

Consumers Union

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A home is more than a place for a family to live. It is a way for that family to build assets. In fact, for most families, a home is their most important asset. Over time, the value of the home can rise and the equity increases. This accumulation of wealth in a home builds family stability and opens new opportunities.

The accumulated value, or equity, can be passed onto future generations, or taken out in the form of a loan. The equity can be used to pay for an education or a business startup, and the home itself can serve a family for generations.

Homeownership also benefits communities and the state. Property taxes pay for schools and for the operation of local government. More importantly, families that own homes have a stake in the success of communities—and a stable group of homeowners assures stability in neighborhoods.

That is why predatory home lending is such a threat to Texas. Predatory lenders target vulnerable borrowers and sell them high cost loans under unfair conditions that can lead to foreclosure. Not all higher interest loans are predatory. But a high cost loan combined with other practices can be predatory. Predatory loan practices include:

- Interest rates that have little relation to the credit worthiness of the borrower
- Excessive fees that must be paid for a loan, or are rolled into the amount borrowed
- Little consideration of the ability of the borrower to repay
- Loans made on the basis of the equity in the home, instead of on the borrower's income



- Single-premium credit insurance that is rolled into the loan
- Prepayment penalties designed to lock borrowers into abusive loans
- Failing to move qualified borrowers to a lower-priced “prime” loan
- Home improvement scams where lenders pay (and borrowers must repay) despite low-quality or unfinished work

Lenders that make credit available to people with blemished or no credit histories are called “subprime” lenders. These loans are made at far higher rates than standard loans. Predatory loans are generally a subset of subprime loans; they are made at high subprime rates, but also include one or more of the characteristics described above.

An analysis of Home Mortgage Disclosure Act (HMDA) data from 1998 shows that in major Texas cities, African-American neighborhoods appear to be targeted by subprime lenders for home refinance loans, indicating the possibility that these communities are being victimized by predatory lenders.

In low-income Black neighborhoods in Dallas, eight out of the 10 top lenders were subprime lenders. For the same incomes in white Dallas areas, only two out of 10 were subprime. In Houston, six out of 10 were subprime in Black neighborhoods, with only one out of 10 in white neighborhoods. This pattern holds true in all major Texas cities. Regardless of income, 27 percent of

Predatory Lending

In some neighborhoods in Texas, subprime lenders make most of the existing home secured refinance loans. These loans cost more and can result in default or loss of equity.

Black borrowers statewide refinance their home through a subprime lender, compared to 15.3 percent of Hispanic borrowers, and only 6.3 percent of white borrowers.

It is difficult to imagine, when income is controlled, that there could be such dramatic differences between borrowing patterns—that minority borrowers would simply end up borrowing from high cost subprime lenders. Instead, these patterns indicate the possibility that these communities may be targeted by predatory lenders.

Texas sought to address abusive home equity lending and enacted prohibitions against many of the practices that have plagued borrowers in other states. However, loans with excessive interest rates have no special borrower protections in Texas law.

Recommendations

- Expand predatory lending protections to all home-secured loans;
- Limit costs of loans;
- Prohibit unfair loan terms and practices;
- Assure that all Texas borrowers get the lowest cost loan for which they qualify.

In Short

Predatory loans are made without consideration of the borrower's ability to repay. Instead, lenders base the loan on the amount of equity available in the home and offer terms that borrowers cannot hope to meet. Prepayment penalties lock borrowers into bad loans, and people who can't keep up face foreclosure.