

## Predatory Lending Warning Signs

### Balloon Payments

The lender gets the homeowner into a loan that is due in full at the end of a short period of time, perhaps even as short as two years. They'll tell the homeowner that this time is for them to re-establish a good credit rating so they can refinance into a more favorable loan. At the end of the balloon period the homeowner will *have to* pay off or refinance. Usually, two years is not enough time for homeowners to resolve their financial crisis and re-establish good credit, so they will likely move from one high interest loan to another, plus they'll have to pay closing costs all over again.

### Negative Amortization

You usually find these with real hard-money lenders. Payments on the loan don't even equal the monthly interest charges. Interest then accrues and compounds, while the principle is never touched. For example, on a \$100,000 loan at 12% for 15 years, the monthly P & I payment would normally be \$1,200 – \$1,000 for interest and \$200 for principle in month one, with an ever larger share going towards principle in succeeding months. Under the negative amortization loan, they would set you up with a monthly payment of, say, \$950, for the purpose of keeping your monthly payment "affordable." However, your interest isn't paid down — indeed it's increasing — and your principle isn't even touched. They sometimes do these in conjunction with a balloon payment, so you're really stuck.

### Multiple Refinancing: "Flipping"

Similar to the balloon payment scheme. They get you into a less-than-desirable loan, with instructions to come back in two to five years to refinance to a better loan. Then do that again, then do that again. Each time, they'll re-amortize the loan back to a 30-year loan, and include hefty closing costs.

The other thing they might do is get you into a high interest loan, then call you back in six months and say that they've got a great new loan product and they can refinance you now at two points less. In fact, they could have always sold you the lower-interest loan, but they made more commission on the higher interest loan, and they now want the double closing costs.

### Unnecessary Debt Consolidation

Homeowners take unsecured credit debt and put it against the house in the interest of lowering their overall monthly debt payments. However, they've now put their house at risk, and stretched payments (like car payments) that may have ended in four years to a full 15-30 years. Where homeowners should be especially wary is if the lender makes it mandatory that they consolidate all other debt into the home loan. That could be a warning sign of a lender who will not distribute all loan proceeds. See below.

### Failure to Distribute Loan Proceeds

Lender requires that the homeowner consolidate and pay off all other debts such as credit cards, car loans, etc. They roll that into one big loan, and claim they will pay off those debts with the proceeds of the loan. They never distribute the loan proceeds, and the homeowner is not aware of that until they begin to get late notices from the other creditors. By then, the lender has usually disappeared from town. (**Note:** Sometimes it is legitimate that the lender will want to make sure that all other debt is paid off so that they and you know that you don't have a lot of other monthly obligations — so evaluate your own situation for this issue.)

### High Closing Costs

Standard closing costs are typically two-to-four percent. My contact at a somewhat reputable sub-prime lender says that they charge four-to-six percent. However, we've seen closing costs as high as 25%! They'll also confuse you by having all sorts of charges, but calling some of them fees, some of them origination points and some of them discount points. Ask what each one is for — *specifically*.

### Large Broker Fees and/or Phantom Broker

Tied into high closing costs are large broker fees, sometimes paid to a person you never met or talked to. They also might try to charge the broker fees multiple times under the settlement statement.

### Prepayment Penalties

Often with refinanced loans, lenders charge a prepayment penalty if you pay off the loan within the first two, three or five years. The amount is often equal to six months' interest. You may be able to "buy down" the amount of prepayment penalty, i.e., pay 1% in costs up front to reduce the prepayment penalty from five to three years.

### Contractor-Arranged Financing

This is a multiple scam, often done against seniors. A "contractor" will knock on the door, say that they're in the neighborhood doing work and have a special deal for home repair work. While they're at it, they can arrange financing for the project with a lender under a pre-approved financing package. The contractor will help the homeowner fill out the paperwork, submit it to the lender, get paid, then disappear. The lender then tells the homeowner that regardless of the work getting done, they've dispersed the funds, and the homeowner is liable for the loan.

Another scam is that the repair person will complete the work halfway then disappear, leaving the homeowner in even more of a bind. To complete the job, the homeowner will need to borrow even more money and hire another contractor.

A third scam is that the contractor will do such a shoddy job that the homeowner will incur greater costs trying to fix up that bad job.

## Bait & Switch

Lenders misrepresent terms. They'll quote a homeowner interest rate of, say, 7% fixed when they first call about a loan. Then once they pull the credit report and investigate the income and employment, they'll say the situation doesn't look quite as strong as they thought it would and the homeowner has been bumped to a higher-risk credit rating, so now the interest will be 10% and adjustable. What happens for many homeowners is they've let out a sigh of relief after the first meeting, they're counting on this refinance to dig them out of the hole, they feel like they have no choice, and they go ahead with the higher interest rate loan.

## Unnecessary Escrow Accounts & Advance Payments

This is an easy place for unscrupulous lenders to hide excess fees and charges. The whole escrow process is so confusing to most folks they don't know how to track who is paid what or when it is paid. Look for double billing.

For more information on ways to avoid the trap of a predatory loan, please call Solid Ground's **Predatory Lending Hotline** at **206.694.6864**.

## Foreclosure Scams

### Equity Skimming

A person will go to the courthouse to find names and addresses of properties for which lenders have started foreclosure proceedings. They'll knock on the homeowner's door and promise to get the homeowner out of trouble by paying off the mortgage and may offer the homeowner a chance to lease-back-to-buy their home, or promise the homeowner a sum of money when the property is sold. The buyer will have the homeowner deed the property over to them, then collect rent payments. They don't actually make the mortgage payments, and the house goes to foreclosure after all. Homeowners need to know that signing over your deed to someone else does not necessarily relieve them of their obligation on the loan.

### Phone Counseling Agencies

Some groups calling themselves "counseling agencies" will offer to perform services for a fee, i.e., negotiate a forbearance agreement or a short sale. These are things that the homeowner may well be able to do themselves, or are available for free from a nonprofit agency. If the homeowner has any doubt, they can call the HUD.

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