What is Predatory Lending?

Predatory lending occurs when a mortgage loan with unwarranted high interest rates and fees is set up to primarily benefit the lender or broker. The loan is not made in the best interest of the borrower, often locks the borrower into unfair loan terms and tends to cause severe financial hardship or default.

To determine if a loan is predatory in nature, ask yourself these questions:

- Does your past credit history justify the high rate and fees charged?
- Is the loan being made on the basis of your ability to repay the loan and not solely on the value of the property?
- Have the loan's terms been fairly represented and explained to you?
- Does the type of loan and the loan services provided meet your needs and interests?

If you answered "NO" to any of these questions, there is a possibility the loan is predatory in nature. For consumers to avoid falling prey to these abusive practices, they must be smart and informed shoppers.

Know the Terms

Mortgage Lender: A bank, savings institution, or mortgage company that offers home loans.

Mortgage Broker: An individual or firm that matches borrowers to lenders and loan programs for a fee. Anyone who acts as a go-between and gets a fee or other compensation.

Annual Percentage Rate (APR): Cost of the credit, which includes the interest and all other finance charges. If APR is more than .75 to 1 percentage point higher than the interest rate you were quoted, there are significant fees being added to the loan.

Points: Fees paid to the lender to obtain the loan. One point is equal to 1% of the loan amount. Points should be paid at the time of the loan. If your lender insists on prepayment of these fees, find a new lender or broker.

Prepayment Penalty: Fees required to be paid by you if the loan is paid off early. Try to avoid any prepayment penalty that lasts more than 3 years or is for more than 1-2% of the loan amount. Certain high rate/high cost loans may not have prepayment penalties under state and federal laws.

Balloon Payment: Large payment due at the end of a loan. This happens when a borrower has a low monthly payment covering only interest and a small portion of the principal, leaving almost the whole loan amount due in one payment at the end.

Yield Spread Premium: Payment to the broker for selling a higher interest rate loan than would otherwise be charged for that borrower. It must be disclosed to the borrower at the time of the loan and is generally acceptable if there are no other broker fees and this is how the broker is getting paid for his or her services.

Appraisal: A determination of the value of a home by a third party who is hired by the lender to assure the home has enough value to pay off the loan should the borrower default. Beware of inflated appraisals, particularly when a second appraisal has to be conducted because the first one was too low to justify the loan.

Loan Origination Fees: Fees paid to the lender or broker for handling the paperwork in arranging the loan. These are prepaid finance charges paid at the loan closing and are included in your APR calculation. Like "points," if you are asked to pay the fees before the closing, find a new lender or broker.

Don't Become a Victim:

A Guide to Predatory Lending

Ohio Department of Commerce
Division of Financial Institutions

Office of Consumer Affairs
Helping Ohioans Borrow Smart

BORROW SMART

Bob Taft
Governor

Gary Suhadolnik
Director

Tips to Avoid Predatory Lending

- Only deal with licensed mortgage lenders and brokers or those operating under and subject to federal and state regulations. To determine if your broker or lender is licensed by the State of Ohio, contact the Division of Financial Institutions at 614.728.8400 or www.com.state.oh.us/dfi.
- Read and get copies of everything you sign in connection with your mortgage.
- Beware of "Bait & Switch" tactics where the lender or broker makes an offer with one set of terms and then pressures you to sign a loan with more expensive rates and hidden costs.
- Make sure your monthly payments are affordable, and that you are NOT comparing apples to oranges when looking at the old vs. the new payment. Be sure that if the escrow of taxes and insurance is part of your old payment, it is included in your new payment when comparing price savings.
- Make sure the rate and terms quoted by your lender and/or broker are given to you in writing and do not significantly vary from those presented at closing.
- Do NOT shop based solely on lower monthly payments. Payments may be lower if the loan has a balloon payment or a variable rate. Unless you expect falling mortgage rates, a higher income or a better credit rating in the future, these loans eventually cost you more.
- Do NOT sign blank forms. Forms should be completely filled out with no blank boxes or spaces.
- Beware of door-to-door home improvement offers where the contractor offers to find you the necessary financing to make the improvements.
- Never falsely state or allow others to falsely state your income. You won't have your dream home very long if you can't afford to make the payments.
- Do not fall for scams from out-of-state businesses claiming to arrange mortgage loans for an advance fee or with the advance purchase of special loan insurance. Sending them a money order to a post office box or mail drop will likely be the last time you see your money.

Call the Office of Consumer Affairs Consumer Lending Toll Free Hotline

1-866-278-0003

or write to us at

Division of Financial Institutions
Office of Consumer Affairs
77 South High Street, 21st Floor
Columbus, Ohio 43215-6120
www.com.state.oh.us

- Remain current on your present mortgage obligations until closing and disbursement of new loan proceeds. If you are paying other debts off as part of the loan, remain current on them as well. Falling behind on your current debt while waiting to get your new loan will hurt you in the long run.
- Borrow only what you need and can afford to pay back. If you need $5,000 to pay for a home improvement, there is usually little sense refinancing your existing mortgage and paying $6,000 in closing fees to arrange the loan.
- Understand that if you consolidate your credit card debt and other consumer debt into your mortgage or home equity line of credit to have one lower overall monthly payment, nonpayment of the loan could cause you to lose your home. Also, any monthly savings will disappear if you accumulate credit card debt again.
- Know your credit rating and qualify for the loan you deserve. There is no reason to pay high rates and fees if you can qualify for better terms.
- If a deal seems to be too good to be true, it probably is!