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# The Need for Predatory Mortgage Education: Expert Views

**Abstract**
This article describes the results of an exploratory study of predatory mortgage lending. The purposes were to gain insights into the salient characteristics of victims of predatory mortgage lending and identify the most effective means of victim protection in order to guide Extension efforts to educate consumers. Twelve mortgage-lending professionals were interviewed in-depth. They identified educational efforts by Extension educators and other nonprofit organizations as the best and most effective means of reducing the losses caused by predatory mortgage lending. Study findings can help Extension staff identify target audiences and the most effective educational strategies concerning predatory mortgage lending practices.

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## Introduction

The financial security of American families is receiving increased and needed attention in the Cooperative Extension System. No group, from rural farm families to urban dwelling minorities, is spared the complexity of today's financial world. Unfortunately, low-income, minority, and aging households, those who can least afford it, continue to experiment with fringe banking services such as pawnshops, check cashers, rent-to-own furnishings, automobile subprime financing, and second tier credit cards, making it difficult for them to achieve long-term financial stability. Educational programming through the Cooperative Extension System has begun to address many financial problems that plague vulnerable families, yet one issue has still received little, if any attention in the Cooperative Extension network; the issue of subprime and predatory mortgage lending practices.

Subprime home loans, loans with higher than traditional rates and fees, have been shown to drain household resources one payment at a time, and can contribute to delinquency, foreclosure, and bankruptcy (Lord, 2005). Subprime home loans are seven times more prone to delinquency and foreclosure than traditional home loans and can have a more devastating effect on a family than any other financial product because of the magnitude of the transaction (Joint Center for Housing, 2006).

The volume of subprime housing loans in 2005 alone was well over half a trillion dollars, representing approximately 20% of the 2005 mortgage origination dollar value (Joint Center for Housing, 2006). By comparison, payday-lending volume is only about $40 million in a single year

(Center for Responsible Lending, 2004). In spite of the costs and risks, trends indicate that over one in five home-buying families in 2007 will enter into one of these potentially wealth-stripping loans.

Though subprime loans are designed for those with poor credit history, numerous studies have found that these higher priced loans are actually targeted at the elderly, minority, and low-income populations regardless of credit score, because of their vulnerabilities (Calem, Hershaff, & Wachter, 2004; Newman & Wyly, 2002; Schill & Wachter, 1993; Zimmerman, Wyly, & Botein, 2002). The most egregious of these unethical actions have been dubbed "predatory lending."

Ideal customers for predatory lenders are persons who have done little or no shopping, have presupposed that because of little or damaged credit that they cannot qualify for a loan, or those with significant amounts of equity already built up in their homes. Such customers are often clustered in low-income, minority, and elderly neighborhoods and are therefore easy to target (Lord, 2005). With little regulation by states or housing industries, educators and non-profit organizations are currently the only defense these families have in understanding and avoiding these mortgage pitfalls.

## Objectives

Given that the direct losses of consumer wealth from predatory mortgage lending exceeds $9.1 billion nationally, and that the monetary losses and family stresses from foreclosures are incalculable (Stein 2001), there is a need for additional information to guide efforts to target and educate consumers about predatory lending practices. Among the objectives of the exploratory study reported here, several were directly applicable to potential Extension efforts. They purported to:

1. Identify salient characteristics of the victims of predatory mortgage loans.

2. Describe optimal educational strategies that Extension personnel can easily implement to help reduce predatory mortgage lending.

## Methods

As opposed to victims of predatory mortgage lending, mortgage-lending professionals were the focus of the study reported here because victim perspectives have been reported in previous works, and research indicates that even victims do not fully understand the extent to which they were victimized. Therefore expert views, in this case, can *increase our understanding of predatory lending practices* (Lord 2005; Special Committee on Aging 2004).

Qualitative methodology was used because of the exploratory nature of this research. In-depth interviews were conducted with 12 mortgage lending professionals, using the tree and branch method of interviewing (Rubin & Rubin, 2005), in which several open-ended questions were asked, followed by probes that were used to explore themes, concepts, and ideas introduced by the interviewees. The end result was an array of comments that branched from the main questions, all of which stemmed from or described the main topic.

### Sample

Twelve mortgage lending professionals, defined as persons whose careers require regular, full-time contact with mortgage borrowers, mortgage lenders, or both, were recruited to participate in the study, using a snowball or chain sampling process in which initial interviewees refer additional potential interviewees (Patton, 2002). Duties of a mortgage lending professional ranged from education and counseling, to regulation or business. These professionals dealt with mortgage borrowers and lenders on a regular, full-time basis and, therefore, were in a key position to witness their daily interactions. As an incentive to participate, interviewees were offered a comprehensive written report of the final results.

The final sample of mortgage lending professionals included four consumer advocates, four industry advocates, and four neutral participants who averaged over 15 years of experience in nearly every conceivable area of the mortgage lending market. While it is possible that an industry advocate was a subprime or predatory lender, there was no attempt to classify them as such in order to maximize participation of all types of lending professionals. Table 1 offers a summary of their demographic characteristics.

**Table 1.**
Respondent Characteristics (n=12)

| | **Predisposition** | | |
|---|---|---|---|
| | **Consumer Advocates** | **Industry Advocates** | **Neutral Participants** |
| **Number** | 4 | 4 | 4 |

| | | | |
|---|---|---|---|
| **Male** | 1 | 4 | 2 |
| **Female** | 3 | 0 | 2 |
| **Mean years of experience** | 8 | 13 | 24 |

### Data Collection Procedures

The first author conducted all interviews and led data analysis. He took notes during the interviews to capture verbal responses and nonverbal cues, such as tone of voice, attitude, and expressions. Interviews were audio recorded and transcribed verbatim for analysis. Data coding began through labeling sections of the text by topic. To be consistent with interviewees' notions, "in vivo" codes, the terms supplied by participants, were used whenever possible. In this step, each interview was treated on an individual basis.

Content of the major categories was divided into several descriptive categories. The material was then reread; this time the researcher added more specific codes for the material in the descriptive categories. The interview content at this point was treated collectively. Codes were organized into a narrative or description of predatory lending and potential solutions to predatory lending as supported by the evidence. This method of managing and analyzing qualitative data was performed using the computer software program NVivo7 (QSR International, 2005). All authors reviewed codes, with discrepancies discussed and resolved.

## Results

### Research Objective One: Victim Characteristics

#### *Personal Attributes*

Participants described victims as likely to be those young and inexperienced, those with some cognitive impairment, or those of minority status who may have struggled with language facility. One homebuyer explained that young borrowers are exploited because of their naivety. Similarly, older adults are a popular target, especially for refinancing or equity based loans, because of the build-up of home equity accumulated over a lifetime.

Minority group members also tend to be victimized disproportionately, though most interviewees cited language barriers as the real cause of vulnerability. This vulnerability can lead to instances of "lending cannibalism," involving a lender or broker of the same ethnic background taking advantage of minority borrowers because of assumed trust and lack of other options. A prime example is found in a 2006 news article, in which a prominent Latino community member was involved in deceptive home-loan practices with Latino families who trusted her (Sanchez & Mitchell, 2006).

Several participants explained that there are so many diverse characteristics that could make someone susceptible to unfair loans that it is perfectly reasonable to assume that anyone could potentially be a victim.

#### *Emotional Characteristics*

Emotional characteristics also play a key role in borrower vulnerability. Feelings of desperation are a common byproduct of excessive debt, and mortgage debts are perhaps the most pressing because missing only one or two payments can send the borrower into a panic to avoid foreclosure, which can lead in turn, to hasty, unwise acts.

Peer pressure can be an emotional stimulant that can lead borrowers to make uninformed home-buying decisions. One housing counselor related an example: "They weren't even thinking about buying a home until they heard their friends had one . . . their friends [told them], 'Hey, go ahead and get one too.'"

The desire for instant credit or instant gratification also was an emotional factor. A financial counselor related an instance in which a client had just come out of bankruptcy and instantly entered the home-buying market. This client was not deterred by high interest rates; she wanted a house immediately, despite potential long-term consequences. Even the initial consequences were quite severe as she entered 100% financing, the first 80% at double the prime rate and the last 20% at quadruple the prime rate.

#### *Inadequate Financial Skills*

Financial characteristics of borrowers also play a large role in a borrower's susceptibility to unfair lending practices. Particularly in the mortgage market, borrowers often find themselves lost in inches of paper work that are comprised of legal disclosures designed to protect the consumer. A regional lending manager explained, "I would dare say a very, very small percentage of the population understand what they are signing, and understand the terms of their loan."

### Research Objective Two: How to Reduce Predatory Lending

#### *Insufficient Prohibitive Legislation*

Many participants described positive aspects of subprime lending, but felt that legislation designed to separate unscrupulous subprime lenders from legitimate subprime lenders was ineffective. They did not view most actions and loan features as inherently unfair; rather, loans simply become unfair only when misused. However, participants were in full support of legislative efforts to increase the amounts of financial education in schools and communities.

#### *Financial Education*

Unanimously, all participants in the study endorsed comprehensive financial education of consumers. Consumer education was recognized in previous literature, but has rarely, if ever, been emphasized as the chief method of consumer protection. Yet participants stressed that the importance of this method of protection cannot be overemphasized.

##### Home-Loan Education

Home-buying/home-loan classes are a way for consumers to be educated about the process before entering a home-loan transaction. One homebuyer counselor asserted, "Number one is that consumers need to be educated, through [home]buyer education courses where predatory lending is covered in detail." But these courses are often limited to a single day, and some felt that they simply need more time to truly educate a borrower. A housing specialist remarked, "I think it needs a little more time . . . .We go fast and hard, and try to get everything in that is going to help them."

A crucial aspect of homebuyer education is optimal timing of courses. Ideally, as noted by one homebuyer educator, education should target people before they enter the home-buying process, "We would love to have people come just because they're interested in buying a home, that's our ideal home buyer student . . . because they go in fully armed and ready, and once you call a predatory lender once or twice on what he's doing, he stops."

##### Financial Literacy Programs

Extension educators can work with local/state schools. As good as homebuyer education may be, the experts admitted that it was only a temporary solution to a much larger problem: a general lack of financial literacy among all Americans. One educator exclaimed, "I think everyone should be required to have personal finance classes before they are out in the world. It's basic education that all high school seniors or juniors should have."

Extension educators can work with teachers to implement financial literacy programs for all students. Previously developed curriculums such as the National Endowment for Financial Education High School Financial Planning Program®, and Jump$tart® programs, and state and local initiatives such as The University of Nevada Extension's Money on the Bookshelf, and the University of Illinois Extension's Welcome to the Real World were designed with Extension educators in mind, and can be easily incorporated into existing school system subject matter.

#### *Additional Partnerships*

Efforts that result in education and borrower protection can originate in venues other than the classroom. Study participants noted that the involvement of individuals acting as consumer advocates in community groups and in legislative efforts aimed at financial education can have a lasting effect for reducing borrower vulnerability. Establishing such partnerships can create a system by which consumers can quickly escape bad loan situations and avoid future lending hazards.

According to participants, one very helpful consumer resource is a fair housing committee. The purpose of such committees is to create a comprehensive solution to individual cases of predatory mortgage lending. The solution includes legal action, counseling, and education; credit rehabilitation programs; and alternative financing options to help borrowers exit bad loans as quickly as possible. These committees require widespread cooperation of community members and significant amounts of funding, but show tremendous potential as a tool for assisting victims, according to the participants. Extension agents with good ties to the community could be instrumental in facilitating such groups.

Additional consumer support is found in neighborhood revitalization programs targeted specifically at vulnerable neighborhoods. Some neighborhood revitalization committees already exist on relatively small levels, according to one participant who has worked with them. In spite of their small size, this participant felt that they were very successful at helping revitalize the skills and abilities of the residents in some of the most vulnerable neighborhoods.

## Conclusions

Participants felt that the greatest shortcoming in the mortgage-lending environment was not a policy problem, but rather the lack of consumer knowledge and know-how when it comes to shopping for and understanding mortgages. The most effective prevention efforts will likely involve a combination of policy and educational improvements, but the educational component should not be minimized. Extension educators can play a particularly vital role in preventing further predatory mortgage lending through directly educating citizens and in orchestrating community activism to advance the financial literacy opportunities available to borrowers and consumers in general. Future studies should address optimal methods and amounts and timing of financial education efforts.


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