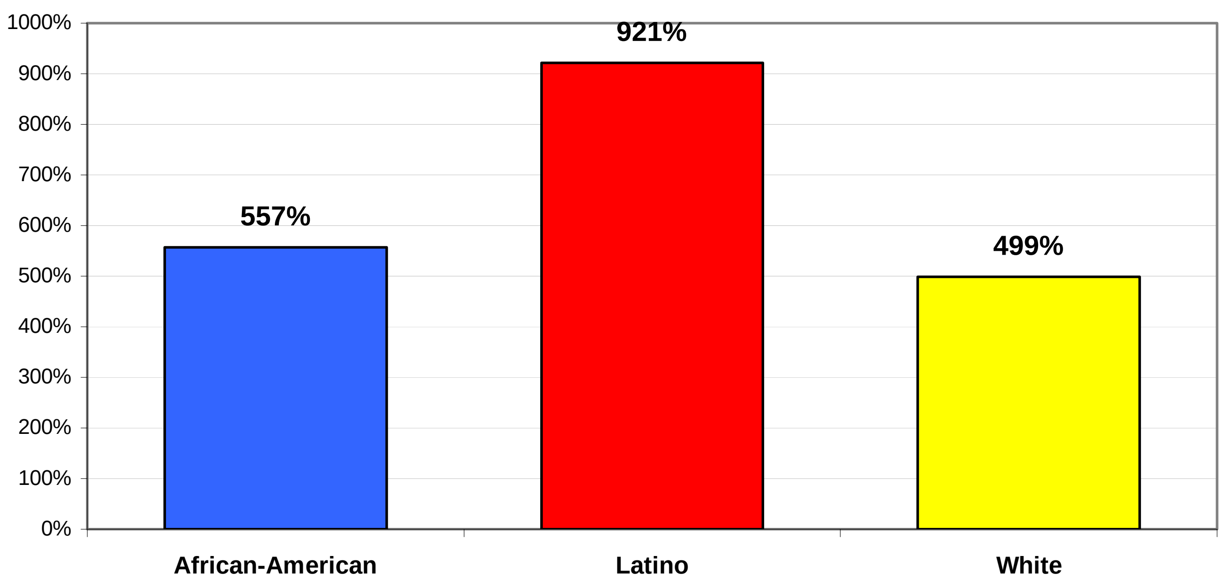
The Growth of Subprime Refinance Loans

In 1993, subprime lenders made almost 80,000 home refinance loans. In 2001, subprime lenders made over 700,000 refinance loans – almost nine times more than in 1993.

Growth from 1993 to 2001 in Home Refinance Loans

Race	Subprime			Prime		
	1993	2001	Change	1993	2001	Change
African-American	9,747	66,052	+577%	150,597	171,899	+14%
Latino	4,565	46,624	+921%	193,377	296,145	+53%
White	48,763	292,182	+499%	4,957,388	4,328,768	-13%

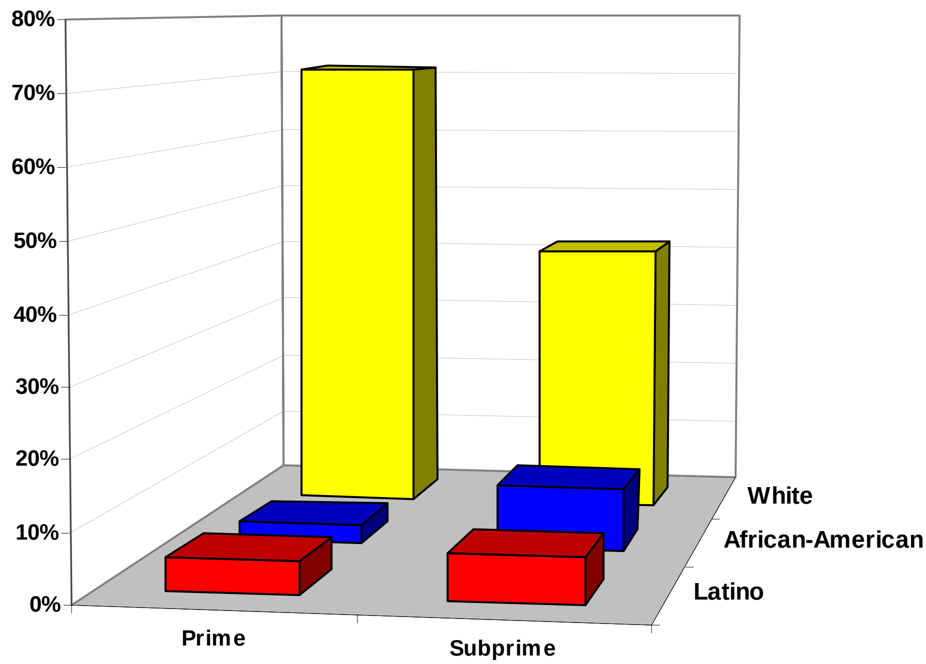
Growth in Subprime Refinance Lending by Borrower Race 1993-2001



Minorities Receive a Larger Share of Loans Made by Subprime Lenders Than of Prime Lenders

In 2001, African-Americans received 15.37% of all the refinance loans made by subprime lenders where the borrower's race was indicated, and 3.38% of the loans by prime lenders where borrower race was indicated, a 4.5 times difference. Latinos received 10.85% of all the refinance loans by subprime lenders, a 2.1 times greater share than the 5.82% they received of the refinance loans made by prime lenders where borrower race was indicated. In comparison, white homeowners received 67.99% of the subprime loans where borrower race was indicated but an even greater 85.20% of the loans by prime lenders.

Share of Refinance Loans by Lender Type and Borrower Race



Race Not Available for Subprime Refinance Loans

While there has been a large increase in the number of all types of mortgages reported with 'Race Not Available or Unknown' an especially large number of refinance loans, and subprime refinance loans in particular, are reported without the borrower's race.

Nationally, 38.7% of the refinance loans made by subprime lenders were reported without the borrower's race – well over twice as much as the 16.4% of refinance loans made by prime lenders which were reported without the borrower's race. While subprime lenders accounted for 10.3% of the total refinance loans made in the country last year, they made 21.4% of the refinance loans on which the borrower's race was not indicated.

This 'silence' about race on many loans means that the data reported here most likely understates the actual concentration of subprime lending to minority borrowers. There is no reason to believe that the distribution of refinance loans on which no race is indicated is different from that of loans where the race of the borrower is recorded. Thus, when the data including race tells us that 28 percent of refinance loans to African American borrowers are from subprime lenders, it is likely that more of the race unrecorded subprime than prime loans went to African American borrowers, and the actual portion of all refinance loans to African American borrowers from subprime lenders is greater than 28%. This proposition is supported by the fact that data on the concentration of subprime lending by neighborhood characteristic, which is not vulnerable to this silence, reveals still greater levels of concentration than the data on borrower characteristics.

It is unfortunate for a large and increasing portion of the data crucial to understanding lending patterns to be obscured in this way, particularly since we do not believe that there is any practical barrier to recording the race of the borrower in many instances where it is not in fact recorded – far fewer than 34.9% of subprime refinance loans take place without face to face contact.

In sixty-six of the sixty-seven metropolitan areas examined in this report, at least one in every five subprime refinance loans were reported with no race indicated. In contrast, at least 20% of prime refinance loans were reported without the borrower's race in just twenty-six of the sixty-seven metropolitan areas. In over half of the sixty-seven metropolitan areas, more than one-third of the subprime refinance loans had no race for the borrower and over 50% of the subprime refinance loans had no borrower race indicated in thirteen of the metropolitan areas examined.

The ten metropolitan areas in which the largest percentage of the subprime refinance loans were recorded with "Race Not Available" were: Pittsburgh, PA (60.6% race not available); Pine Bluff, AR (58.9%); Lake Charles, LA (55.1%); Las Cruces, NM (52.9%); Columbus, OH (52.8%); Little Rock, AR (52.6%); Hartford, CT (52.5%); Philadelphia, PA (52.3%); Waterbury, CT (52.3%); Houma, LA (51.6%).

The ten metropolitan areas in which the smallest percentage of the subprime refinance loans were recorded with "Race Not Available" were: San Francisco, CA (18.1%); San Jose, CA (20.4%); Chicago, IL (21.7%); San Diego, CA (22.7%); Los Angeles-Long Beach, CA (23.6%); Orange County, CA (25.0%); Denver, CO (26.0%); Oakland, CA (26.9%); Portland, OR (27.0%); Phoenix-Mesa, AZ (27.7%).

The ten areas which had the greatest difference between the percentage of prime refinance loans reported as “Race Not Available” and the percentage of subprime refinance loans reported as “Race Not Available” were: Washington, DC (82.0%); Columbus, OH (42.8%); Pittsburgh, PA (33.4%); New Orleans, LA (24.5%); Providence, RI (23.8%); Memphis, TN (21.6%); Jacksonville, FL (21.4%); Hartford, CT (21.00%); New Haven, CT (20.9%); Bridgeport, CT (20.8%).

The ten metropolitan areas which had the least difference between the percentage of subprime refinance loans reported as “Race Not Available or Unknown” and the percentage of prime refinance loans reported as “Race Not Available or Unknown” were: Houma, LA (0.9%); Portland, OR (6.9%); Albuquerque, NM (7.7%); Miami, FL (7.8%); Pine Bluff, AR (9.4%); Chicago, IL (9.5%); Tucson, AZ (9.8%); San Antonio, TX (10.0%); Seattle, WA (10.2%); Detroit, MI (10.3%).

As part of the Federal Reserve’s revisions this year to HMDA, mortgage lenders will be required to inquire about the race of telephone applicants, beginning with the data collected in 2003.[25]

[25] For a full explanation of the Federal Reserve’s HMDA changes, see the February 7, May 2, and June 21 news releases at http://www.federalreserve.gov/boarddocs/press/bcreg/2002/.

PREDATORY LENDING AND HOMEBUYING

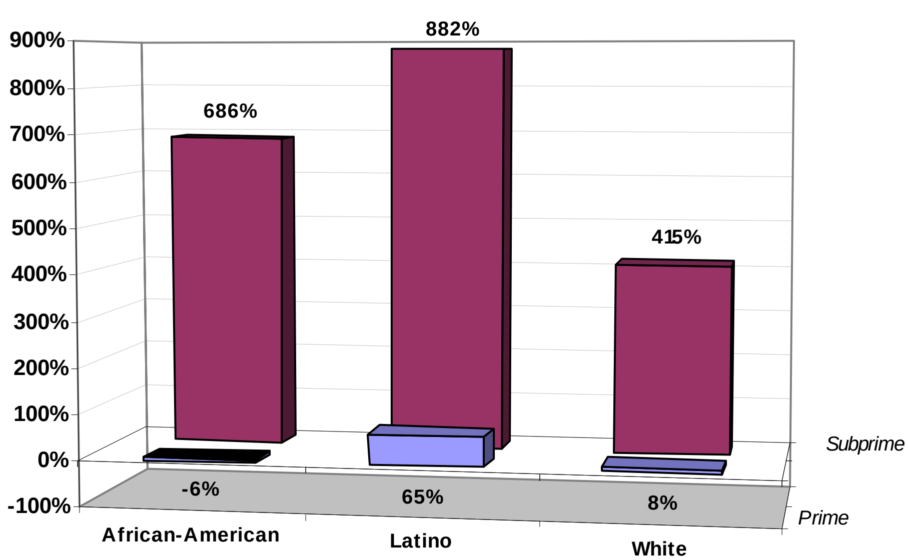
The Growth of Subprime Purchase Loans

While refinance loans make up the greatest portion of subprime lending, subprime lenders are increasing their share of the home purchase market. In 1993, subprime lenders made just 24,000 home purchase loans, which represented 1% of all the conventional home purchase loans made in the country.[26] In 2001, subprime lenders increased that number by twelve times to over 297,000 home purchase loans, or 9.0% of all the conventional home purchase loans. Unlike subprime refinance lending, which slightly declined from 1999 to 2001, subprime purchase lending continued to grow, rising from 2000 to 2001 as well.

While all communities experienced this increase in the number of subprime purchase loans, the growth in subprime lending to minorities has been greater than for whites and has been especially steep since 1995. The number of subprime purchase loans to African-American homebuyers has risen 686% from 4,614 loans in 1995 to 36,285 loans in 2001. The number of prime conventional purchase loans received by African-American homebuyers in 2001 was 6% *less* than the number received in 1995. Subprime purchase loans increased 882% to Latino homebuyers during this time, while prime loans rose just 65%. White homebuyers also saw a larger percentage increase in subprime loans than in prime loans – a 415% increase in the number of subprime loans and an 8% increase in the number of prime loans.

	Prime Lender Loans			**Subprime Lender Loans**		
	1995	**2001**	**Change**	**1995**	**2001**	**Change**
African-American	112,463	106,076	-6%	4,614	36,285	+686%
Latino	121,457	200,848	+65%	3,483	34,207	+882%
White	2,001,711	2,157,570	+8%	32,224	165,829	+415%

Change in Conventional Purchase Lending by Lender Type and Bororwer Race 1995-2001



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[26] Schessele, Randall M. 1999, 2000, 2001. U.S. Department of Housing and Urban Development.

Subprime Loans as a Percentage of Conventional Purchase Loans[27]

Purchase loans for manufactured housing make up a larger percentage of conventional loans received by African-Americans and Latinos than of those received by whites. Subprime loans made up 25.5% of conventional home purchase loans received by African-Americans in 2001 and 14.6% of the conventional home purchase loans to Latinos, but just 7.1% of the loans to whites.

Percentage of Conventional Purchase Loans That Are from Subprime Lenders

Race	1993	1995	1999	2001
African-Americans	2.7%	3.9%	23.1%	25.5%
Latinos	1.6%	2.8%	12.0%	14.6%
Whites	0.8%	1.6%	4.8%	7.1%

In comparative terms, this means that in 2001, African-American homebuyers were 3.6 times more likely than white homebuyers to receive a subprime loan and Latinos were 2.0 times more likely to receive a subprime loan than white homebuyers.

The racial disparity remains when comparing minority borrowers with white borrowers of the same income. 18.93% of the conventional purchase loans received by upper-income African-Americans were from subprime lenders, as were 12.71% of the conventional purchase loans received by upper-income Latinos. In contrast, only 5.84% of the purchase loans received by upper-income whites were from subprime lenders.

This means that upper-income African-American homebuyers were 3.2 times more likely to receive a subprime loan than upper-income white homebuyers and upper-income Latinos were 2.2 times more likely than whites to receive a subprime loan.

In addition, upper-income African-Americans and Latinos were even more likely than low-income whites to receive a subprime loan.

[27] "All Loans" excludes loans made by manufactured housing lenders.

Minorities Receive a Much Larger Share of Home Purchase Loans from Subprime Lenders than from Prime Lenders

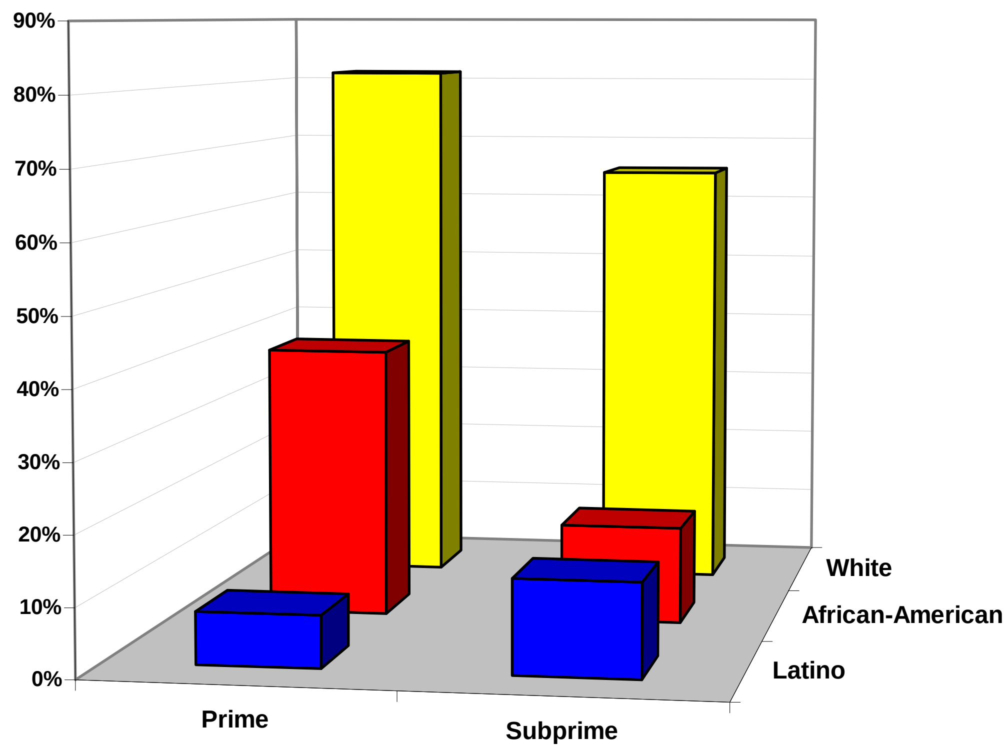
In 2001, African-Americans received 12.21% of all the subprime purchase loans made in the United States, a 3.5 times larger share than the 3.51% of prime purchase loans they received. Latinos received 11.51% of the subprime loans, almost double their 6.64% share of prime loans. In contrast, whites received 55.80% of the subprime purchase loans, but 71.36% of the prime loans.

Share of Subprime Purchase Loans Received

Borrower Race	1993	1995	1999	2001
African-American	8.3%	9.0%	13.5%	12.2%
Latino	5.9%	6.8%	8.5%	11.5%
White	60.5%	62.7%	49.6%	55.8%

If we exclude the loans where no borrower race was indicated (15% of the subprime loans and 12% of the prime lender loans), African-Americans received 14.30% of the subprime loans where race was indicated, 3.6 times greater than the 4.00% they received of the loans by prime lenders where the borrower race was indicated. Latinos received 13.49% of the subprime lender loans, a 1.8 times greater share than the 7.57% they received of the purchase loans by prime lenders. White borrowers received 65.38% of the loans by subprime lenders but 81.32% of the loans by prime lenders.

The share received by African-Americans and Latinos has increased significantly since 1993 while the share received by whites has declined since then.



Subprime Lending in Minority Communities

There is a greater concentration of subprime loans in minority neighborhoods. Subprime lenders represent more than one-fifth, 22.71% of the conventional home purchase loans made in neighborhoods where minorities constitute 80-100% of the population. In 50-80% minority communities, 15.52% were from subprime lenders. In contrast, less than one in thirteen refinance loans 7.42% were from subprime lenders in heavily white communities (0-20% minority population.).

Subprime Lender Share of Refinance Loans by Census Tract % Minority

	0-20% Minority	**20-50% Minority**	**50-80% Minority**	**80-100% Minority**
Subprime Lender Loans	179,779	71,420	24,322	18,367
Prime Lender Loans	2,241,898	506,029	132,372	62,493
% Subprime	7.42%	12.37%	15.52%	22.71%

In comparative terms, homeowners in 80-100% minority communities were 3.1 times more likely to receive a subprime refinance loan than homeowners in heavily white communities (0-20% minority population). Homeowners in neighborhoods with 50-80% minority population were 2.1 times more likely to receive a subprime loan when refinancing than homeowners in heavily white neighborhoods.

Subprime Purchase Lending in Specific Metropolitan Areas

Greatest and Least Concentrations of Subprime Loans

Greatest Concentration of Subprime Purchase Loans to African-American Homebuyers

In every city,[28] subprime lenders represented at least one out of every nine conventional purchase loans made to African-Americans. In 10 cities, subprime lenders made at least one out of every three purchase loans made to African-Americans: Memphis, New Haven, Cleveland, St. Louis, Ft. Wayne, Gary, Riverside-San Bernardino, Indianapolis, Chicago and Detroit.

MSA		Subprime Lender Loans	Prime Lender Loans	% Subprime
Memphis	TN	959	1232	43.77%
New Haven	CT	106	181	36.93%
Cleveland	OH	730	1261	36.66%
St. Louis	MO	890	1538	36.66%
Ft. Wayne	IN	35	65	35.00%
Gary	IN	116	219	34.63%
Riverside-San Bernardino	CA	728	1411	34.03%
Indianapolis	IN	306	596	33.92%
Chicago	IL	2622	5158	33.70%
Detroit	MI	1546	3073	33.47%

Least Concentration of Subprime Purchase Loans to African-American Homebuyers

MSA		Subprime Lender Loans	Prime Lender Loans	% Subprime
Baltimore	MD	427	1945	18.00%
New Orleans	LA	154	721	17.60%
Stamford-Norwalk	CT	32	155	17.11%
Jersey City	NJ	28	138	16.87%
Minneapolis-St. Paul	MN	169	838	16.78%
Washington	DC	1441	7464	16.18%
Bergen-Passaic	NJ	64	332	16.16%
Nassau-Suffolk	NY	220	1279	14.68%
Boston	MA	157	1066	12.84%
New York	NY	638	4782	11.77%

[28] Rankings exclude cities where fewer than 50 conventional purchase loans were made to African-Americans or Latinos. Fewer than 50 purchase loans were made to African-Americans in Sioux Falls, SD; Las Cruces, NM; and Houma, LA. Fewer than 50 purchase loans were made to Latinos in Sioux Falls, SD; Pine Bluff, AR; Houma, LA; Baton Rouge, LA; and Lake Charles.

Greatest Concentration of Subprime Purchase Loans to Latino Homebuyers

MSA		Subprime Lender Loans	Prime Lender Loans	% Subprime
Waterbury	CT	59	93	38.82%
Providence	RI	125	258	32.64%
San Jose	CA	841	2165	27.98%
Portland	OR	183	491	27.15%
New Haven	CT	62	208	22.96%
San Diego	CA	1155	3927	22.73%
San Francisco	CA	326	1141	22.22%
Riverside-San Bernardino	CA	2071	7473	21.70%
Oakland	CA	1069	4093	20.71%
San Antonio	TX	673	2714	19.87%

Least Concentration of Subprime Purchase Loans to Latino Homebuyers

MSA		Subprime Lender Loans	Prime Lender Loans	% Subprime
Indianapolis	IN	19	175	9.79%
New Orleans	LA	26	249	9.45%
Columbus	OH	12	118	9.23%
Ft. Worth-Arlington	TX	183	1833	9.08%
Ft. Wayne	IN	7	71	8.97%
St. Louis	MO	23	235	8.91%
Cincinnati	OH	10	127	7.30%
Cleveland	OH	32	409	7.26%
Milwaukee	WI	49	709	6.46%
Wilmington	DE	7	121	5.47%

Greatest Concentration of Subprime Purchase Loans to White Homebuyers

MSA		Subprime Lender Loans	Prime Lender Loans	% Subprime
Riverside-San Bernardino	CA	4599	22874	16.74%
Los Angeles-Long Beach	CA	6689	42206	13.68%
Stockton-Lodi	CA	540	3500	13.37%
San Diego	CA	3608	23521	13.30%
Portland	OR	3058	20489	12.99%
Pine Bluff	AR	28	196	12.50%
Orange County	CA	3238	24614	11.63%
Oakland	CA	2097	16469	11.29%
San Jose	CA	895	7065	11.24%
San Francisco	CA	1118	8832	11.24%

Least Concentration of Subprime Purchase Loans to White Homebuyers

MSA		Subprime Lender Loans	Prime Lender Loans	% Subprime
Gary	IN	226	4817	4.48%
Indianapolis	IN	663	14814	4.28%
Cleveland	OH	872	20449	4.09%
New York	NY	1224	29721	3.96%
New Orleans	LA	237	6428	3.56%
Minneapolis-St. Paul	MN	1504	41339	3.51%
Bergen-Passaic	NJ	285	7860	3.50%
Stamford-Norwalk	CT	132	3891	3.28%
Newark	NJ	411	12233	3.25%
Milwaukee	WI	391	15688	2.43%

Greatest Concentration of Subprime Purchase Loans to Minority Neighborhoods (80-100% Minority Population)[29]

MSA		Subprime Lender Loans	Prime Lender Loans	% Subprime
Jacksonville	FL	113	77	59.47%
St. Louis	MO	294	268	52.31%
Indianapolis	IN	135	137	49.63%
Cleveland	OH	512	553	48.08%
Toledo	OH	33	36	47.83%
Detroit	MI	892	1006	47.00%
Memphis	TN	239	283	45.79%
Providence	RI	37	44	45.68%
Baton Rouge	LA	38	47	44.71%
New Haven	CT	31	39	44.29%

Least Concentration of Subprime Purchase Loans to Minority Neighborhoods (80-100% Minority Population)

MSA		Subprime Lender Loans	Prime Lender Loans	% Subprime
Sacramento	CA	8	42	16.00%
Houston	TX	334	1780	15.80%
Las Cruces	NM	21	130	13.91%
Bergen-Passaic	NJ	37	240	13.36%
New York	NY	850	5594	13.19%
Stockton-Lodi	CA	52	343	13.16%
Washington	DC	432	2898	12.97%
Ft Worth-Arlington	TX	23	160	12.57%
Boston	MA	84	597	12.33%
Seattle	WA	11	164	6.29%

[29] Excludes cities where fewer than 50 conventional home purchase loans were made in census tracts with 80-100% minority population: Sioux Falls, SD; Brockton, MA; Waterbury, CT; Ft. Wayne, IN; Lake Charles, LA; Little Rock, AR; Houma, LA; Pine Bluff, AR; Stamford-Norwalk, CT; Portland, OR.

Greatest and Least Disparity in Subprime Home Purchase Lending

Most Disparate MSAs for African-American Homebuyers

MSA		Subprime Share of Loans to African-Americans	Subprime Share of Loans to Whites	Disparity
Cleveland	OH	36.66%	4.09%	9.0
Milwaukee	WI	21.28%	2.43%	8.8
Indianapolis	IN	33.92%	4.28%	7.9
Gary	IN	34.63%	4.48%	7.7
Ft. Wayne	IN	35.00%	4.60%	7.6
St. Louis	MO	36.66%	4.89%	7.5
Chicago	IL	33.70%	4.78%	7.1
Jacksonville	FL	32.77%	5.14%	6.4
Memphis	TN	43.77%	7.14%	6.1
Newark	NJ	18.68%	3.25%	5.8

Least Disparate MSAs for African-American Homebuyers

MSA		Subprime Share of Loans to African-Americans	Subprime Share of Loans to Whites	Disparity
Stockton-Lodi	CA	29.47%	13.37%	2.2
Portland	OR	28.19%	12.99%	2.2
Pine Bluff	AR	27.69%	12.50%	2.2
Phoenix-Mesa	AZ	22.14%	10.32%	2.2
Boston	MA	12.84%	5.82%	2.2
Riverside-San Bernardino	CA	34.03%	16.74%	2.0
Los Angeles-Long Beach	CA	27.80%	13.68%	2.0
Orange County	CA	23.74%	11.63%	2.0
San Jose	CA	21.24%	11.24%	1.9
Sacramento	CA	20.80%	10.77%	1.9
San Diego	CA	23.98%	13.30%	1.8
San Francisco	CA	19.00%	11.24%	1.7

Most Disparate MSAs for Latino Homebuyers

MSA		Subprime Share of Loans to Latinos	Subprime Share of Loans to Whites	Disparity
Stamford-Norwalk	CT	17.58%	3.28%	5.4
Waterbury	CT	38.82%	7.93%	4.9
Providence	RI	32.64%	9.03%	3.6
Hartford	CT	18.66%	5.40%	3.5
Minneapolis-St. Paul	MN	11.41%	3.51%	3.3
Newark	NJ	10.57%	3.25%	3.3
Bergen-Passaic	NJ	11.63%	3.50%	3.3
Jersey City	NJ	17.21%	5.34%	3.2
Springfield	MA	17.53%	5.71%	3.1
New Haven	CT	22.96%	7.77%	3.0

Least Disparate MSAs for Latino Homebuyers

MSA		Subprime Share of Loans to Latinos	Subprime Share of Loans to Whites	Disparity
Columbus	OH	9.23%	5.66%	1.6
Dallas	TX	12.04%	7.43%	1.6
Tampa-St. Petersburg	FL	12.10%	7.39%	1.6
Ft. Lauderdale	FL	14.61%	9.04%	1.6
Sacramento	CA	16.03%	10.77%	1.5
Stockton-Lodi	CA	18.19%	13.37%	1.4
Orange County	CA	16.06%	11.63%	1.4
Riverside-San Bernardino	CA	21.70%	16.74%	1.3
Cincinnati	OH	7.30%	6.21%	1.2
Ft. Worth-Arlington	TX	9.08%	7.81%	1.2
Los Angeles-Long Beach	CA	16.61%	13.68%	1.2
Wilmington	DE	5.47%	6.63%	0.8

Most Disparate MSAs for Homebuyers in Minority Neighborhoods (80-100% Minority Population)

MSA		Subprime Share of Refinance Loans		Disparity
		80-100% Minority Population	0-20% Minority Population	
Fresno	CA	20.97%	1.04%	20.2
Indianapolis	IN	49.63%	4.69%	10.6
Jacksonville	FL	59.47%	5.78%	10.3
Milwaukee	WI	27.00%	2.69%	10.0
Cleveland	OH	48.08%	4.95%	9.7
St. Louis	MO	52.31%	6.03%	8.7
Toledo	OH	47.83%	5.54%	8.6
Columbus	OH	41.33%	4.96%	8.3
Newark	NJ	22.92%	3.21%	7.1
Kansas City	MO	38.42%	5.66%	6.8
Minneapolis-St. Paul	MN	27.16%	3.98%	6.8

Least Disparate MSA for Homebuyers in Minority Neighborhoods

MSA		Subprime Share of Refinance Loans 80-100% Minority Population	0-20% Minority Population	Disparity
Phoenix-Mesa	AZ	19.82%	10.55%	1.9
Ft. Lauderdale	FL	19.11%	10.34%	1.8
San Francisco	CA	17.17%	10.62%	1.6
Ft . Worth-Arlington	TX	7.84%	12.57%	1.6
Los Angeles-Long Beach	CA	18.74%	12.53%	1.5
Sacramento	CA	16.00%	10.98%	1.5
Orange County	CA	16.59%	11.57%	1.4
Riverside-San Bernardino	CA	18.05%	17.07%	1.1
Stockton-Lodi	CA	13.16%	11.90%	1.1
Seattle	WA	6.29%	8.70%	0.7

The Exclusion of Low-Income and Minority Neighborhoods from the Economic Mainstream

Predatory lenders have been able to get away with abusive practices in part because they are exploiting the history of racial discrimination and neighborhood redlining by traditional financial institutions.

In October 2002, ACORN released a report entitled *The Great Divide*, which examined 2001 loan data for the nation as a whole, as well as for 68 metropolitan areas. The report found continuing and even growing racial and economic disparities in home purchase mortgage lending. Nationally, African-American mortgage applicants were rejected 2.31 times more often than white applicants, and Latinos were denied 1.53 times more often than whites. Conventional purchase originations to African-Americans fell by 7.8% compared to the previous year. The report also found that while low and moderate income neighborhoods comprise 25.7% of the country, these neighborhoods only received 11.7% of the loans. Furthermore, residents of low and moderate income neighborhoods were 3.1 times more likely to be turned down for a loan than residents of upper-income neighborhoods.[30]

This statistical analysis has been corroborated by a report from the Urban Institute, prepared for HUD, which concluded that minority homebuyers face discrimination from mortgage lenders. The report cited "paired testing" which showed that minorities were less likely to receive information about loan products, received less time and information from loan officers, and were quoted higher interest rates.[31]

The Great Divide also found that many metropolitan areas had much more alarming disparities in their mortgage lending than the national average. For instance, in Chicago and Milwaukee, African-Americans were more than five times more likely than whites to be denied for a conventional loan. As described in this report, when African-American borrowers do receive a loan, their likelihood of receiving a subprime loan relative to white borrowers is also among the highest in the country. African-Americans in Milwaukee were nearly nine times more likely than whites to receive a subprime loan when buying a house with a conventional loan and in Chicago were over seven times more likely.

Banks have for the most part abandoned low-income and minority neighborhoods. A study by economists at the Federal Reserve found that the number of banking offices in low and moderate income areas decreased 21% from 1975 to 1995, while the total number of banking offices in all areas rose 29% during this same period. This is significant because studies have documented that the proximity of a bank's branches to low and moderate income neighborhoods is directly related to the level of lending made by the bank in those neighborhoods.[32]

In 2001, one-quarter of families with incomes below 80% of the area median income did not have a bank account.[33] Having a bank account is a basic, yet important, entry point into the mainstream economy and traditional financial services. A bank account can help a consumer handle their finances, save money, and establish the type of credit which is often a prerequisite to receiving a conventional loan. In addition, having an account establishes a relationship with a bank, which makes it more likely

[30] The report examined applications for conventional home purchase loans. Low and moderate income neighborhoods are defined as census tracts in which the median income is below 80% of the median income for the entire metropolitan area. Upper income neighborhoods are census tracts in which the median income is more than 120% of the area's median income.
[31] "Discrimination in Metropolitan Housing Markets: National Results from Phase I of HDS2000," The Urban Institute, November 2002.
[32] *The Community Reinvestment Act After Financial Modernization: A Baseline Report*, U.S. Treasury Department, April 2000.
[33] *The State of the Nation's Housing: 2001*, Harvard University Joint Center for Housing Studies, p. 29.

that the consumer will contact that bank regarding loans and other services. Furthermore, the consumer will also be contacted by the bank as it markets its other products, such as mortgages, to its existing customer base.[34]

The ten million American families without bank accounts represent a substantial market of consumers who require alternative financial services. In response, a "fringe economy" has emerged made up of check-cashing stores, pawnshops, and payday lenders, which are then able to overcharge lower income consumers. Many of these "shadow banks" are funded by mainstream banks. For instance, Wells Fargo, the seventh largest bank in the country, has arranged more than $700 million in loans since 1998 to three of the largest check cashers: Ace Cash Express, EZ Corp., and Cash America.[35] Payday lenders are also increasingly trying to rent out national bank charters to avoid state consumer protection laws.

The exclusion of low-income and minority communities from traditional banking services has also translated into a lack of the financial knowledge that could help consumers receive loans with more reasonable terms. For instance, a study by Benedict College found that half of African-Americans with good credit ratings were not aware of it.[36]

These factors have created an environment that was ripe to be picked by predatory lenders who aggressively target these underserved communities with a bombardment of mailings, phone calls, and door-to-door solicitations. Sales to the captive audience of the subprime market are driven by inappropriate and deceptive marketing practices that encourage potential borrowers to believe that they have no better credit options for their legitimate credit needs.

While the faces of predatory lenders may appear to be those of small-time crooks, the kingpins behind predatory lending can be found among some of the world's largest financial institutions, and in fact, many of the same institutions which created the situation by their failure to serve certain communities are now opportunistically reaping the profits.

Sometimes these institutions have direct ownership of subprime lending subsidiaries, such as Citigroup and Citifinancial. In 1999, Citifinancial had 1,170 branch offices and recorded a 77% increase in net income to $390 million.[37] This was prior to its acquisition of Associates, the nation's largest consumer lender, which had 1,300 branches of its own branches in the U.S. and in 1999 had $1.5 billion in profits, its 25th consecutive year of record earnings. In other cases, these institutions, particularly investment firms, bankroll predators by securitizing their mortgages and selling them to investors. The major Wall Street investment banks' involvement in the subprime market has grown substantially in recent years, securitizing $18.5 billion in subprime loans in 1997 up to $56 billion in 2000.[38]

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[34] *The Community Reinvestment Act After Financial Modernization: A Baseline Report*, U.S. Treasury Department, April 2000..
[35] "Easy Money," *Business Week*, April 24, 2000.
[36] *The State*, February 22, 2000.
[37] "Easy Money," *Business Week*, April 24, 2000.
[38] "Predatory Lending Document Could Target CitiFinancial," *Dallas Morning News*, by Anuradha Raghunathan, September 13, 2002, Business section.

Many Borrowers in Subprime Loans Should Have Qualified for a Lower Cost Loan

The fact that a part of the boom in subprime lending, especially to minorities, results from the neglect of certain communities by 'A' lenders is further underlined by the considerable evidence that many borrowers in subprime loans could have qualified for 'A' loans at lower rates.

Franklin Raines, the Chairman of Fannie Mae, has stated that as many as half of all borrowers in subprime loans could have instead qualified for a lower cost conventional mortgage, which according to Raines, could save a borrower more than $200,000 over the life of a thirty year loan.[39]

This conclusion is supported by other sources. *Inside Mortgage Finance* published a poll of the 50 most active subprime lenders which also found that up to 50 percent of their mortgages could qualify as conventional loans.[40] Freddie Mac has estimated that as many as 35 percent of borrowers who obtained mortgages in the subprime market could have qualified for a lower cost conventional loan.[41] In an investigation of subprime lenders, the Department of Justice found that approximately 20% of the borrowers had FICO credit scores above 700,[42] significantly higher than the minimum score of 620 which is usually required to receive a prime interest rate. The CEO of HSBC, which recently announced plans to purchase the US's largest subprime lender, Household International, said in a recent interview that 63% of Household's customer base (including consumers with car loans, credit cards, and unsecured loans) has prime credit.[43]

The most obvious consequence for borrowers who have been improperly steered into subprime loans is that they are unnecessarily paying more than they should. In the loans that were examined by the Department of Justice, the borrowers were paying interest rates of 11 and 12 percent and 10 to 15 points of the loan in fees, while borrowers with a prime loan had 7 percent interest rates and just 3 or 4 points of the loan in fees.

A trade group for subprime lenders, the National Home Equity Mortgage Association (NHEMA), stated that from 1997 to 1999, subprime loans had an average interest rate between 2.5% and 4.0% above the rate that prime borrowers are charged.[44] NHEMA also estimated that subprime lender charge an average of 1.5 to 3 percentage points more in fees than conventional lenders.[45] Many borrowers in subprime loans are, however, charged significantly more than these figures.

As discussed in this report, subprime loans are disproportionately made to lower income borrowers. This means that subprime lenders are overcharging those homeowners who can already least afford it. A subprime loan with inappropriately high costs can impact homeowners in several ways.

The added expense increases the likelihood that the homeowner will be unable to make the mortgage or other payments on time, which hurts their credit, and thus keeps them trapped in the subprime market with unfavorable loan terms. The higher costs also strip homeowners of their hard-earned equity and prevent

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[39] Business Wire, "Fannie Mae has Played Critical Role in Expansion of Minority Homeownership Over Past Decade," March 2, 2000.
[40] *Inside B&C Lending*, June 10, 1996.
[41] "Automated Underwriting," Freddie Mac, September 1996.
[42] "Making Fair Lending a Reality in the New Millennium," Fannie Mae Foundation, 2000.
[43] "HSBC: Why the British Are Coming: Chairman John Bond explains why the usually cautious British bank paid a 30% premium to acquire American lender Household," *Business Week Online*, November 18, 2002, Daily Briefing.
[44] Jeffrey Zeltzer, Executive Director, National Home Equity Mortgage Association-NHEMA, remarks to HUD-Treasury Task Force on Predatory Lending, Atlanta, GA, April 26, 2000.
[45] "Widow paying a price for high-cost loan," *Orange County Register*, by Kate Berry, April 16, 2000.

them from building future equity. Furthermore, having a subprime loan means that the homeowner is more likely to be subject to a host of predatory practices, beyond just higher rates and fees, which will be discussed in more detail in the next section. All of these factors make it more likely that the homeowner will ultimately and unnecessarily lose their house in foreclosure.

PREDATORY LENDING PRACTICES

The reach and effect of abusive practices by predatory lenders have increased along with the dramatic growth of the subprime industry. The following are some of the more common predatory practices.

Financing Excessive Fees into Loans

Predatory lenders often finance huge fees into loans, stripping thousands of dollars in hard-earned equity and racking up additional interest in the future. Borrowers in predatory loans are routinely charged fees of just under 8% of the loan amount in fees, compared to the average 1%-2% assessed by banks to originate loans. Once the paperwork is signed and the rescission period expires, there is no way to get that equity back, and borrowers frequently lose up to $10,000 or $15,000 from their home while receiving little, if any, benefit from the refinancing. The damage is compounded at higher interest rates as borrowers often pay tremendous interest costs in the several years it can take just to pay down the fees. Typically, the loan fees are kept below 8% in order to stay under the HOEPA fee threshold established by federal law, which would then require additional disclosures to the borrower and a few very limited consumer protections.

> *A couple bought a house in need of substantial repairs for $2,500 from a previous owner who had fallen behind on his property taxes. To do some repairs, they took out a home-equity loan for $49,990, which was greatly inflated by 7.0 discounts points for $3,499, and $502 in third-party charges, as well as credit insurance policies totaling $4,992. Despite all the discount points paid, the loan's interest rate was 11.1%. After making all their payments for six months, the couple refinanced to a $78,247 mortgage to take out some additional equity. Again, the lender financed in 7.0 discount points – $5,477 – plus another $541 in third-party charges, while the interest rate increased to 11.9%.*

Charging Higher Interest Rates Than A Borrower's Credit Warrants

While the higher interest rates charged by subprime lenders are intended to compensate lenders for taking a greater credit risk, too many borrowers are unnecessarily paying higher interest rates. Borrowers with perfect credit are regularly charged interest rates 3 to 6 points higher than the market rates; with some subprime lenders, there simply is no lower rate, no matter how good the credit. According to a rate sheet used by the Associates in the spring of 2000, their lowest interest rate for a borrower with excellent credit and a low loan-to-value ratio was over 10%, and since then Household borrowers with excellent credit were seeing rates above 11%. And for borrowers with imperfect credit, rates are frequently much higher than even somewhat blemished credit would reasonably warrant, as well as for what the industry describes as standard rates for B, C, or D borrowers.

> *A couple with children had bought a house with a variable interest rate mortgage that had stayed between 8% and 9%, and they had always been careful to make their payments on time. A few years later, they took out a second mortgage but subsequently were convinced that it would be easier to consolidate and make just one mortgage payment each month. The refinanced mortgage for $157,077 did not pay off all the debts that had been promised and included over $11,588 in the lender's financed fees. Despite all the discount points and their excellent credit record (the husband had a FICO score of 643, Empirica of 675, and Beacon of 700), the loan contained an interest rate of 10.8%. After talking with an ACORN Housing Corporation loan counselor, they were able to refinance the mortgage to a 6% interest rate, which will save them several hundred dollars a month but not restore any of their lost equity.*

Making Loans Without Regard to the Borrower's Ability to Pay

Some predatory lenders make loans based solely on a homeowner's equity, even when it is obvious that the homeowner will not be able to afford their payments. Especially when there is significant equity in a home, the lender can turn a profit by reselling the house after foreclosure. Until that happens, the borrower is stuck with exorbitant monthly payments.

In other cases, the opportunity to strip away huge amounts of home equity drives the origination of clearly unaffordable mortgages. For mortgage brokers, the immediate opportunity to legally take away several thousand dollars of home equity more than offsets the eventual consequences of the loan, which will be dealt with by the holder on the secondary market. Similarly, personal commissions may push loan officers at mortgage companies to make loans that cannot be repaid.

A couple purchased their home through a special low-rate mortgage at 5% interest and monthly payments of $746. Shortly thereafter, they received an open-end second mortgage with a credit limit of $35,000, an initial advance of $36,800, an origination fee of $1,840, and a variable interest rate that started at 22.4%. The second mortgage's monthly payments of $742 were clearly unaffordable on the husband's monthly income as a janitor of $1,800 and the $546 they receive from SSI to help care for their hearing-impaired daughter. Without any other options, the couple was forced to sell their house and buy another less expensive one, but not before losing an additional $3,000 on a prepayment penalty.

Prepayment Penalties

More than two-thirds of subprime loans have prepayment penalties, compared to less than 2% of conventional prime loans.[46] The penalties come due when a borrower pays off their loan early, typically through refinancing or a sale of the house. The penalties remain in force for periods ranging from the first two to five years of the loan, and are often as much as six months interest on the loan. For a $100,000 loan at 11% interest, the penalty would be over $5,000, which would be financed into the new loan. For borrowers who refinance or sell their houses during the period covered by the prepayment penalty, the penalty functions as an additional and expensive fee on the loan, further robbing them of their equity.

Lenders argue that prepayment penalties protect them against frequent turnover of loans, and that as a result of the higher rates which investors are willing to pay for loans with prepayment penalties, they are able to charge borrowers lower interest rates. The truth is, however, that very large and quite predictable numbers of borrowers in subprime loans do refinance within the period covered by the prepayment penalty and may well end up paying more in the penalty than they "saved" even if their interest rate was reduced. It is particularly pernicious when prepayment penalties keep borrowers trapped in the all too common situation of paying interest rates higher than they should be.[47]

[46] HUD-Treasury Report on Predatory Lending, p. 90.
[47] See also the discussion below on how prepayment penalties interact with yield-spread premiums to trap borrowers in excessive interest rates.

Borrowers are frequently unaware that their loans contain a prepayment penalty. Some lenders' agents simply fail to point it out, while others deliberately mislead borrowers, telling them they can refinance later to a lower rate, without informing them of the prepayment penalty that will be charged. Even the most knowledgeable borrowers can easily the prepayment penalty amid the mounds of paperwork, and end up robbed of additional equity or trapped in an excessive rate because the penalty boosts up their loan-to-value ratio.

In a significant step forward in September, the federal Office of Thrift Supervision changed a rule interpretation that effectively restored a number of state laws providing varying levels of consumer protections against prepayment penalties. The state Attorneys General's settlement with Household also represents a major advance in requiring the country's largest subprime lender to limit all of its prepayment penalties to the loan's first two years, both retroactively and prospectively.

A homeowner got involved with a subprime lender and received a 16% interest rate despite having had excellent credit and having made all his payments on time. He was subsequently solicited by another subprime lender to refinance to a 7% interest rate, but the loan turned out much differently from what was promised. The new loan amount of $210,363 contained a financed origination fee of $15,251 and a single-premium credit life insurance policy for $5,113. Despite all the discount points, the interest rate was 11.2%, which he was locked into by a three-year prepayment penalty for $6,000. He tried to refinance with a prime lender, but the subprime lender refused to provide a payoff amount and then eventually quoted a penalty of $11,000 to the prime lender. At that point, the prime lender refused to refinance because the new loan would have exceeded the appraised value of the home.

Loans for Over 100% Loan to Value

Some lenders regularly make loans for considerably more than a borrower's home is worth with the specific intents of maximizing their debt and thus their payments, and trapping them as customers for an extended period. Even borrowers with excellent credit have no way to escape from a high rate loan if they are 'upside down' and owe more than their home is worth. Borrowers are frequently unaware that they owe much more than their homes are worth, and even more frequently unaware of the consequences. In the face of criticism from Wall Street and longstanding pressure from ACORN, in the spring of 2002 Household quietly eliminated its common practice of using extremely high-rate open-end second mortgages that push borrowers' LTV ratios above 100%.

A couple had bought their house with a 30-year mortgage for $137,000 at a 7.8% interest rate, and six months later they took out first a personal loan and then a second mortgage for $10,000 to buy some furniture. The lender kept soliciting them to increase their indebtedness and told them that they were two months behind on the second mortgage and could face foreclosure if they didn't consolidate their mortgages. The lender appraised their home for $165,000, which the couple thought would be the amount of their new loan, but the lender financed in its fees to raise the actual principal to $177,104, which was made at a 10.8% interest rate. Making it worse, the loan includes a three-year prepayment penalty for almost $10,000, and they found out they were only one month behind on the second mortgage. Despite the husband's middle credit score of 646, which is considered 'A' credit by many lenders, the couple now finds it impossible to refinance because the LTV ratio is over 100%.

Yield Spread Premiums

A yield spread premium is compensation paid by a lender to a mortgage broker for the broker's success in getting the borrower to accept a higher interest rate than the lender would have given the borrower at their standard, or "par," rate. Brokers usually receive this kickback on top of an already large origination fee financed into the borrower's loan. While brokers typically try to create the impression with borrowers that they are trying to secure the best possible loan, yield spread premiums create an obvious financial incentive for brokers to increase the loan costs. In the text of a proposed rule that would change how the premiums are disclosed but would not alter their fundamentally abusive nature, HUD estimates that lenders annually pay brokers $15 billion to increase borrower's interest rates – the same amount that borrowers pay in origination charges.[48]

Yield-spread premiums further harm borrowers in that the financial incentives often drive lenders to insist that the loans include prepayment penalties. Since by definition a yield-spread premium pushes the borrower into an excessive interest rate, borrowers who later realize their actual interest rate are more likely to refinance out of the loan. To reduce the likelihood that borrowers will refinance out and to ensure their profits even if they do, lenders often require brokers to also include a prepayment penalty when the interest rate is inflated due to a yield-spread premium.

A couple refinanced their mortgage through a broker, receiving a new balance of $109,200. Of this amount, $11,030 went toward various closing costs and fees, of which $5,138 went directly to the broker. On top of that amount, the lender paid the broker a yield-spread premium of $3,276 for putting the couple in a variable interest rate that starts at 12.3% and can go as high as 18.3%. In addition, the loan contains a two-year prepayment penalty for over $2,000 if they would try to refinance to a lower rate.

Home Improvement Scams

Some home improvement contractors deliberately target their marketing efforts to lower income neighborhoods where homes are in most need of repairs, and where the owners are unable to pay for the service. The contractor tells the homeowner they will arrange for the financing to pay for the work and refers the homeowner to a specific broker or lender, even driving them to the lender or broker's office. Sometimes the contractor begins the work before the loan is closed, so that even if the homeowner has second thoughts about taking the loan, they are forced into it in order to pay for the work. The lender may then make the payments directly to the contractor, which means that the homeowner has no control over the quality of the work. As a result, the work may not be done properly or even at all, but the homeowner is still stuck with a high-interest, high fee loan.

A homeowner hired a home improvement contractor to gut and rehab a large portion of her house. The contractor had a special arrangement with a mortgage company wherein the checks were made out directly to the contractor, rather than jointly to the borrower and the contractor. The contractor cashed checks totaling $52,000 but failed to perform the promised work, leaving the homeowner to pay off the 10% interest rate loan without having the work completed. After taking similar advantage of at least five other consumers, the contractor changed its name and relocated to a different address.

[48] Docket No. FR-4727-P-01, *Federal Register*, July 29, 2002, p. 49170.

Single Premium Credit Insurance

Credit insurance is insurance linked to a specific debt or loan which will pay off that particular debt if the borrower loses the ability to pay either because of sickness (credit health insurance), death (credit life insurance), or losing their job (credit unemployment insurance). It is rarely promoted in the 'A' lending world, but it has been aggressively and deceptively sold in 'single premium' form in connection with higher cost loans, and then financed into the home loans, costing borrowers equity in their homes, and forcing them to pay higher interest charges.

With 'single premium' policies, instead of making regular monthly, quarterly, or annual payments as people do with other insurance policies, the credit insurance is paid in one lump sum payment, which may be as high or even higher than $10,000, especially if borrowers are sold multiple forms of credit insurance, as is frequently the case. This premium is then financed into the loan, increasing the loan amount (and since the loan amount is higher, the lender's origination fees also increase), and the borrower must then pay monthly interest on the amount of the insurance premium. While the coverage on a single premium policy usually lasts for only 5 years, the borrower pays for it, and pays interest on it, over the 30 years of the home loan. After those 5 years and the coverage has expired, the remaining loan balance is usually higher than the original balance would have been minus the policy, meaning that the policy prevents the borrower from building up any equity. Typically, single premium credit insurance policies cost four to five times as much as monthly-paid credit insurance and over ten times as much as term life insurance policies, and of course the cost of these alternative products are not staked against the borrowers home.

Over the last couple years, a huge amount of attention to the damage inflicted by single-premium credit insurance has forced most major lenders to phase out the sale of this product. The HUD-Treasury report recommended the prohibition of such policies on all mortgages, Fannie Mae and Freddie Mac announced that they would refuse to purchase loans with financed credit insurance, and state laws enacted in North Carolina, California, Georgia, and New York have effectively prohibited the policies on all mortgages. At the end of last year, the Federal Reserve recognized that single-premium credit insurance policies function as an additional fee in counting the premiums toward the HOEPA points and fees threshold.

While all of these steps represent a huge breakthrough, unscrupulous lenders and brokers are shifting over to debt cancellation and suspension agreements, which technically do not provide insurance and can avoid some of the regulations but essentially function the same way. Other lenders are setting up the same incentive systems to reward loan officers' sales of monthly-paid credit insurance policies. While monthly-paid policies are not as damaging as the single-premium policies, such incentives push loan officers to slip in the policies without the borrower's consent, and borrowers frequently encounter the bureaucratic runaround when they try to cancel the policies.

A couple moved into their house with a 30-year mortgage at 6.8%. After encountering some financial problems, they responded to a solicitation and took out a second mortgage. When their car broke down a year later, they went back to the same lender, who told them they could only take out additional equity by refinancing their first mortgage. They agreed and the new first mortgage included single-premium credit life and disability insurance policies that increased their loan amount by $4,699 and $3,211, respectively. While the credit insurance and fees together comprised over 18% of their new principal, the loan's 15.0% interest rate meant that policies would have cost them tens of thousands more over the life of the loan. They are now trapped in the excessive rate as a result of having all their equity stripped away, and the husband suffered a heart attack from the stress caused by the loan and the extra hours he is having to put in at work.

Balloon Payments

Mortgages with balloon payments are arranged so that after making a certain number of regular payments (often five or seven years worth, sometimes 15), the borrower must pay off the remaining loan balance in its entirety, in one "balloon payment." About ten percent of subprime loans have balloon payments.[49]

There are specific circumstances where balloon payments make sense for some borrowers in loans at 'A' rates, but for most borrowers in subprime loans they are extremely harmful. Balloon mortgages, especially when combined with high interest rates, make it more difficult for borrowers to build equity in their home. After paying for some number of years on the loan, with the bulk of the payments going, as they do in the early years of a loan, to the interest, homeowners with balloon mortgages are forced to refinance in order to make the balloon payment. They incur the additional costs of points and fees on a new loan, and they must start all over again paying mostly interest on a new loan, with another extended period, usually thirty years, until their home is paid for.

In addition, many borrowers are unaware that their loan has a balloon payment, that their monthly payments are essentially only paying interest and not reducing their principal, and that the balloon will ultimately force them to refinance.

A senior citizen who lives on his Social Security income was convinced to take out a $14,450 second mortgage by a mortgage broker to help pay for his daughter's education. The broker promised that the loan would be paid off after five years of monthly payments of $209 and that he'd get a 10% interest rate, but when he got to closing it listed 13% (the broker received a yield-spread premium of $8,500). He didn't want to sign, but the broker told him he could refinance to a lower rate after a year. After making all his payments, he was shocked to learn that he faced a balloon payment for $14,000. When he called the lender in a panic, the lender told him there was no cause to worry and that he could easily refinance with them.

[49] HUD-Treasury Report on Predatory Lending, p. 92..

Negative Amortization

In a negatively amortized loan, the borrower's payment does not cover all of the interest due, much less any principal. The result is that despite regularly making the required monthly payment, the borrower's loan balance increases every month and they lose, rather than build, equity. Many borrowers are not aware that they have a negative amortization loan and don't find out until they call the lender to inquire why their loan balance keeps going up. Predatory lenders use negative amortization to sell the borrower on the low payment, without making it clear that this payment will cause the principal to rise rather than fall.

A woman took out a 10-year home-equity loan for $45,377 at an interest rate of 12.7%. She had taken out the loan because she thought that the monthly payments of $671 were affordable, not realizing that those payments would not cover the interest generated, let alone pay down any of the principal. She has made all of her payments for over a year, but her loan balance continues to rise.

Loan Flipping

Flipping is a practice in which a lender, often through high-pressure or deceptive sales tactics, encourages repeated refinancing by existing customers and tacks on thousands of dollars in additional fees or other charges each time. Some lenders will intentionally start borrowers with a loan at a higher interest rate, so that the lender can then refinance the loan to a slightly lower rate and charge additional fees to the borrower. This kind of multiple refinancing is never beneficial to the borrower and results in the further loss of equity. Flipping can also take place when competing lenders refinance the same borrowers repeatedly, promising benefits each time which are not delivered or which are outweighed by the additional costs of the loan.

A woman had bought her house over thirty years ago for $20,000. Now seventy-two years old, she has been targeted for repeated refinancings. In a five-year period, her loan was flipped seven times, with high financed fees and high rates each time. After one lender flipped her a third time, she was foreclosed on and lost her house.

Property Flipping

Property flipping is an elaborate scam in which unsuspecting first-time homebuyers are sold houses in serious states of disrepair for prices far above what the houses are actually worth.

The typical "property flip" begins with an investor or real estate company purchasing a distressed property for as little as a couple of thousand dollars. After doing minimal cosmetic or even no work to the property, the owner finds a buyer, frequently targeting low-income, minority families. The buyers have no agent representation of their own and no real estate knowledge, putting them at the mercy of the seller/owner. The seller/owner abuses this position by lying about the condition of the house, promising to make visibly-needed repairs, setting the sales price at far above the property's actual value, and referring the buyer to a subprime lender or broker.

Many subprime lenders will only make a purchase loan if the loan is for 80% or less of the value of the property. In these instances, the property seller uses a number of schemes in order for it to appear that the buyer has the required down payment of 20% or more. The seller first sets the sales price far above what the property is actually worth, then the seller falsifies the buyer's deposit and will often create a second mortgage, which exists on paper only. The key to the scam is having a lender or broker that will utilize appraisers who will support the property's inflated sales price. In exchange for their participation, the lender or broker is compensated by the fees and additional charges on the loan, which are often excessive.

Buying one's first house is often a major milestone in life and an important step towards achieving economic self-sufficiency, but the swindlers involved in property flipping have made the experience one of the worst things to ever happen to their victims. While there are no hard numbers about how many families have been victimized by property flipping, the problem reached epidemic proportions in many cities before the authorities were even aware that a problem existed. And although the economic downturn has played a role, HUD's failure to implement adequate reforms has contributed to the highest ever delinquency rates on FHA loans.[50]

A man bought his home for $120,000, but immediately realized that promised repairs had never been completed. When he removed some floorboards in the kitchen that had been severely damaged by termites, he realized that the kitchen floor was being held up by carjacks. The house also had enormous electrical wiring problems, damaged back doors, and a number of other problems. When the contractor refused to do the work, the man began putting aside $1,000 a month to do the repairs on his own. He kept making the mortgage payments, but then lost his job and without any financial cushion because of the extra repair costs he fell behind and eventually lost his home to a sheriff's sale.

Aggressive and Deceptive Marketing – The Use of Live Checks in the Mail

Much of the competition between lenders in the subprime industry is not based on the rates or terms offered by the different lenders, but on which lender can reach and "hook" the borrower first. Predatory lenders employ a sophisticated combination of "high tech" and "high touch" methods, using of multiple lists and detailed research to identify particularly susceptible borrowers (minority, low-income, and elderly homeowner) and then mailing, phoning, and even visiting the potential borrowers in their homes to encourage them to take out a loan.

One of the methods used routinely and successfully by predatory lenders is the practice of sending "live checks" in the mail to target homeowners. The checks are usually for several thousand dollars, and the cashing or depositing of the check means the borrower is entering into a loan agreement with the lender. The appeal of the checks is that are a fast and easy way for a homeowner to obtain cash.

This initial loan is just an entry point into the financial life of the homeowner. The loan has an artificially high interest rate and monthly payment, in order for the predatory lender to be able to offer the homeowner an opportunity to refinance it, along with other debts, into another loan at a slightly

[50] "2nd Quarter Foreclosure Rates Highest in 30 Years", *Washington Post*, by Sandra Fleishman, September 14, 2002, p. H1.

lower rate. The predatory lender's ultimate goal is to get the homeowner to refinance their entire mortgage with them.

> *A man bought his house with a 6.9% fixed interest rate mortgage for around $67,000 and monthly payments of $447. He has a serious heart condition, and a lender began sending him live checks in the mail. The first one he cashed resulted in an unsecured loan at an extremely high interest rate for $2,500, which he used to pay off medical and other bills as working became more difficult. After he cashed another check or two, the lender began soliciting him to take out a second mortgage. He ended up receiving an open-end line of credit with an initial advance of $26,000 on a credit limit of $25,000, which "reduced" his interest rate to 23.9%. The monthly payments are $580 – significantly higher than the first mortgage, which has about two and a half times as large a balance. The loan also included an origination fee of $1,300 and a five-year prepayment penalty for nearly $2,500.*

RECOMMENDATIONS

For Legislators and Regulators

Congress should not preempt the ability of state legislatures and local officials to protect their constituents from predatory lending abuses. The measures enacted so far have not affected the prime market or restricted access to credit, while setting basic protections against some of the most common abuses that strip home equity, trap borrowers in excessive interest rates, and force families out of their homes.

Congress, state legislatures, and local officials should pass strong anti-predatory lending legislation that would protect consumers from abusive practices, which have been especially targeted at lower-income and minority communities. The legislation should follow the basic structure of S. 2438 – Senator Paul Sarbanes' bill in the 107th Congress[51] – in strengthening the protections provided in the federal Home Ownership Equity Protection Act (HOEPA), extending those protections to more borrowers in high-cost home loans, and establishing penalties for violating the law that are more in line with the damage caused to borrowers.

Federal banking regulators, in their evaluations of a bank's CRA performance, should give closer scrutiny to a bank's involvement in predatory lending. Regulators should consider not just the number of loans the bank originates to low-and moderate-income borrowers, but also the quality of those loans. In addition, banks that make high-cost loans directly or through their subsidiaries or purchase high-cost loans with predatory terms should be penalized under CRA for those activities, not rewarded.

Congress should increase the funding level for HUD's Housing Counseling Program well beyond the $20 million provided in FY 2002; it should be funded at least to the $40 million dollar level included in the Senate Appropriations Committee bill this year to increase the availability or housing counseling for potential predatory lending victims. To come closer to meeting the demand for such services, the annual funding level should be increased in future years to $100 million. Fannie Mae, Freddie Mac, mortgage lenders, and state and local governments should mandate and expand funding for programs that provide basic information about lending and enable people to protect themselves from predatory practices. The most effective tool for helping minority and lower-income families to become successful homeowners is high quality loan counseling and home buyer education by community based entities.

Federal and State regulators should increase their scrutiny of predatory lending practices, including examining the interest rates and other costs of loans as well as their distribution. Federal and state authorities should devote the necessary resources to investigating and prosecuting lending abuses.

The federal banking regulators must not worsen the problematic impact of credit scoring by penalizing lenders for making 'A' loans to any borrower with a credit score below 660. Unfortunately, the regulators are proposing higher capital requirements for lenders making such loans under a July 12 Federal Register notice regarding data collection on subprime loans made or

[51] Rep. John LaFalce introduced nearly identical legislation, HR 1051, in the 107th Congress.

purchased by banks and thrifts. Such a step could arbitrarily and unfairly exclude millions of consumers from the low rates and fees provided in the prime market, significantly raising the cost of homeownership for those families. In the final rule, the regulators also should follow the industry practice of classifying loans as subprime or not based on the rates and fees, not on the borrower's characteristics, and make public the data on subprime loan volume engaged in by banks and thrifts.

The Federal Reserve must follow through on collecting information on high-cost mortgages under HMDA, which is scheduled to begin in 2004. This will provide regulators, elected officials, and the public with the clearest picture to date on the concentration of high-cost mortgages in various communities and population groups.

For Lenders

All lenders that engage in subprime lending should pledge adherence to a meaningful "Code of Conduct" that includes: fair pricing; limits on financed fees and interest rates to those consistent with the actual credit risk represented by the borrower; avoidance of abusive and equity stripping loan terms and conditions, such as balloon payments, prepayment penalties, and single premium credit insurance; full and understandable disclosures of loan costs, terms, and conditions; a loan review system that rejects fraudulent or discriminatory loans; making no loans which clearly exceed a borrower's ability to repay; and not refinancing loans where there is no net benefit to the borrower. These lenders should review their loan portfolios and compensate borrowers whose loans clearly violate this code.

Lenders should quit sending in their high-priced lobbyists to try and stave off anti-predatory lending legislation. Prime lenders should especially be supportive of providing borrowers with protections on high-cost home loans, since they have a direct interest in discouraging unscrupulous lenders and brokers from refinancing borrowers out of prime loans into mortgages with much higher costs.

Lenders that offer prime as well as subprime products should establish uniform pricing and underwriting guidelines for all of their lending subsidiaries and for all of the communities in which they do business, so that consumers in lower-income and minority communities do not receive worse terms because of where they live or the color of their skin. All 'A' lenders should increase their outreach and loan volume in underserved communities for their prime loan products.

Lenders should fund nonprofit housing counseling agencies to work with low and moderate income borrowers in the subprime market. Consumers need correct information to make informed loan decisions in the complex and often misleading subprime market transactions. Housing counselors are able to review income, credit, debts, and loan products to help the borrower find the best loan product for their needs and avoid predatory loan terms. Housing counseling agencies that provide one-on-one and classroom counseling have been found to reduce ninety-day delinquency rates by 34 percent and 26 percent, respectively.[52]

[52] "Prepurchase Homeownership Counseling: A Little Knowledge is a Good Thing," by Abdighani Hirad and Peter Zorn, in *Low-Income Homeownership: Examining the Unexamined Goal,* ed. Nicolas Retsinas and Eric Belsky, 2002, p. 147.

For Consumers

<u>To Protect Yourself From Predatory Lenders</u>

Before you begin loan shopping, visit your local non-profit housing counseling center to set up an appointment with a counselor to evaluate your financial situation and to discuss your loan needs. ACORN Housing Corporation, a HUD-certified housing counseling agency, has offices in 29 cities, which are listed at www.acornhousing.org. You can also call HUD toll-free at 1-800-569-4287 for a list of the certified counseling agencies nearest you.

You can and should also talk with a housing counselor to evaluate the loan offers you are receiving if you are already in the middle of the loan process. Many of the borrowers who receive high cost loans could have qualified for a lower cost loan from a bank.

Ignore high-pressure solicitations, including home visit offers. Before you sign anything, take the time to have an expert – such as a housing counselor or lawyer – look over any purchase agreement, loan offer from a lender or broker, or any other documents.

Don't agree to or sign anything that doesn't seem right, even if the seller or lender tells you that "it's the only way to get the loan through" or "that's the way it's done." Look over everything you sign to make sure all your information is correct, including your income, debts, and credit. Do not sign blank loan documents or documents with blank spaces "to be filled out later."

Before closing your loan, get a copy of your loan papers with the final loan terms and conditions so you have enough time to examine them. If anything is dramatically different at closing, don't sign it.

Don't accept a lender's statement that you have bad credit without reviewing your credit report yourself for mistakes and inaccuracies and having an independent person evaluate your credit report.

Make sure you are comparing apples to apples. Know exactly what debts will and will not be paid and if your new payment will include taxes and insurance. You should also understand if the payment being quoted is sufficient to pay off the loan or only goes toward the interest.

Be wary of any lender or broker who encourages you to refinance your first mortgage if that's not what you are looking to do or if they encourage you to add more and more of your other debts into the loan.

Think twice about borrowing more than the value of your house. Some lenders may make loans for more than your house is worth, up to a 125% loan to value. Owing more than your house is worth can prevent you from selling your house or refinancing to a better rate in the future.

Beware of loan terms and conditions that may mean higher costs for you:

- High points and fees: Bank loans usually cost 1-3% of the loan amount for points and fees to the lender. If you are being charged more, find out why. Then shop around.
- Single premium credit insurance or debt cancellation agreements: This kind of insurance is very expensive compared to other insurance policies, and paying it up front requires you to pay interest on it as well. Beware.
- Prepayment Penalty: Many subprime loans include prepayment penalties, which require you to pay thousands of dollars extra if you sell the house or refinance your loan within the first several years of the loan. Make sure you know if the loan you are being offered has a prepayment penalty, how long it is in effect, and how much it will cost. If there is a chance that you will refinance or sell your home during that time, you need a loan without a prepayment penalty.
- Balloon Payments: Balloon mortgages have the payments structured so that after making all your monthly payments for several years, you still have to make one big "balloon payment" that is almost as much as your original loan amount.
- Adjustable Rates: Beware of low "teaser" introductory rates on adjustable mortgages because many of these adjustable rate loans only adjust one way – up. If your loan has a fixed initial rate, make sure you know when and by how much the interest rate will increase and what your new monthly payments will be. Find out the highest rate your can go to and what the monthly payments would be at that rate. Don't count on a promise that the lender will refinance the loan before your payments increase.
- Mandatory Arbitration: Some predatory lenders include mandatory arbitration clauses in their home loans. Signing these can mean giving up your right to sue in court if the lender does something that is illegal.

Be Careful with Debt Consolidation Loans. If you are thinking of a debt consolidation loan, be aware that although it may lower your monthly payments in the short term, you may end up paying more in total over time. Also, there is an important difference between most of your bills – such as for credit cards – and mortgage debt. When you consolidate other bills with your mortgage, you increase the risk of losing your home if you can't make the payment.

Watch Out for Property Flipping Scams When Buying a Home. A property flipper buys a house cheap and then sells it to an unsuspecting homebuyer for a price that far exceeds its real value. Too often, the buyer finds out after closing that the home needs major repairs they can't afford and they lose the house in foreclosure.

- Have an independent home inspector make sure the house is in good condition. This should be in addition to the appraisal that the bank orders. While an appraisal estimates the value of your home, a good home inspection will identify needed repairs. Do your own homework to find a good inspector – an inspector recommended by the seller may not be working in your interest.

- Make sure you have your own Realtor or real estate agent who is working for you. Never deal directly with a seller or a seller's agent unless you have extensive real estate experience. Having your own Realtor will not cost you anything more because they are paid out of the sales price of the house.

- If the seller agreed to make repairs to the home, conduct a final walk-through to make sure the repairs have been completed before the loan closing.

Look Out for Home Improvement Scams. Some home improvement contractors work together with lenders and brokers to take advantage of homeowners who need to make repairs on their homes. They get the homeowner to take out a high-interest, high-fee loan to pay for the work, and then the lender pays the contractor directly. Too often, the work is not done properly or even at all.

- Get several bids from different home improvement contractors. Don't get talked into borrowing more money than you need.

- Check with the state Attorney General's office to see if they have received any complaints about the contractor.

- Don't let a contractor refer you to a specific lender to pay for the work. Shop around with different lenders in order to make sure that you are getting the best possible loan.

- Make sure any check written for home improvements is not written directly to the contractor. It should be in your name only or written to both you and the contractor, and you should not sign over the money until you are satisfied with the work they have completed.

If you feel that you have been discriminated against or are a victim of predatory lending call ACORN at 1-877-692-0233 or e-mail us at acorndcadmin@acorn.org to become part of our campaign against predatory lending.

METHODOLOGY

This report analyzes data released by the Federal Financial Institutions Examination Council (FFIEC) about the lending activity of more than 7,600 institutions covered by the Home Mortgage Disclosure Act (HMDA). HMDA requires depository institutions with more than $32 million in assets as well as mortgage companies which make substantial numbers of home loans to report data annually to one of the member agencies of the FFIEC--the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation, the National Credit Union Administration, the Office of the Comptroller of the Currency, and the Office of Thrift Supervision--and to the Department of Housing and Urban Development (HUD). The reporting includes the number and type of loans correlated by the race, gender, income, and census tract of the applicants, and the disposition of those applications, in each Metropolitan Statistical Area (MSA) where loans are originated.

HMDA data does not distinguish between prime and subprime loans. In order to analyze the subprime market, we used the list of subprime lenders developed by HUD, and considered loans made by lenders on that list as subprime loans. HUD also maintains a list of manufactured housing lenders, and we considered loans made by these lenders as manufactured housing loans. Loans made by lenders that were not on either list were considered as prime loans. HMDA data does distinguish between government insured and conventional loans. We considered only conventional home purchase and conventional refinance loans in this report.

We are grateful for the work of Randall M. Scheessele with the U.S. Department of Housing and Urban Development whose research was used to measure the growth of subprime lending.

The report examines figures for the nation as a whole, as well as for sixty-seven individual metropolitan areas: Little Rock, AR; Pine Bluff, AR; Phoenix-Mesa, AZ; Tucson, AZ; Fresno, CA; Los Angeles-Long Beach, CA; Oakland, CA; Orange County, CA; Riverside-San Bernardino, CA; Sacramento, CA; San Diego, CA; San Francisco, CA; San Jose; CA; Stockton-Lodi, CA; Denver, CO; Bridgeport, CT; Hartford, CT, New Haven, CT; Stamford-Norwalk, CT; Waterbury, CT; Wilmington, DE; Washington, DC; Ft. Lauderdale, FL; Jacksonville, FL; Miami, FL; Orlando, FL; Tampa-St. Petersburg, FL: Atlanta, GA; Chicago, IL; Ft. Wayne, IN: Gary, IN; Indianapolis, IN; Baton Rouge, LA; Houma, LA; Lake Charles, LA; New Orleans, LA; Boston, MA; Brockton, MA; Springfield, MA; Baltimore, MD; Detroit, MI; Minneapolis-St. Paul, MN; Kansas City, MO; St. Louis, MO; Bergen-Passaic, NJ; Jersey City, NJ; Newark, NJ; Albuquerque, NM; Las Cruces, NM; New York City, NY; Nassau-Suffolk, NY; Cincinnati, OH; Cleveland, OH; Columbus, OH; Toledo, OH; Portland, OR; Philadelphia, PA; Pittsburgh, PA; Providence, RI; Sioux Falls, SD; Memphis, TN; Dallas, TX; Fort Worth-Arlington, TX; Houston, TX; San Antonio, TX; Seattle, WA; and Milwaukee, WI.

In making lists of those metropolitan areas with the most and least concentrated lending, and with regard to other similar characteristics, we have excluded those metropolitan areas which had fewer than 50 loans originated to the group in question.