

Office of the Attorney General Civil Rights Division

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Don't Be A Victim Of Predatory Lending*

Predatory lending refers to the practice of causing people to take out bad mortgage loans. These loans strip the equity from a house and often put the homeowner in foreclosure. The loans are bad because they contain high charges, unnecessary insurances or other products, or burdensome terms. Women, senior citizens and other minorities and persons with low to moderate incomes are more likely to be victims of predatory lending.

Predatory lenders use high pressure and deceptive sales tactics to lure people into their web. They may send a home improvement contractor to your house to convince you to make some repairs. When the job is finished, you wind up with a new or second mortgage containing charges or terms you cannot afford to meet **and** shoddy repair work. They may send a flyer or check in the mail stating that you have been specially selected to participate in a program designed to reduce your debt or save you money on your mortgage at no additional cost to you. If you have credit problems or think you may not qualify for a traditional bank loan because of age, income or other problems, they tell you not to worry because they can still get you a low-cost loan. These are all promises designed to trick you into getting a bad, predatory loan. If it sounds too good to be true, it probably is too good to be true and you need to walk away and contact a reputable lender, financial consultant and/or attorney for advice.

* The following information is not intended to provide you with a complete analysis of predatory lending practices and/or remedies. Each loan must be examined on a case-by-case basis to determine if predatory lending has, in fact, occurred. If you feel that you have been a victim of predatory lending, please contact an attorney.

Know The Terms Of Your Contract

Listed below are a few terms that are often used in the lending industry. Recognizing them is your initial step to understanding a loan contract and making an informed borrowing decision. Before you sign any loan document, be sure to review the following terms in the contract:

- **Know the Annual Percentage Rate (APR)** - This is the cost of your credit as a yearly rate. When shopping for a loan, compare the APR offered by various lenders. You also need to understand what is included in the APR. Certain costs and fees may not be included in this calculation, yet they may significantly affect your loan. Also, beware of any increase in the APR that you were initially quoted and what you end up with.
- **Know the Finance Charge** - The finance charge is the dollar amount the credit will cost you. It is based on the APR, the amount borrowed and the length of the loan. Beware of inflated fees!
- **Know the Amount Financed** - This is the dollar amount of the credit that is provided to you by your lenders.
- **Know if You are Paying “Points”** – “Points” are fees you pay to a lender to obtain a real estate secured loan. These prepaid finance charges are *not* refundable. Traditional lenders charge points, but they are usually in exchange for a lower interest rate or some other benefit for the consumer. In a predatory loan, the consumer usually receives little or no benefit from the points.

Predatory Lending Checklist

BEWARE OF:

- **High Interest Rates** - The interest rate will vary depending on a variety of market factors, but generally, interest rates over 9% have been considered high since the mid-90s. If you have credit problems, you may have to pay a higher interest rate. However, you still need to shop around for the best rate. There are more options today for people with credit problems than there have been in the past. Also, some credit problems may be explained sufficiently to enable you to qualify for a better rate. You need to know what your credit rating is and shop around.
- **High up-front fees** - Many predatory lenders tell you there will not be any up front or out of pocket fees. This is not true. They charge very high up front fees, but are rolling them into the loan. People tend to overlook or minimize their effect since they do not have to pay them prior to closing. This is a mistake. These fees are inflated, often unnecessary duplicates, and strip the equity from your home.

- **Pre-payment penalties** - These are fees charged for repaying the loan earlier than stated in the mortgage documents. These sometimes amount to thousands of dollars, so you should give special attention to pre-payment penalty terms.
- **Loans for more than the value of your house** - The lender often inflates the value of your home so you can get a larger loan. If you do not know how much your house is really worth in the market, have it appraised yourself by a reputable appraiser. If anyone is willing to lend you more than the house is worth, you know it is a bad deal.
- **Repeated refinancing or “Flipping”** - A loan is flipped when it is refinanced within a short period of time for a higher amount. Flipping is very dangerous because it rapidly eats up the equity in your home. With each flip or refinancing, you pay more costs and fees and generally receive little, if any, benefits.
- **Home Improvement Scams** - Some predatory lenders use local home improvement contractors to solicit business for them.
- **Balloon payments** - In this kind of loan, the initial loan payments are almost entirely applied to the interest on the loan. You pay the balance of the principal, often up to 85% of the original loan amount, at the end of your loan period. Consumers are often unaware of the large balloon payment. Even if they are aware of it, the predatory lender may have told them not to worry about it because they can refinance when the balloon becomes due. This sets you up for “flipping” later.
- **Required credit insurance** - Credit life insurance and credit disability insurance are not required to get your loan. This may increase the total cost of your loan.
- **Penalties for Late Payments** - Be aware of what the penalties are for late payments. Predatory loans may contain severe penalties for late payments such as escalating daily interest rates.
- **Mandatory arbitration clauses (giving up your right to sue in court)** - It is never a good idea to give up your legal rights in court. An arbitrator does not have to give reasons for their decisions or follow the law.
- **Negative Amortization** - This involves a system of repayment of a loan in which the loan does not amortize over the term. Instead, the amount of the monthly payment is insufficient to pay off accrued interest and the principal balance therefore increases each month. At the end of the loan term, the borrower owes more than the amount originally borrowed. A balloon payment at the end of the loan is often a feature of negative amortization.
- **Open End Mortgages** - Although the loans are called “open end” loans, in fact they are not. Instead of creating a line of credit from which the borrower may withdraw cash when needed, the lender advances the full amount of the loan to the borrower at the outset. The loans are non-amortizing, meaning that the payments are interest only so that no credit will be replenished. Because the payments are applied only to interest, the balance is never reduced.

- **“Bait and Switch” Tactics** - Where a lender initially offers one set of terms, but then pressures the borrower into signing a contract with more expensive terms and hidden fees.
- **Debt Consolidation Loans** - These loans trade unsecured debt- such as credit cards or medical bills - into debt that is secured with your house. This has been a very popular lure for predatory lenders in recent years. People are told they can write off mortgage interest but cannot write off interest from credit cards under current tax laws. While this may be true depending on your tax status, it is a very risky move and should not be done lightly. It is risky because if you default on the mortgage, you can lose your home. If you default on your credit card bill, you may be sued, but you will not lose your homestead in Florida for credit card bills.

Predatory Lending Guidelines

Prior to signing a mortgage contract or refinancing your home, go over the following guidelines to assist you in making an educated decision:

Manage your money and credit. Evaluate your income and expenses and borrow within your budget. Don't overstate earnings or give false information to qualify for a loan. Don't become house poor. Remember there are more costs associated with buying a house than mortgage costs. A person's credit is his or her own responsibility. Pull your credit report before you shop. Since terms of a loan are heavily dependant on it, the credit report is critical in helping consumers understand and carefully navigate the home-financing process.

Look around for the best loan. Visit several creditable lenders. Compare interest rates, fees and points, and go over all the terms and conditions of the loan. Talk with family, friends and neighbors about where they obtained their mortgages and their experiences. The differences may surprise you and could help you save a fortune!

Review the whole mortgage contract carefully. Don't wait until you get to the closing table to see the final papers. Early requests for the “attorney package” should greatly avoid a pressured situation. This is an easy fix for that common problem. Make sure you fully understand all the terms and responsibilities of the contract before signing.

Question the terms and conditions of the loan! Review the contract to make sure that the terms and conditions you have talked about are clearly written in the loan documents.

Consult with a trusted financial advisor or attorney before signing a loan document. Do not sign a blank form or one with facts that are incorrect (particularly the cost of the home, your employment information and income information). Remember, do not allow yourself to be forced to sign a document that you are uncomfortable with or do not understand. Know your rights to cancel the loan application. The law allows you three days to cancel the loan application after you have signed it. Report any suspicious activity to the Office of Civil Rights, 110 South East 6th Street, 10th Floor, Ft. Lauderdale, Florida, 33301 at (954)712-4600 or to the Florida Department of Financial Services, 200 East Gaines Street, Tallahassee, FL 32399-0300 at 1-800-342-2762.