Predatory lending kills home dreams

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Property in declining neighborhoods does not appreciate in value. Because home ownership is the number one means of wealth creation for average families, neighborhood blight cannot be separated from the challenge of wealth creation and the burden of intergenerational economic marginality.

Neighborhood blight results in tax delinquency when property that has failed to gain value is abandoned by heirs or absentee landlords. An eroding tax base has implications for amenities that can attract employers, such as education. That in turn has ripple implications for family income and routes to wealth creation.

When blight spreads to once-healthy neighborhoods, wealth creation is further undermined.

Our community has a clear need for early and continuing education in financial literacy to prepare families better for home ownership and other financial decisions.

At the same time, we have a corresponding need to understand better the dynamics of the housing market and the role that subprime or predatory lenders play in eroding equity and enabling ill-prepared buyers to become ill-prepared – and too often short-term – homeowners.

Policies that do not enable buyers to become successful home owners not only diminish the odds of building equity for those buyers, but also threaten the wealth-creating investments of other home owners. The public and private sectors and nonprofit groups should work together to increase the odds of successful home ownership, particularly in neighborhoods characterized by alarming concentrations of subprime lending and mortgage foreclosures.

According to data collected for the MemphisDEBT collaborative for 1999 through 2001, the highest rates of mortgage foreclosure in Memphis are in neighborhoods that have low poverty rates but high activity among subprime lenders. The U.S. Department of Housing and Urban Development definition of subprime lending specifies that at least 50 percent of a subprime lender's mortgages are to "B" and "C" applicants – those with higher-risk credit history and higher debt-to-income ratios.

Too many Memphis neighborhoods have an abundance of moderately priced homes that appeal to first-time buyers and also a concentration of subprime lending. In some neighborhoods, between one and two out of every three new mortgages is financed by a subprime lender. Some such lenders have approval rates that approach 100 percent of applicants, compared with more typical approval rates in the range of 50 percent.

Subprime lending may become predatory lending when marginally qualified buyers are referred by brokers who work with lenders, and profits are front-loaded to minimize the risk associated with default.

The Memphis Area Legal Services and attorney Richard Fields are investigating cases where up-front mortgage fees run as much as 17.8 percent of the loan. Fees are recouped in the first years of loan repayment. In the event of foreclosure, lenders may recoup their investment from the Federal Housing Administration for FHA-guaranteed mortgages, or property may be quickly resold if brokers maintain a steady stream of eager buyers. About half of the foreclosures in Memphis appear to be on FHA-financed mortgages.

In some Memphis neighborhoods, foreclosure rates run as high as one in five owner-occupied homes over a three-year period. Foreclosure and high residential turnover are accompanied by deferred maintenance and in some cases abandonment.

How do neighborhoods rebound from decline while creating wealth for the residents? Home ownership remains the number one strategy for wealth creation, but to fulfill that strategy, home ownership must be an obtainable goal.

The prospective home owner must become financially literate. At the same time, public policy should support "wraparound" home ownership counseling – and lending options – for first-time buyers most likely to do business with subprime lenders. Such collaboration among the public sector, nonprofits (for home ownership counseling) and the private sector (for new financial tools available to wraparound participants) will not only create wealth but also save neighborhoods.

Creating financially savvy consumers through financial literacy programs and assisting prospective homeowners creates healthy, revitalized neighborhoods, fortifies the tax base and generates personal and community wealth. We need to think both in terms of long-term prevention of bankruptcy and foreclosure and shorter-term intervention to mitigate the impact of subprime and predatory lending.

Many groups and individuals are working diligently on these issues. Their impact is being felt through efforts such as the MemphisDEBT collaborative's studies of predatory lending and problem properties, Hope VI initiatives and the UPTOWN Revitalization Project.

But such efforts – and others undertaken by groups that include the University of Memphis, Memphis Tomorrow, the RISE Foundation, Memphis Area Legal Services, the Hyde Family Foundations, the Memphis Shelby Crime Commission, the Federal Reserve Bank and United Way – have the potential of much greater impact if we leverage our resources into one formidable collaborative effort.