Predatory Lending Fuels Rise in Foreclosures
by Joe Lamport
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A crush of foreclosures in Queens, Brooklyn and the Bronx is raising alarms and leading many to call on city and state authorities to do more to go after the unscrupulous people at mortgage brokerage firms, at banks and on Wall Street who, they say, are fueling the problem.

“We’ve been predicting this for years,” said Oda Friedheim, an attorney at the Legal Aid Society in Queens. “Many lenders have developed really abusive loan practices that target communities of color and any vulnerable people.”

Through March, more than 1,200 foreclosures had been filed this year in Queens on one- to four-family properties, a 57 percent increase over the same period last year. About 3,600 were filed in all of 2006 in the borough, according to the www.nedap.org Neighborhood Economic Development Advocacy Project. In Brooklyn, over 1,100 foreclosures had been filed from January to March compared to about 3,300 for all of last year.

Foreclosures have been increasing for the last several years. The city will likely see more than 10,000 foreclosures this year – almost twice what it saw as recently as 2004.

The surge in foreclosures is at least partly linked to predatory lending practices of brokers and lending institutions. For years, housing advocates in Queens particularly have been calling for tougher action against unscrupulous brokers who convince homeowners and first-time homebuyers to take loans on bad terms. When the borrowers can’t pay the loans, the lender can take the property. As a result, foreclosures lead to the loss of housing for senior citizens and other low-income people, pull wealth out of neighborhoods and rob the city of property tax revenue, at least temporarily.

The problem is nationwide. As many as 2.2 million Americans will face the loss of their homes over the next several years because they will not be able to repay the loans they have taken, according to a report by the Center for Responsible Lending.

Sup-Prime Lending

The problems leading up to the rash of foreclosures are complicated, but subprime loans are at the root of the increase.

Subprime lending has been a critical part of the nation’s housing boom for over a decade, allowing a lot of people who would otherwise not be able to buy a home to do so. The loans charge higher rates of interest and, in their worst forms – referred to as predatory lending – the loans are foisted upon people in deceitful ways, have exorbitant hidden fees and apply significant penalties if the borrower tries to get out of them later. The rate of subprime lending in New York City has more than tripled since 2002, according to the Furman Center for Real Estate.

The rates of subprime lending here are higher than the national averages. About 23 percent of home purchase loans are subprime, up from just 6.5 percent in 2002. Nationally, the proportion of home purchase loans that are subprime is 17 percent.

Friedheim sees the city’s numbers as ominous. “The subprime market is going bust and so we will see more foreclosures,” she said.

There are two types of cases where someone gets a subprime loan. In the first of the two scenarios, a person who already owns a home wants to refinance the mortgage in order to, say, make significant repairs to the home. In the second scenario, someone is trying to buy a first home. Eager to achieve such a milestone, the buyer neglects to study carefully the conditions of the loan being offered.

Unscrupulous mortgage brokers and the lending industry prey on both groups of people.

Kevin Squires, a loan officer at a Queens mortgage company, said the first scenario is common as homeowners are bombarded daily with offers to refinance their homes. The advertisements blare across virtually every medium: A man walking along a city street recently was wearing a bright orange street that declared in large letters, “We buy homes: 856-541-9000.” Late night ads promise “no fees, no hidden costs.”

The brokers are particularly interested in those who already own the home, Squires said. “If you have someone who owes $150,000 but their house is worth $450,000, then they have $300,000 equity in their home,” Squires explained. “The only way they can pull that out is by doing a refinance.” But if the borrower’s credit is not up to par, he or she must go to a mortgage broker and get a non-conventional loan. If the borrower cannot meet the terms of that loan, he or she could lose their home.

But homeowners and first-time homebuyers with good credit are becoming victims of predatory lending as well, said Cathy Mickens of Neighborhood Housing Services in Jamaica, Queens.

“It has spread throughout the community,” Mickens said, affecting middle-income and high-income people as well as those with lower incomes. Some people who could have gone to a conventional lender and qualified for a standard mortgage will instead go to a predatory lender who promises to provide the loan quickly and with no documents required. Often, Mickens said, the result is “a disaster.”

Who Is to Blame?

While some have suggested that borrowers are at fault because of their zeal to own a home or get quick money, unscrupulous mortgage brokers, lending institutions and Wall Street investors, motivated by greed and racism, are the driving force.

Brokers and banks have often “intentionally disregarded the facts of the income of the borrower,” Friedheim said. “Even when they see the income and it’s totally predictable that the person cannot afford it, they’ll give the loan anyway.”

Brokers are motivated to foist these loans on borrowers because the brokers get commissions and face no financial losses if the borrower defaults and a foreclosure is initiated.

Once the unscrupulous brokers find a willing homeowner, they effectively prevent the person from comparison shopping: They provide a home appraiser and attorney who help convince the homeowner or homebuyer to sign the loan.

“Eighty to 85 percent of [the subprime mortgage brokers working in low-income communities] operate unethically,” Squires said. “I don’t have anything concrete to prove that figure, but of all the loans I have seen, most people who end up going to these brokers become victims of predatory lending.”

A chain of incentives in the lending industry drives predatory lending. Unscrupulous mortgage brokers chase homeowners and first-time homebuyers because banks will pay the brokers commissions. The banks, in turn, are motivated by the profits they can make by packaging the loans and selling them to Wall Street investors. The investors, of course, are interested in the rates of return on these investments.

“One concern we’ve had is that the market incentives actually favor predatory lending,” said Mary Moore of the Center for Responsible Lending, a nonprofit, non-partisan organization based in Durham, North Carolina, that studies lending issues. “There are a lot of strong reasons from a business perspective to do it.”

On the other hand, Moore said, “brokers have no obligation to give their borrowers the best deal. They get paid whether the loan gets foreclosed or not.”

The Lending Gap

Predatory lending is an acute problem in the city's poorer neighborhoods. On the surface, that seems understandable: Subprime loans are meant for risky borrowers who must pay higher interest rates because they are, well, risky. But one study by the Center for Responsible Lending showed that African American and Latino borrowers who would qualify for loans from prime lending institutions are steered toward the subprime market.

Over half of African Americans who get a mortgage get subprime loans, the study showed. For Latinos, the rate was 42 percent. But for whites it was just 19 percent.

"We think there's discrimination going on," Moore said. "It's well known that often brokers steer African Americans and Latinos to subprime loans even when they qualify for other loans."

Data on subprime lending in the city from the Furman Institute showed the concentration of these types of loans in the city's poorer neighborhoods. Brownsville and Jamaica, both largely African-American communities, were the highest ranking community districts for subprime lending. In both, roughly 52 percent of home purchase loans involved subprime loans. The top 15 districts include overwhelmingly African American and Latino communities in the city, including Highbridge in the Bronx and Bedford-Stuyvesant in Brooklyn.

"It's reverse redlining," Friedheim said, referring to lending practices where banks refuse to loan money to people living in certain neighborhoods – neighborhoods where African Americans and Latinos live. "These neighborhoods don't have banking services and predatory lenders target them."

What can be done?

The City Council's committees on Consumer Affairs and Civil Rights will hold a joint meeting on predatory lending in the hearing room of 250 Broadway on April 30 at 10 a.m.

Advocates are urging elected officials to address the problem aggressively.

For starters, they want the city to expand the mayor's 2005 initiative providing assistance to people purchasing or refinancing a home. The mayor's "Preserve Assets and Community Equity" program has involved raising public awareness about predatory lending in the hardest hit communities and has included providing counseling to homeowners and community groups on the problem, referring victims to attorneys and helping homeowners find financial help.

Advocates said the city should also increase funding to legal service providers to deal with the problem. Advocates, including those at the organization I work for, want elected official to establish a right to counsel for low-income seniors who face foreclosure actions and housing court cases. They also are urging lawmakers to strengthen laws restricting high-cost loans.

"You need multiple strategies to deal with this problem," Friedheim said. "The federal government and regulatory agencies have to develop tighter rules. There have to be strong legislative efforts to make sure lenders are accountable when they give an unaffordable loan."

In 2003, the New York State Legislature passed an anti-predatory lending law. But it only applies to loans up to $300,000. Advocates say that, in light of increases in housing costs, the law should be amended to cover larger loans.

State legislators are currently considering a law on lending for home improvements. Among other things, it would prohibit mortgage brokers from also acting as home improvement contractors. But the bill has been introduced in the Assembly annually since 2003, and the Senate has yet to consider it formally.

Mandated to do so or not, banks should apply good loan-making rules, said Moore of the Center for Responsible Lending. The center applauded an announcement that Freddie Mac, the federally chartered mortgage finance company, would no longer buy subprime loans with terms and conditions that often lead to foreclosures.

"Something serious has got to happen," Mickens said. "The neighborhoods are at risk now and it's just going to tear the whole community apart."

Joe Lamport is the assistant director of the City-Wide Task Force on Housing Court, a coalition of community housing organizations.