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The Border Effect—Subprime and Predatory Lending on the Texas-Mexico Border

By

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The Border Effect—Subprime and Predatory Lending on the Texas-Mexico Border

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Dedication

This Professional Report is dedicated to my parents, Grant and Marianela Milner, for their many sacrifices and constant love and support; to Professor Paul Dawson of Oberlin College, who believed in me, helped me believe in myself, taught me how to think analytically, and for spending four years preparing me for policy school; and finally, to my incredibly strong, loving, supportive and very patient Arthur for *everything*.

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The Border Effect—Subprime and Predatory Lending on the Texas-Mexico Border

by

Michelle Marie Milner, M.P.Aff.

The University of Texas at Austin, 2007

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This report analyzes data from the Federal Financial Institutions Examination Council (FFIEC) relating to the activity of lending institutions covered by the Home Mortgage Disclosure Act (HMDA) along the Texas-Mexico Border for which data was available, (Brownsville, El Paso, Laredo, and McAllen) including the disposition of loan applications and the rate spread for all originated loans. It examines not only inter-group comparisons between racial/ethnic and socio-economic categories of borrowers, but also intra-group comparisons for these categories across the Texas Border region (considered separately as though it were the “51st State”), the U.S., and Texas. This report concludes the following: (1) with regard to both conventional home purchase loans and refinance loans, Border applicants are more likely to be turned down for a loan than borrowers in the U.S. or Texas, suggesting that the Border in its entirety is being subjected to lending discrimination in the form of redlining; and (2) regardless of borrower characteristics (Black, Hispanic, white, low to moderate income, middle income, or upper income) and type of loan (home purchase or refinance), a Border borrower is almost without exception more likely to receive a subprime or high cost loan than a borrower with comparable characteristics in the U.S. or Texas, suggesting that the Border region is also being subjected to targeting by subprime lenders resulting in reverse redlining and/or; (3) steering of Border applicants to higher rate loans as compared to applicants with comparable characteristics in the U.S. or Texas.

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Chapter 1. Introduction

Homeownership is the cornerstone of the American dream. Consequently, the United States can boast a high rate of homeownership of 69%¹ with 72 million homeowners.² Yet few Americans can afford to purchase a home without taking out a loan. Consequently, equal access to mortgage lending is an issue of vital interest to our society, one that has sparked lively research, debate, and legislative intervention over the past thirty years. While no one has suggested that individuals who are genuinely less creditworthy should have equal access to credit, the consistent finding in past research that access to credit is unequal across racial/ethnic and socio-economic lines has generated significant concern and controversy. This is particularly true since it is minorities and low-income groups whose access to credit has been comparatively impaired, a phenomenon with inescapable connections to historical trends of discrimination in other areas of society.

The data presented in this report reveal dramatic trends regarding access to credit and discriminatory lending practices in the Texas Border region. However, unlike previous research on lending practices, this report does not focus solely on inter-group comparisons between racial/ethnic and socio-economic categories of borrowers. Rather, this report goes further and examines intra-group comparisons for these categories across large-scale geographical regions, namely the Texas Border region, the U.S., and Texas. As a result, this report is able to provide some preliminary answers regarding whether the Texas Border region, which is already known to differ from the U.S. and Texas in regard to other critical indicators, also differs in how its residents are treated by lenders.

The remainder of this report is organized as follows:

Chapter two – the History of Housing and Mortgage Discrimination – provides a brief history of housing and mortgage discrimination in the United States, the legislative remedies that were enacted to address these issues, and places the topic of subprime and predatory lending in the proper historical context.

Chapter three – the Rise of Subprime and Predatory Lending- provides an overview of the evolution of the subprime mortgage market and delineates the practices which are considered “predatory” in nature and cause a net harm to the borrower.

Chapter 4 – Disparity Studies – provides a review of the most relevant literature and research on the topic of mortgage lending in general as well as subprime lending, the disparities that exist between different ethnic/racial groups and socio-economic classes, and what the research reveals as to why such disparities exist.

Chapter 5 – The Texas Border as the 51st State – provides a demographic profile of the 1254 mile stretch spanning the Texas side of the Rio Grande River from El Paso in the west to Brownsville at the southernmost tip of the state, treating this region as though it were the “51st State,” separate from the rest of Texas and the United States. The data presented clearly demonstrate that if the Border region were the 51st state it would rank among the lowest of the states in positive socio-economic indicators and among the top in negative indicators.

Chapter Six – The Border Study: Analysis of 2004 HMDA Data – focuses on the Border region and the patterns and trends regarding mortgage lending in the region and in comparison to Texas (excluding the Border region) and the United States as a whole (using the National aggregate data). This Chapter concludes that the Border region is treated differently from both Texas and the United States.

Chapter Seven - The Current Legal Context – presents the laws and regulations at the federal and state level that are designed to regulate mortgage lending and high cost mortgage lending. The current state of the law is described in some detail in order to provide a context for the recommendations made in this report.

Chapter Eight – Solutions to Subprime and Predatory Lending – presents a variety of research, legislative, and regulatory policy solutions at the federal, state, and local level to improve the regulation of subprime lending and combat predatory lending.

¹ Freddie Mac Reporter Factbook, *U.S. Homeownership Rates 1996-2005*. Online. Available: <http://www.freddiemac.com/news/factbook/pdf>. Accessed: July 12, 2007.

² Richard Lord, *American Nightmare: Predatory Lending and the Foreclosure of the American Dream* (Monroe: Common Courage Press, 2005), p. 16.

Chapter 2. History of Housing and Mortgage Lending Discrimination

One cannot fully understand the phenomena of subprime and predatory lending prevalent in the United States today without placing these contemporary practices in the context of earlier housing practices and public policy that initially promoted racial discrimination and segregation rather than opposing it.

Early Discriminatory Practices

In 1933, a federal housing policy advisor ranked fifteen ethnic and racial groups in terms of their impact on property values in a report he authored for the Federal Housing Administration (FHA).¹ The groups who reportedly had the most negative impact were Negroes and Mexicans.² The FHA, therefore, concluded in its 1938 *Underwriting Manual*:

If a neighborhood is to retain stability, it is necessary that the properties shall continue to be occupied by the same social and racial classes. A change in social or racial occupancy generally contributes to instability and a decline in values.³

In addition, the FHA openly advocated use of restrictive covenants based on race that guaranteed residential housing would be occupied by the same race when the property changed hands.⁴

The same racial bias existed in the private sector. In 1932, Fredrick Babcock, a leading real estate theoretician, noted as follows:

There is one difference in people, namely race, which can result in very rapid decline. Usually such declines can be partially avoided by segregation and this device has always been in common usage in the South where white and negro [sic] populations have been separated.⁵

Furthermore, until 1950 the Code of Ethics of the National Association of Realtors specifically stated the following:

A Realtor should never be instrumental in introducing into a neighborhood a character of property or occupancy, members of any race or nationality, or any individual whose presence will clearly be detrimental to property values in the neighborhood.⁶

Years later a related practice came to light whereby banks refused to lend to borrowers in minority and low-income neighborhoods. It was called “redlining,”⁷ and there was evidence that both the federal government and private sector were complicit in this practice.⁸

Redlining

The term “redlining” is said to have been coined by community activists in the late 1960’s in Chicago’s Austin neighborhood who protested what they believed to be unfair lending practices⁹ and disinvestment of old urban neighborhoods.¹⁰ They used the term to refer to the red lines that savings and loans associations had drawn around areas where they refused to make loans.¹¹ According to researcher, Amy Hillier, investigations of redlining that exposed (the use of) maps with actual red lines are the exception, however, at the center of this conceptualization is the idea that redlining is spatial in nature.

Those interested in housing and the allocation of credit such as scholars, fair housing advocates, journalists, and public policy officials generally agree that redlining involves ideas about creditworthiness that do not have to do with the actual mortgage applicant and everything to do with the location of the property.¹² Thus, redlining, refers specifically to discrimination on the basis of the neighborhood or area rather than on the individual characteristics of the applicant.¹³ However, focus on spatial relationships or statistical associations between the characteristics of an area (racial, socio-economic, etc.) and mortgage outcomes is also considered legitimate.¹⁴

Although the practice did not become a controversial issue until the late 1960’s and early 1970’s, redlining had been a common practice since the 1930’s, when the Home Owners’ Loan Corporation (HOLC) used coded maps that highlighted in red areas

considered too risky for real estate investment.¹⁵ HOLC had created the maps after originating a million mortgages to homeowners who were on the verge of losing their homes during the Depression.¹⁶ These maps categorized neighborhoods in more than two hundred cities across the country according to their stage of decline.¹⁷ In the late 1970's, Kenneth Jackson, the researcher who discovered the maps, argued that the FHA as well as private lenders used the maps when considering where to make loans and thus connected these maps to the practice of redlining.¹⁸ However, the connection between the HOLC maps and the institutionalization of redlining practices has been questioned by Hillier, who points to other maps and sources of information as the primary decision-making tools in the home lending process.¹⁹

According to Hillier, during the 1930's and 1940's the FHA had a large collection of maps that included census-tract and block level data for different cities across the country.²⁰ The FHA was a leader in promoting neighborhood risk ratings following the Depression era as its *Underwriting Manual* contained a detailed rating system that encouraged appraisers to consider the stability of an area and protect it from "adverse influences," generally referring to Blacks and other racial/ethnic minorities, (as cited above).²¹

Although it is clear that redlining has a history long before it was named in the late 1960's, it was further revealed to be in practice at the national level in 1968, as the President's National Advisory Panel on Insurance in Riot-Affected Areas found evidence that lenders were drawing red lines on maps.²² The panel quoted an underwriting guide that advised against insuring areas considered high risk:

A good way to keep this information available and up to date is by the use of a red line around the questionable areas on territorial maps centrally located in the Underwriting Division for ease of reference by all underwriting personnel.²³

Moreover, the Douglas Commission (The National Commission on Urban Problems) found similar evidence in 1969:

There was evidence of a tacit agreement among all groups—lending institutions, fire insurance companies, and FHA—to block off certain areas of cities within “red lines” and not to loan or insure within them.²⁴

Reverse Redlining

In recent years, the discovery by researchers that subprime lending is more prevalent in low-to-moderate income and/or minority neighborhoods has given rise to the concept of “reverse redlining.” According to a HUD/Treasury 2000 report, *Curbing Predatory Home Mortgage Lending: A Joint Report*, reverse redlining involves the specific targeting of residents of disadvantaged areas for credit on unfair terms²⁵ wherein these neighborhoods are believed to be affirmatively targeted by subprime lenders for less favorable loans rather than excluded from consideration altogether.

Steering

Concurrent with the concept of reverse redlining is “steering,” which is the practice of directing consumers to high cost loans based on their race, economic status, or lack of financial sophistication rather than based on their credit histories or credit risk.²⁶ This practice particularly onerous as in 2001 the Fannie Mae Foundation reported that as many as 35% to 50% of the borrowers in the subprime market could have qualified for a lower cost loan.²⁷

Public Policy Addresses Discrimination

The first federal public policy initiative to combat housing discrimination came in 1962 when President Kennedy issued Executive Order 11063, which required federal agencies to “take all necessary and appropriate action to prevent discrimination” in all housing programs receiving federal support.²⁸ Subsequently, in 1965 the Commissioner of FHA announced a change in its policies, which had historically redlined Black and other minority neighborhoods to exclude them from its insurance coverage.²⁹

In 1968, the U.S. Supreme Court ruled that the Civil Rights Act of 1866, which technically made racial discrimination in all contracts illegal, extended this protection to real estate transactions.³⁰ In that same year the Fair Housing Act was passed.

The Fair Housing Act of 1968

The Fair Housing Act (FaHa) is Title VIII of the Civil Rights Act of 1968. This piece of legislation is the principal law governing mortgage discrimination. It explicitly outlaws discrimination in housing on the basis of race, color, sex, religion, and national origin in the sale or rental of housing,³¹ the terms and conditions under which housing would be made available, the advertising of housing, and the extension of credit for housing.³² The agencies charged with enforcement of the law were the U.S. Department of Housing and Urban Development (HUD) and the Department of Justice.³³ As amended, FaHa provides:

It shall be unlawful for any person or other entity whose business includes engaging in residential real estate—related transactions to discriminate against any person in making available such a transaction, or in the terms or conditions of such a transaction, because of race, color, religion, sex, handicap, familial status, or national origin.³⁴

It also provided incentives for lenders to serve minority and low-income areas.³⁵ Several federal courts concluded that FaHa bans redlining and the Supreme Court also held that it prohibits racial steering.³⁶

The enforcement of FaHa was considered weak and there was strong evidence of continuing discrimination from the Housing Market Practices Survey and other sources, which led to the Fair Housing Amendments of 1988 (FaHAA).³⁷ The amendments included removal of the limit on punitive damages in civil housing discrimination law suits, lengthened the statute of limitations in such suits to 2 years and to 1 year for complaints to HUD, established a system of administrative law judges with the authority to impose penalties for complaints brought before HUD for hearing, authorized civil penalties and damage awards to be paid to the U.S. Treasury, and allowed the Secretary of HUD to initiate cases.³⁸

FaHa is generally considered the centerpiece of antidiscrimination law; however, other laws such as the Equal Credit Act, the Home Mortgage Disclosure Act, and the

Community Reinvestment Act are also key components of the public policy response to discrimination in housing and access to credit.

The Equal Credit Opportunity Act of 1974

Congress passed the Equal Credit Opportunity Act (ECOA) in 1974. It added Title VII to the Consumer Protection Act of 1968 and prohibited discrimination on the basis of sex and marital status.³⁹ In 1976, Title VII was amended to include the protected classes of race, color, religion, national origin, age, and source of income from public programs.⁴⁰ As amended, ECOA states:

It shall be unlawful for any creditor to discriminate against any applicant, with respect to any aspect of a credit transaction—on the basis of race, color, national origin, sex or marital status, or age (provided the applicant has the capacity to contract).⁴¹

Both FaHa and ECOA prohibit discrimination “on the basis of” characteristics that define protected classes.⁴² Additionally, in 1994 the Interagency Task Force on Fair Lending issued a clarification on what these laws made illegal:

“Overt discrimination,” when a lender blatantly discriminates on a prohibited basis;

“Disparate treatment,” when a lender treats applicants differently based on one of the prohibited factors; and

“Disparate impact,” when a lender applies a practice uniformly to all applicants but the practice has a discriminatory effect on a prohibited basis and is not justified by business necessity.⁴³

As with FaHA, regulators and the courts have also interpreted ECOA to include prohibition of the practice of redlining.⁴⁴

It was concern over redlining and geographic disparities in lending that led Chicago organizers to work with Senator William Proxmire of Wisconsin, who sponsored both the Home Mortgage Disclosure Act (HMDA) and the Community Reinvestment Act (CRA).⁴⁵

The Home Mortgage Disclosure Act of 1975

William Proxmire's Senate Bill 1281 was passed by Congress as the Home Mortgage Disclosure Act (HMDA) of 1975.⁴⁶ It was based on a Chicago city ordinance passed in 1974 that intended to expose redlining of lower-income central areas of the city.⁴⁷ HMDA requires most lending institutions to disclose to the public information about applications for home loans and originations and purchases of home loans made during the calendar year.⁴⁸

Initially, it did not contain all the provisions sought by community groups, such as the inclusion of mortgage companies as opposed to only depository institutions, data on race or income of applicants, data on the disposition of loan applications, business loan data, or deposit data.⁴⁹ However, the legislation, which was opposed by the bank lobby, did require commercial banks and thrifts with federally insured deposits and assets of \$10 million or more to disclose census tract level⁵⁰ mortgage lending data in urban areas annually.⁵¹ HMDA was renewed in 1980 and made permanent in 1987.⁵² It was amended by the Financial Institutions Reform, Recovery and Enforcement Act of 1989 (FIRREA), which substantially changed the implementation of HMDA.⁵³ The amendments expanded HMDA reporting requirements to include detailed information on not only loans that were originated, but also on all loan applications, including from whom applications were received by race, gender, income, census tract of the property, and the disposition of each application.⁵⁴

In 2002, further substantive changes were made by the Federal Reserve Bank, which enforces Regulation C implementing HMDA, which issued a Rule regarding disclosure requirements that increased the types and amount of information to be made available for applications made beginning in 2004.⁵⁵ The number of non-depository lenders subject to reporting requirements was expanded to include non-depository institutions with more than \$25 million in mortgage loans⁵⁶ (the asset-size exemption is tied to the Consumer Price Index).⁵⁷ Previously, non-depository lenders had to report lending data only if their residential lending (home purchase and refinance loans) during the previous year equaled or exceeded 10 percent of total loan originations.⁵⁸

The Rule change also expanded the data collected about loan applicants' ethnicity and race. The standards for the classification of data regarding an applicant's race and ethnicity were made to conform to those established by the OMB, which allows individuals to select multiple racial and ethnic categories.⁵⁹ Previously, loan applicants could not designate both race and ethnicity but had to categorize themselves as being of Hispanic origin *or* as being in one of five racial categories (Asian or Pacific Islander, black, white, or other).⁶⁰ For data collected beginning in 2004, applicants could designate more than one racial category *and* one of two ethnicities (either Hispanic or not Hispanic).⁶¹ For example, the author of this report would be designated as white and Hispanic. The applications and loans are not counted twice, however, because the aggregate data is separated by ethnicity and race so each loan is only counted once.

In addition, lenders were required to report the pricing spread (also referred to as the "rate spread") between the annual percentage rate (APR) of the loan and the rate on Treasury securities of comparable maturity for loans with spreads equal to or greater than 3 percentage points for first liens and 5 percentage points for second liens.⁶² The APR was chosen as the measure of a loan's pricing because it was held to be the best single measure of the "true" cost of the loan because it reflects the interest rate and fees paid for each loan.⁶³ Loans with an APR less than 3.0 percentage points below the rate on a comparable Treasury security are considered prime rate loans. Loans with spreads at or above 3 percentage points greater than the rate for a comparable Treasury security are considered high cost or subprime.

This change was important to researchers and CRA examiners because it revealed that the level of subprime lending was not accurately measured in the HMDA data prior to 2004, as loans made by HUD identified subprime lenders were counted as subprime and loans made by all other lenders were counted as prime rate loans.⁶⁴ Therefore, the number of subprime loans originated by prime lenders was unknown. The new requirement to report the rate spread of each originated loan captures all prime and subprime loans required to be reported in the HMDA data.

Moreover, the new Rule required lenders to identify especially high cost loans as defined by the Homeownership and Equity Protection Act (HOEPA).⁶⁵ HOEPA requires extra disclosures to borrowers because the loans are exceptionally expensive. Loans covered by HOEPA include only home equity and refinance loans. Those that are first-liens are reported under HOEPA if the APR of the loan is 8 percentage points higher than the rate on a comparable Treasury security for a first-lien loan or 10 percentage points higher for a second-lien.⁶⁶ (See Chapter 7 for a complete discussion of HOEPA).

Although HMDA is essentially a disclosure requirement for lenders, its passage into law, with subsequent amendments and changes, was important because the data, although limited in scope, can be used as a screening tool to identify lenders that may warrant closer review for fair lending concerns⁶⁷ and help ascertain if lenders are denying fair and reasonable financing to qualified applicants based on improper factors such as race or ethnicity or are engaged in redlining or reverse redlining.

The Community Reinvestment Act of 1977

The Community Reinvestment Act (CRA) is Title VIII of the Housing and Community Development Act of 1977. The CRA is the first piece of legislation that directly targets the practice of redlining.

In the preamble to the CRA, Congress made the following findings:

- (1) regulated financial institutions are required by law to demonstrate that their deposit facilities serve the convenience and needs of the communities in which they are chartered to do business;
- (2) the convenience and needs of communities include the need for credit as well as deposit services; and
- (3) regulated financial institutions have continuing and affirmative obligations to help meet the credit needs of the local communities in which they are chartered.⁶⁸

CRA applies to federally insured institutions, national banks, thrifts, and state chartered commercial and savings banks.⁶⁹ A key provision of the CRA, as originally enacted, was the addition of a new assessment component to the examination process

for financial institutions. Specifically, federal supervising agencies (mainly the Federal Reserve Board, Office of the Comptroller of the Currency, Federal Deposit Insurance Corporation, and Office of Thrift Supervision) were required to assess a financial institution's record of meeting the credit needs of its entire community—expressly including low- and moderate-income neighborhoods—and to take this record into account in, for example, deciding whether to approve an application for a new branch or other major change.⁷⁰ In 1988, however, it was reported in hearings before the Senate Banking Committee that 97 % of institutions examined over the 11-year period received one of the two highest ratings (on a five-point scale).⁷¹

In 1989 FIRREA mandated public disclosure of each institution's CRA rating and performance evaluation, created a four-tiered descriptive rating system (outstanding, satisfactory, needs to improve, or substantial non-compliance) to replace the prior numeric scale, and required the regulators to prepare a detailed written evaluation of the lender's CRA record and an explanation of the basis for the rating.⁷²

In 1995, new regulations expanded the evaluation criteria for larger institutions to make them more rigorous and performance based, as community advocates argued that CRA evaluations relied too heavily on the *efforts* depository institutions made to meet the needs of the their communities rather than on results.⁷³ They include the following:

- (1) the lending test, which looks at the amount of local lending and distribution of loans by neighborhood and borrower characteristics;
- (2) the investment test, which looks at the level of community development investment, including grants to community development corporations, affordable-housing developers, and small businesses; and
- (3) the service test, which looks at services provided to low- and moderate-income markets.⁷⁴

Significantly, a provision in the original enactment of the CRA allows third parties to participate in the review process and actually challenge a bank or thrift's application for expansion, etc.⁷⁵ Although applications are rarely denied under the CRA, the costly delay factor commonly associated with a third party challenge has enabled this

provision to be effectively used by community groups and others to force financial institutions to negotiate reinvestment or other voluntary solutions.⁷⁶ That is not to say that institutions subject to CRA review are forced into making unprofitable loans as evidenced by the fact that in 2000 the Federal Reserve Board found CRA-related lending was profitable for the vast majority of covered lenders.⁷⁷

Nonetheless, in 1998 CRA came under attack by Texas Senator Phil Gramm, who denounced the law as an “extortionist tax” on banks and began to call for a repeal of the Act or a “safe harbor” for the 98% of banks that had been awarded satisfactory or outstanding ratings by regulators.⁷⁸ Subsequently, the Gramm-Leach-Bailey Act (GLBA), also known as the Financial Services Modernization Act of 1999, was passed and weakened some CRA requirements. Under the law, small banks (those with assets below \$250 million) are examined by regulators once every five years with an “outstanding” rating and once every four years with a “satisfactory” rating.⁷⁹ Prior to GLBA these lenders had been evaluated every two years.⁸⁰

In addition, specifically with regard to mortgage lending, in the past few years the impact of CRA has declined in importance because the institutions under its purview (commercial banks and thrifts) have steadily lost market share in the home lending arena.⁸¹ The share of home purchase mortgage⁸² loans subject to intensive review under CRA declined from 36.1% to 29.5% between 1993 and 2000.⁸³ In some cities this share is below 10%.⁸⁴ Further, there is evidence that the impact of the CRA has been weakened by improper influence exerted by lenders. Congressman Henry B. Gonzalez announced serious allegations about the Federal Reserve’s examination process in 1994.⁸⁵ Gonzalez reported that he received information from a former Federal Reserve Bank examiner that documented evidence that violations of the CRA were found and then replaced by supervisors’ language that indicated the bank was eager to comply with consumer lending laws.⁸⁶

¹ Gregory D. Squires, "The Rough Road to Reinvestment" in *Organizing Access to Capital: Advocacy and the Democratization of Financial Institutions*, ed. Gregory D. Squires (Philadelphia: Temple University Press, 2003), p. 3.

² Ibid.

³ Ibid., pp. 3-4.

⁴ Ibid., p. 4.

⁵ Gregory D. Squires and Sally O'Connor, *Color and Money: Politics and Prospects for Community Reinvestment in Urban America* (Albany: State University of New York, 2001), p. 4.

⁶ Ibid.

⁷ Richard Lord, *American Nightmare: Predatory Lending and the Foreclosure of the American Dream* (Monroe: Common Courage Press, 2005), p. 40.

⁸ Guy Stuart, *Discriminating Risk: The U.S. Mortgage Lending Industry in the Twentieth Century* (Ithaca: Cornell University Press, 2003), p. 10.

⁹ Amy Hillier, "Spatial Analysis of Historical Redlining: A Methodological Exploration," *Journal of Housing Research*, vol. 14, Issue 1 (2003), p. 139. Online. Available: http://www.fanniemae.foundation.org/programs/jhr/pdf/jhr_1401_hillier.pdf. Accessed: June 28, 2007.

¹⁰ Gregory D. Squires, "The Rough Road to Reinvestment" in *Organizing Access to Capital: Advocacy and the Democratization of Financial Institutions*, p. 8.

¹¹ Amy Hillier, "Spatial Analysis of Historical Redlining: A Methodological Exploration," p. 139.

¹² Ibid., p.138.

¹³ Ibid.

¹⁴ Ibid., and p.140.

¹⁵ Ibid., p. 143.

¹⁶ Ibid.

¹⁷ Ibid.

¹⁸ Ibid.

¹⁹ Ibid.

²⁰ Ibid.

²¹ Ibid., p. 144.

²² Ibid., p. 139.

²³ Ibid.

²⁴ Ibid.

²⁵ U.S. Department of Housing and Urban Development (HUD) and U.S. Department of Treasury (Treasury), *Curbing Predatory Home Mortgage Lending: A Joint Report* (June 2000), p. 53. Online. Available: <http://www.huduser.org>. Accessed: September 20, 2006.

²⁶ Ibid., p. 72.

²⁷ James Carr and Jenny Sheutz, *Financial Services in Distressed Communities: Issues and Answers*, (Fannie Mae Foundation, August 2001). Online. Available: <http://www.fanniemaefoundation.org>. Accessed: July 12, 2006.

²⁸ John Yinger, *Closed Doors, Opportunities Lost: The Continuing Costs of Housing Discrimination* (New York: Russell Sage Foundation, 1995), p. 187.

²⁹ Guy Stuart, *Discriminating Risk: The U.S. Mortgage Lending Industry in the Twentieth Century*, p. 10.

³⁰ Amy Hillier, "Spatial Analysis of Historical Redlining: A Methodological Exploration," p. 142.

³¹ John Yinger, *Closed Doors, Opportunities Lost: The Continuing Costs of Housing Discrimination*, p. 188.

³² Gregory D. Squires, "The Rough Road to Reinvestment" in *Organizing Access to Capital: Advocacy and the Democratization of Financial Institutions*, p. 7.

³³ Stephen Ross and John Yinger, *The Color of Credit: Mortgage Discrimination, Research Methodology, and Fair-Lending Enforcement* (Cambridge: The MIT Press, 2002), p. 31.

³⁴ Ibid.

³⁵ Gregory D. Squires, "The New Redlining," in *Why the Poor Pay More: How to Stop Predatory Lending*, ed. Gregory D. Squires (Westport: Praeger Publishers, 2004), p. 8.

³⁶ John Yinger, *Closed Doors, Opportunities Lost: The Continuing Costs of Housing Discrimination*, p. 188.

³⁷ Ibid., p.190.

³⁸ Ibid.

³⁹ Guy Stuart, *Discriminating Risk: The U.S. Mortgage Lending Industry in the Twentieth Century*, pp. 10-11.

⁴⁰ Ibid., p. 11.

⁴¹ Stephen Ross and John Yinger, *The Color of Credit: Mortgage Discrimination, Research Methodology, and Fair-Lending Enforcement*, p. 30.

⁴² Ibid., p. 33.

⁴³ Guy Stuart, *Discriminating Risk: The U.S. Mortgage Lending Industry in the Twentieth Century*, pp. 192-193.

⁴⁴ Ibid.

⁴⁵ Gregory D. Squires, "The Rough Road to Reinvestment" in *Organizing Access to Capital: Advocacy and the Democratization of Financial Institutions*, p. 8.

⁴⁶ Joe Mariano, "Where the Hell Did Billions of Dollars for Reinvestment Come From?" in *Organizing Access to Capital: Advocacy and the Democratization of Financial Institutions*, p. 33.

⁴⁷ William Apgar, et al., *The 25th Anniversary of the Community Reinvestment Act: Access to Capital in an Evolving Financial Services System* (Cambridge, Mass.: The Joint Center for Housing Studies, March 2002), p. 19. Online. Available: <http://www.jch.harvard.edu/research/crareport.html>. Accessed: June 10, 2007.

⁴⁸ U.S. Federal Reserve Bank, *New Information Reported under HMDA and Its Application in Fair Lending Enforcement* (Washington, D.C., 2005), p. 344. Online. Available: http://www.federalreserve.gov/pubs/bulletin/2005/summer05_hmda.pdf. Accessed: March 1, 2007.

⁴⁹ Joe Mariano, "Where the Hell Did Billions of Dollars for Reinvestment Come From?" in *Organizing Access to Capital: Advocacy and the Democratization of Financial Institutions*, p. 33.

⁵⁰ Gregory D. Squires, "The Rough Road to Reinvestment" in *Organizing Access to Capital: Advocacy and the Democratization of Financial Institutions*, p. 9.

⁵¹ Joe Mariano, "Where the Hell Did Billions of Dollars for Reinvestment Come From?" in *Organizing Access to Capital: Advocacy and the Democratization of Financial Institutions*, p. 33.

⁵² John Yinger, *Closed Doors, Opportunities Lost: The Continuing Costs of Housing Discrimination*, p. 64.

⁵³ Ibid.

⁵⁴ Guy Stuart, *Discriminating Risk: The U.S. Mortgage Lending Industry in the Twentieth Century*, p. 10.

⁵⁵ U.S. Federal Reserve Bank, *New Information Reported under HMDA and Its Application in Fair Lending Enforcement*, p. 344.

⁵⁶ William Apgar, et al., *The 25th Anniversary of the Community Reinvestment Act: Access to Capital in an Evolving Financial Services System*, p. 12.

⁵⁷ Gregory D. Squires, "The Rough Road to Reinvestment" in *Organizing Access to Capital: Advocacy and the Democratization of Financial Institutions*, p. 9.

⁵⁸ Ibid.

⁵⁹ U.S. Federal Reserve Bank, *New Information Reported under HMDA and Its Application in Fair Lending Enforcement*, p. 351 (emphasis in original document).

⁶⁰ Ibid (emphasis in original document).

⁶¹ Ibid., p. 352.

⁶² Ibid., p. 350.

⁶³ Ibid.

⁶⁴ Association of Community Organizations for Reform Now (ACORN), *The High Cost of Credit: Disparities in High-priced Refinance Loans to Minority Homeowners in 125 American Cities* (Chicago, Ill., February 2004), p.1. Online. Available: <http://www.acorn.org>. Accessed: January 28, 2006.

⁶⁵ William Apgar, et al., *The 25th Anniversary of the Community Reinvestment Act: Access to Capital in an Evolving Financial Services System*, p. 12.

⁶⁶ Richard Lord, *American Nightmare: Predatory Lending and the Foreclosure of the American Dream*, p. 182.

⁶⁷ U.S. Federal Reserve Bank, *New Information Reported under HMDA and Its Application in Fair Lending Enforcement*, p. 390.

⁶⁸ Section 801 of Title VIII of the Act of October 12, 1977 (Pub. L. No. 95-128; 91 Stat. 1147), effective October 12, 1977; codified as 12 U.S.C. 2901(a). Online. Available: <http://www.fdic.gov/regulations/laws/rules/6500-2515.html>. Accessed: August 8, 2007.

⁶⁹ U.S. Office of the Comptroller of the Currency Administrator of National Banks, *Community Reinvestment Act Information*. Online. Available: <http://www.occ.treas.gov/crainfo.htm>. Accessed: August 9, 2007.

⁷⁰ Section 801 of Title VIII of the Act of October 12, 1977 (Pub. L. No. 95-128; 91 Stat. 1147), effective October 12, 1977; codified as 12 U.S.C. 2903.

⁷¹ William Apgar, et al., *The 25th Anniversary of the Community Reinvestment Act: Access to Capital in an Evolving Financial Services System*, p. 20.

⁷² Ibid., p. 21.

⁷³ Ibid p. 22 (emphasis in original document).

⁷⁴ Gregory D. Squires, "The Rough Road to Reinvestment" in *Organizing Access to Capital: Advocacy and the Democratization of Financial Institutions*, p. 11.

⁷⁵ Ibid., p. 10.

⁷⁶ Ibid.

⁷⁷ Ibid., p.12.

⁷⁸ Matthew Lee, "Community Reinvestment in a Globalizing World" in *Organizing Access to Capital: Advocacy and the Democratization of Financial Institutions*, p. 144.

⁷⁹ Gregory D. Squires, "The Rough Road to Reinvestment" in *Organizing Access to Capital: Advocacy and the Democratization of Financial Institutions*, p. 18.

⁸⁰ Ibid.

⁸¹ Gregory D. Squires, "Predatory Lending: Redlining in Reverse," *Shelterforce Online*, Issue #139 (January/February 2005), p. 4. Online. Available: <http://www.nhi.org/online/issues/139/redlining.html>. Accessed: July 15, 2007.

⁸² William Apgar, et al., *The 25th Anniversary of the Community Reinvestment Act: Access to Capital in an Evolving Financial Services System*, p. v.

⁸³ Gregory D. Squires, "Predatory Lending: Redlining in Reverse," *Shelterforce Online*, p. 4.

⁸⁴ William Apgar, et al., *The 25th Anniversary of the Community Reinvestment Act: Access to Capital in an Evolving Financial Services System*, p.iii.

⁸⁵ Robert Auerbach, *Deception and Abuse at the Fed: Henry B. Gonzalez Battles the Greenspan Bank* (Austin: University of Texas Press, 2007) (forthcoming). pp. 129-130.

⁸⁶ Ibid.

Chapter 3. Rise of Subprime and Predatory Lending

High-cost or subprime lending was virtually non-existent prior to 1980 because most states had legislated caps on interest rates and fees for home loans. However, beginning in the 1980's, this changed with several key pieces of federal legislation which pre-empted restrictive state banking laws. By the mid 1990's there was strong growth in the subprime lending market. The growth was so robust that the market share of subprime loans doubled from 1995 to 2005 going from 10.2% to 20% respectively¹.

Table 3.1
Total Subprime Loan Originations and Market Share
1995 – 2005

<u>Year</u>	<u>Total Subprime Originations (billions)</u>	<u>Total Subprime Market Share</u>
1995	\$65.0	10.2%
1996	\$96.8	12.3%
1997	\$124.5	14.5%
1998	\$150.0	10.3%
1999	\$160.0	12.2%
2000	\$138.0	13.2%
2001	\$173.3	8.4%
2002	\$213.0	7.9%
2003	\$332.0	8.8%
2004	\$530.0	19.0%
2005	\$665.0	20.0%

Adapted from: Federal Reserve Bank of St. Louis, "The Evolution of the Subprime Mortgage Market," by Souphala Chomsisengphet and Anthony Pennington-Cross. *Review* (January/February 2006), p. 37. Online. Available: <http://www.research.stlouisfed.org/publications/review>; and Spotlight on Financial Services, *Forecasts and Statistics* (March 2005). Online. Available: <http://www.spotlightonfinance.org>; and Center for Responsible Lending, *Latino Homes at Risk*, 2005. Online. Available: <http://www.responsiblelending.org>.

It should be noted, however, that until recently the vast majority of subprime loans were refinances. In 2000 HUD reported that 80% of all subprime originations were subprime.² However, even in 2006, subprime refinance loans accounted for 56% of all subprime originations.³ Even though proponents of the subprime lending market claim that it has created the opportunity of homeownership for people who would otherwise be shut out of the housing market due to blemished credit, it is clear that most subprime lending is for refinancing and consolidating consumer debt and not for the purchase of a home.

Federal Banking Deregulation and Tax Reform Open Door to Subprime Lending

Depository Institutions Deregulation Monetary Control Act of 1980

The Depository Institutions Deregulation Monetary Control Act of 1980 (DIDMCA) expanded the generous variable rate ceiling previously established for national banks to all federally insured banks and thrifts, preempting state usury standards for “interest, discount points, finance charges, or other charges” on loans secured by first mortgages on homes.⁴ Previously, banks could only avoid state usury laws by issuing second lien loans. However, with the advent of DIDMCA, all lenders could now offer higher interest rates on home refinance and equity lines of credit as well.⁵

Alternative Mortgage Transaction Parity Act of 1982

Along similar lines, the Alternative Mortgage Transaction Parity Act of 1982 (AMTPA) further loosened lending regulations for non-national banks to permit the use of variable interest rate loans and loans with balloon payments.⁶

Tax Reform Act of 1986

By ending the tax deduction previously available for consumer loans, the Tax Reform Act of 1986 (TRA) created significant incentive for homeowners to convert consumer debt into mortgage debt since mortgage interest became the sole form of tax-deductible interest.⁷ As a result, this made even subprime mortgage debt cheaper than consumer debt for many homeowners.⁸

Gramm-Leach-Bailey Financial Services Modernization Act of 1999

The Gramm-Leach-Bailey Financial Services Modernization Act of 1999 (GLBA), which allowed consolidation between banking, insurance, and securities institutions, made it easier for each of these types of entities to enter into each other's lines of business. Ultimately, this led to a significant reduction in the percentage of mortgage loans made by commercial banks and savings institutions, with the gap being filled by mortgage banking affiliates of depository institutions, independent mortgage banks, insurance companies, and other institutions not regulated by the federal government, including subprime and predatory lenders.⁹

Securitization Facilitates Subprime Lending

Creation of the Mortgage-Backed Security

In addition to the loosening of lending regulations under the federal legislation discussed above, another major factor in the rise of subprime lending was the rapid increase in popularity of the mortgage-backed security in the 1980's and 1990's.¹⁰

Interest in the mortgage-backed security, a tradable asset consisting of a bundled stream of mortgage payments from multiple borrowers plus the value of the mortgaged homes, was piqued in the 1980's with regard to prime mortgage loans as a result of a number of factors, including the Secondary Mortgage Market Enhancement Act of 1984, which removed many of the direct costs to organizations interested in securitizing their home loans, and the TRA, which permitted multiple classes of securities to be issued from the same pool of mortgages without triggering unfavorable tax treatment.¹¹

By the mid-1990's, investors became comfortable enough with the reliability of returns on mortgage-backed securities to begin to be interested in the higher risk subprime mortgage-backed security.¹² Subsequently, both the subprime lending market and the trading of subprime MBS skyrocketed. In 1994, \$11 billion in subprime MBS were sold, representing 32% of the total value of subprime mortgages for the year.¹³ By 2003, \$203 billion in subprime MBS were sold, representing 61% of the total value of

subprime mortgages for the year, a record of \$332 billion in subprime originations, an 18-fold increase in nine years.¹⁴

Table 3.2
Subprime Loan Securitization 1994-2003

<u>Year</u>	<u>Subprime loans made</u>	<u>Subprime loans turned into securities</u>	<u>Percentage of subprime loans securitized</u>
1994	\$35 billion	\$11 billion	32%
1995	\$65 billion	\$18 billion	28%
1996	\$97 billion	\$38 billion	40%
1997	\$125 billion	\$66 billion	53%
1998	\$150 billion	\$83 billion	55%
1999	\$160 billion	\$60 billion	37%
2000	\$138 billion	\$56 billion	41%
2001	\$173 billion	\$76 billion	44%
2002	\$241 billion	\$133 billion	55%
2003	\$332 billion	\$203 billion	61%

Source: Richard Lord, *American Nightmare: Predatory Lending and the Foreclosure of the American Dream* (Monroe: Common Courage Press, 2005), p. 20.

The increased liquidity generated by the use of MBS allowed non-bank entities to emerge as the primary providers of subprime loans.¹⁵ From 1993 to 1999, the number of HUD-identified subprime lenders rose from 49 to 251.¹⁶

Prime, Subprime and Predatory Lending

The home mortgage market can be broken down into three components: (1) the prime market, which services low risk borrowers with strong credit; (2) the subprime market, which services higher risk borrowers who lack strong credit for one reason or another; and (3) the predatory market, which targets unsophisticated borrowers who are for various reasons vulnerable to predatory, hard-sell tactics.¹⁷ What sets predatory lenders apart is that legitimate subprime lenders seek conduct business with borrowers on a more or less fair basis, while predatory lenders knowingly seek to do business with subprime borrowers on an exploitative basis.¹⁸

Predatory Practices

Predatory lending encompasses a variety of onerous practices that result in net harm to the borrower such as delinquency, foreclosure, and bankruptcy.¹⁹ In 2001 the Coalition for Responsible Lending estimated that predatory lending cost borrowers \$9.1 billion dollars per year.²⁰ A predatory loan may include one or more of the attributes described below.

High Interest Rates

Although predatory loans are commonly associated with a high interest rate, a higher than prime interest rate alone does not necessarily make a loan “predatory,” since it is generally acknowledged that there are legitimate subprime loans designed for borrowers with impaired credit or similar issues that disqualify them from receiving a conventional prime loan.²¹ In theory, charging an interest rate that is higher than the prevailing and competitive rate is reasonable to compensate for the additional risk posed by the borrower’s impaired credit.²²

However, there is evidence that actual credit losses play only a small role in the interest rate paid by subprime borrowers. In fact, actual losses are typically less than one percent of the outstanding loan balance per annum.²³ It is therefore only partly correct to state that subprime mortgage rates are higher because the credit risk is higher than in the prime market. More specifically, rates from 2-10% higher cannot be accounted for by costs associated with higher credit risk.²⁴

Accordingly, one way to classify a subprime loan as “predatory” is if the interest and fees charged exceed what is required to offset any added risk of lending to a borrower with imperfect credit.²⁵ Further, a subprime loan may also be classified as “predatory” if it has a combination of “predatory” attributes, not merely a high interest rate.²⁶ By comparison, a prime rate loan can also be “predatory,” depending on what other attributes it has.²⁷

Excessive Points and Fees

It has been estimated that the average subprime borrower pays a fee equal to 7% of the loan amount,²⁸ compared with an average fee of 1.1% for conventional prime rate borrowers.²⁹ Since the higher interest rate associated with subprime loans more than offsets the corresponding credit losses,³⁰ there is no clear justification for charging higher fees.³¹ It has been estimated that exorbitant fees (defined as fees greater than 5% of the loan amount plus any lender or third party refinancing fees where there is no tangible net benefit to the borrower) cost 750,000 families \$1.8 billion each year.³²

Similarly, “points” charged to the subprime borrower, commonly in the 5 to 8% range, do not appear to be related to covering the cost of increased credit risk, nor to the “buying down” of interest rates.³³ Instead, in the subprime market, “points” are used primarily to reward sales efforts and cover higher loan origination costs, going mainly to mortgage brokers and retail lenders.³⁴

Prepayment Penalties

It has been estimated that 80% of subprime loans contain prepayment penalties, compared to 2% in the competitive conventional prime market.³⁵ Typically, subprime prepayment penalties extend up to 5 years.³⁶ A prepayment penalty may be considered predatory in that it locks the borrower into a higher interest rate even though the borrower might improve his or her credit rating or ability to pay prior to expiration of the prepayment penalty period, in effect prohibiting the borrower from refinancing at a lower interest rate and saving perhaps thousands of dollars in interest payments. Nevertheless, more than 50% of subprime loans are typically pre-paid in less than 5 years.³⁷

It would be rational to choose a loan with a prepayment penalty only if the borrower were certain he or she would not be able to refinance at a better rate during the penalty period.³⁸ The 80% prevalence of prepayment penalty loans in the subprime market suggests borrowers may lack complete information.³⁹ It is also inexplicable why so many borrowers in the subprime market “choose” such penalties compared to so few in the prime market.⁴⁰

In the end, the primary economic impact of prepayment penalties in the subprime market is to benefit the lender at the expense of the borrower, and the prevalence of this pattern has led to the suggestion that such penalties are “no more than deferred fees that investors fully expect to receive and borrowers never expect to pay.”⁴¹ It is estimated that subprime prepayment penalties cost 850,000 families \$2.3 billion each year.⁴²

Balloon Payments

A balloon payment is due at the end of a fixed-rate loan term when regular monthly installments have not fully paid down the principal amount.⁴³ In 1999, about 10% of subprime loans had a balloon payment.⁴⁴

A borrower who takes out a loan with a balloon payment can benefit from lower monthly payments in the short run.⁴⁵ However, in the high-cost market, borrowers must typically refinance in order to cover the balloon payment or face default.⁴⁶ This creates a situation in which predatory lenders are able to offer refinancing with high points, fees, and closing costs.⁴⁷ Such borrowers have little alternative but to accept the terms offered, resulting in higher payments and greater opportunity for lenders to “flip” loans.⁴⁸

The HUD Taskforce has reported that balloon payment loans in the subprime market are problematic both because there is a tendency for lenders to fail to disclose and for borrowers to fail to know about or understand the consequences of such loan terms.⁴⁹

Flipping

Loan flipping refers to the repeated refinancing of a home loan through which, without benefit to the borrower, the lender profits from high origination fees, points, closing costs, prepayment penalties, and other costs, thereby steadily eroding the borrower’s equity in their home.⁵⁰ It is also referred to as “equity stripping.” Refinancing may be offered as a way for the borrower to “catch up” on delinquent payments,⁵¹ or may be offered as a way to “fix” the lender’s current loan terms, which may include an adjustable rate, balloon payment, or other onerous terms.⁵² In combination, a balloon payment and prepayment penalty can operate as a “double whammy” in which the balloon payment drives the borrower to refinance, and the

prepayment penalty makes it very expensive to do so,⁵³ making the flip even more profitable for the lender.

Negative Amortization

Negative amortization is another equity stripping practice. In a negatively amortized home loan, the monthly payment is less than the amount of interest due, causing the principal to actually increase rather than decrease over time,⁵⁴ resulting in a corresponding loss of equity in the home. Although quantified data regarding the prevalence of negative amortization in the subprime market is lacking,⁵⁵ anecdotal evidence suggests some unwitting homeowners have ended up with a negatively amortizing mortgage.⁵⁶ Given the lack of benefit or economic rationale for such a practice (outside the limited context of a “reverse mortgage” or similar practice designed to purposefully convert home equity into an income stream), its use may rely on lack of understanding by the borrower or deceptive practices by the lender.⁵⁷

A close cousin to negative amortization is the zero amortization or “interest-only” loan in which the borrower makes a minimum payment for a period of time, covering only interest due, and contributing nothing towards the principal.⁵⁸ After five or ten years, payments are typically accelerated to cover both interest and principal, resulting in a monthly payment amount that virtually ensures default.⁵⁹ Recent television advertisements have ironically referred to this type of loan as a “smart loan.”

Single Premium Credit Insurance

There are four common types of home loan credit insurance: life, disability, unemployment, and property.⁶⁰ Credit insurance pays off the loan balance in the event of the borrower’s death, disability, etc.⁶¹ Typically, such insurance covers only the first five to seven years of the loan period.⁶²

Although credit insurance paid on a monthly basis may have some value for the borrower, single premium credit insurance generally does not.⁶³ This is because the single premium for the entire life of the policy is collected up front and simply added to the financed loan amount and therefore strips equity from the homeowner.⁶⁴ The

borrower then pays interest on this amount for the life of the loan and typically has not even begun to reduce the principal balance by the time the coverage expires.⁶⁵ As a result, when a borrower moves or refinances after the insurance expires, the entire amount of the premiums is essentially stripped out of the borrower's home equity.⁶⁶ Further, lump-sum insurance products, when financed into the cost of the loan, provide no actuarial benefit to the borrower.⁶⁷

A group of subprime lenders recently self-reported a single premium credit insurance penetration rate of 50-57%.⁶⁸ By comparison, for conventional loans, the penetration rate has been found to be about 6%.⁶⁹

Lenders have a strong incentive to push single premium credit insurance since they receive, on average, a 30% commission, and have no incentive to seek out providers with the lowest premiums.⁷⁰

Further, consumers report a number of abusive practices associated with credit insurance, including being misled to believe such insurance was required for the loan to be approved, being misled that the insurance lasted for the life of the loan, and in some cases not even being informed such insurance was included in the loan transaction.⁷¹

It has been estimated financed credit insurance costs 500,000 families \$2.1 billion yearly.⁷²

Mandatory Arbitration Clauses

A home loan may include, as a precondition to receiving the loan, a mandatory arbitration clause. A mandatory arbitration clause forces the borrower to submit any dispute regarding the loan to binding arbitration rather than litigation in court before a judge or jury.⁷³ There are currently no legal restrictions on the use of arbitration clauses in home loan agreements.⁷⁴ Arbitration clauses in high-cost home loans operate to the borrower's detriment by depriving the borrower of a jury trial before his or her peers.⁷⁵ Such clauses may also contain other disadvantageous terms that, for example, limit the borrower's right to factual discovery, require the borrower to bear the entire cost of the arbitration, require the arbitration to be held in an inconvenient distant location, preclude

class actions, and deny or delay the opportunity for emergency relief such as a restraining order or preliminary injunction.⁷⁶

Mortgage Brokers / Yield Spread Premiums

A yield spread premium is a cash bonus paid by a lender to a mortgage broker for getting a borrower to sign up for a loan with an interest rate higher than the best rate for which the borrower is actually qualified.⁷⁷ Typically, the higher the interest rate, the higher the bonus received by the broker.⁷⁸ It amounts to a legal “kickback” to mortgage brokers and it is estimated that they originate 45% of all mortgage loans and up to 71% of subprime loans⁷⁹.

Although the rationale offered to justify this practice is that it helps borrowers who otherwise could not afford upfront closing costs by spreading such costs over time through the higher interest rate,⁸⁰ the fact is that borrowers do not benefit from a yield spread premium—typically receiving 25 cents of benefit for each dollar paid.⁸¹

The use of yield spread premiums is widespread in the subprime market, involving hundreds of mortgage lenders and thousands of brokers, and reportedly may be found in as many as 90% of all subprime loans.⁸² Further, yield spread premiums are commonly used in conjunction with pre-payment penalties, which the lender imposes to ensure recovery of the cost of the premium.⁸³

Yield spread premiums are estimated to cost borrowers \$3 billion a year.⁸⁴

Targeting

Targeting is a predatory practice because it method by which lenders reverse redline and/or steer borrowers to higher priced mortgage loans.⁸⁵ According to HUD, high cost lenders specifically target and aggressively solicit homeowners (for refinance loans) in predominantly lower-income and minority communities, generally where there may be a lack of access to mainstream financial services.⁸⁶

Outright Fraud

Most of the predatory practices described in this paper are not illegal. However, predatory lending may also involve practices that constitute outright fraud and are clearly illegal, including such practices as misleading or incomplete disclosure of loan terms,⁸⁷ bait-and-switch tactics,⁸⁸ improper solicitation of fraudulent gift letters and under capitalized co-signers, charging discount points without reducing the interest rate,⁸⁹ falsifying information on loan forms (e.g., borrower's income information),⁹⁰ backdating documents,⁹¹ and even forging signatures.⁹²

Outright fraud may also involve more elaborate practices such as "asset flipping," in which appraisers, lenders, investors, and real estate brokers conspire in a scheme to purchase a dilapidated property, perform cosmetic repairs, over-appraise the improvements, and resell at an unjustly inflated price, forcing the buyer to take on more debt than the property is worth.⁹³ To complete the scheme, a buyer is selected who cannot actually afford the loan terms offered, so the property can be foreclosed upon and the flipping cycle can begin all over again.⁹⁴

¹ Federal Reserve Bank of St. Louis, "The Evolution of the Subprime Mortgage Market," by Souphala Chomsisengphet and Anthony Pennington-Cross. *Review* (January/February 2006), p. 37. Online. Available: <http://www.research.stlouisfed.org/publications/review>. Accessed: August 24, 2007.

²U.S. Department of Housing and Urban Development (HUD) and U.S. Department of Treasury (Treasury), *Curbing Predatory Home Mortgage Lending: A Joint Report* (June 2000), p. 2. Online. Available: <http://www.huduser.org>. Accessed: September 20, 2006.²

³ Testimony of Michael D. Calhoun, Center for Responsible Lending, before the U.S. House Committee on Financial Services Subcommittee on Financial Institutions and Consumer Credit, Washington, D.C., March 27, 2007. Online. Available: <http://www.responsiblelending.org>. Accessed: October 8, 2007.

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Chapter 4. Disparity Studies

While issues surrounding housing and mortgage lending discrimination resulted in passage of several landmark pieces of legislation that began in the 1980's which made subprime lending possible, the topic did not spark the interest of researchers until the 1990s.¹

A significant precursor to this body of research was a Pulitzer-Prize-winning series of articles by reporter Bill Dedman, entitled "The Color of Money," published in the *Atlanta Journal Constitution*.² These newspaper articles documented local lending trends that appeared to evidence discrimination, including the fact that black neighborhoods were receiving relatively little funding for mortgages.³

Another precursor to this body of research was newly available information about lending practices, including race and ethnicity data for individual loan applicants, which was required to be reported under changes made to the Home Mortgage Disclosure Act in 1989.⁴ The data, which revealed loan denial rates by racial and ethnic categories as well as geographic location, first became available in 1991.⁵

The Federal Reserve Bank of Boston Study

In 1992, the Federal Reserve Bank of Boston published a watershed study of racial discrimination in mortgage lending.⁶ This study, commonly referred to as the "Boston-Fed Study," used econometric methods and HMDA and other data to model lending decisions.⁷ Looking at white, Hispanic, and Black loan applicants within comparable economic classes, the study found a wide disparity in the rate at which loans were being denied for each ethnic group, namely whites were denied least often and Blacks were denied most often.⁸

More specifically, the Boston Fed Study found that "even after controlling for financial, employment, and neighborhood characteristics, Black and Hispanic mortgage

applicants in the Boston metropolitan area are roughly 60% more likely to be turned down [for a loan] than whites.”⁹

The original Boston Fed Study attracted much attention and controversy, including commentary from both defenders and detractors, as well as further study and analysis of the data.¹⁰ In response to the comments and criticism generated by the Boston Fed Study, its authors revised and republished it in 1996.¹¹ This time around, they concluded that Black and Hispanic loan applicants were approximately 80% more likely to be rejected for a home mortgage than comparable white applicants.¹²

The Color of Credit

In 2002, researchers Stephen Ross and John Yinger published The Color of Credit, perhaps the most influential re-examination and further exploration of the results of the Boston Fed Study. Based on further analysis of the Boston Fed data, Ross and Yinger concluded that the Boston Fed’s authors did not fully account for variations in underwriting standards across lenders and, as a result, failed to rule out the possibility that minority-white disparities in loan approval might simply reflect such underwriting variations rather than discrimination.¹³

To address this issue, Ross and Yinger re-evaluated the Boston Fed data in conjunction with comparable HMDA data, which included identification of particular loans with particular lenders.¹⁴ This re-assessment led Ross and Yinger to conclude that although underwriting standards did in fact vary across lenders, such variations had no impact on the minority-white disparity in loan approval rates.¹⁵ Thus, Ross and Yinger ultimately concurred in the conclusion that the Boston Fed data provided “strong evidence” of discrimination in mortgage lending.¹⁶

Moreover, Ross and Yinger conclude that the impact of idiosyncratic variations in underwriting standards on the minority-white disparity in loan approval is more likely explained by disparate-impact discrimination than business necessity.¹⁷

Two Steps Back: The Dual Mortgage Market, Predatory Lending, and the Undoing of Community Development

A major limitation of the Boston Fed Study and related studies is that it dealt exclusively with loan denials. It was not until the late 1990s, after significant expansion of the subprime market, that the specific issue of loan pricing discrimination came to the fore.¹⁸

In 1999, Immergluck and Wiles of the Woodstock Institute analyzed HMDA data from 1993 to 1998 for the six county Chicago, Illinois MSA.¹⁹ They found that in predominantly Black neighborhoods, 28% of conventional home purchase loan originations were made by subprime lenders, as compared to 8% in predominantly white neighborhoods.²⁰ Further, in low to moderate income neighborhoods, 22 % of conventional home purchase loan originations were made by subprime lenders, as compared to 7% for upper income neighborhoods.²¹

In addition, they found that in predominantly Black neighborhoods, 53% of home refinance loans were made by subprime lenders, as compared to 9% in predominantly white neighborhoods.²² Further, in low to moderate income neighborhoods, 69% of home refinance loans were made by subprime lenders, as compared to 9% in upper income neighborhoods.²³

However, segmentation of the refinance market was stronger by race than by income, as there was a difference of 41 percentage points between the proportion of refinance loans made by subprime lenders in Black middle income neighborhoods compared to white middle income neighborhoods.²⁴

Additionally, Immergluck and Wiles found that banks, thrifts, and bank-owned mortgage companies were the leading lenders in white neighborhoods whereas independent mortgage companies dominated Black neighborhoods.²⁵ Moreover, the largest prime lenders focused their marketing efforts on white areas whereas the leading lenders in black areas tended not to have a significant marketing presence in white areas.²⁶

Furthermore, multivariate regression analysis confirmed that the racial composition of neighborhoods explained the greatest amount of variation in subprime lending, followed by education level, median home value, and whether the neighborhood was mixed-minority.²⁷

Credit Risk and Mortgage Lending: Who Uses Subprime and Why?

In 2000, in a study commissioned by the Mortgage Bankers Association of America (including subprime lenders), researchers Pennington-Cross, Yezer, and Nichols of the Research Institute for Housing America analyzed data from 39 MSAs in regard to the use of prime, subprime, and FHA financing for home purchase loans.²⁸

This study found that households considered high risk due to blemishes in credit history and high levels of consumer debt were most likely to use subprime financing.²⁹ They found little evidence to support the theory that subprime lenders serve primarily low to moderate income households.³⁰ Rather, their analysis revealed that 48 % of subprime loans were made to moderate and high income borrowers.³¹ They concluded this was because subprime lenders required higher down payments to compensate for poor credit histories or high amounts of consumer debt.³² Consequently, they rejected the theory that subprime lenders concentrate their efforts on or target underserved areas or low to moderate income borrowers as such borrowers tend to lack the savings or assets required by such lenders for higher down payments.³³

Regarding race, however, borrower demographic results indicated that even after controlling for borrower income, debt, and credit history, Black, Hispanic and Native American borrowers were more likely to use FHA and subprime financing than white borrowers.³⁴

The Broken Credit System: Discrimination and Unequal Access to Affordable Loans by Race and Age

The National Community Reinvestment Coalition (NCRC) published their study of subprime lending in 10 metropolitan areas (MSAs) in 2003. The researchers analyzed

HMDA, credit bureau, and U.S. Census Bureau data using regression analysis to predict the level of subprime lending at the census tract level in each of the MSAs.³⁵

Lack of a credit score had a positive impact on the degree of subprime lending in a majority of the MSAs.³⁶ That is, the level of high cost refinance and home purchase lending increased in a statistically significant fashion as the percentage of neighborhood residents with no credit scores increased.³⁷

The median household income of a census tract was statistically significant in 4 of 10 MSAs for both subprime refinance and home purchase lending. The researchers note, however, that the coefficient values were very small. Therefore, the income variable had a small impact on the level of high cost lending in the census tracts.³⁸

Race, however, proved to be the variable that had the most significant impact on the level of high cost lending. The level of refinance subprime lending increased as the percentage of Blacks in a neighborhood increased in 9 of 10 MSAs.³⁹ Even after controlling for risk and housing stock characteristics, the effect of the percentage of Black population on the portion of subprime loans in a census tract was positive in all MSAs.⁴⁰ The same was true in 6 of 10 MSAs with respect to subprime home purchase lending.⁴¹ Similarly, the level of high cost refinance lending increased as the proportion of Hispanics within a census tract increased in 3 of 10 MSAs. However, the proportion of Hispanics in a census tract was positive and significant in only 1 MSA with respect to subprime home purchase lending.⁴²

Neighborhood Distribution of Subprime Mortgage Lending

In 2002, Paul Calem, Kevin Guillen and Susan Wachter published “The Neighborhood Distribution of Subprime Mortgage Lending.” These researchers sought to extend the literature on the spatial distribution of subprime lending with a focus on testing the robustness of previous findings regarding minority and low income concentrations.⁴³ Their study added to the existing literature by analyzing data at the city level in Chicago and Philadelphia in order to identify the factors associated with “in-city” concentrations of subprime loans.⁴⁴ They also studied the spatial concentration of

subprime lending across census tracts within each city by investigating risk measures along with tract demographic variables.⁴⁵ The tract level risk variables included the proportion of individuals that had low credit ratings and the proportion without credit ratings using data from a national credit bureau.⁴⁶ They also analyzed lending at the borrower level using a logit regression where they related whether a loan was subprime to both tract and borrower characteristics.⁴⁷

They reported that the proportion of borrowers with low credit scores and those without credit scores were mostly statistically significant, particularly for refinance loans, indicating that the increased credit risk of individuals in a neighborhood was associated with a larger share of subprime loans.⁴⁸ Therefore, neighborhood risk composition was a strong indicator of the proportion of subprime lending within a tract and the relative likelihood that a borrower would obtain a high cost loan.⁴⁹

With regard to race, the results indicated that in both cities, approximately half of the increase in subprime lending found to be associated with an increase in the percentage of the Black homeowner population across neighborhoods was explained by the “spatial distribution of individual credit ratings.”⁵⁰ However, even after taking account other variables, in both cities there remained a strong geographic concentration of subprime lending in neighborhoods with a large population of Black homeowners.⁵¹ Further, at the individual borrower level, the results indicated that regardless of the neighborhood where they are located, Black borrowers have a “relatively high likelihood of obtaining a subprime rather than a prime loan.”⁵²

Neighborhood Patterns of Subprime Lending: Evidence from Disparate Cities

In 2004, Paul Calem and Jonathan Hershauff of the Board of Governors of the Federal Reserve, and Susan Wachter of the Wharton School at the University of Pennsylvania, followed up on the 2002 Calem, Guillen and Wachter report. The 2004 study, “Neighborhood Patterns of Subprime Lending: Evidence from Disparate Cities,” estimated models of prime versus subprime allocation of loans for seven cities (Atlanta,

Baltimore, Chicago, Dallas, Los Angeles, New York, and Philadelphia) in 1997 and 2002.⁵³

These researchers found that neighborhood credit quality and property risk, when statistically significant, were positively associated with high cost refinance loans.⁵⁴ The neighborhood credit quality variables were more strongly related to relative likelihood of a subprime loan origination in 1997 than in 2002.⁵⁵ There was also a strong association between the capitalization rate and high cost lending in a subset of cities, from which the researchers speculate that subprime lenders, to some degree, may be extending credit in areas where prime lenders were hesitant to due to risks associated with property value.⁵⁶

Additionally, in each city and year, the neighborhood level of educational attainment, neighborhood median income, and borrower income, when statistically significant, were inversely associated with subprime borrowing.⁵⁷ In 2002, in every city, the relative chance of a subprime origination was inversely related to the proportion of neighborhood residents with a bachelor's degree. This was the case in only 3 of the 7 cities in 1997.⁵⁸ Moreover, all else being equal (controlling for other variables), education levels were consistently (inversely) related to subprime lending in all 7 cities in both years.⁵⁹

With regard to race, these researchers found that in each of the 7 cities, for both years, minority status (Black, Hispanic or Asian) was significantly related to the level of high cost lending.⁶⁰

Subprime Lending: Neighborhood Patterns Over Time

In April of 2005, Jonathan Hershaff, Susan Wachter, and Karl Russo presented further results, presumably from the 2004 study discussed above, in an unpublished report entitled "Subprime Lending: Neighborhood Patterns Over Time" at the *Promises and Pitfalls Conference* of the Federal Reserve System's Fourth Community Affairs Research Conference.⁶¹ They reported the results from their research in regard to changing patterns of subprime lending in 7 major U.S. cities between 1997 and 2002.⁶²

Overall, they found that high cost lending had grown significantly over the 5-year period, particularly in areas with large Hispanic concentration as well as in areas with lower levels of education, but had expanded less in low-income areas than elsewhere.⁶³

Lower median income had a lower correlation with subprime lending in 2002 than in 1997.⁶⁴ In 2002, a zip code area with a 10% higher median family income had a 50% higher growth rate in subprime originations, when all other demographic variables were controlled for.⁶⁵ In city-level regressions, the coefficients of low area income changed from uniformly positive and significant in 1997 to low levels of significance in 2002.⁶⁶ This result suggests that, all else being equal, low-income areas had become less attractive to subprime lenders and neighborhood risk measures had become more significant in 2002.⁶⁷

An area's level of educational achievement, holding all other variables constant, was consistently a significant determinant of the number of subprime originations.⁶⁸ In 2002, the variable for those with a bachelor's degree was strongly inversely correlated with subprime lending over time. At the zip code level, a 20 percentage point increase of individuals with a bachelor's degree was associated with a nearly 200 percentage point reduction in the rate of subprime lending growth.⁶⁹

With respect to race/ethnicity, in the city level regressions, the significance of minority composition in relation to the level of high cost lending in the area increased over time.⁷⁰ Subprime loan growth was higher in areas with more Hispanic households.⁷¹ At the zip code level, an increase in the Hispanic population from 10% to 20% was associated with a 70% higher subprime growth rate in that zip code area.⁷² Black households, holding other variables constant, continued to be strongly associated with subprime lending in 2002.⁷³

Subprime Lending and the Border

Risk or Race? Racial Disparities in Subprime Mortgage Lending 2002

Analysis of data from studies that included Border cities reveals that subprime lending occurs at a very high rate on the Border. The largest such study, Risk or Race:

Racial Disparities in Subprime Mortgage Lending, was published by the Center for Community Change in 2002. This study, like others, found that Black and Hispanics were disproportionately represented in the subprime home refinance mortgage market.⁷⁴ Further, this study found that the disparity between white and other minority borrowers grew at upper-income levels and was greater for higher-income Black homeowners than for lower-income white homeowners.⁷⁵

The study was based on 2000 HMDA data for refinance loans from 331 metropolitan statistical areas (MSAs), 27 of which were in Texas. Analysis of data from the 4 Border MSAs squarely established the region as the leader in subprime refinance lending in 2000 with a rate of 42.2%⁷⁶ In other words, among all refinance loans that were originated on the Border, 42.2% were subprime.

Table 4.1
Subprime Home Refinance Loan Incidence in Border MSAs 2000

	<u>Rank</u>	<u>Total Refinance Loans</u>	<u>Total Subprime Loans</u>	<u>Percent Subprime</u>
El Paso	1	1767	845	47.8
Laredo	3	342	155	45.3
McAllen ⁷⁷	18	1345	506	37.6
Brownsville ⁷⁸	<u>29</u>	<u>795</u>	<u>286</u>	<u>35.9</u>
		4249	1792	42.2%

Adapted from: Calvin Bradford, *Risk or Race? Racial Disparities and the Subprime Refinance Market*. (Washington, D.C.: Neighborhood Revitalization Project of the Center for Community Change, May 2002), p. 28. Online. Available: <http://www.communitychange.org>.

The frequency of subprime refinance lending on the Border was 60% higher than the study's overall U.S. sample rate (national urban total for all 331 MSAs) of 25.3%.⁷⁹ The probability of such an origination in El Paso, with an incidence of 47.8%, and Laredo with an incidence of 45.3%, was almost twice as high. McAllen's rate was 50% higher than that for the U.S., and in Brownsville, a noteworthy 1 in 3 (36%) originations were high-cost.

The remaining Texas cities also had a high degree of subprime lending, as 22 of the 23 MSAs had a rate higher than that of the overall sample. Bryan-College Station was the sole exception, where only 18.7% of the originations were subprime.

Table 4.2
Home Refinance Subprime Loan Incidence in Texas MSAs 2000

	<u>Rank</u>	<u>Total Refinance Loans</u>	<u>Total Subprime Loans</u>	<u>Percent Subprime</u>
Corpus Christy	2	1061	497	46.8
Kileen/Temple	4	683	306	44.8
Beaumont/P.Arthur	5	1160	516	44.5
San Antonio	8	5270	219	41.9
Galveston/Tex City	10	944	393	41.6
Victoria	20	220	82	37.3
Houston	30	14552	5195	35.7
Sherman/Dennison	34	509	179	35.1
Amarillo	41	961	328	34.1
Lubbock	45	711	241	33.9
Brazoria	50	829	277	33.4
Wichita Falls	57	412	135	32.4
Texarkana	65	463	148	31.9
San Angelo	71	293	91	31.1
Dallas	75	13276	4049	30.5
Longview/Marshall	78	651	198	30.4
Tyler	94	540	158	29.3
Austin/San Marcos	113	5709	1599	28.0
Odessa/Midland	116	663	185	27.9
Waco	117	564	157	27.8
Ft.Worth/Arlington	143	6485	180	26.1
Abeline	144	292	76	26.0
Bryan-Coll. Station	259	<u>3174</u>	<u>594</u>	<u>18.7</u>
		59,422	15,803	26.6%

Adapted from: Calvin Bradford, *Risk or Race? Racial Disparities and the Subprime Refinance Market*. (Washington, D.C.: Neighborhood Revitalization Project of the Center for Community Change, May 2002), pp. 28-34. Online. Available: <http://www.communitychange.org>

However, the subprime penetration rate for non-border Texas MSAs was substantially lower than that on the Border, as Border borrowers were given high cost loans 58% more frequently than their non-Border Texas counterparts.

ACORN Research

The Association of Community Organizations for Reform Now (ACORN), the largest community organization of low and moderate income families, has also published a number of reports on home mortgage lending. Their report, *Separate and Unequal: Predatory Lending in America* issued in 2004 analyzed 2002 HMDA conventional home purchase and refinance mortgage data. The report compiled data from 7,700 lending institutions and examined this data for the nation as a whole and for 117 MSAs.⁸⁰ Included in the sample were nine Texas cities, three of which were in the Border region.

Conventional Home Mortgages

For conventional home purchase loans, the study reported a national subprime lending rate of 10.3%. The Border region had a higher rate of 11.4%.

Table 4.3
Conventional Home Purchase Subprime Loan Incidence for Border MSAs 2002

	<u>Total Conventional Home Purchase Loans</u>	<u>Total Subprime Loans</u>	<u>Percent Subprime</u>
Brownsville ⁸¹	1927	175	9.8
El Paso	3179	461	14.5
Laredo	<u>1042</u>	<u>63</u>	<u>6.0</u>
	6148	699	11.4%

Adapted from: Association of Community Organizations for Reform Now (ACORN), *Separate and Unequal: Predatory Lending in America*, (Chicago, Ill., February 2004). Summary of Findings for each MSA. Online. Available: <http://www.acorn.org>.

Among Border MSAs, two of three had subprime lending rates lower than the study's overall rate of 10.3%. Laredo had the lowest incidence of such loans with a rate of 6.0%, followed by Brownsville where 9.8% of all originations were subprime. By

contrast, El Paso's subprime rate was more than twice as high as Laredo's with a rate of 14.5%

There were six non-Border Texas cities in the 331MSA sample with an overall subprime lending rate just below that for the Border region at 11.1%.

Table 4.4
Conventional Home Purchase Subprime Loan Incidence for Texas MSAs 2002

	<u>Total Conventional Home Purchase Loans</u>	<u>Total Subprime Loans</u>	<u>Percent Subprime</u>
Austin	17,674	1,461	8.3
Corpus Christi	2,194	197	9.0
Dallas	46,840	5,509	11.8
Ft. Worth/Arlington	20,222	2,306	12.5
Houston	54,458	5,908	10.8
San Antonio	<u>12,589</u>	<u>1,708</u>	<u>13.6</u>
	153,977	17,089	11.1%

Adapted from: Association of Community Organizations for Reform Now (ACORN), *Separate and Unequal: Predatory Lending in America*, (Chicago, Ill., February 2004). Summary of Findings for each MSA. Online. Available: <http://www.acorn.org>.

Among Texas MSAs, four (Houston, Dallas, Ft. Worth/Arlington, and SanAntonio) had higher subprime lending rates than the national rate of 10.3%. Austin had the lowest subprime incidence with a rate of 8.3%, and San Antonio had the highest with a rate of 13.6%.

Refinance Loans

With respect to refinance loans, in the overall national sample, one in ten (10.4%) were subprime.⁸² The rate of subprime refinance originations on the Border, however, was over 70% higher (18.0%). Further, the Border rate was twice as high as the total rate for Texas MSAs (9.2%).

Table 4.5
Conventional Home Refinance Subprime Loan Incidence for Border MSAs 2002

	Total Refinance <u>Loans</u>	Total Subprime <u>Loans</u>	Percent <u>Subprime</u>
Brownsville	1,679	307	18.3
El Paso	3882	698	18.0
Laredo	<u>866</u>	<u>153</u>	<u>17.7</u>
	6427	1158	18.0%

Adapted from: Association of Community Organizations for Reform Now (ACORN), *Separate and Unequal: Predatory Lending in America*, (Chicago, Ill., February 2004). Summary of Findings for each MSA. Online. Available: <http://www.acorn.org>.

For all the Border MSAs, at least one in six refinance originations (18%) were subprime. Laredo had the lowest rate at 17.7%, and both the Brownsville and El Paso rates were only slightly higher, at 18.3% and 18.0%, respectively.

The overall rate of subprime originations for Texas MSAs was 11.1%, compared to the Border region, which had a rate of 18.0%.

Table 4.6
Conventional Home Refinance Subprime Loan Incidence for Texas
MSAs 2002

	Total Refinance <u>Loans</u>	Total Subprime <u>Loans</u>	Percent <u>Subprime</u>
Austin/San Marcos	28,321	2,675	9.4
Corpus Christie	2,451	356	14.5
Dallas	63,784	6,346	10.0
Ft. Worth/Arlington	26,060	2,602	10.0
Houston	57,786	7,454	12.9
San Antonio	<u>15,739</u>	<u>2,190</u>	<u>13.9</u>
	194,141	21,623	11.14%

Adapted from: Association of Community Organizations for Reform Now (ACORN), *Separate and Unequal: Predatory Lending in America*, (Chicago, Ill., February 2004). Summary of Findings for each MSA. Online. Available: <http://www.acorn.org>.

Austin had the lowest subprime lending rate at 9.4%, and San Antonio the highest at 13.9%.

Further, consistent with the trends identified in other studies, this study found that minority borrowers and low-income borrowers were more likely to receive a subprime home purchase loan or refinance loan than white and higher-income borrowers.⁸³

Conclusion

In summary, the studies described above, which represent only a small portion of the total research conducted on mortgage lending over the past fifteen years, uniformly conclude that racial/ethnic and socio-economic disparities are undeniably at play in the current mortgage lending market. Further, the research generally suggests that although the overt discrimination formerly prevalent in the industry has been legislatively banned, in its wake minority and lower income borrowers continue to experience unequal access to credit and pricing discrimination in the home lending arena. Further, there is evidence of a high rate of subprime lending on the Border.

¹ Stephen Ross and John Yinger, *The Color of Credit: Mortgage Discrimination, Research Methodology, and Fair-Lending Enforcement* (Cambridge: The MIT Press, 2002), p. 3.

² Ibid.; and Gregory D. Squires and Sally O'Conner, *Color and Money: Politics and Prospects for Community Reinvestment in Urban America* (Albany, State University of New York Press 2001), p. 1-2.

³ Stephen Ross and John Yinger, *The Color of Credit: Mortgage Discrimination, Research Methodology, and Fair-Lending Enforcement*, p. 3.

⁴ Ibid.

⁵ Ibid.

⁶ Guy Stuart, *Discriminating Risk: The U.S. Mortgage Lending Industry in the Twentieth Century* (Ithaca: Cornell University Press, 2003), p. 11.

⁷ Ibid.

⁸ Ibid., p. 11-12.

⁹ Stephen Ross and John Yinger, *The Color of Credit: Mortgage Discrimination, Research Methodology, and Fair-Lending Enforcement*, p. 4, quoting Munnell, et al., 1992, p. 2.

¹⁰ Guy Stuart, *Discriminating Risk: The U.S. Mortgage Lending Industry in the Twentieth Century*, p. 12.

¹¹ Stephen Ross and John Yinger, *The Color of Credit: Mortgage Discrimination, Research Methodology, and Fair-Lending Enforcement*, p. 4.

¹² Ibid., p. 5.

¹³ Ibid., p. 12.

¹⁴ Ibid.

¹⁵ Ibid.

¹⁶ Ibid.

¹⁷ Stephen Ross and John Yinger, *The Color of Credit: Mortgage Discrimination, Research Methodology, and Fair-Lending Enforcement*, p. 212.

¹⁸ Federal Reserve Bank of St. Louis, "The Evolution of the Subprime Mortgage Market," by Souphala Chomsisengphet and Anthony Pennington-Cross. *Review* (January/February 2006), p. 36-37. Online. Available: <http://www.research.stlouisfed.org/publications/review/06/01/chompenncross.pdf>. Accessed: August 24, 2007.

¹⁹ Daniel Immergluck and Marti Wiles, *Two Steps Back: The Dual Mortgage Market, Predatory Lending, and the Undoing of Community Development* (Chicago, Ill.: Woodstock Institute, 1999), p. ii. Online. Available: <http://www.woodstockinst.org>. Accessed: November 21, 2006.

²⁰ Ibid., p. 18.

²¹ Ibid.

²² Ibid., p. 20.

²³ Ibid.

²⁴ Ibid., p. 26.

²⁵ Ibid., p. 30.

²⁶ Ibid., p. 31.

²⁷ Ibid., p. 26.

²⁸ Pennington-Cross, et al., *Credit Risk and Mortgage Lending: Who Uses Subprime and Why?* Research Institute for Housing America, working paper No. 00-03 (Arlington, Va., September 2000), p. 3. Online. Available: <http://www.housingamerica.org>. Accessed: July 18, 2006.

²⁹ Ibid., p. 16.

³⁰ Ibid.

³¹ Ibid.

³² Ibid.

³³ Ibid., p. 17.

³³ Ibid., p. 17.

³⁴ Ibid., p. 13.

³⁵ The National Community Reinvestment Coalition, *The Broken Credit System: Discrimination and Unequal Access to Affordable Loans by Race and Age – Subprime Lending in Ten Large Metropolitan Areas* (November 2003), p. 20. Online. Available: <http://www.ncrc.org>. Accessed: November 2, 2006.

³⁶ Ibid.

³⁷ Ibid.

³⁸ Ibid., p. 33.

³⁹ Ibid., p. 7.

⁴⁰ Ibid., p. 32.

⁴¹ Ibid., p. 31.

⁴² Ibid., p. 32.

⁴³ Paul Calem, Kevin Gillen, and Susan Wachter, "Neighborhood Distribution of Subprime Mortgage Lending," October 2002, p.1 (preliminary draft). Cited with the permission of Susan Wachter. Online. Available: <http://www.realestate.wharton.upenn.edu/pdf/404.pdf>. Accessed: June 24, 2007.

⁴⁴ Ibid.

⁴⁵ Ibid.

⁴⁶ Ibid.

⁴⁷ Ibid., p. 2.

⁴⁸ Ibid., p. 11.

⁴⁹ Ibid., p. 14.

⁵⁰ Ibid.

⁵¹ Ibid.

⁵² Ibid.

⁵³ Paul Calem, Jonathan Hershaff, and Susan Wachter, "Neighborhood Patterns of Subprime Lending: Evidence from Disparate Cities," *Housing Policy Debate*, vol.15, Issue 3 (2004), p. 603-604. Online. Available: <http://www.fanniemae.foundation.org>. Accessed: November 11, 2006.

⁵⁴ Ibid., p. 611.

⁵⁵ Ibid., p. 615.

⁵⁶ Ibid., p. 618.

⁵⁷ Ibid., p. 611.

⁵⁸ Ibid., p. 615.

⁵⁹ Ibid., p. 620.

⁶⁰ Ibid., p. 618.

⁶¹ Jonathan Hershaff, Susan Wachter, and Karl Russo, "Subprime Lending: Neighborhood Patterns Over Time," (paper presented to the conference of "Promises and Pitfalls" at the Federal Reserve System's Fourth Community Affairs Research Conference, April 2005). Cited with the permission of Susan Wachter. Online. Available: http://www.chicagofed.org/2005_conf_paper_session1_wachter.pdf. Accessed: June 24, 2007.

⁶² Ibid., p. 3.

⁶³ Ibid., p. 16.

⁶⁴ Ibid.

⁶⁵ Ibid., p. 13.

⁶⁶ Ibid., p.15.

⁶⁷ Ibid., pp. 15-16.

⁶⁸ Ibid., p. 10.

⁶⁹ Ibid., p. 13-14.

⁷¹ Ibid., p. 13.

⁷² Ibid.

⁷³ Ibid., p. 16.

⁷⁴ Calvin Bradford, *Risk or Race? Racial Disparities and the Subprime Refinance Market*, (Washington, D.C.: Neighborhood Revitalization Project of the Center for Community Change, May 2002), p. vi. Online. Available: <http://www.communitychange.org>. Accessed: January 26, 2006.

⁷⁵ Ibid.

⁷⁶ Calvin Bradford, *Risk or Race? Racial Disparities and the Subprime Refinance Market*, Table 2, p. 28.

⁷⁷ The McAllen MSA includes: McAllen, Edinburg, and Mission.

⁷⁸ The Brownsville MSA includes: Brownsville, Harlingen, and San Benito.

⁷⁹ Calvin Bradford, *Risk or Race? Racial Disparities and the Subprime Refinance Market*, Table 2, p. 28.

⁸⁰ Association of Community Organizations for Reform Now (ACORN), *Separate and Unequal: Predatory Lending in America* (Chicago, Ill., February 2004), p. 65. Online. Available: <http://www.acorn.org>. Accessed: January 28, 2006.

⁸¹ The Brownsville MSA includes: Brownsville, Harlingen, and San Benito.

⁸² Association of Community Organizations for Reform Now (ACORN), *Separate and Unequal: Predatory Lending in America*, p. 13.

⁸³ Ibid., p 1 and p. 3.

Chapter 5. The Texas Border as the 51st State

The Texas border with Mexico is a unique place, distinctly different from the rest of Texas with an identity and subculture all its own. It stretches from El Paso in the west 1254 miles along the north side of the Rio Grande River to Brownsville at the southernmost tip of Texas, where each city along the way has a sister city across the border in Mexico.¹ (See Appendix for a map of the “Texas - Mexico Border Region”).

There is a high degree of confluence between Texas border cities and their counterparts in Mexico. In Texas, about 60 million legal pedestrians, trucks, cars, and rail cars crossed into the U.S. from Mexico from October 2004 to September 2005.² In Texas, 23 international crossings serve as overland ports of entry for trade with Mexico.³ Trade between the U.S. and Mexico surged up to 13.1% per year following passage of the NAFTA Agreement from 1994-1997 compared to an annual rate of close to 11% from 1990-1994.⁴

However, all is not well on the Border. If the Border region of Texas were considered the “51st state,” the 43 counties that make up the region would rank dead last among all states in per capita personal income, and first in poverty and unemployment.⁵

The Texas State Comptroller’s Office has released several reports over the past decade that examines various socio-economic indicators on the Border and highlight areas of serious concern. Together, these reports show that these areas of concern reflect long-standing trends that continue to the present day.

1998 Texas Comptroller Report

In 1998, Texas Comptroller John Sharp released an extensive report entitled, “Bordering the Future: Challenge and Opportunity on the Texas Border.” In the report, the Border region was defined as an area comprised of 43 counties beginning at the Texas/New Mexico state line in Anthony, Texas, continuing through El Paso and across to San Antonio on Interstate Highway 10, then down Interstate 37 to Corpus Christi on

the Gulf Coast.^{6 7} The report compared the Border region to the rest of Texas and the U.S. using 50 different indicators of health and prosperity.

Overall, the Comptroller's findings were not encouraging:

If the Texas border region were a state unto itself, its governor might be calling out the National Guard, or petitioning Congress and the White House for emergency relief. Certainly, the region is rich in potential. But statistics show that Border residents, on average, are worse off than their fellow Americans. Too many are too poor, too many cannot find good-paying jobs, and too few are adequately educated—and that is just the beginning of a by-the-numbers litany that distinguishes Texas south of Interstate Highway 10.⁸

More specifically, the Comptroller found that in 1995, the twenty counties with lowest per capita income within the state were all border counties, and not a single border county ranked in the twenty counties with highest per-capita income.⁹ In fact, the Border region was home to more poor residents than could be found in at least ten other states plus Washington, D.C., *combined*.¹⁰

Further, the Comptroller found that if the 43-county Texas Border region had comprised the 51st U.S. state, it would have ranked first in the following categories: poverty (29.5% in 1993); schoolchildren in poverty (38% of 5 to 17-year-olds in 1993); unemployment (8% in 1997); and percent of non-high-school-graduate adults (37.3% in 1990). By comparison, Texas as a whole had better rankings in each of these same categories (6th, 5th, 10th, and 12th, respectively), and excluding the Border counties, would have ranked even better (13th, 14th, 40th, and 14th, respectively).

In addition, the Comptroller found that the Border region would have ranked 21st in percent of population with some college education but no degree (19.2% in 1990); 24th in recent growth in annual average pay (3.8% from 1995 to 1996); and 30th in total personal income (\$60.3 billion in 1995). Texas as a whole, by comparison, again had better rankings (14th, 8th, and 3rd, respectively), and excluding the Border counties again would generally have fared even better (13th, 7th, and 3rd, respectively).

Table 5.1
Comparative Socioeconomic Indicators for Texas and the Texas
Border Region - 1998

Where the 43 County Texas Border Region Would Rank Among all States		Where the 211 County Texas Non-Border Region Would Rank Among all States		Where Texas Ranks Among All States	
1 st	Poverty Rate (29.5% in 1993)	13 th	(17% in 1993)	6 th	(19.6% in 1993)
1 st	Sch. Children in Poverty (38% in 1993)	14 th	(22.5% in 1993)	5 th	(26.1% in 1993)
1 st	Unemployment Rate (8% in 1997)	40 th	(3.7% in 1997)	10 th	(5.4% in 1997)
1 st	Percent Adults Not H.S. Grad. (37.3% in 1990)	14 th	(25.7% in 1990)	12 th	(27.9% in 1990)
21 st	Percent Adults Some College, No Degree (19.2% in 1990)	13 th	(21.5% in 1990)	14 th	(21.1% in 1990)
24 th	Recent Growth Av. Annual Pay (3.8% fr. 1995 to 1996)	7 th	(4.7% fr. 1995 to 1996)	8 th	(4.6% fr. 1995 to 1996)
30 th	Total Personal Income (\$60.3 billion in 1995)	3 rd	(\$336.8 billion in 1995)	3 rd	(\$397.1 billion in 1995)

Adapted from: Texas Comptroller of Public Accounts, "The Border: Where we Stand," in *Bordering on the Future: Challenge and Opportunity in the Texas Border* (Austin, Tx., 1998). Online.

Available: <http://www.window.state.tx.us>.

Furthermore, the Comptroller found that the Border region would have ranked close to the bottom in the following categories: 44th in percent of population with a bachelor's degree as highest education attained (10.3% in 1990); 46th in average annual pay (\$22,541 in 1996); 49th in percent of households with a telephone (88.7% in 1990); and 51st in per capita personal income (\$15,570 in 1995). Not surprisingly, Texas as a whole fared better (17th, 15th, 42nd, and 30th, respectively), and better still excluding the Border region (15th, 11th, 38th, and 21st, respectively).

Table 5.2
Comparative Socioeconomic Indicators for Texas and the Texas
Border Region - 1998

Where the 43 County Texas Border Region Would Rank Among all States		Where the 211 County Texas Non-Border Region Would Rank Among all States		Where Texas Ranks Among All States	
44 th	Percent Adults Bachelor's Degree Highest Earned (10.3% in 1990)	15 th	(14.7% in 1990)	17 th	(13.9% in 1990)
46 th	Av. Annual Pay (\$22,541 in 1996)	11 th	(\$29, 293 in 1996)	15 th	(\$28,140 in 1996)
49 th	Percent Households With Telephone (88.7% in 1990)	38 th	(92% in 1990)	42 nd	(91.4% in 1990)
51 st	Per Capita Personal Income (\$15,570 in 1995)	21 st	(\$22,556 in 1995)	30 th	(\$21,119 in 1995)

Adapted from: Texas Comptroller of Public Accounts, "The Border: Where we Stand," in *Bordering on the Future: Challenge and Opportunity in the Texas Border* (Austin, Tx., 1998). Online.
Available: <http://www.window.state.tx.us>.

Of further interest, the following indicators illustrate how the population on the Border differs from the rest of Texas: the Border region would have ranked first in percent of population that spoke Spanish at home (57.1% in 1990); third in percent of population that was foreign born (14.9% in 1990); and sixth in average annual population growth during the 1990's (2.4% annual growth from 1990 to 1996). The corresponding rankings for Texas as a whole were 2nd, 8th, and 9th, respectively, and 5th, 13th, and 11th excluding the Border region.

Table 5.3
Comparative Population Characteristics of Texas and the Texas
Border Region 1998

Where the 43 County Texas Border Region Would Rank Among all States		Where the 211 County Texas Non-Border Region Would Rank Among all States		Where Texas Ranks Among All States	
1 st	Percent Population Speaks Spanish at Home (57.1% in 1990)	5 th	(13.4% in 1990)	2 nd	(22.1% in 1990)
3 rd	Percent Population Foreign Born (14.9% in 1990)	13 th	(7.5% in 1990)	8 th	(9% in 1990)
6 th	Av. Annual Pop. Growth in 1990's (2.4% fr. 1990 to 1996)	11 th	(1.8% fr. 1990 to 1996)	9 th	(1.9% fr. 1990 to 1996)

Adapted from: Texas Comptroller of Public Accounts, "The Border: Where we Stand," in *Bordering on the Future: Challenge and Opportunity in the Texas Border* (Austin, Tx., 1998). Online.
 Available: <http://www.window.state.tx.us>.

The trends evident from these statistics continued in the Comptroller's update report issued in 2001.

2001 Texas Comptroller Report

In January of 2001, Texas Comptroller Carole Keeton Strayhorn updated her predecessor's assessment of the Border with a new report entitled, "The Border: Where We Stand." This report yielded results similar to the 1998 report—that is, Texas Border counties consistently fared less well than their non-border counterparts and Texas as a whole.

Table 5.4
Comparative Socioeconomic Indicators for Texas and the Texas
Border Region 2001

Where the 43 County Texas Border Region Would Rank Among all States		Where the 211 County Texas Non-Border Region Would Rank Among all States		Where Texas Ranks Among All States	
1 st	Poverty Rate (26.8% in 1997)	17 th	(14.3% in 1997)	6 th	(16.7% in 1997)
1 st	Sch. Children in Poverty (33.8% in 1997)	17 th	(18.9% in 1997)	9 th	(22.1% in 1997)
1 st	Unemployment Rate (7.5% in 1999)	27 th	(4.0% in 1999)	16 th	(4.6% in 1999)
1 st	Percent Adults Not H.S. Grad. (37.3% in 1990)	14 th	(25.7% in 1990)	12 th	(27.9% in 1990)
21 st	Percent Adults Some College, No Degree (19.2% in 1990)	13 th	(21.5% in 1990)	14 th	(21.1% in 1990)
43 rd	Recent Growth Av. Annual Pay (2.9% fr. 1998 to 1999)	8 th	(4.6% fr. 1998 to 1999)	12 th	(4.4% fr. 1998 to 1999)
29 th	Total Personal Income (\$74.2 billion in 1998)	3 rd	(\$425.9 billion in 1995)	3 rd	(\$508.6 billion in 1995)
44 th	Percent Adults Bachelor's Degree Highest Earned (10.3% in 1990)	15 th	(14.7% in 1990)	17 th	(13.9% in 1990)
46 th	Av. Annual Pay (\$25,287 in 1999)	11 th	(\$33,712 in 1999)	15 th	(\$32,254 in 1999)
49 th	Percent Households With Telephone (88.7% in 1990)	38 th	(92% in 1990)	42 nd	(91.4% in 1990)
51 st	Per Capita Personal Income (\$18,390 in 1998)	18 st	(\$27,165 in 1998)	26 th	(\$25,803 in 1998)

Adapted from: Texas Comptroller of Public Accounts, *The Border: Where we Stand*, January 2001 Update, (Austin, Tex., January 2001). Online. Available: <http://www.window.state.tx.us>.

Three months later, in March of 2001, the Comptroller released another update, this time targeting the 14 Texas counties whose boundaries actually touch the U.S. border with Mexico.¹¹ This report showed that conditions on the actual border are worse than the broader 43-county region examined earlier.

That is, in regard to selected categories discussed above, a comparison of the narrower 14-county border region with the original 43-county border region yields the following results: higher poverty (34.0% versus 26.8% in 1997); more schoolchildren in poverty (40.5% of 5 to 17-year-olds in 1997 versus 33.8% in 1997); higher unemployment (11.4% versus 7.5% in 1999); less total personal income (\$27.2 billion versus \$74.2 billion); less recent growth in annual average pay (1.9% versus 2.9%); less average annual pay (\$22,368 versus \$25,287); and less per-capita personal income (\$14,224 versus \$18,390). In addition, according to a report on the Border economy by the Federal Reserve Bank of Dallas, per capita income along the Texas-Mexico Border are among the lowest in the nation, ranging from 38% of U.S. per capita income in Eagle Pass to 60% in El Paso, compared with a state average of 94%.¹²

Table 5.5
Comparative Socioeconomic Indicators for the 14 County Texas
Border Region and the 43 County Texas Border Region 2001

	14-County Actual Border Region	43-County Border Region
Poverty Rate	(34.0% in 1997)	(26.8% in 1997)
Sch. Children in Poverty	(40.5% in 1997)	(33.8% in 1997)
Unemployment Rate	(11.4% in 1999)	(7.5% in 1999)
Recent Growth Av. Annual Pay	(1.9% fr. 1998 to 1999)	(2.9% fr. 1998 to 1999)
Total Personal Income	(\$27.2 billion in 1998)	(\$74.2 billion in 1998)
Av. Annual Pay	(\$22,368 in 1999)	(\$25,287 in 1999)
Per Capita Personal Income	(\$14,224 in 1998)	(\$18,390 in 1998)

Adapted from: Texas Comptroller of Public Accounts, *The Border: On the Brink* (Austin, Tex., March 2001). Online. Available: <http://www.window.state.tx.us>.

The report, published in 2001, also found that a substantial percentage of Border residents spend an excessive proportion of income on housing, (30 % of income is generally considered acceptable), as housing is considered affordable to only one in three Border residents.¹³

Again, the trends evident from these statistics continued in the Comptroller's next update report issued in 2003.

2003 Texas Comptroller Report

In 2003, the Comptroller's Office released its most recent update, entitled "The Border: Snapshot," which confirmed the earlier trends discussed above.

Comparing the 14-county actual border region with the original 43-county border region and the rest of Texas yields the following results: higher poverty (29.1% versus 22.9% and 12.4% in 2000); more schoolchildren in poverty (35.3% versus 28.8% and 15.8% in 2000); higher unemployment (10.7% versus 7.9% and 6.0% in 2002); lower percent of population 25 years and over with a bachelor's degree (9.3% versus 11.2% and 16.6% in 2000); lower percent of population 25 years and over with a post-graduate degree (5% versus 6.3% and 7.9% in 2000); higher percent of population 25 years and over without a high school diploma (43.2% versus 33.6% and 22.2% in 2000); and less per-capita personal income (\$16,493 versus \$18,347 and \$22,865 in 2001).

Table 5.6
Comparative Socioeconomic Indicators for the Texas Border Region
and the 211 County Texas Non-Border Region 2003

	14-County Actual Border Region	43-County Border Region	211-County Non- Border Region
Poverty Rate	(29.1% in 2000)	(22.9% in 2000)	(12.4% in 2000)
Sch. Children in Poverty	(35.3% in 2000)	(28.8% in 2000)	(15.8% in 2000)
Unemployment Rate	(10.7% in 2002)	(7.9% in 2002)	(6.0% in 2002)
Percent Adults Not H.S. Grad.	(43.2% in 2000)	(33.6% in 2000)	(22.2% in 2000)
Percent Adults Some College, No Degree	(17.6% in 2000)	(20.7% in 2000)	(22.7% in 2000)
Percent Adults Bachelor's Degree Highest Earned	(9.3% in 2000)	(11.2% in 2000)	(16.6% in 2000)
Percent Adults Post-Graduate Degree	(5.0% in 2000)	(6.3% in 2000)	(7.9% in 2000)
Recent Growth Av. Annual Pay	(3.1% fr. 2001 to 2002)	(2.4% fr. 2001 to 2002)	(0.4% fr. 2001 to 2002)
Total Personal Income	(\$32.4 billion in 2001)	(\$87.7 billion in 2001)	(\$520.8 billion in 2001)
Av. Annual Pay	(\$24,550 in 2002)	(\$28,011 in 2002)	(\$37,734 in 2002)
Per Capita Personal Income	(\$16,493 in 2001)	(\$18,347 in 2001)	(\$22,865 in 2001)

Adapted from: Texas Comptroller of Public Accounts, *The Border Snapshot*, (Austin, Tex., November 2003). Online. Available: <http://www.window.state.tx.us>.

Conclusion

In summary, the Texas Comptroller data demonstrate that year after year residents of the Texas Border region continue to fare less well than their counterparts in the rest of Texas and the United States on a broad range of socio-economic indicators, including poverty rate, level of education, wages, and related factors. In addition to

these indicators, there is a high rate of subprime home mortgage lending on the Border, as discussed in detail in Chapter 6.

¹ Texas Comptroller of Public Accounts, *Bordering on the Future: Challenge and Opportunity in the Texas Border* (Austin, Tx., 1998), p. 1. Online. Available: <http://www.window.state.tx.us.border/ch01/ch01/html>. Accessed: July 2, 2007.

² State Senator Eliot Shapleigh, "Demographics of the Border Region," in *Texas Borderlands: Frontier of the Future* (2007). p. 1. Online. Available: <http://www.shapleigh.org>. Accessed: May 12, 2007.

³ State Senator Eliot Shapleigh, "The State of Border Transportation and Security" in *Texas Borderlands: Frontier of the Future* (2007), p. 1.

⁴ State Senator Eliot Shapleigh, "Demographics of the Border Region" in *Texas Borderlands: Frontier of the Future* (2007), p. 2.

⁵ Ibid., p.1.

⁶ Texas Comptroller of Public Accounts, *Bordering on the Future: Challenge and Opportunity in the Texas Border* (Austin, Tx., 1998), p. 4.

⁷ Note: In this report the Texas Border region includes 43 Texas counties south of Interstate 10 and west of Interstate 37: Atascosa, Bandera, Bexar, Brewster, Brooks, Cameron, Crockett, Culberson, Dimmit, Duval, Edwards, El Paso, Frio, Hidalgo, Hudspeth, Jeff Davis, Jim Hogg, Jim Wells, Kennedy, Kerr, Kimble, Kinney, Kleberg, La Salle, Live Oak, Maverick, McMullen, Medina, Nueces, Pecos, Presidio, Real, Reeves, San Patricio, Starr, Sutton, Terrell, Uvalde, Val Verde, Webb, Willacy, Zapata and Zavala.

⁸ Ibid., p 5.

⁹ Ibid.

¹⁰ Ibid (emphasis in original document).

¹¹ Note: The 14 County Border region includes the following Counties: Brewster, Cameron, El Paso, Hidalgo, Hudspeth, Jeff Davis, Kinney, Maverick, Presidio, Starr, Terrell, Val Verde, Webb, and Zapata.

¹² Federal Reserve Bank of Dallas, "The Border Economy: Introduction," p. 1, by Mine Yucel in *Border Economy* (Dallas, Tx., June 2001). Online. Available: http://www.dallasfed.org/research/border/tbe_statistics.pdf. Accessed: May 12, 2007.

¹³ Federal Reserve Bank of Dallas, “Housing Affordability: Outlook Improving Along the Border,” p.15, by Toby Cook in *Border Economy* (Dallas, Tx., June 2001).

Chapter 6. The Border Study: Analysis of 2004 HMDA Data

Overview

This study analyzes data released to the public by the Federal Financial Institutions Examination Council (FFIEC) relating to the activity of lending institutions covered by the Home Mortgage Disclosure Act (HMDA), including the disposition of loan applications and the rate spread for all conventional home purchase and refinance originated loans. It focuses on the level of home mortgage denials and subprime originations among Border region borrowers and compares the levels to those experienced by borrowers in Texas and the U.S.

Methodology

All data analyzed is included in the Appendix in spreadsheet format as to consolidate and calculate data. The data is available by individual Metropolitan Statistical Areas (MSAs) and for the entire United States in aggregate. Thus, the regions of Texas and the Border are defined by a group of MSAs and the U.S. is defined by the aggregate data for the United States. The percentage of loan denials and subprime originations is also reported as a ratio – a disparity ratio. A ratio of 1.00 indicates no disparity between the two groups being compared. A ratio above or below 1.0 indicates a disparity between the two groups being compared.

Regions

Three separate regions were analyzed: the Texas Border, the State of Texas not including the Border, and the United States.

The Texas Border is defined as the four MSAs along the Texas-Mexico border for which HMDA data is available:

Brownsville MSA – Brownsville and Harlingen

El Paso MSA – El Paso

Laredo MSA – Laredo

McAllen MSA – McAllen, Edinburg and Pharr

(See the “Texas-Mexico Border Region” map in the Appendix).

The State of Texas, not including the Border, is defined as the following nine major MSAs from around the state:

Amarillo MSA - Amarillo

Austin MSA – Austin and Round Rock

Corpus Christi MSA – Corpus Christi

Dallas MSA- Dallas, Plano and Irving

Fort Worth MSA – Fort Worth and Arlington

Houston MSA – Houston, Baytown and Sugarland

Lubbock MSA - Lubbock

Midland MSA - Midland

San Antonio MSA – San Antonio

(See “Metropolitan Statistical Areas of Texas - 2004” map in the Appendix).

The **United States** is defined to include all fifty states, including Texas and the Texas Border.

Loan Types

This study deals only with home purchase loans and refinance home loans. Data on home purchase loans includes only conventional, first lien, 1-4 family, owner-occupied dwellings, excluding manufactured homes. Government backed loans (FHA, VA, FmHA) are also excluded.

Similarly, data on refinance loans includes only conventional, first lien, 1-4 family, owner-occupied dwellings, excluding manufactured homes. Government backed loans (FHA, VA, FmHA) are also excluded.

Prime loans are defined as loans for which no pricing data was reported. They had an APR equal to or less than three percentage points above the rate on comparable Treasury securities.

Subprime or high-cost loans are loans for which pricing data was reported, wherein the rate spread of the APR of the loan was at least three points above the rate on comparable rate Treasury securities at the time of the origination. Since the HMDA data does not include the dates of loan applications or loan terms, the actual APR of loans originated cannot be determined. However, the 30-year Treasury rates in 2004 ranged from 4.67% to 5.54%, therefore, subprime first lien mortgages had a beginning threshold from 7.67% to 8.54% in 2004.¹

Borrower Characteristics

With regard to race, HMDA borrowers are assigned to a single category. Likewise, borrowers are assigned to one ethnicity category. For purposes of this study, to avoid double counting, borrowers of Latino ethnicity are not included in the racial categories of white or black. For example, a borrower with the attributes Latino and white is counted as Latino and not white.

Income

With respect to income, borrowers are assigned to one of three categories, low to moderate income, middle income and upper income based on a percentage comparison of their reported income to the median family income of the applicable MSA.

The **low-income** category corresponds to reported income less than 50% of median family income.

The **moderate income** category corresponds to reported income between 51% and 79% of median family income. (In this report low and moderate income borrowers are combined into the low to moderate income category).

The **middle income** category corresponds to reported income between 80% and 119% of median family income.

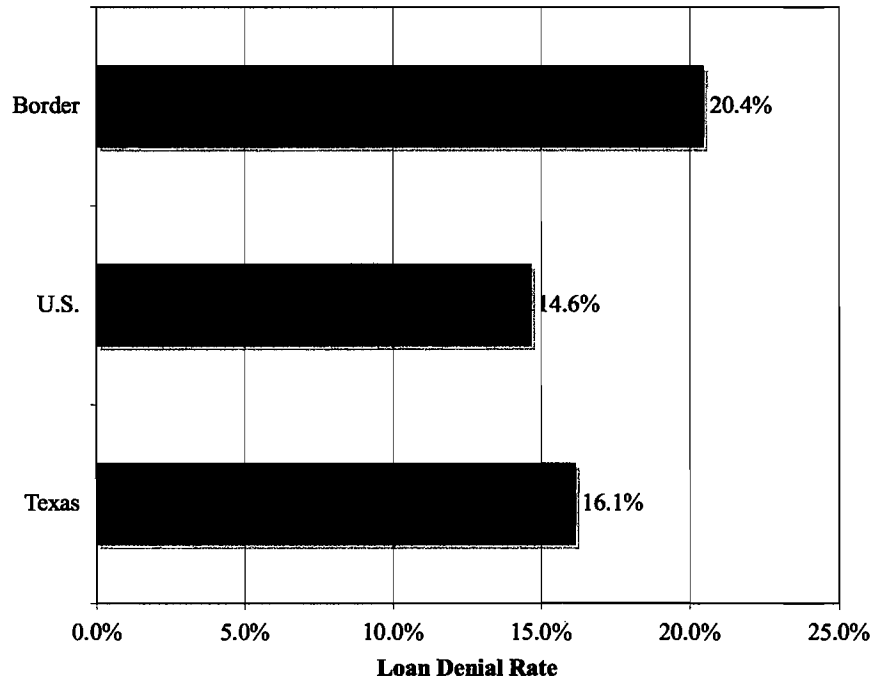
The **upper income** category corresponds to reported income greater than 120% of median family income.

Conventional Home Purchase Loans

Denials

Border applicants are denied conventional home purchase loans more frequently than U.S. or Texas applicants. One in five (20.4%) Border applicants were denied such a loan as compared to 14.6% of U.S. and 16.1% of Texas applicants. Among Border applicants, those from McAllen had the highest likelihood of being denied a loan with a 23.4% rate of denial and Laredo had the lowest with a 17.9% denial rate. In Texas, Austin had the lowest denial rate of 13.5 % and San Antonio had the highest with a rate of 19.1%. (See Appendix - Table 1 “Conventional Home Purchase Loans: Loan Application Denials and Subprime Incidence” for the data for the U.S. and each MSA within each region).

Figure 6.1
2004 Conventional Home Purchase Loan Denials by Region



Adapted from: the Federal Financial Institutions Examination Council 2004 HMDA data – Aggregate Table 7-2 for the U.S. and each MSA. Online. Available: <http://www.ffiec.gov/hmda>.

Therefore, Border applicants were 1.4 times or 40% more likely to be denied a loan as compared to U.S. applicants and 1.3 times or 30% more likely to be denied over their Texas counterparts.

Table 6.1
Conventional Home Purchase Loan Denials and Disparity Ratios By Region

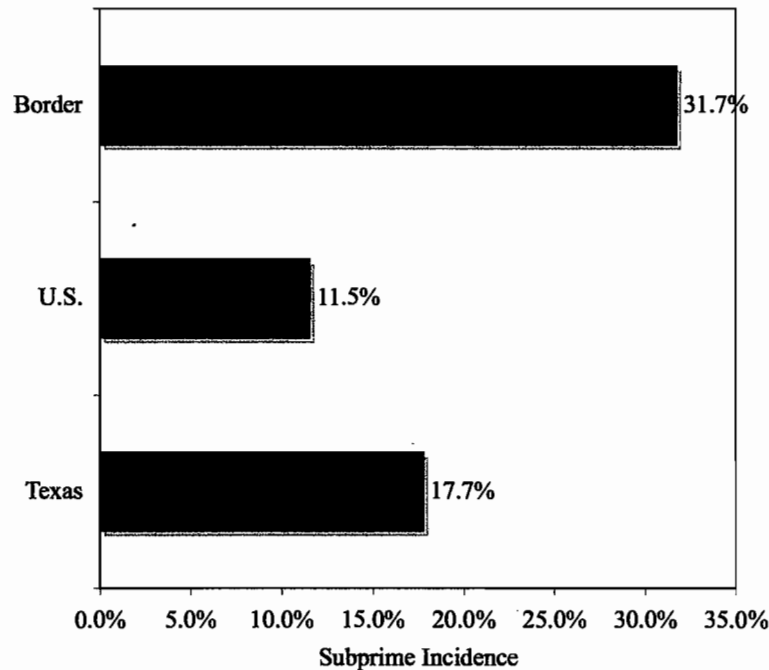
	<u>Denial rate</u>	<u>Disparity Ratio</u>
Border	20.4%	
U.S.	14.6%	1.4
Texas	16.1%	1.3

Adapted from: the Federal Financial Institutions Examination Council 2004 HMDA data – Aggregate Table 7-2 for the U.S. and each MSA. Online. Available: <http://www.ffiec.gov/hmda>.

Conventional Home Purchase Subprime Incidence

The overall incidence of subprime lending on the Border is much higher than in the U.S. or Texas. Among Border applicants who did receive a loan, almost one-third (31.7%) were subprime. Within the Border region, McAllen had the highest subprime penetration rate of 41.5% and El Paso had the lowest rate of 21.1%. Therefore, at least one in five conventional home purchase originations on the Border were high cost. Among Texas cities, Houston had the highest percentage of subprime originations with a rate of 21.3% and Austin had the lowest penetration rate of 8.8%. (See Appendix -Table 1 “Conventional Home Purchase Loans: Application Denials and Subprime Incidence” for the data for each MSA within each region).

Figure 6.2
2004 Conventional Home Purchase Subprime Loan Incidence By Region



Adapted from: the Federal Financial Institutions Examination Council 2004 HMDA data – Aggregate Table B for the U.S. and each MSA. Online. Available: <http://www.ffiec.gov/hmda>.

The subprime penetration rate of 31.7% along the Border was nearly triple (2.8) the frequency among U.S. borrowers and more than double (1.8) the rate as compared to Texas borrowers.

Table 6.2
Conventional Home Purchase Subprime Loan Incidence and Disparity Ratios by Region

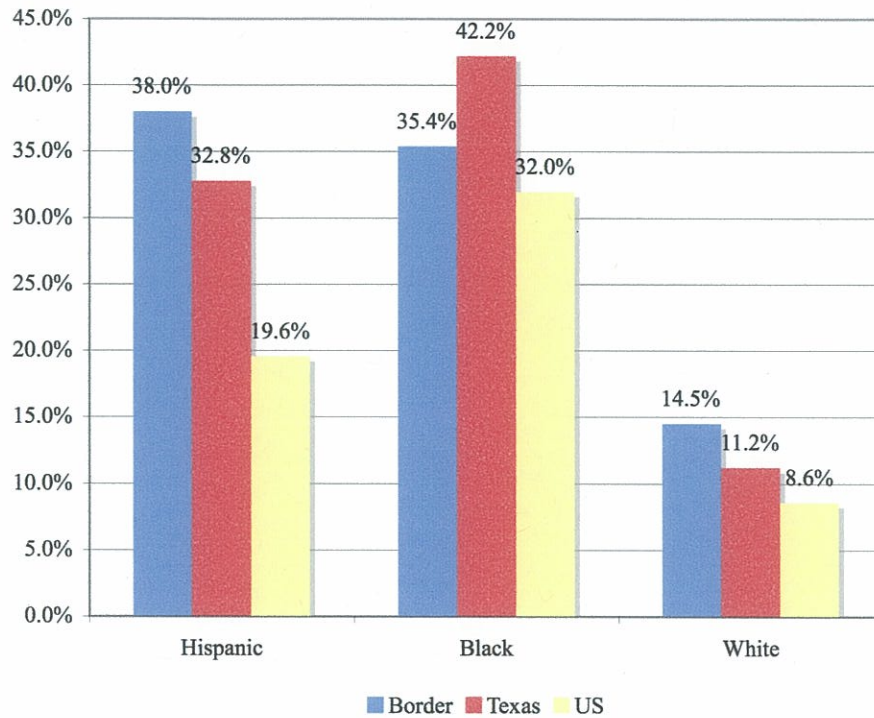
	<u>Subprime Originations</u>	<u>Disparity Ratio</u>
Border	31.7%	
U.S.	11.5%	2.8
Texas	17.7%	1.8

Adapted from: the Federal Financial Institutions Examination Council 2004 HMDA data – Aggregate Table B for the U.S. and each MSA. Online. Available: <http://www.ffiec.gov/hmda>.

Racial Disparities

The results of this study are consistent with other research that has highlighted the racial disparities that exist in subprime lending among minority borrowers as compared to white borrowers. Minority borrowers in all regions received high cost loans at a much higher rate than white borrowers.

Figure 6.3
Conventional Home Purchase Subprime Loan Incidence by Race



Adapted from: the Federal Financial Institutions Examination Council 2004 HMDA data – Aggregate Table 11-3 for the U.S. and each MSA. Online. Available: <http://www.ffiec.gov/hmda>.

Overall, among all borrowers, Black borrowers in Texas had the greatest likelihood of receiving a subprime loan with an incidence of 42.2%, followed by Border Hispanics with a frequency of 38.0%. Among white borrowers, those from the Border had the greatest risk of receiving a high cost loan with a high cost origination rate of 14.5%. (See Appendix - Table 2 “Conventional Home Purchase Loans: Pricing Data by Race” for the data for each MSA within each region).

Comparison of Hispanic Borrowers to White Borrowers

Among Border borrowers, Hispanics experienced the highest level of subprime originations. Nearly two-fifths (38%) of all loans to Border Hispanic borrowers were subprime. They were 2.6 times more likely to receive a high cost loan as compared to

Border white borrowers who received this type of loan only 14.5% of the time. The disparity between Hispanic and white borrowers on the Border was higher than that between U.S. Hispanic and white borrowers which was 2.3, but lower than that between Texas Hispanic and white borrowers with a disparity ratio of 2.9

Table 6.3
Conventional Home Purchase Loans:
Hispanic to White Comparative Subprime Incidence and Disparity Ratios

	<u>Hispanic Subprime</u>	<u>White Subprime</u>	<u>Disparity Ratio</u>
Border	38.0%	14.5%	2.6
US	19.6%	8.6%	2.3
Texas	32.8%	11.2%	2.9

Adapted from: the Federal Financial Institutions Examination Council 2004 HMDA data – Aggregate Table 11-3 for the U.S. and each MSA. Online. Available: <http://www.ffiec.gov/hmda>.

Therefore, Hispanics in each region were at least twice as likely to be given a subprime loan as compared to white borrowers.

Comparison of Black Borrowers to White Borrowers

Among the individual cities that make up the Border region there were only a small number of loans made to Black residents. Grouped together as one region, however, there were a total of 130 loans, 85 of which were in El Paso. Of those loans, over one-third (35.4%) were subprime. Border Black borrowers were two and a half times (2.5) more likely to receive a high priced loan as compared to Border white borrowers whose subprime origination rate was 14.5%.

Table 6.4
Conventional Home Purchase Loans:
Black to White Comparative Subprime Incidence and Disparity Ratios

	<u>Black Subprime</u>	<u>White Subprime</u>	<u>Disparity Ratio</u>
Border	35.4%	14.5%	2.5
US	32.0%	8.6%	3.7
Texas	42.2%	11.2%	3.8

Adapted from: the Federal Financial Institutions Examination Council 2004 HMDA data – Aggregate Table 11-3 for the U.S. and each MSA. Online. Available at: <http://www.ffiec.gov/hmda>.

It is important to note, however, that while the subprime penetration rate was higher among Border Blacks (35.4%), than for U.S. Blacks (32.0%), the disparity ratio between Border Black and white borrowers was 2.5 as opposed to the much wider ratio between U.S. Black and white borrowers, which was 3.7. Similarly, the Border Black to white disparity was much lower in comparison to that of Texas Blacks and whites wherein Texas Black borrowers were also nearly four times (3.8) more likely to receive a subprime loan over their white counterparts.

Intra-racial Disparities Across Regions

However, the focus of this report is to study the relationship between the market penetration rate of subprime lending and the Border region. As such, the data was further analyzed with respect to the subprime incidence and disparities within the same racial/ethnic group across the regions. (See Appendix - Table 2 “Conventional Home Purchase Loans: Pricing Data by Race” for the data for the U.S. and each MSA within each region).

Comparison of Hispanic Borrowers Across All Regions

Hispanics who reside on the Border were at a disadvantage compared to Hispanics elsewhere with respect to the likelihood of acquiring a subprime conventional home purchase loan.

Table 6.5
Conventional Home Purchase Subprime Loan Incidence and Disparity Ratios Among Hispanic Borrowers Across All Regions

	<u>Subprime Originations</u>	<u>Disparity Ratio</u>
Border Hispanic	38.0%	
U.S. Hispanic	19.6%	1.9
Texas Hispanic	32.8%	1.2

Adapted from: the Federal Financial Institutions Examination Council 2004 HMDA data – Aggregate Table 11-3 for the U.S. and each MSA. Online. Available at: <http://www.ffiec.gov/hmda>.

Border Hispanics were nearly twice (1.9) as likely to receive a high priced loan than if they had purchased a home elsewhere in the U.S., but residence on the Border posed a lesser disadvantage as compared to Hispanics in Texas, although Border Hispanics were still 20% more likely to receive such a loan.

Comparison of Black Borrowers Across All Regions

The analysis across regions among Black borrowers revealed that application for a loan as a Border resident increased the risk of a subprime origination by 10% as compared to U.S. borrowers. Interestingly, the opposite is true for Border Black borrowers as compared to Texas Blacks with a disparity ratio of .84.

Table 6.6
Conventional Home Purchase Subprime Loan Incidence and Disparity
Ratios Among Black Borrowers Across All Regions

	<u>Subprime Originations</u>	<u>Disparity Ratio</u>
Border Black	35.4%	
U.S. Black	32.0%	1.1
Texas Black	42.2%	.84

Adapted from: the Federal Financial Institutions Examination Council 2004 HMDA data – Aggregate Table 11-3 for the U.S and each MSA. Online. Available at: <http://www.ffiec.gov/hmda>.

In other words, Black borrowers who applied for loans on the Border were 16% less likely to receive a subprime loan than if they had applied from elsewhere in Texas. However, it is important to note that there were only 130 loans in the entire Border region and Black Texas borrowers had an exceptionally high subprime origination incidence of 42%.

Comparison of White Borrowers Across All Regions

As previously noted, overall, white borrowers in all three regions were least likely to be given a subprime loan as compared to minority borrowers.

Table 6.7
Conventional Home Purchase Subprime Loan Incidence and Disparity
Ratios Among All Borrowers Across All Regions

	<u>Hispanic</u> <u>Subprime</u>	<u>Black</u> <u>Subprime</u>	<u>White</u> <u>Subprime</u>
Border	38.0%	35.4%	14.5%
US	19.6%	32.0%	8.6%
Texas	32.8%	42.2%	11.2%

Adapted from: the Federal Financial Institutions Examination Council 2004 HMDA data – Aggregate Table 11-3 for the U.S and each MSA. Online. Available at: <http://www.ffiec/hmda>.

The region where the loan was originated, however, affected the probability of receiving such a loan - even for white borrowers.

Table 6.8
Conventional Home Purchase Subprime Loan Incidence Among White Borrowers Across All Regions

	<u>Subprime Originations</u>	<u>Disparity Ratio</u>
Border White	14.5%	
U.S. White	8.6%	1.7
Texas White	11.2%	1.3

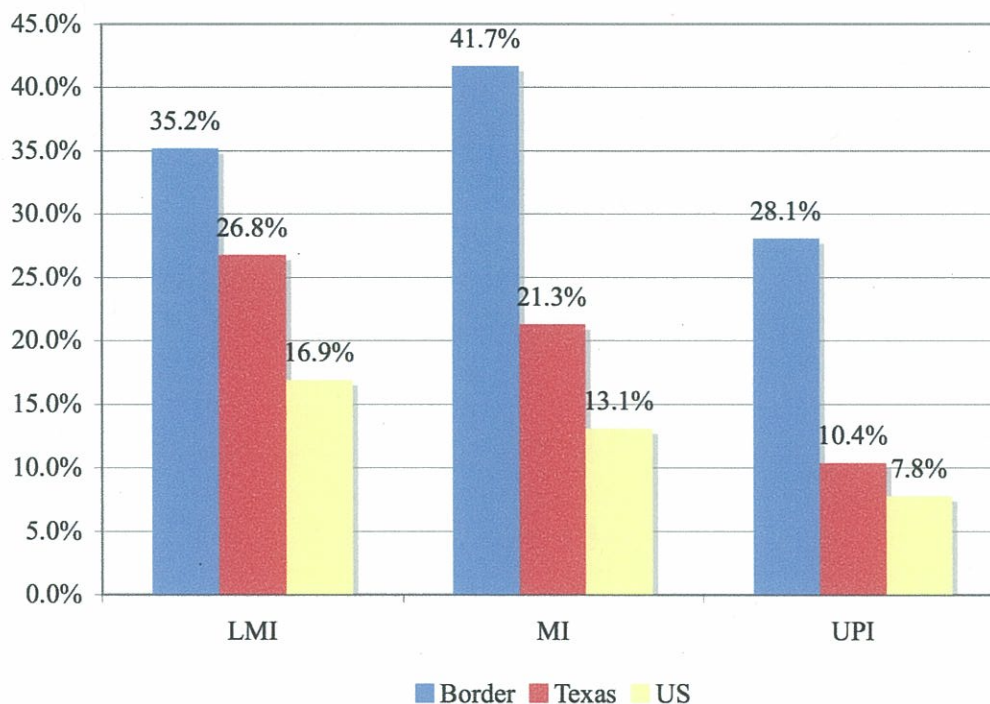
Adapted from: the Federal Financial Institutions Examination Council 2004 HMDA data – Aggregate Table 11-3 for the U.S and each MSA. Online. Available at: <http://www.ffiec.gov/hmda>.

For Border white borrowers, one in seven (14.5%) loans were subprime as opposed to 8.6% for U.S. whites and 11.2% for white Texans. Therefore, white borrowers who reside on the Border were 70% (1.7) more likely to receive such a loan over their U.S. counterparts and had a 30% (1.3) greater chance of a subprime origination than white borrowers who purchased a home elsewhere in Texas.

Income Disparities

In general, the distribution of the subprime market penetration of conventional home purchase loans was higher among all income groups on the Border as compared to similarly economically situated borrowers in the U.S. and Texas. (See Appendix - Table 3 “Conventional Home Purchase Loans: Pricing Data By Borrower Income” for the data for the U.S. and each MSA within each region).

Figure 6.4
Conventional Home Purchase Subprime Loan Incidence By Income



Adapted from: the Federal Financial Institutions Examination Council 2004 HMDA data – Aggregate Table 11-3 for the U.S and each MSA. Online. Available: <http://www.ffiec.gov/hmda>.

On the Border, Middle Income (MI) borrowers had the greatest probability of a subprime origination with a frequency of 41.7%, followed by Low to Moderate Income (LMI) borrowers with a rate of 35.2%, and Upper Income (UPI) borrowers at 28.1%. The distribution in the U.S. was different, where approximately one in six originations (16.9%) to LMI borrowers were subprime, followed by MI borrowers who had a rate of 13.1%, and UPI borrowers for whom less than one in ten originations (7.8%) were high cost. Texas had the same pattern as the U.S. where LMI borrowers had the highest level of subprime market penetration with a rate of 26.8%, followed by MI borrowers who received high priced loans 21.3% of the time, and UPI borrowers also for whom one in ten (10.4%) originations were subprime.

Disparities Between Borrowers by Income

Comparison of Low to Moderate Income Borrowers to Upper Income Borrowers

As cited above, and perhaps surprisingly, Border LMI borrowers did not experience the highest rate of subprime lending, as their probability of a subprime origination was 35.2%. However, they were 30% (1.3) more likely to receive such a loan as opposed to Border UPI borrowers for whom the subprime penetration rate was 28.1%. This disparity, however, is much lower than that between U.S. LMI and UPI borrowers wherein LMI borrowers had more than double (2.2) the likelihood of a subprime origination with a probability of 16.9% over UPI borrowers for whom 7.8% of loans were high cost. Texas LMI borrowers received subprime loans 26.8% of the time, a rate almost triple (2.6) that over their UPI counterparts, who had a subprime origination rate of 10.4%.

Table 6.9
Conventional Home Purchase Subprime Loans:
Low to Moderate Income to Upper Income Comparative Subprime
Incidence and Disparity Ratios

	<u>LMI</u> <u>Subprime</u>	<u>UPI</u> <u>Subprime</u>	<u>Disparity</u> <u>Ratio</u>
Border	35.2%	28.1%	1.3
US	16.9%	7.8%	2.2
Texas	26.8%	10.4%	2.6

Adapted from: the Federal Financial Institutions Examination Council 2004 HMDA data – Aggregate Table 11-3 for the U.S and each MSA. Online. Available: <http://www.ffiec.gov/hmda>.

Therefore, while Border LMI borrowers had the greatest incidence of subprime originations, the disparity between themselves and their UPI counterparts was the smallest among all three regions. This appears to indicate that the high level of subprime lending on the Border is more evenly distributed among borrowers across all

income brackets as compared to the U.S. and Texas where LMI borrowers are given high priced loans at least twice as often as UPI borrowers.

Comparison of Middle Income Borrowers to Upper Income Borrowers

Unlike the distribution in the other two regions, where LMI borrowers had the greatest frequency of subprime loans, Border MI borrowers had the highest incidence of subprime originations with a rate of 41.7%, which was 50% (1.5) higher than for Border UPI borrowers for whom the rate was 28.1%. This is only 20% higher than the disparity between U.S. MI and UPI borrowers which was 1.7, but was lower than the disparity between Texas MI and UPI borrowers wherein MI borrowers were twice (2.1) as likely to receive such a loan over borrowers in the upper income bracket.

Table 6.10
Conventional Home Purchase Subprime Loans:
Middle Income to Upper Income Comparative Subprime Incidence
and Disparity Ratios

	<u>MI</u> <u>Subprime</u>	<u>UPI</u> <u>Subprime</u>	<u>Disparity</u> <u>Ratio</u>
Border	41.7%	28.1%	1.5
US	13.1%	7.8%	1.7
Texas	21.3%	10.4%	2.1

Adapted from: the Federal Financial Institutions Examination Council 2004 HMDA data – Aggregate Table 11-3 for the U.S and each MSA. Online. Available: <http://www.ffiec.gov/hmda>.

As was the case with Border LMI borrowers, although Border MI borrowers had the highest incidence of subprime originations among the three regions, the disparity between them and Border UPI borrowers was the lowest with a disparity ratio of 1.5, once again indicating that high cost loans are more evenly distributed among the different economic classes of borrowers on the Border.

Intra-Income Disparities Across Regions

Comparison of Low to Moderate Income Borrowers Across All Regions

As with the analysis of racial disparities across regions, the data was reviewed in the same manner with respect to income level. Border LMI borrowers were at a disadvantage as compared to LMI borrowers from the other regions with respect to their likelihood of acquiring a subprime home purchase loan.

Table 6.11
Conventional Home Purchase Subprime Loan Incidence Among Low to Moderate Income Borrowers Across All Regions

	<u>Subprime Originations</u>	<u>Disparity Ratio</u>
Border LMI	35.2%	
U.S. LMI	16.9%	2.1
Texas LMI	26.8%	1.3

Adapted from: the Federal Financial Institutions Examination Council 2004 HMDA data – Aggregate Table 11-3 for the U.S and each MSA. Online. Available: <http://www.ffiec.gov/hmda>.

Border LMI Borrowers were at least twice (2.1) as likely to receive a subprime rate as compared to economically similar borrowers in the U.S. with a probability of 16.9% and 30% (1.3) more likely than LMI borrowers from elsewhere in Texas.

Comparison of Middle Income Borrowers Across All Regions

Middle Income borrowers in the Borderland experienced the highest level of subprime originations of all borrowers with a frequency of 41.7%.

Table 6.12
Conventional Home Purchase Subprime Loan Incidence Among Middle Income Borrowers Across All Regions

	<u>Subprime Originations</u>	<u>Disparity Ratio</u>
Border MI	41.7%	
U.S. MI	13.1%	3.2
Texas MI	21.3%	2.0

Adapted from: the Federal Financial Institutions Examination Council 2004 HMDA data – Aggregate Table 11-3 for the U.S and each MSA. Online. Available: <http://www.ffiec.gov/hmda>.

Correspondingly, the disparities between Border MI borrowers and MI borrowers from the other regions were also the largest. Border MI borrowers received subprime loans at a rate over three times (3.2) higher than U.S. MI borrowers and twice (2.0) the rate as compared to similarly economically situated Texans.

Comparison of Upper Income Borrowers Across All Regions

Even upper income borrowers from the Border were at a disadvantage due to their geographic location.

Table 6.13
Conventional Home Purchase Subprime Loan Incidence Among Upper Income Borrowers Across All Regions

	<u>Subprime Originations</u>	<u>Disparity Ratio</u>
Border UPI	28.1%	
U.S. UPI	7.8%	3.6
Texas UPI	10.4%	2.7

Adapted from: the Federal Financial Institutions Examination Council 2004 HMDA data – Aggregate Table 11-3 for the U.S and each MSA. Online. Available: <http://www.ffiec.gov/hmda>.

Moreover, Border UPI borrowers had the greatest disparity ratios between themselves and their U.S. and Texas counterparts as compared to the disparities between the other income groups, despite the lower level of incidence (as compared to all other Border borrowers). They were over three and a half (3.6) times more likely than U.S. UPI borrowers to acquire a subprime loan and 2.7 times more likely to be awarded a high cost loan as compared to Texas UPI borrowers.

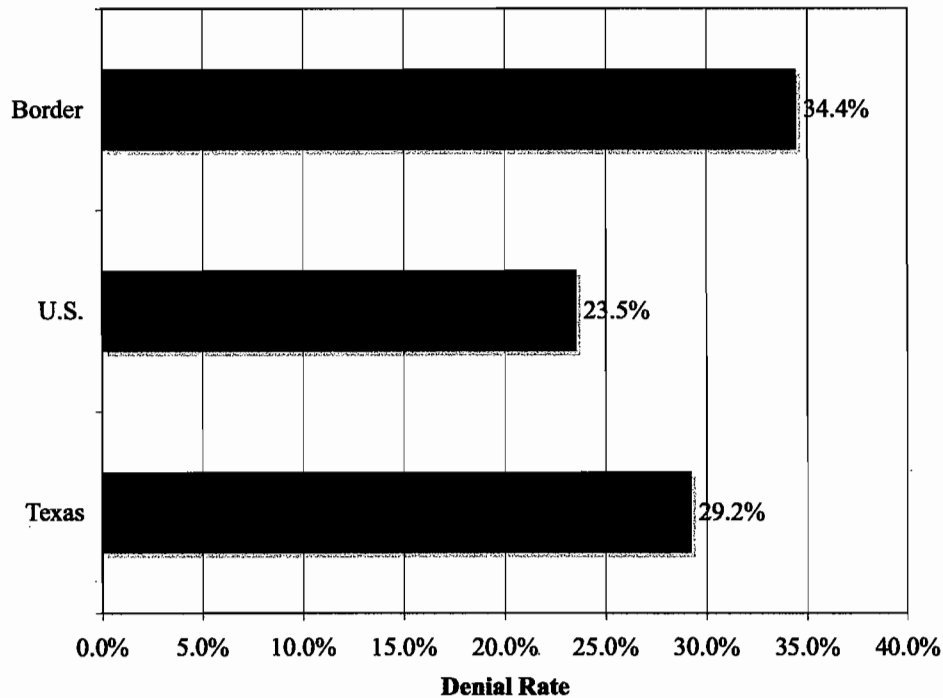
Conventional Home Refinance Loans

Although there is a relatively high market penetration rate of subprime lending in the conventional home purchase market, it is in the home refinance market where such lending is dominant. According to Eric Stein of Coalition for Responsible Lending, in 2001, 80% of all subprime loans were refinance loans².

Denials

The rate of denials for a refinance loans is higher in all three regions as compared to the denial rates for home purchase loans. Once again, Border borrowers were denied much more frequently than borrowers from the U.S. and Texas. Among Border applicants, those from Laredo were denied refinance loans the most with a frequency of 38.0% and applicants from El Paso had the lowest rate of denial with probability of 32.3%. In Texas, applicants from Midland had the highest denial rate of 31.9% and applicants from Austin were denied the least frequently with an incidence of 26.8%. (See Appendix - Table 4 “Conventional Home Refinance Loans: Denials and Subprime Incidence” for the data for the U.S. and each MSA within each region).

Figure 6.5
2004 Conventional Home Refinance Loan Denials by Region



Adapted from: the Federal Financial Institutions Examination Council 2004 HMDA data – Aggregate Table 7-3 for the U.S and each MSA. Online. Available: <http://www.ffiec.gov/hmda>.

Among Border applicants for refinance loans, 34.4% were denied as compared to a 23.5% denial rate for U.S. applicants and a 29.2% rate for applicants in Texas.

Table 6.14
Conventional Home Refinance Loan Denials and Disparity Ratios By Region

	<u>Denial rate</u>	<u>Disparity Ratio</u>
Border	34.4%	
U.S.	23.5%	1.5
Texas	29.2%	1.2

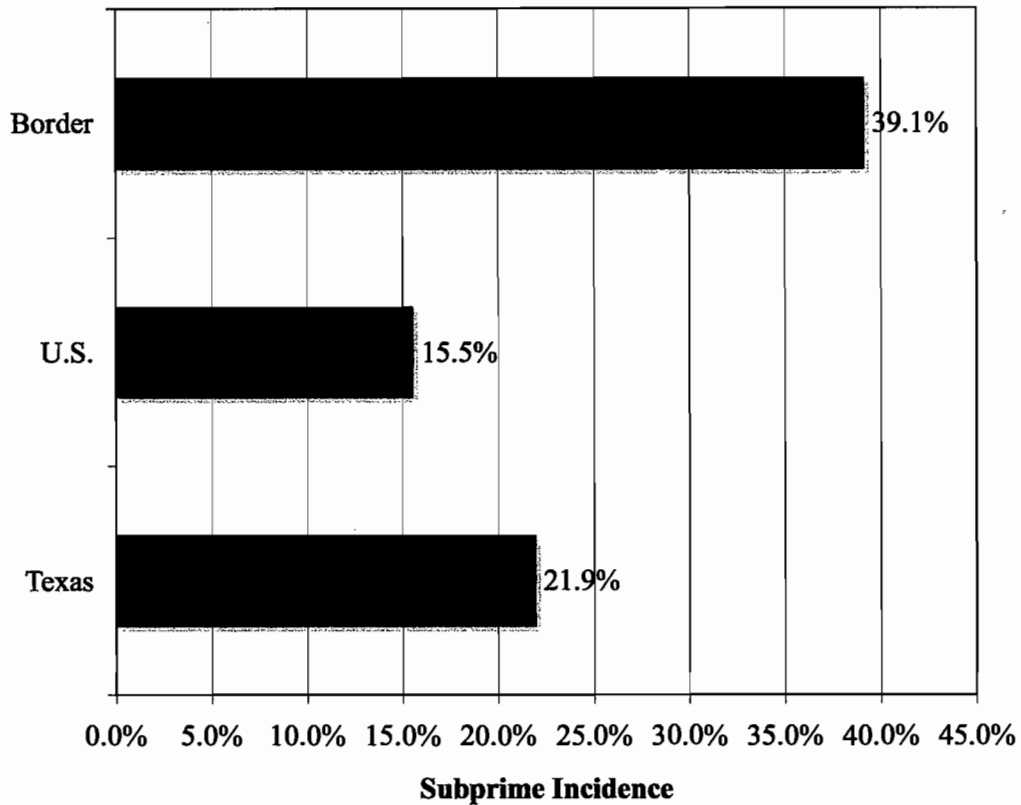
Adapted from: the Federal Financial Institutions Examination Council 2004 HMDA data – Aggregate Table 7-3 for the U.S and each MSA. Online. Available: <http://www.ffiec.gov/hmda>.

Therefore, Border applicants were 50% (1.5) more likely to be denied a refinance loan over U.S. applicants and 20% (1.2) more likely to have their application rejected as compared to Texas applicants.

Conventional Home Refinance Subprime Incidence

Among Border applicants who were awarded a refinance loan, over one-third (39.1%) were subprime wherein Brownsville had the highest frequency of 42.7% and El Paso had the lowest rate of 35.6%. U.S. applicants received high cost loans 15.5% of the time and approximately one in five (21.9%) loans to Texas applicants were high cost as well. Among Texas cities, Corpus Christi had the highest percentage of subprime originations of 30.4% and Austin had the lowest frequency of 14.2%. (See Appendix - Table 4 “Conventional Home Refinance Loans: Denials and Subprime Incidence” for data for the U.S. and each MSA within each region).

Figure 6.6
2004 Conventional Home Refinance Subprime Loan Incidence By Region



Adapted from: the Federal Financial Institutions Examination Council 2004 HMDA data – Aggregate Table B for the U.S and each MSA. Online. Available: <http://www.ffiec.gov/hmda>.

The Border subprime refinance lending rate of 39.1% was, therefore, two and a half times greater (2.5) than that for U.S. borrowers and nearly twice (1.8) the rate for Texas borrowers.

Table 6.15
Conventional Home Refinance Subprime Loan Incidence and Disparity
Ratios by Region

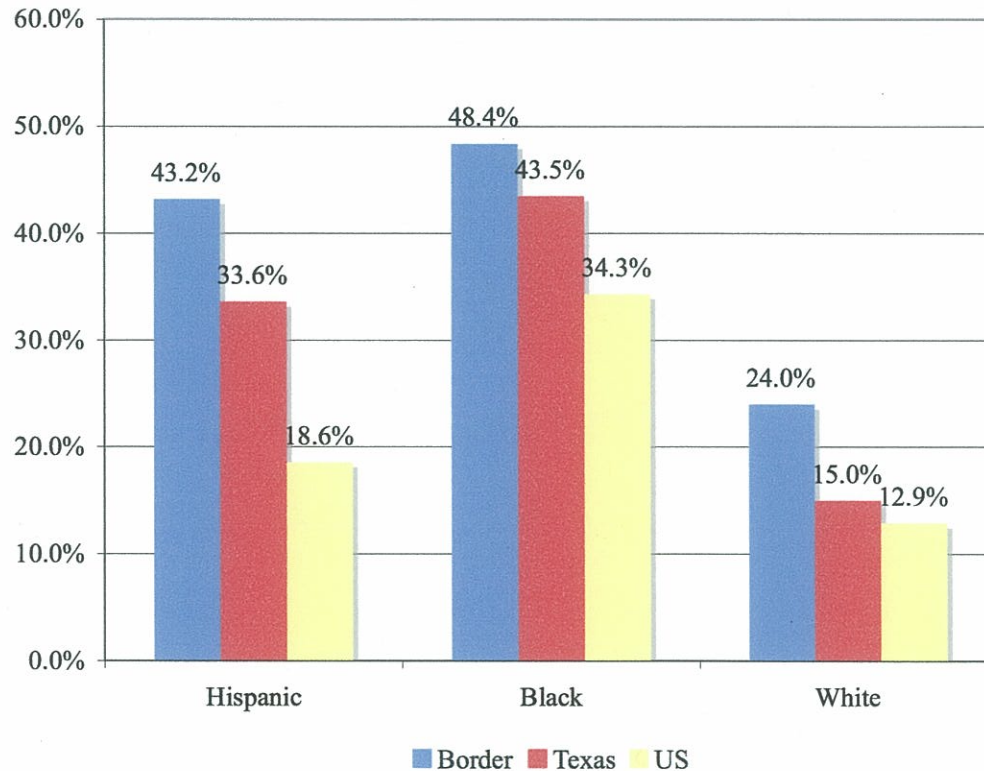
	<u>Subprime Originations</u>	<u>Disparity Ratio</u>
Border	39.1%	
U.S.	15.5%	2.5
Texas	21.9%	1.8

Adapted from: the Federal Financial Institutions Examination Council 2004 HMDA data – Aggregate Table B for the U.S and each MSA. Online. Available: <http://www.ffiec.gov/hmda>.

Racial Disparities

Border borrowers, irrespective of race or ethnicity, were awarded refinance loans at a subprime rate more frequently than for conventional home purchase loans. Additionally, as was the case in home purchase lending, minority borrowers in all regions received high cost loans at a significantly higher rate than did white borrowers. (See Appendix - Table 5 “Conventional Home Refinance Loans: Pricing Data By Race” for the data for each MSA within each region).

Figure 6.7
Conventional Home Refinance Subprime Loan Incidence by Race



Adapted from: the Federal Financial Institutions Examination Council 2004 HMDA data – Aggregate Table 11-7 for the U.S and each MSA. Online. Available: <http://www.ffiec.gov/hmda>.

In general, all borrowers from the Border experienced the highest incidence of high cost refinance originations. Border Black borrowers had the highest rate, as almost half (48.4%) of their loans were subprime, followed by Hispanics with a frequency of 43.2%, and white borrowers with a rate of 24.0%.

Comparison of Hispanic Borrowers to White Borrowers

The pattern of disparity between minority and white borrowers with regard to home purchase loans was not repeated in the refinance arena. Border Hispanics did not experience the highest level of subprime originations, as they did for home purchase loans, although the rate was very high at 43.2%. They had nearly twice (1.8) the risk of

receiving such a loan as compared to Border white borrowers for whom approximately one-quarter (24%) were subprime. This disparity ratio between Border Hispanic and white borrowers however, was greater than that between U.S. Hispanic and white borrowers with a ratio of 1.5, but less than that between Texas Hispanic and white borrowers wherein Hispanics were over twice (2.2) as likely to receive such a loan over their white counterparts.

Table 6.16
Conventional Home Refinance Loans:
Hispanic to White Comparative Subprime Incidence and Disparity Ratios

	<u>Hispanic Subprime</u>	<u>White Subprime</u>	<u>Disparity Ratio</u>
Border	43.2%	23.9%	2.0
US	34.3%	12.8%	2.7
Texas	43.5%	15.0%	2.9

Adapted from: the Federal Financial Institutions Examination Council 2004 HMDA data – Aggregate Table 11-7 for the U.S and each MSA. Online. Available: <http://www.ffiec.gov/hmda>.

Therefore, Hispanics in each region were at least 1.5 or 50% more likely to receive a subprime refinance loan as compared to white borrowers.

Comparison of Black Borrowers to White Borrowers

Once again, as was the case with home purchase loans, there were only a small number of loans made to Black borrowers on the Border. There were a total of 124 loans, of which 100 were originated in El Paso (see Appendix - Table 5 “Conventional Refinance Loans: “Pricing Data By Race” for data on each MSA within each region). Almost half (48.4%) of all the refinance loans made to Border Black borrowers were high cost. They were twice (2.0) as likely to receive such a loan as compared to Border white borrowers.

Table 6.17
Conventional Home Refinance Loans:
Black to White Comparative Subprime Incidence and Disparity Ratios

	<u>Black Subprime</u>	<u>White Subprime</u>	<u>Disparity Ratio</u>
Border	48.4%	23.9%	2.0
US	34.3%	12.8%	2.7
Texas	43.5%	15.0%	2.9

Adapted from: the Federal Financial Institutions Examination Council 2004 HMDA data – Aggregate Table 11-7 for the U.S and each MSA. Online. Available: <http://www.ffiec.gov/hmda>.

Although they had the highest incidence of subprime originations among all borrowers, the disparity ratio between Border Black and white borrowers, however, was the lowest of all three regions. U.S. Black borrowers were given high cost loans at a rate of 34.3%, but that is a rate 2.7 times higher than for white borrowers, whose subprime origination probability was 12.8%. The disparity between Texas Black and white borrowers was the greatest, wherein Black borrowers had triple (2.9) the risk of acquiring a high cost loan over their white counterparts, whose subprime origination rate was 15.0%.

Therefore, Black borrowers, irrespective of their geographical location, were at least twice as likely (2.0) to obtain a subprime refinance loan as compared to all white borrowers.

Intra-racial Disparities Across Regions

As with home purchase loans, the data on refinance loans was further analyzed to reveal the impact applying for a loan as a Border resident had on the probability of a subprime refinance origination.

Comparison of Hispanic Borrowers Across all Regions

Border Hispanics had the highest percentage of subprime originations in contrast to Hispanics in the other regions.

Table 6.18
Conventional Home Refinance Subprime Loan Incidence and Disparity Ratios Among Hispanic Borrowers Across All Regions

	<u>Subprime Originations</u>	<u>Disparity Ratio</u>
Border Hispanic	43.2%	
U.S. Hispanic	18.6%	2.3
Texas Hispanic	33.6%	1.3

Adapted from: the Federal Financial Institutions Examination Council 2004 HMDA data – Aggregate Table 11-7 for the U.S and each MSA. Online. Available: <http://www.ffiec.gov/hmda>.

Hispanics who reside in the Borderland and applied for a home refinance loan were more than twice (2.3) as likely to receive a high cost loan as opposed to U.S. Hispanics and had a 30% (1.3) greater probability as compared to Texas Hispanics.

Comparison of Black Borrowers Across All Regions

As cited above, almost half (48.4%) of all refinance loans made to Border Black borrowers were high cost.

Table 6.19
Conventional Home Refinance Subprime Loan Incidence and Disparity Ratios Among Black Borrowers Across All Regions

	<u>Subprime Originations</u>	<u>Disparity Ratio</u>
Border Black	48.4%	
U.S. Black	34.3%	1.4
Texas Black	43.5%	1.1

Adapted from: the Federal Financial Institutions Examination Council 2004 HMDA data – Aggregate Table 11-7 for the U.S and each MSA. Online. Available: <http://www.ffiec.gov/hmda>.

They had almost one and a half (1.4) times a greater risk for this type of loan than if they borrowed in the U.S. region where the probability of such an origination was 34.3%. The disparity was less between Border and Texas Black borrowers wherein Border Blacks had a 10% greater chance of receiving a high cost loan than if they had applied from elsewhere in Texas. This result, however, may be due to the low number of subprime refinance loans made to Black borrowers within the Border region.

Comparison of White Borrowers Across All Regions

Once again, white borrowers in all three regions had the lowest probability of receiving a subprime loan as compared to minority borrowers.

Table 6.20
Conventional Home Refinance Subprime Loan Incidence and Disparity Ratios Among All Borrowers Across All Regions

	<u>Hispanic Subprime</u>	<u>Black Subprime</u>	<u>White Subprime</u>
Border	43.2%	48.4%	24.0%
US	18.6%	34.3%	12.8%
Texas	33.6%	43.5%	15.0%

Adapted from: the Federal Financial Institutions Examination Council 2004 HMDA data – Aggregate Table 11-7 for the U.S and each MSA. Online. Available: <http://www.ffiec.gov/hmda>.

White Border borrowers, however, were at a distinct disadvantage over white borrowers who reside in the other regions.

Table 6.21
Conventional Home Refinance Subprime Loan Incidence Among White Borrowers Across All Regions

	<u>Subprime Originations</u>	<u>Disparity Ratio</u>
Border White	24.0%	
U.S. White	12.8%	1.9
Texas White	15.0%	1.6

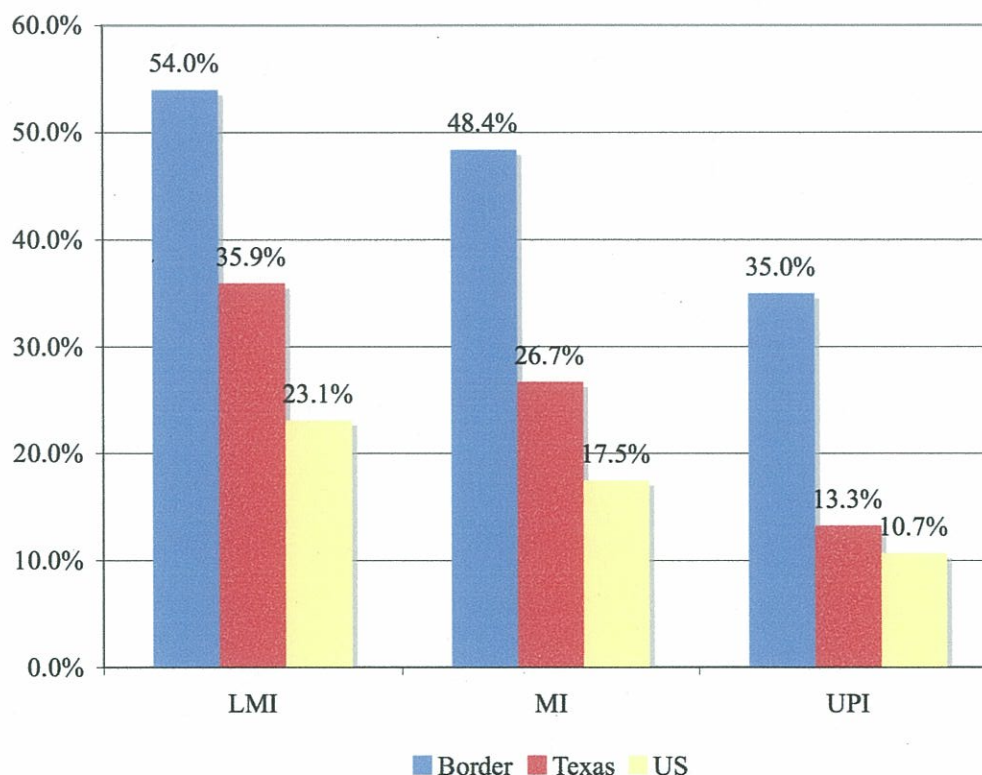
Adapted from: the Federal Financial Institutions Examination Council 2004 HMDA data – Aggregate Table 11-7 for the U.S and each MSA. Online. Available: <http://www.ffiec.gov/hmda>.

Border white borrowers were nearly twice (1.9) as likely as a U.S. white borrower to receive a high cost loan, with an incidence of 24%, as compared to 12.8% for U.S. white borrowers and they were 60% (1.6) more likely to receive such a loan as compared to Texas white borrowers to whom subprime loans were given 15% of the time.

Income Disparities

Border borrowers of home refinance loans had a higher rate of subprime originations in each income bracket as compared to U.S. and Texas borrowers, although in each region LMI borrowers had the highest incidence and UPI borrowers the lowest. An astounding 54% of all refinance loans to Border LMI borrowers were subprime, followed by MI borrowers with a frequency of 48.4% and UPI borrowers had the fewest high cost originations with a rate of 35.0%. (See Appendix – Table 6 “Conventional Home Refinance Loans: “Pricing Data by Borrower Income” for the data for the U.S. and each MSA within each region).

Figure 6.8
Conventional Home Refinance Subprime Loan Incidence By Income



Adapted from: the Federal Financial Institutions Examination Council 2004 HMDA data – Aggregate Table 11-7 for the U.S and each MSA. Online. Available: <http://www.ffiec.gov/hmda>.

The distribution of high cost loans for U.S. borrowers mirrors the pattern observed on the Border as U.S. LMI borrowers had the greatest incidence of subprime originations with a rate of 23.1%. U.S. MI borrowers had a high cost frequency of 17.5% and UPI borrowers were the least likely to receive such a loan with a 10.7% level of probability. Over one-third (35.9%) of all loans to Texas LMI borrowers were subprime as were 26.7% to MI borrowers. UPI borrowers in Texas had the lowest risk of a subprime origination among Texans with a probability of 13.3%.

Comparison of Low to Moderate Income Borrowers to Upper Income Borrowers

The majority (54%) of all refinance loan originations to Border LMI borrowers were high cost in contrast to UPI borrowers for whom the subprime origination probability was 35%. Although the incidence of high cost lending was higher for Border LMI borrowers than for U.S. LMI borrowers, with a frequency of 23.1%, Border LMI borrowers were only one and a half times (1.5) more likely to receive such a loan as compared to Border UPI borrowers. U.S. LMI borrowers had more than double (2.2) the probability of receiving such a loan over borrowers in the UPI bracket whose likelihood of a high cost origination was 10.7%. In Texas, LMI borrowers had almost triple (2.7) the probability of receiving a high cost loan in contrast to UPI borrowers whose risk of a subprime originations was 13.3%.

Table 6.22
Conventional Home Refinance Loans:
Low to Moderate Income to Upper Income Comparative Subprime
Incidence and Disparity Ratios

	<u>LMI</u> <u>Subprime</u>	<u>UPI</u> <u>Subprime</u>	<u>Disparity</u> <u>Ratio</u>
Border	54.0%	35.0%	1.5
US	23.1%	10.7%	2.2
Texas	35.9%	13.3%	2.7

Adapted from: the Federal Financial Institutions Examination Council 2004 HMDA data – Aggregate Table 11-7 for the U.S and each MSA. Online. Available: <http://www.ffiec.gov/hmda>.

Therefore, as was the case with home purchase loans, although Border LMI borrowers experienced the highest incidence of subprime refinance originations, the disparity ratio between themselves and Border UPI borrowers was the smallest among all three regions. This implies therefore, that while the subprime incidence is very high on the Border, the high cost lending is spread out more evenly among borrowers of different economic means.

Comparison of Middle Income Borrowers to Upper Income Borrowers

Almost half (48.4%) of all refinance loans to Border MI borrowers were high cost. They were 40% (1.4) more likely to receive such a loan in contrast to Border UPI whose rate of incidence was 35%. Although MI borrowers from the U.S. had a subprime lending rate that was less than half (17.5%) that of Border MI borrowers, the disparity ratio of high cost originations (1.6) was greater between them and their UPI counterparts whose subprime frequency was 10.7%. Texas MI borrowers also had a level that was much lower (26.7%) than similar Border borrowers, however, their risk of receiving such a loan was double (2.0) that of their UPI counterparts with a rate of 13.3%.

Table 6.23
Conventional Home Refinance Loans:
Middle Income to Upper Income Comparative Subprime Incidence and
Disparity Ratios

	<u>MI</u> <u>Subprime</u>	<u>UPI</u> <u>Subprime</u>	<u>Disparity</u> <u>Ratio</u>
Border	48.4%	35.0%	1.4
US	17.5%	10.7%	1.6
Texas	26.7%	13.3%	2.0

Adapted from: the Federal Financial Institutions Examination Council 2004 HMDA data – Aggregate Table 11-7 for the U.S and each MSA. Online. Available: <http://www.ffiec.gov/hmda>.

Once again, as was the case with Border LMI and Border UPI borrowers, Border MI borrowers had a significantly higher incidence of subprime refinance originations,

but the disparity between themselves and their UPI counterparts was the smallest among all three regions which again reflects that the very elevated level of subprime lending on the Border is more evenly distributed among borrowers of varying economic means than in the other regions.

Intra-Income Disparities Across Regions

Comparison of Low to Moderate Income Borrowers Across Regions

As previously noted, Border LMI borrowers had the highest probability of a subprime origination of all income groups in all regions with a rate of 54%.

Table 6.24
Conventional Home Refinance Subprime Loan Incidence Among Low to Moderate Income Borrowers Across All Regions

	<u>Subprime Originations</u>	<u>Disparity Ratio</u>
Border LMI	54.0%	
U.S. LMI	23.1%	2.3
Texas LMI	35.9%	1.5

Adapted from: the Federal Financial Institutions Examination Council 2004 HMDA data – Aggregate Table 11-7 for the U.S and each MSA. Online. Available: <http://www.ffiec.gov/hmda>.

This level is approximately two and a half times (2.3) higher than for U.S. LMI borrower whose rate of subprime frequency was 23.1% and 50% (1.5) greater than for similar borrowers in Texas who received subprime loans 35.9% of the time. It is noteworthy that although Border LMI borrowers had the greatest incidence of subprime originations of all income groups in all regions, the disparities between themselves and comparable borrowers in the U.S. and Texas were the smallest in contrast to the disparities between the other income groups across all three regions.

Comparison of Middle Income Borrowers Across Regions

Almost half (48.4%) of all refinance loans made to Border MI borrowers were subprime. They had the second highest level of high cost originations among all borrowers in all regions.

Table 6.25
Conventional Home Refinance Subprime Loan Incidence Among
Middle Income Borrowers Across All Regions

	<u>Subprime Originations</u>	<u>Disparity Ratio</u>
Border MI	48.4%	
U.S. MI	17.5%	2.8
Texas MI	26.7%	1.8

Adapted from: the Federal Financial Institutions Examination Council 2004 HMDA data – Aggregate Table 11-7 for the U.S and each MSA. Online. Available at: <http://www.ffiec.gov/hmda>.

They had almost triple (2.8) the probability of receiving such a loan in contrast to U.S. MI borrowers whose subprime frequency rate was 17.5% and nearly double (1.8) that of similar Texas borrowers for whom over one-quarter (26.7%) of loans were subprime.

Comparison of Upper Income Borrowers Across Regions

Upper Income Border borrowers in each region had the lowest level of high cost originations compared to all lower income borrowers.

Table 6.26
Conventional Home Refinance Subprime Loan Incidence Among
Upper Income Borrowers Across All Regions

	<u>Subprime Originations</u>	<u>Disparity Ratio</u>
Border UPI	35.0%	
U.S. UPI	10.7%	3.3
Texas UPI	13.3%	2.6

Adapted from: the Federal Financial Institutions Examination Council 2004 HMDA data – Aggregate Table 11-7 for the U.S and each MSA. Online. Available at: <http://www.ffiec.gov/hmda>.

Despite this lower rate of subprime incidence, Border UPI borrowers had the highest probability of a subprime origination among all UPI borrowers from all regions. They had over triple (3.3) the rate compared to U.S. UPI borrowers and were 2.6 times more likely to receive such a loan in contrast to similarly situated Texas borrowers.

Moreover, the spread in the disparities between Border UPI borrowers and the UPI borrowers from the other regions was the greatest. Therefore, compared to borrowers in each income bracket who reside in other regions, UPI borrowers on the Border had the highest risk of a subprime origination.

Conclusions

The data presented in this report reveal dramatic trends in mortgage lending on the Border. First, in regard to both conventional home purchase loans and refinance loans, Border applicants are more likely to be turned down for a loan than borrowers in the U.S. or Texas. This suggests that the Border, in its entirety, is being subjected to the older, traditional form of lending discrimination known as redlining. In concrete terms, as a result, 1 out of every 5 Border loan applicants seeking to buy a home is shut out from the opportunity to participate in the American dream of home ownership.

Second, regardless of borrower characteristics and type of loan, a Border borrower is generally more likely to receive a subprime loan than a borrower in the U.S. or Texas. That is, whether Black, Hispanic, or white, or LMI, MI, or UPI, or seeking a home purchase loan or refinance loan, a Border borrower is almost without exception more likely to receive a subprime loan than a borrower with comparable characteristics in the U.S. or Texas.³ This suggests that, unless living on Border soil and breathing Border air somehow make borrowers engage in less creditworthy behavior, the Border region in its entirety is being affirmatively targeted for subprime loans at a greater rate than the U.S. or Texas, thereby subjecting it to the newer form of lending discrimination known as reverse redlining.

¹ U.S. Federal Reserve Bank, *New Information Reported under HMDA and Its Application in Fair Lending Enforcement* (Federal Reserve Bulletin, 2005), p. 370. Online. Available: http://www.federalreserve.gov/pubs/bulletin/2005/summer05_hmda.pdf. Accessed: March 1, 2007.

² Eric Stein, *Quantifying the Economic Cost of Predatory Lending*, (Durham, Nc.: Coalition for Responsible Lending, October 2001), p. Online. Available: <http://www.responsiblelending.org>. Accessed: July 7, 2007.

³ The sole exception is the .84 disparity ratio between Border Blacks and Texas Blacks, a statistic that is vitiated by the low number of loans involved and the exceptionally high rate of subprime loans for Texas Blacks.

Chapter 7. The Current Legal Context

As discussed in Chapter 3, subprime lending and most practices that can be defined as predatory lending are not illegal. Laws such as the Fair Housing Act, the Equal Credit Opportunity Act, and the Community Reinvestment Act, while still in effect, do not outlaw such practices, but rather focus on protecting consumers against housing discrimination and unequal access to credit. Likewise, the Home Mortgage Disclosure Act focuses on other issues, providing for loan disclosure requirements to the government and help regulators identify lenders who should be investigated for engaging in redlining or loan price discrimination.

Similarly, the laws that govern mortgage and high cost mortgage lending, presented here, such as the Truth in Lending Act, the Real Estate Settlement and Procedures Act and the Homeownership and Equity Protection Act are limited and do not protect consumers from predatory lending practices, but rather are primarily designed to ensure that the borrower is informed about the terms of the loan.

Federal Law

The Truth in Lending Act

The Truth in Lending Act (TILA) was passed in 1968 as Title I of the Consumer Credit Protection Act.¹ It applies to closed-end loans (such as mortgages) and requires lenders to clearly disclose to borrowers the finance charge, the Annual Percentage Rate (APR), the amount financed, and the total of all payments.² Before TILA was enacted, lenders could advertise the same interest rate but each calculate it differently.³

Under TILA the APR is supposed to be a “benchmark” figure for borrowers to consider the real costs of credit for a loan and to allow for comparison shopping of credit.⁴ The APR is defined as a combination of the contract interest rate and the cost of the some of the fees rolled into the loan balance.⁵ This information is given to the borrower as the “Federal Truth in Lending Disclosure Statement” and is provided at the

closing.⁶ The finance charge is considered the total dollar amount of the loan including the interest and other costs such as origination fees, discount points, and private mortgage insurance.⁷ Significant exceptions to the definition of the finance charge are that it does not have to include fees for credit reports, property appraisals and inspection, notary costs, title examination, title insurance, property survey, or the preparation of deed of trust or settlement documents.⁸ TILA also provides for the right to rescind the home equity or refinance loans within three days of the closing or three days after the borrower is provided with the required disclosures.⁹

Borrowers can sue over TILA violations in the amount of twice the finance charge (although not more than \$2,000) and reasonable attorney's fees.¹⁰ At the time it was enacted TILA was considered important as its purpose was to assure "an informed use of credit...and assure a meaningful disclosure of credit terms,"¹¹ however, it does not stop predatory lending practices as it provides very limited recourse for victims of lenders who violate the law's requirements.

The Real Estate Settlement and Procedures Act

The Real Estate Settlement and Procedures Act (RESPA) was enacted in 1974. It applies to "federally related mortgage loans" secured with a mortgage on a one-to-four family residential property, which includes most home purchase loans, assumptions, refinances, home improvement loans, and home equity lines of credit.¹² In enacting RESPA, Congress intended to stop abuses that lead to increased settlement costs.¹³

It requires that fees that are part of the closing process be clearly disclosed to the borrower¹⁴ and that the lender provide a HUD Special Information Booklet¹⁵ containing information to help the borrower understand the costs of settlement services and a Good Faith Estimate (GFE) of the amount or the range of charges for specific settlement services in the transaction.¹⁶ HUD has interpreted RESPA to require that the charges disclosed on the GFE bear a reasonable relationship to the actual charges;¹⁷ however, it fails to define "reasonable relationship," and imposes no penalty on lenders who provide an inaccurate or incomplete GFE.¹⁸

At or before closing the borrower is required to receive the Uniform Settlement Statement (HUD-1) that delineates the final costs associated with both the loan and, if applicable, the purchase transaction.¹⁹ Further, Section 8 (a) prohibits kickbacks, referral fees, and unearned fees²⁰ to other parties involved in the mortgage such as real estate agents or contractors.²¹ According to Jeanette Bradley, of the Community Reinvestment Association of North Carolina, this provision includes a prohibition against yield spread premiums if the borrower did not agree to the amount of compensation to the broker.²² In practice, however, yield spread premiums paid to mortgage brokers have not been found to be prohibited. The statute also provides criminal penalties for violations of Section 8, private rights of action for damages, and limited injunctive relief.²³ However, weaknesses in the law include short statutes of limitations and a lack of sanctions for violations of the disclosure provisions concerning settlement costs.²⁴

The Homeownership and Equity Protection Act

The Homeownership and Equity Protection Act (HOEPA) is the only law that deals specifically with high cost, high fee, or high rate mortgages,²⁵ as it creates a category of special “high cost” loans with special protections.²⁶ HOEPA was enacted as part of the Riegle Community Development and Regulatory Improvement Act of 1994 and amended TILA²⁷ to (according to the Federal Reserve) explicitly target predatory lending practices.²⁸ According to the HUD/Treasury report of 2000, the origin of HOEPA was “a concern about ‘reverse redlining,’” although the report acknowledges that instead, it only subjects certain (high cost) loans to enhanced disclosures, restrictions on certain contract terms and private and administrative consumer remedies for violations of the act.²⁹

It covers closed-end home loans (excluding home purchase loans) with specific durations, such as a 15 or 30 year mortgage,³⁰ and applies to first-lien loans if the APR is more than 8 percentage points higher than the rate of comparable Treasury bonds and 10 percentage points higher for second-lien loans.³¹ If, for example, the rate for 30-year Treasury securities is 5%, a first-lien mortgage loan with an APR of 13% is classified as

a HOEPA loan. HOEPA protections are also triggered if the total of certain loan fees exceed 8% of the loan amount.³²

For loans that meet the criteria as “high cost,” HOEPA prohibits balloon payments in the first 5 years;³³ bans prepayment penalties after 5 years;³⁴ forbids negative amortization; restricts payments prepaid from proceeds; outlaws increased interest payments after default;³⁵ and requires that lenders document the income of high-cost borrowers.³⁶ Further, it prohibits lenders from engaging in a “pattern or practice” of extending HOEPA loans based on the home value without regard to the consumer’s ability to repay from sources (income) other than home equity.³⁷ The lender must disclose the APR and the amount of the regular monthly payment, including any balloon payment that might be part of the loan.³⁸ Loan flipping is also prohibited, as a HOEPA loan cannot be refinanced within one year, unless it is clearly in the consumer’s interest to do so.³⁹

These “high cost” loans require certain disclosures in addition to those required by TILA.⁴⁰ Such disclosures must be in “conspicuous type size” and given to the loan applicant at least 3 days before closing.⁴¹ The lender must disclose that the consumer is not required to complete the loan process even though an application has been signed and that the loan creates a mortgage on the consumer’s house that could result in the consumer’s losing the home and any equity in the home if the loan is not repaid.⁴² HOEPA also contains a provision which makes a secondary buyer of the loan liable for any violations or misrepresentations that occurred at the time the loan was extended (referred to as assignee liability).⁴³ According to the Federal Reserve Bank in 2003, such assignee liability makes some secondary market purchasers reluctant to purchase HOEPA loans.⁴⁴

For adjustable-rate HOEPA loans the lender must disclose the APR, the monthly payment, the amount of the highest monthly payment based on the allowable interest rate, and make clear that the interest rate and monthly payment may increase.⁴⁵

The problem with HOEPA is that the threshold for triggering the protections under it are so high that in 2001 the Federal Reserve reported that only 1% of subprime mortgage loans fell within HOEPA's trigger APR and estimated that by 2003 approximately 5% of all loans would qualify as HOEPA loans and provide the intended benefits to consumers.⁴⁶ However, in 2005, after the release of the 2004 HMDA data it was revealed by the Federal Reserve that, in fact, only .003% of all refinance and home improvement loans were classified as HOEPA loans.⁴⁷

The Office of the Comptroller of the Currency

The Gramm-Leach-Bailey Financial Services Modernization Act of 1999 (GLBA) enabled banks and conglomerates to offer a wide variety of financial services.⁴⁸ State usury laws, however, often required that lenders tailor their loan programs to meet unique state law requirements.⁴⁹ On January 7, 2004 the Federal Office of the Comptroller of the Currency (OCC) announced that the institutions it regulates (federally chartered banks and their subsidiaries) would no longer have to comply with state lending (usury) rules.⁵⁰ The OCC supervises approximately 1,900 national banks nationwide, which represent about 28% of all insured commercial banks in the United States, or 57% of the total assets of the banking system.⁵¹

Under the rule change issued by the OCC, state laws are preempted for transactions involving federally chartered banks and their operating subsidiaries. The press release issued by the OCC states, "the application of multiple and often unpredictable state laws interferes with (lenders') ability to plan and manage business, as well as their ability to serve the people, the communities and the economy of the United States."⁵² Ultimately, the OCC rules shield all national banks and operating subsidiaries from oversight, inspection and enforcement by any state authority.⁵³

This move by the OCC is troublesome as it allows federally chartered institutions to "rent" their preemption authority and predatory lenders could seek protection from state laws under the rented charters.⁵⁴ The rules also eliminate a state's ability to form a

local solution to problems and state attorneys general have lost enforcement authority to pursue federally affiliated lenders who engage in predatory practices.⁵⁵

State Law

Although Texas has not adopted any specific anti-predatory lending legislation, according to the Texas Office of Consumer Credit Commissioner (OCCC), Texas has viable protections against predatory lending already in place in existing statutes.⁵⁶ The provisions that address abusive lending practices are contained in the Texas Home Equity Lending Constitutional Amendment (Article XVI, Section 50 (a)), which took effect in 1998;⁵⁷ and SB1581 passed during the 77th legislative session in 1991, which amended the Texas Finance Code.⁵⁸

These provisions provide the following protections:

Equity Stripping

Home Equity Constitutional Amendment

Restricts the amount of equity that can secure the loan to 80%, requiring that some equity remain with the homeowner.

Restricts a borrower to one home equity loan per year, thereby limiting refinance fees and protecting the borrower's equity.

Texas Finance Code

Ensures lenders evaluate a borrower's ability to repay before a loan is made, ensuring that a lender's decision is not based solely upon a borrower's equity (for second mortgages).

Loan Flipping

Home Equity Constitutional Amendment

Restricts a borrower to one home equity loan per year, limiting refinance fees and protecting the borrower's equity

Texas Finance Code

Restricts lenders from contracting for prepayment penalties on loans with interest rates of 12% or more to refinance a loan.

Excessive Fees

Home Equity Constitutional Amendment

Restricts a lender to 3% in fees, limiting the ability of lenders to charge for certain reimbursable costs.

Texas Finance Code

Limits lenders from collecting fees that are not reasonable or authorized.

Insurance

Texas Finance Code

Limits lenders from contracting for insurance where the premium is prepaid in a single installment, without providing a monthly premium alternative where the amount of the insurance is not included in the loan.

Balloon Payments

Home Equity Constitutional Amendment

Prohibits lenders from contracting for balloon payments.

Texas Finance Code

Prohibits lenders from contracting for balloon payments (for second mortgages).

Aggressive Marketing

Home Equity Constitutional Amendment

Requires lenders to provide certain disclosures to borrowers warning that failure to repay the loan could result in the loss of the home.

Texas Finance Code

Requires lenders to provide a disclosure to a borrower warning that the loan could be considered a “high cost home loan” and directing the borrower to locations where counseling can be attained.

Fraud and Abuse

Home Equity Constitutional Amendment

Requires lenders to provide certain disclosures to borrowers warning that failure to repay the loan could result in the loss of the home.

Texas Finance Code

For loans with an interest rate of 12% or higher lenders are required to provide a disclosure to a borrower warning that the loan could be considered a “high cost home loan” and direct the borrower to locations where counseling can be obtained.

Adapted from: Office of Consumer Credit Commissioner “Strategic Plan” 2005-2009. Online. Available at: <http://www.occ.state.tx.us/pages/agency/strat05/index.html>.

The Federal OCC preemption rules adopted in 2004 shield national banks and their subsidiaries from oversight by state authorities, however, the state still maintains authority over non-bank mortgage lending companies owned by financial or bank holding companies (non-bank mortgage lending subsidiaries), such as finance and mortgage companies, which account for an estimated 24% of subprime loan originations.⁵⁹

Conclusions

The federal and state laws and regulations that are currently in place that are designed to regulate mortgage lending have not kept pace with the changes in the mortgage market and are clearly out of date. Thus, they do not protect consumers from

the damage caused by predatory lending. Chapter 8 proposes several approaches to update the role of government with respect to the mortgage lending industry-specifically subprime lenders, and to stop predatory lending practices all together.

¹ U.S. Office of the Comptroller of the Currency Administrator of National Banks, *Truth in Lending: Comptroller's Handbook* (December 2006), p.1. Online. Available: <http://www.occ.treas.gov/handbook/til.pdf>. Accessed: October 10, 2007.

² U.S. Department of Housing and Urban Development (HUD) and U.S. Department of Treasury (Treasury), *Curbing Predatory Home Mortgage Lending: A Joint Report* (June 2000), p. 54. Online. Available: <http://www.huduser.org>. Accessed: September 20, 2006.

³ Ibid.

⁴ Ibid., p. 55.

⁵ Richard Lord, *American Nightmare: Predatory Lending and the Foreclosure of the American Dream*, (Monroe: Common Courage Press, 2005), p. 182.

⁶ Ibid.

⁷ Patricia A. McCoy, "Predatory Lending Practices: Definition and Behavioral Implications," in *Why the Poor Pay More: How to Stop Predatory Lending*, ed. Gregory D. Squires (Westport: Praeger Publishers, 2004), p. 85.

⁸ Philip Relman, et al., "Designing Federal Legislation That Works: Legal Remedies for Predatory Lending," in *Why the Poor Pay More: How to Stop Predatory Lending*, p. 157.

⁹ Richard Lord, *American Nightmare: Predatory Lending and the Foreclosure of the American Dream*, p. 182.

¹⁰ HUD and Treasury, *Curbing Predatory Home Mortgage Lending*, p. 55.

¹¹ Philip Relman, et al., "Designing Federal Legislation That Works: Legal Remedies for Predatory Lending," in *Why the Poor Pay More: How to Stop Predatory Lending*, p. 157 (citing preamble to the Truth in Lending Act).

¹² Ibid., p. 160 (quoting the Real Estate Settlement and Procedures Act).

¹³ HUD and Treasury, *Curbing Predatory Home Mortgage Lending*, p. 55.

¹⁴ Richard Lord, *American Nightmare: Predatory Lending and the Foreclosure of the American Dream*, p. 182.

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- ¹⁵ HUD and Treasury, *Curbing Predatory Home Mortgage Lending*, p. 62.
- ¹⁶ Ibid., p. 55.
- ¹⁷ Ibid.
- ¹⁸ Richard Lord, *American Nightmare: Predatory Lending and the Foreclosure of the American Dream*, p. 182.
- ¹⁹ HUD and Treasury, *Curbing Predatory Home Mortgage Lending*, p. 55.
- ²⁰ Ibid.
- ²¹ Jeanette Bradley, *The Guide to Predatory Lending Research*, (Durham, N.C.: Community Reinvestment Association of North Carolina, June 2000), p. 2.
- ²² Ibid.
- ²³ HUD and Treasury, *Curbing Predatory Home Mortgage Lending*, p.56.
- ²⁴ Ibid.
- ²⁵ Jeanette Bradley, *The Guide to Predatory Lending Research*, p.2.
- ²⁶ Richard Lord, *American Nightmare: Predatory Lending and the Foreclosure of the American Dream*, p. 182.
- ²⁷ HUD and Treasury, *Curbing Predatory Home Mortgage Lending*, p. 53.
- ²⁸ U.S. Federal Reserve Bank, *New Information Reported under HMDA and Its Application in Fair Lending Enforcement* (Washington, D.C., 2005), p. 350. Online. Available: http://www.federalreserve.gov/pubs/bulletin/2005/summer05_hmda.pdf. Accessed: March 1, 2007.
- ²⁹ HUD and Treasury, *Curbing Predatory Home Mortgage Lending*, p. 53.
- ³⁰ Richard Lord, *American Nightmare: Predatory Lending and the Foreclosure of the American Dream*, p. 183.
- ³¹ U.S. Federal Reserve Bank, *New Information Reported under HMDA and Its Application in Fair Lending Enforcement*, p.351.

Note: Prior to December 2001 HOEPA loans were those 10 percentage points higher than comparable Treasury securities for first-lien loans and kept at 10 percentage points higher for second-liens. This change was made by the Federal Reserve Board of Governors.

³² Richard Lord, *American Nightmare: Predatory Lending and the Foreclosure of the American Dream*, p. 183.

³³ Speech by Edward Gramlich, member of the Board of Governors of the Federal Reserve System at the Texas Association Bank Counsel 27th Annual Convention, South Padre Island, Texas. October 9, 2003. Online. Available: <http://www.federalreserve.gov/Boarddocs/speeches/2003>. Accessed: January 21, 2007.

³⁴ Ibid.

³⁵ Philip Relman, et al., "Designing Federal Legislation That Works: Legal Remedies for Predatory Lending," in *Why the Poor Pay More: How to Stop Predatory Lending*, p. 159.

³⁶ Richard Lord, *American Nightmare: Predatory Lending and the Foreclosure of the American Dream*, p. 187.

³⁷ HUD and Treasury, *Curbing Predatory Home Mortgage Lending*, p. 54.

³⁸ Ibid., p. 53.

³⁹ Bankersonline.com, *Complying with HOEPA*, October 1, 2002. Online. Available: <http://www.bankersonline.com>. Accessed: October 10, 2007.

⁴⁰ HUD and Treasury, *Curbing Predatory Home Mortgage Lending*, p. 53.

⁴¹ Ibid.

⁴² Ibid.

⁴³ Speech by Edward Gramlich, member of the Board of Governors of the Federal Reserve System at the Texas Association Bank Counsel 27th Annual Convention, South Padre Island, Texas. October 9, 2003.

⁴⁴ Ibid.

⁴⁵ Philip Relman, et al., "Designing Federal Legislation That Works: Legal Remedies for Predatory Lending," in *Why the Poor Pay More: How to Stop Predatory Lending*, p. 159.

⁴⁶ Speech by Edward Gramlich, member of the Board of Governors of the Federal Reserve System at Cleveland State University, Cleveland, Ohio. March 23, 2001. Online. Available: <http://www.federalreserve.gov.boarddocs/speeches/2001>. Accessed: October 13, 2007.

⁴⁷ U.S. Federal Reserve Bank, *New Information Reported under HMDA and Its Application in Fair Lending Enforcement*, p. 372.

⁴⁸ Texas Office of Consumer Credit Commissioner, *Strategic Plan for the Period 2005-2009* (Austin, Texas, 2005), p. 20. Online. Available: <http://www.occ.state.tx.us/pages/agency/strat05/index.html>. Accessed: May 05, 2007.

⁴⁹ Ibid.

⁵⁰ Richard Lord, *American Nightmare: Predatory Lending and the Foreclosure of the American Dream*, p. 197.

⁵¹ Bankrate.com, *Predatory Lending: Who's Watching Your Back?* by Laura Bruce, November 1, 2005. Online. Available: <http://www.bankrate.com>. Accessed: July 25, 2007.

⁵² Richard Lord, *American Nightmare: Predatory Lending and the Foreclosure of the American Dream*, p. 197.

⁵³ Texas Office of Consumer Credit Commissioner, *Strategic Plan for the Period 2005-2009*, p. 20.

⁵⁴ Ibid.

⁵⁵ Ibid.

⁵⁶ Ibid., p. 15.

⁵⁷ Judon Fambrough, "Potential Pitfalls Face Texas Home Equity Lenders," *Real Estate Center : Letter of the Law*, vol. 12, no. 4 (September 1998), p.1. Online. Available: <http://www.recenter.tamu.edu/pdf/1252.pdf>. Accessed: October 16, 2007.

⁵⁸ Texas Senate Bill 1581, 77th Legislature, regular session (1991). Online. Available <http://www.capitol.state.tx.us/BillLookup/>. Accessed: October 16, 2007.

⁵⁹ Texas Office of Consumer Credit Commissioner, *Strategic Plan for the Period 2005-2009*, p.17.

Chapter 8. Solutions to Subprime and Predatory Lending

Further Research

The research presented in this report should be expanded to include HMDA data for 2005 and 2006. Further, loan denial rates and subprime lending levels should be determined based not only on individual borrower demographics (ethnicity/race and income), but also on corresponding census tract demographics (racial/ethnic composition and income characteristics).

In addition to the aggregate data publicly available on the FFIEC website, the analysis should include the complete data set, which can be purchased from the FFIEC. This would permit more in-depth analysis through the combination of the ethnicity/race and income variables (e.g., percent subprime in LMI white/Hispanic/Black borrowers; moderate income in white/Hispanic/Black borrowers, etc.).

Use of the complete data sets would also permit more in-depth analysis of the level of subprime lending by individual lenders, allowing researchers to ascertain which lenders are the primary subprime lenders on the Border, to whom they lend by race, income, and neighborhood composition, and whether such lenders are national, state, or local entities. This is important because prior research shows local banks in El Paso have loan-to-deposit ratios which reveal that hundreds of millions of dollars El Paso depositors have put in local banks (loan payments and deposits) have been exported to other communities.¹

Federal Legislative Recommendations

Truth in Lending Act

Although the Truth in Lending Act contains provisions requiring lenders to clearly disclose to borrowers the terms of the loan, additional specific requirements would be helpful. For example, in December 2002, Texas Attorney General Greg Abbot obtained a judgment of \$7.5 million against Household International, Inc. and its

subsidiaries—Household Finance Corp. and Beneficial Corp—for engaging in deceptive lending practices.² One such practice was presenting loan documents in English to borrowers who were Spanish dominant or did not understand English at all.³ Household Finance was court ordered to “provide Spanish language loan documents in all branch offices that are certified by Household to conduct Spanish language transactions...Household shall also make available a one-page disclosure of key terms in Spanish in certified branch offices to those borrowers whose primary language is Spanish.”⁴ Accordingly, the Truth in Lending Act should be amended to require that loan documents be made available in the dominant secondary language for each state or area in which the lender is certified to conduct business (such as Spanish, Vietnamese, etc.).

The Real Estate Settlement and Procedures Act

RESPA should be amended to require the following:

1. The Good Faith Estimate of the cost of the loan should be provided earlier in the mortgage application process. The GFE should be required to be given to the applicant at least 10 days prior to the scheduled closing instead of 3 days to allow the applicant time to review and understand all of the costs and perhaps seek out another lender without the pressure of the imminent closing.
2. Language that currently requires the GFE to have merely a “reasonable relationship” to the actual closing costs should be eliminated. There needs to be a strictly defined allowable difference between the closing costs listed on the GFE and the actual final closing costs.
3. Lenders in violation of the defined allowable difference between the GFE and final closing costs should be penalized for each violation.
4. Section 8(a) should be expanded to include prohibition of yield spread premiums paid to mortgage brokers, including criminal penalties for violations.

The Homeownership and Equity Protection Act

HOEPA should be amended to require the following:

1. Allow home purchase and open-ended lines of credit to qualify as HOEPA loans.

2. Lower the threshold that defines a loan as “high cost” and places it under HOEPA to 6 percentage points above Treasury rates for first-lien loans and 8 percentage points for second-liens.
3. Lower the fee threshold to place loans under HOEPA disclosures and protections from 8 % of the loan amount to 6 %.
4. Prohibit balloon payments that come due anytime before the 15th year of the loan for 30 year mortgage loans and 10 years for 15 year mortgage loans.
5. Ban prepayment penalties after the 3rd year of the loan.
6. Prohibit all mandatory arbitration clauses.
7. Require that lenders regularly report borrowers’ payment history to credit bureaus so borrowers will have the opportunity to refinance high cost loans at the earliest possible opportunity should their credit history improve.

The Community Reinvestment Modernization Act

Congress should enact the Community Reinvestment Modernization Act (HR1289) introduced in March 2007 by Eddie Bernice Johnson (D-TX) and Luis Gutierrez (D-IL), the key features of which are the following:⁵

1. The CRA Modernization Act calls for the expansion of the CRA to include bank lending through mortgage brokers, mortgage companies, insurance firms, and securities companies.⁶
2. Each of these lenders would be subject to CRA exams by the Federal Reserve or the appropriate regulatory agency.

The passage of the Act could significantly impact predatory lending as the Federal Reserve found that 34.3% of home purchase loans originated by non-CRA covered lenders were subprime in 2005, whereas only 5.1% of the home purchase loans originated by depository institutions subject to CRA examination were subprime.⁷ Although not currently proposed, the Act should also award lenders credit on their CRA evaluations if they end steering along with policies to “promote” borrowers from subprime to prime loans and penalize them for the predatory practice of steering borrowers to a subprime loan when they qualify for a prime rate loan.

Other Federal Legislative Recommendations

Further federal legislation regarding predatory lending should include the following provisions:

Loan Flipping

Ban all “loan flipping” unless the refinancing of a loan will provide a net benefit to the borrower.

Single Premium Credit Insurance

Single premium credit insurance should be banned from all home loans as purchasing such insurance up front in a lump sum does not benefit borrowers. Such insurance should be allowable if spread out and purchased on a monthly basis.

Liability for Lenders

All mortgage lenders should be held liable for fraudulent or illegal acts committed by brokers or contractors from whom borrowers were referred.

Increase Penalties

All penalties should be enforced and increased for violations of TILA, RESPA and HOEPA.

Level the Playing Field

Despite the 2004 ruling by the OCC which preempts states’ ability to regulate national banks, lenders such as non-bank mortgage lending companies owned by financial or bank holding companies are still subject to individual states’ efforts to curb predatory lending.⁸ Thus, the subprime lending industry faces a patchwork of different rules in different states.⁹ In November 2003, Margot Saunders of the National Consumer Law Center went before Congress and proposed a solution that would make life easier for both lenders and consumers.¹⁰ Her proposal:

Ban the financing of points, application fees, broker fees and closing costs. Make lenders pay those costs out of their own pockets. That would encourage lenders, who have more information and power than individual consumers, to negotiate closing costs and fees down to their lowest possible level. Instead of making money at the closing, lenders would have to make their profits by collecting interest.¹¹

According to Saunders, the interest rate would go up, perhaps even as much as a half percentage point or more; however, market forces would keep the interest rate hikes relatively modest because consumers would be newly empowered to shop around for the best loan.¹² With only the interest rate varying from loan to loan, the average consumer would be able to effectively compare lenders' competing offers.

Regulatory Recommendations

HMDA Data

The Federal Reserve Board should issue new rules under HMDA to require lenders to report more information about loan applications, originated loans and borrowers in include the rate spread, fees, debt-to-income ratio, FICO score and percent of the borrower's income that is to be paid toward the loan. This data is already collected by the lenders in every loan application and would not pose an added burden to them. Further, it would assist the Federal Reserve and other regulatory agencies to determine which lenders are engaged in non-risk based pricing and practices that involve disparate treatment of borrowers or result in a negative disparate impact with regard to the denial and pricing of loans for borrowers who are members of protected classes as well as those engaged in redlining and reverse redlining.

State Level Policy Recommendations

Research

Border legislators should secure funding from the State of Texas to conduct more sophisticated research, such as multivariate regression analysis of combined HMDA and

proprietary credit bureau data, to gain further insight into why loan denial rates and subprime originations are so prevalent on the Border and determine appropriate policy responses to address the problem.

Improve Financial Literacy in Texas

In 2005, the 79th Texas Legislature enacted HB 900, sponsored by Representative Norma Chavez (D - El Paso), which requires that workforce development programs throughout the state provide training in financial literacy.¹³ HB 900 states:

The commission and local workforce development boards shall ensure that each workforce development program offered in this state include training in financial literacy.¹⁴

The program, however, was not funded. It was to be paid for through the “donation of services, money, or property that the commission determines furthers the financial literacy training program.”¹⁵ Border legislators should work together to secure state funding for this program so that those who are trained through the local workforce development programs are guaranteed to have at least a basic level of financial literacy.

Also in 2005, the 79th Texas Legislature enacted Senate Bill 851, sponsored by Senator Eliot Shapleigh (D – El Paso) and Representative Beverly Wooley (R – Houston), which directed the Texas Education Agency to:

Establish and implement a financial literacy pilot program to provide students in participating school districts with the knowledge and skills necessary as self-supporting adults to make critical decisions relating to personal financial matters.¹⁶

The program, run by the Texas Jumpstart Coalition in conjunction with a number of state agencies and was funded by a \$40,500 grant from the National Credit Union Foundation.¹⁷ It was limited, however, to 25 school districts but the El Paso Independent School district participated in the pilot program.¹⁸ This program needs to be fully funded by the State and expanded to include all Border region school districts.

Self-Help

In 1999, the Texas legislature set aside \$5.6 million for a pilot program initiated by the Low Income Border Housing Coalition known as the “Texas Bootstrap Housing Loan” program, wherein loans were provided directly to low-income families to build their own homes.¹⁹ Two-thirds of the funds were targeted for the Texas-Mexico Border region. Under this program, borrowers supply at least 60% of the labor to build their own home in exchange for favorable credit terms and lower interest rates.²⁰ The program was designed to build on and expand on the success of non-profit organizations that operate such “self-help” programs in the colonias and Border counties. One such example is the Lower Valley Housing Corporation (Fabens, Texas).²¹ The Texas Legislature needs to assess the success of the Texas Bootstrap Housing Loan program and, if determined to have been successful, expand it and increase funding for it.

Conclusions

If homeownership is indeed the American dream, subprime and predatory lending can rob both potential and current homeowners of that dream by stripping them of their equity. This is not to deny that subprime lending can actually create an opportunity for homeownership for those with damaged credit who might not otherwise be able to access the credit necessary for the purchase of a home. Subprime lending can also be helpful in refinance lending, as the equity in the home can be used to reduce more expensive consumer debt. However, problems arise when subprime loans are made to borrowers on a basis that is not strictly risk-based, thereby resulting in pricing discrimination, including when borrowers or geographic regions such as neighborhoods, cities or a large portion of a state are targeted by subprime lenders or when applicants are steered to high cost loans when unnecessary.

As shown in this report, the 2004 HMDA data demonstrate that the Texas Border region has very high levels of loan denials and subprime originations, as well as disparity ratios that run across race and class categories in comparison to the U.S. and Texas. The reasons for this are unclear and merit further investigation by researchers and policy

makers. The recommendations cited here, however, can help remedy, limit, or combat the effect of high cost loans for all consumers—including those on the Border.

¹ Daniel de Robles, et al., *Four Prominent Banks in El Paso: Do They Invest Capital in the Local Economy at Rates Comparable to Other Markets?* El Paso Community Scholars (El Paso, Tx., July 1999), p. 4. Online. Available: <http://www.communityscholars.org>. Accessed: January 28, 2006.

² “Attorney General Abbott Wins \$7.5 Million Texas Settlement With Consumer Finance Giant: Household International Inc. Cited for Deceptive Lending Practices,” Office of the Texas Attorney General, December 16, 2002 (press release). Online. Available: <http://www.oag.state.tx.us>. Accessed: January 21, 2007.

³ State Senator Eliot Shapleigh, “Housing Challenges on the Border” in *Texas Borderlands: Frontier of the Future 2007*, p. 17. Online. Available: <http://www.shapleigh.org>. Accessed: May 12, 2007.

⁴ Ibid., p.16.

⁵ “CRA Modernization Bill Introduced, Communities Stand to Receive Trillions,” National Community Reinvestment Coalition, March 2, 2007 (press release). Online. Available: <http://www.ncrc.org>. Accessed: October 11, 2007.

⁶ Ibid.

⁷ National Community Reinvestment Coalition, *30th Anniversary of The Community Reinvestment Act: Trillions of Dollars of Loans and Investments for Low and Moderate Income Communities*, (Washington, D.C., 2007), p.3. Online. Available: <http://www.ncrc.org>. Accessed: October 11, 2007.

⁸ Texas Office of Consumer Credit Commissioner, *Strategic Plan for the Period 2005-2009*, (Austin, Texas., 2005). p. 17. Online. Available: <http://www.occ.state.tx.us/pages/agency/strat05/index.html>. Accessed: May 05, 2007.

⁹ Richard Lord, *American Nightmare: Predatory Lending and the Foreclosure of the American Dream*, (Monroe: Common Courage Press, 2005), p. 204.

¹⁰ Ibid., p. 205.

¹¹ Ibid.

¹² Ibid.

¹³ Texas House Bill No 900, Section 1. Subchapter A Chapter 302 Labor Code Sec. 302.0027, 79th Legislature, regular session (2005). Online. Available: <http://www.capitol.state.tx.us/BillLookup/>. Accessed: October 19, 2007.

¹⁴ Ibid.

¹⁵ Ibid.

¹⁶ State Senator Eliot Shapleigh, "Access to Capital and Credit" in *Texas Borderlands: Frontier of the Future* (2007), p. 25. Online. Available: <http://www.shapleigh.org>. Accessed 05/12/07; and Texas Jumpstart Coalition, *Jump\$art Coalition for Personal Financial Literacy*. Online. Available: <http://www.txjumpstart.org>. Accessed: October 20, 2007.

¹⁷ Texas Jumpstart Coalition, *Jump\$art Coalition for Personal Financial Literacy*. Online. Available: <http://www.txjumpstart.org>. Accessed: May 12, 2007.

¹⁸ Ibid.

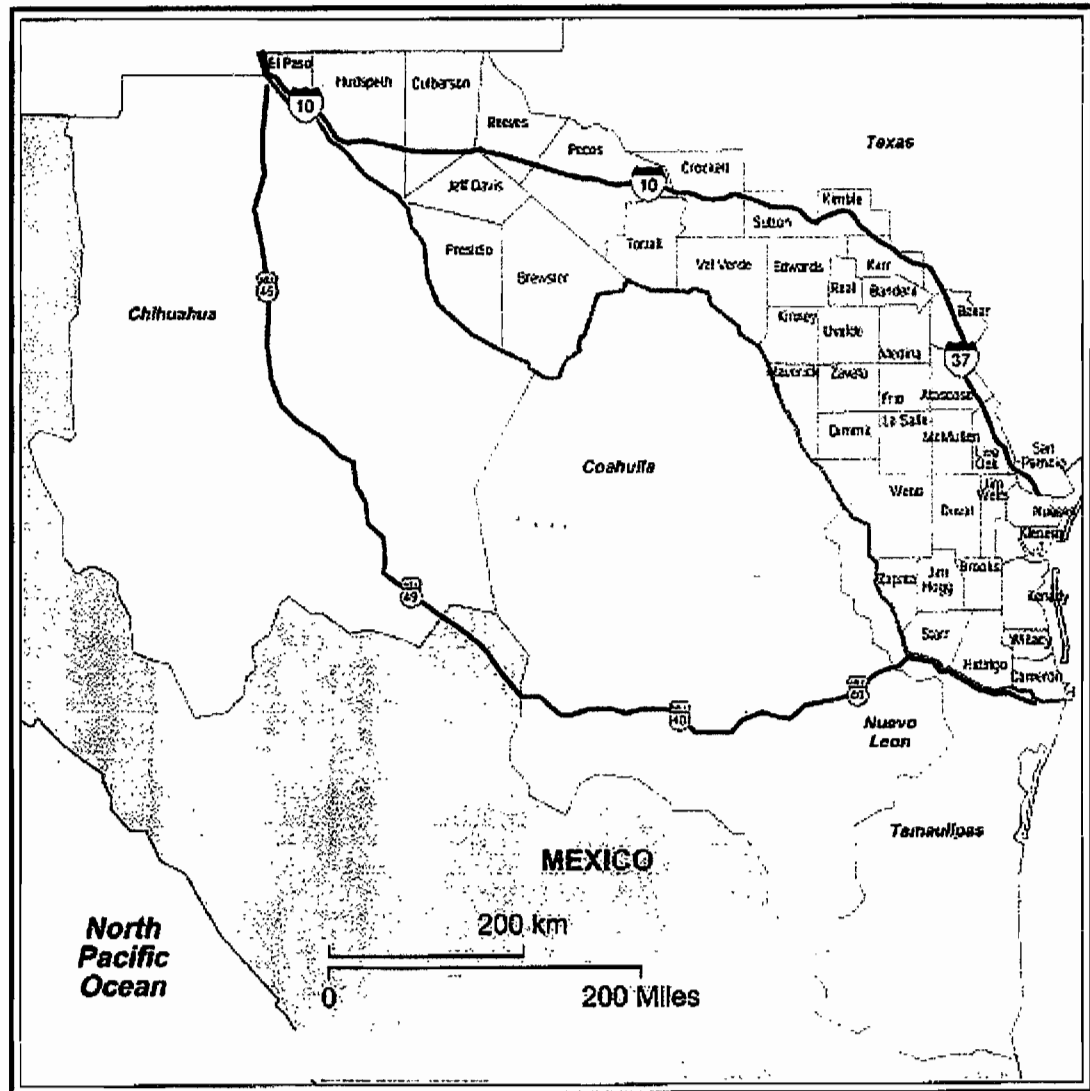
¹⁹ John Henneberger, "Affordable Housing on the Border," *Borderlines* 65, vol. 8 no. 3 (March 2000). Texas Low Income Housing Information Service, p.6. Online. Available: <http://irc-online.org/us-mex/borderlines/2000/bl65comp.html>. Accessed: May 19, 2007.

²⁰ Ibid.

²¹ Ibid. This author has personally observed the innovative manner in which this program has successfully assisted many low-income families who would not otherwise ever have become homeowners. In addition, this program has been in existence for over 15 years.

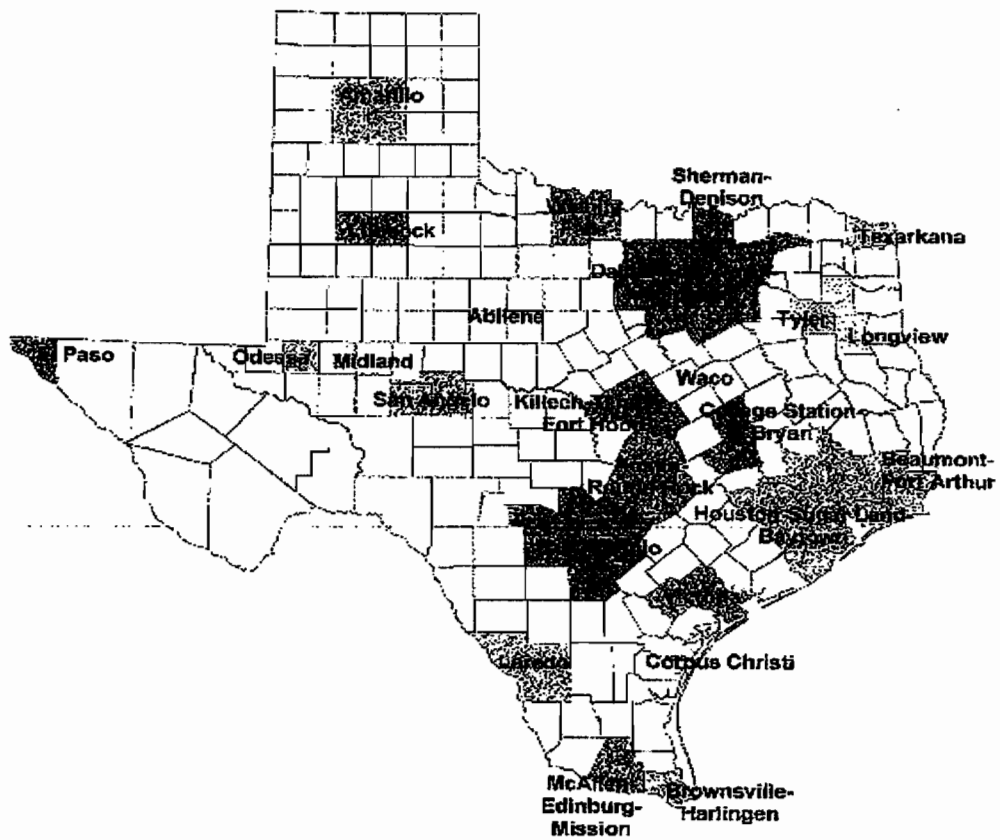
APPENDIX

Texas – Mexico Border Region



Source: Texas Comptroller of Public Accounts, *Bordering on the Future: Challenge and Opportunity in the Texas Border* (Austin, Tx., 1998). Online.
Available: <http://www.window.state.tx.us.border>.

Metropolitan Statistical Areas of Texas – 2004



Source: Texas State Data Center and Office of the State Demographer.
Online. Available: <http://www.tx.utsa.edu>.

TABLE 1
CONVENTIONAL HOME PURCHASE LOANS:
LOAN APPLICATION DENIALS AND SUBPRIME INCIDENCE

BORDER MSAs

	TOTAL APPS	# DENIED	% DENIED	TOTAL LOANS	RPD	% SUBPRIME
BVILLE/HRLNGN	5651	1153	20.40%	1744	620	35.55%
EL PASO	11222	2096	18.68%	4534	955	21.06%
LAREDO	3756	672	17.89%	1491	556	37.29%
MCALLN/ED/PHAR	9619	2254	23.43%	3380	1403	41.51%
BORDER TOTALS	30248	6175	20.41%	11149	3534	31.70%

UNITED STATES

US TOTALS	8791323	1281870	14.58%	3759103	433902	11.54%
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**DR-- BORDER TO
US**

1.40

2.75

TEXAS MSAs

	TOTAL APPS	# DENIED	% DENIED	TOTAL LOANS	RPD	SUBPRIME
AMARILLO	5050	906	17.94%	2181	234	10.73%
AUSTIN/R ROCK	50932	6896	13.54%	19085	1675	8.78%
CORPUS CHIRSTI	9291	1639	17.64%	3412	605	17.73%
DALLAS/PLA/IRV	139486	20470	14.68%	53627	8726	16.27%
FTWRTH/ARLTN	61501	9520	15.48%	23615	4231	17.92%
HOUS/BAY/SUG	198642	34163	17.20%	74251	15818	21.30%
LUBBOCK	5121	793	15.49%	2059	285	13.84%
MIDLAND	2659	451	16.96%	1269	250	19.70%
SAN ANTONIO	47400	9045	19.08%	16574	2958	17.85%
TEXAS TOTALS	520082	83883	16.13%	196073	34782	17.74%

D R-- BORDER TO TEXAS

1.27

1.79

RPD = REPORTED PRICING DATA/SUBPRIME LOANS

DR = DISPARITY RATIO

Adapted from: 2004 HMDA Data Aggregate Tables 7-2, 11-3 and Table B for the U.S. and each M.S.A.

Online. Available: <http://www.ffiec.gov>.

TABLE 2
CONVENTIONAL HOME PURCHASE LOANS:
PRICING DATA BY RACE

BORDER MSA _s	BLACK		HISPANIC		WHITE		RPD	% PRIME	% SUBPRIME	TOTAL LOANS	NPD	RPD	% PRIME	% SUBPRIME		
	TOTAL LOANS	NPD	TOTAL LOANS	NPD	TOTAL LOANS	NPD										
BVILLE/HARLING	85	59	26	2188	735	74.83%	25.15%	987	878	109	88.96%	11.04%				
EL PASO	7	1	6	1233	501	59.37%	40.63%	126	101	25	80.16%	19.84%				
LAREDO	20	11	9	1279	1238	50.81%	49.19%	508	423	85	83.27%	16.73%				
MCALL/NIED/PHAR																
TOTAL	130	84	46	4850	2968	62.04%	37.96%	1998	1709	289	85.54%	14.46%				
DR--RACE--BORDER	BORDER BLACK TO BORDER WHITE												2.45	2.62		
UNITED STATES	BLACK	237532	161591	75941	HISPANIC	411123	330498	80625	80.39%	19.61%	2364055	2160525	203530	91.39%	8.61%	
DR--US BLACK TO US WHITE	US HISPANIC TO US WHITE												2.28	1.68		
DR-- BORDER BLACK TO US BLACK	BORDER HISPANIC TO US HISPANIC												1.94	1.30		
TEXAS MSA _s	BLACK	TOTAL LOANS	NPD	RPD	% PRIME	% SUBPRIME	TOTAL LOANS	NPD	RPD	% PRIME	% SUBPRIME	TOTAL LOANS	NPD	RPD	% PRIME	% SUBPRIME
AMARILLO	17	14	3	82.35%	21.43%	164	123	41	75.00%	25.00%	1682	1526	156	90.73%	9.27%	
AUSTIN/RR/ROCK	530	416	114	78.49%	17.65%	2145	1678	467	78.23%	21.77%	12250	11466	784	93.60%	6.40%	
CORPUS CHRISTI	56	42	14	75.00%	21.51%	870	585	285	67.24%	32.76%	1905	1685	220	88.45%	11.55%	
DALLAS/PL/RV	4859	2920	1939	60.09%	25.00%	7250	4694	2556	64.74%	35.26%	30047	27032	3015	89.97%	10.03%	
FTWTH/ARLTN	1596	953	643	59.71%	39.91%	3021	1950	1071	64.55%	35.45%	14188	12310	1878	86.76%	13.24%	
HOUSTON/SUG	8531	4602	3939	53.94%	40.29%	15733	10487	5246	66.66%	33.34%	34684	30180	4504	87.01%	12.99%	
LUBBOCK	25	13	12	52.00%	46.17%	208	144	64	69.23%	30.77%	1614	1441	173	89.28%	10.72%	
MIDLAND	15	9	6	60.00%	40.00%	177	59	88	33.33%	49.72%	951	822	129	86.44%	13.56%	
SAN ANTONIO	520	368	152	70.77%	40.00%	4803	3345	1458	69.64%	30.36%	8198	7295	903	88.99%	11.01%	
TOTAL	16149	9337	6822	57.82%	42.24%	34371	23065	11276	67.11%	32.81%	105519	93757	11762	88.85%	11.15%	
DR--TEXAS BLACK TO TEXAS WHITE	TEXAS HISPANIC TO TEXAS WHITE												2.94	1.30		
DR-- BORDER BLACK TO TEXAS BLACK	BORDER HISPANIC TO TEXAS HISPANIC												1.16			
NPD = NO PRING DATA REPORTED / PRIME LOANS RPD = REPORTED PRING DATA / SUPRIME LOANS DR_ DISPARITY RATIO																

Adapted from: 2004 HMDA Aggregate Data Table 11-3 for the U.S. and each MSA. Online. Available: <http://www.ffiec.gov>.

TABLE 3
CONVENTIONAL HOME PURCHASE LOANS:
PRICING DATA BY INCOME

[illegible]

UNITED STATES,

[illegible]

TEXAS MSA

[illegible]

NPD = NO PRICING DATA REPORTED / PRIME LOANS
RPD = REPORTED PRICING DATA / SUBPRIME LOANS
DR = DISPARITY RATIO

Adapted from: 2004 HMDA Data Table 11-3 for the U.S. and each MSA.
Online. Available: <http://www.ffiec.gov>.

TABLE 4
CONVENTIONAL HOME REFINANCE LOANS:
LOAN APPLICATION DENIALS AND SUBPRIME INCIDENCE

BORDER MSAs

	TOTAL APPS	# DENIED	% DENIED	TOTAL LOANS	RPD	% SUBPRIME
BVILLE/HRLNGN	10012	3566	35.62%	2195	937	42.69%
EL PASO	24394	7871	32.27%	5159	1832	35.51%
LAREDO	6109	2319	37.96%	1176	452	38.44%
MCALLN/ED/PHAR	16288	5760	35.36%	3908	1642	42.02%
BORDER TOTALS	56803	19516	34.36%	12438	4863	39.10%

UNITED STATES

US TOTALS	15932711	3750519	23.54%	5727612	886536	15.48%
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DR -- BORDER TO US			1.46			2.53
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TEXAS MSAs

	TOTAL APPS	# DENIED	% DENIED	TOTAL LOANS	RPD	% SUBPRIME
AMARILLO	7583	2145	28.29%	2146	473	22.04%
AUSTIN/R ROCK	66480	17838	26.83%	18229	2592	14.22%
CORPUS CHIRSTI	14337	4461	31.12%	3194	971	30.40%
DALLAS/PLA/IRV	176916	48680	27.52%	49566	9572	19.31%
FTWRTH/ARLTN	88786	25475	28.69%	23430	4931	21.05%
HOUS/BAY/SUG	229376	71689	31.25%	61596	15369	24.95%
LUBBOCK	8067	2301	28.52%	2117	598	28.25%
MIDLAND	3351	1068	31.87%	931	231	24.81%
SAN ANTONIO	70947	20577	29.00%	16526	4132	25.00%
TEXAS TOTALS	665843	194234	29.17%	177735	38869	21.87%

DR -- BORDER TO TEXAS			1.18			1.79
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RPD = REPORTED PRICING DATA / SUBPRIME LOANS

DR = DISPARITY RATIO

Adapted from: 2004 HMDA Aggregate Tables 7-3, 11-7, and Table B for the U.S. and each MSA. Online. Available: <http://www.ffiec.gov>.

TABLE 5
CONVENTIONAL HOME REFINANCE LOANS:
PRICING DATA BY RACE

BORDER MSAs	BLACK		HISPANIC		WHITE		% PRIME	% SUBPRIME	TOTAL LOANS	NPD	RPD	% PRIME	% SUBPRIME	TOTAL LOANS	NPD	RPD	% PRIME	% SUBPRIME	
	TOTAL LOANS		TOTAL LOANS		TOTAL LOANS														TOTAL LOANS
BVILLE/HARLING	7	6	1	85.71%	14.29%	1459	764	695	52.36%	47.64%	326	231	95	70.86%	29.14%				
EL PASO	100	48	52	48.00%	52.00%	3210	1892	1318	58.94%	41.06%	908	718	190	79.07%	20.93%				
LAREDO	4	2	2	50.00%	50.00%	923	554	369	60.02%	39.98%	71	47	24	68.20%	31.80%				
MCALED/PHAR	13	8	5	61.54%	38.46%	2941	1641	1300	55.80%	44.20%	389	293	96	75.32%	24.68%				
TOTAL	124	64	60	51.61%	48.39%	8533	4851	3682	56.85%	43.15%	1694	1289	405	76.09%	23.91%				
DR -- RACE--BORDER																			
1.80																			
2.02																			
U.S. TOTALS	396950	260875	136075	65.72%	34.28%	525549	427719	97830	81.39%	18.61%	3519186	3067636	451550	87.17%	12.83%				
DR -- US BLACK TO US WHITE																			
DR -- BORDER BLACK TO US BLACK																			
US HISPANIC TO US WHITE																			
BORDER HISPANIC TO US HISPANIC																			
1.45																			
2.32																			
BORDER WHITE TO US WHITE																			
1.86																			
TEXAS MSAs																			
BORDER MSAs	BLACK		HISPANIC		WHITE		% PRIME	% SUBPRIME	TOTAL LOANS	NPD	RPD	% PRIME	% SUBPRIME	TOTAL LOANS	NPD	RPD	% PRIME	% SUBPRIME	
	TOTAL LOANS		TOTAL LOANS		TOTAL LOANS														TOTAL LOANS
AMARILLO	53	21	32	39.62%	60.38%	199	132	67	66.33%	33.67%	1491	1239	252	83.10%	16.90%				
AUSTIN/ROCK	702	449	253	63.96%	36.04%	2166	1534	632	70.82%	29.18%	11063	10058	1005	90.92%	9.08%				
CORPUS CHRISTI	62	37	25	59.68%	40.32%	1174	662	512	56.39%	43.61%	1350	1092	258	80.89%	19.11%				
DALLAS/PLRV	4072	2398	1674	58.89%	41.11%	5813	3975	1838	68.38%	31.62%	28798	24889	3909	86.43%	13.57%				
FWTHT/ARLTN	1351	825	526	61.07%	38.93%	2212	1568	644	70.89%	29.11%	14809	12331	2478	83.27%	16.73%				
HOUSTON/BAV/SUG	6450	3434	3016	53.24%	46.76%	11278	7521	3757	66.69%	33.31%	29557	24426	5131	82.64%	17.36%				
LUCKBOCK	55	21	34	38.18%	61.82%	316	171	171	45.89%	54.11%	1388	1121	465	80.76%	19.24%				
MIDLAND	20	12	8	60.00%	40.00%	208	119	89	57.21%	42.79%	552	465	87	84.24%	15.76%				
SAN ANTONIO	570	337	233	59.12%	40.88%	5388	3449	1939	64.01%	35.99%	7116	6053	1063	85.06%	14.94%				
TOTAL	13335	7534	5801	56.50%	43.50%	28754	19105	9649	66.44%	33.56%	96124	81674	14450	84.97%	15.03%				
DR -- TEXAS BLACK TO TEXAS WHITE																			
DR -- BORDER BLACK TO TEXAS BLACK																			
TEXAS HISPANIC TO TEXAS HISPANIC																			
BORDER HISPANIC TO TEXAS HISPANIC																			
2.23																			
1.29																			
BORDER WHITE TO TEXAS WHITE																			
1.59																			
NPD = NO PRICING DATA REPORTED / PRIME LOANS																			
RPD = REPORTED PRICING DATA / SUBPRIME LOANS																			
DR = DISPARITY RATIC																			

Adapted from: 2004 HMDA Aggregate Table 11-7 for the U.S. and each MSA. Online. Available: <http://www.ffiec.gov>.

TABLE 6
CONVENTIONAL HOME REFINANCE LOANS:
PRICING DATA BY INCOME

BORDER MSA*									
LOW INCOME BORROWERS									
TOTAL LOANS	NPD	RPD	% PRIME	% SUBPRIME	MODERATE INCOME	NPD	RPD	% PRIME	% SUBPRIME
BUTLER/HARLNG	59	33	44.07%	55.93%	224	84	140	37.50%	62.50%
EL PASO	163	143	53.27%	46.73%	759	389	370	51.25%	48.75%
LAREDO	17	12	29.41%	70.59%	108	45	63	41.67%	58.33%
MCALL/NEED/PHAR	69	51	26.09%	73.91%	327	129	198	39.45%	60.55%
BORDER TOTALS	451	239	47.01%	52.99%	1418	647	771	45.63%	54.37%
DR -- BORDER LOW TO BORDER UPI	212			1.51	BORDER MOD TO BORDER UPI	859	1010	45.96%	54.04%
				LMI TOTAL	BORDER LMI TO BORDER UPI			1.54	
UNI TED STATES INCOME									
US TOTALS	408355	106876	73.83%	26.17%	1128345	879977	248368	77.99%	22.01%
DR--US LOW TO US UPI				2.44	US MOD TO US UPI			2.05	
DR--BORDER LOW TO US LOW				2.02	BORDER MOD TO US MOD			2.47	
				LMI TOTAL	1536700	1181456	355244	76.88%	23.12%
					US LMI TO US UPI			2.16	
					BORDER LMI TO US LMI			2.34	
TEXAS MSA*									
LOW INCOME BORROWERS									
TOTAL LOANS	NPD	RPD	% PRIME	% SUBPRIME	MODERATE INCOME	NPD	RPD	% PRIME	% SUBPRIME
AMARILLO	178	65	63.48%	36.52%	410	293	117	71.46%	28.54%
AUSTIN/RCK	1469	469	68.07%	31.93%	3662	2799	863	76.43%	23.57%
CORPUS CHRSTI	151	71	47.02%	52.98%	434	221	213	50.92%	49.08%
DALLAS/PLA/RV	2398	1519	61.22%	38.78%	9122	6299	2823	69.05%	30.95%
FTWTH/ARL/TN	1780	1096	61.57%	38.43%	4705	3181	1524	67.61%	32.39%
HOUS/BAY/SUG	3920	2190	55.87%	44.13%	11851	7309	4542	61.67%	38.33%
LUBBOCK	105	53	50.48%	49.52%	342	187	155	54.68%	45.32%
MIDLAND	46	31	67.39%	32.61%	167	100	67	59.88%	40.12%
SAN ANTONIO	1172	660	56.31%	43.69%	2848	1666	1182	58.50%	41.50%
TEXAS TOTALS	12738	7612	59.76%	40.24%	33541	22035	11486	65.76%	34.24%
DR--TEX LOW TO TEX UPI				3.02	TEX MOD TO TEX UPI			2.57	
DR--BORDER LOW TO TEX LOW				1.32	BORDER MOD TO TEX MOD			1.59	
				LMI TOTAL	46279	29667	16612	64.10%	35.90%
					TEXAS LMI TO TEXAS UPI			2.69	
					BORDER LMI TO TEXAS LMI			1.51	
UPPER INCOME									
TOTAL LOANS	NPD	RPD	% PRIME	% SUBPRIME	MIDDLE INCOME	NPD	RPD	% PRIME	% SUBPRIME
593	800	133	74.82%	25.18%	544	407	137	74.82%	25.18%
7418	6875	543	84.38%	15.62%	4572	3867	705	84.38%	15.62%
1665	1281	384	62.34%	37.66%	778	483	293	62.34%	37.66%
22294	19836	2438	76.86%	23.14%	11877	9129	2748	76.86%	23.14%
9886	8665	1221	74.41%	25.59%	5811	4324	1487	74.41%	25.59%
27055	22882	4173	68.72%	31.28%	15461	10625	4836	68.72%	31.28%
1062	853	209	64.72%	35.28%	513	332	181	64.72%	35.28%
413	338	75	68.12%	31.88%	229	156	73	68.12%	31.88%
7770	6501	1269	69.00%	31.00%	3742	2582	1160	69.00%	31.00%
78516	68051	10465	73.30%	26.70%	43527	31907	11620	73.30%	26.70%
TEX MID TO TEX UPI									
2.00									
BORDER UPI TO TEX UPI									
1.81									
TEXAS UPI TO TEX UPI									
2.63									

NPD = NO PRICING DATA REPORTED / PRIME LOANS
RPD = REPORTED PRICING DATA / SUBPRIME LOANS
DR = DISPARITY RATIO

Adapted from: 2004 HMDA Aggregate Table 11-7 for the U.S. and each MSA. Online. Available: <http://www.ftnc.gov>.

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