

NEGATIVE AMORTIZATION

With negative amortization your loan payments are not large enough to repay the loan or even cover the interest charged on the loan. The loan balance increases as you make your payments.

BALLOON PAYMENTS

Some loans offer lower payments because they are calculated over a period longer than the term of the loan. When the loan comes due, you are required to make a lump sum payment to payoff the loan, or to find new financing. Balloon loans may offer a lower interest rate than other loan options, but be sure you understand how the loan operates and have a plan to handle the balloon payment.

PREPAYMENT PENALTIES

Prepayment penalties require you to pay an additional amount if you payoff your loan early or refinance it. Prepayment penalties should be limited to the first few years of the loan and should provide a benefit to you, such as a lower interest rate.

MANDATORY ARBITRATION CLAUSES OR AGREEMENTS

Mandatory arbitration clauses or agreements require you to enter into binding arbitration for any disputes you may have with the lender. In arbitration, an arbitrator has a hearing and makes a determination in the dispute, rather than a judge or jury. You may be required to pay the cost of arbitration. With a mandatory arbitration clause, you are not permitted to sue the lender to enforce your rights.

When refinancing, the borrower usually has the right to cancel the transaction within three business days after the loan closing for any reason, including if the loan terms are not acceptable to the borrower. If you refinance your loan with your current lender, you may only cancel the transaction for the amount of new money advanced to you. If only loan costs for the new loan are added to your old loan's balance, the loan cannot be cancelled.

If you cancel your refinance loan, the lender must return all of the money you paid in relation to that loan, including any amounts that you paid to other parties which provided services in connection with the loan application process.

Be aware that the right to cancel does not apply if you cancel the loan transaction before a closing takes place.

Mortgage brokers and lenders work for themselves and make money by closing loans. The best deal for the borrower may not be the best deal for them. You may obtain a better deal if you shop aggressively for a loan.

Make sure that you examine all of the costs of obtaining a mortgage loan and not simply the monthly loan payment required by the lender.

If you do not understand the documents you receive, get help from a knowledgeable person who is not involved in the loan transaction.

Become an educated borrower. It is your best protection from questionable lending practices!

If you should have a concern about your loan transaction contact the State of Michigan Attorney General's Consumer Protection Division at (877) 765-8388 or the Office of Financial and Insurance Services at (877) 999-6442.

**THIS BROCHURE SHOULD NOT BE USED
IN PLACE OF LEGAL ASSISTANCE. BEFORE
SIGNING MORTGAGE LOAN DOCUMENTS,
SEEK LEGAL ADVICE**



**REAL PROPERTY LAW SECTION
STATE BAR OF MICHIGAN**

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State Bar of Michigan

MORTGAGE LOANS & PREDATORY LENDING



Before you get a mortgage loan to buy a house, or refinance your existing home, you **must** understand certain basic terms and concepts. If you do not, you may not get the most for your money and you may not be adequately protecting your interest in the property.

You may deal with a “mortgage broker” when you first apply for a mortgage loan. The mortgage broker does not loan you money. The mortgage broker finds a “lender” to loan you money in exchange for a mortgage on your home. You will not get a loan unless you meet the requirements of the lender. It is the lender, not the mortgage broker, who defines the “basic loan terms” that you will be asked to agree to in order to get the loan.

BASIC LOAN TERMS

- *Loan Amount* – Amount you are borrowing.
- *Points* – Fee to obtain your loan. Each point is one percent of the loan amount.
- *Closing Costs* – Costs you will be required to pay at closing.
- *Monthly Payment* – Amount you must pay the lender each month until the loan is repaid.
- *Term* – Number of years you have to repay the loan.
- *Pre-Payment Penalty* – Fee charged if you repay the loan early.
- *Interest Rate* – Rate of interest you will be paying for the length of the loan.
 - Fixed or Variable
 - Fixed interest rate remains the same for the term of the loan.

Variable interest rate may increase or decrease over the term of the loan.

➤ **Rate Lock or Float**

Rate Lock – interest rate does not change between application and loan closing.

Rate Float – interest rate may increase or decrease between application and loan closing.

- *Annual Percentage Rate (APR)* - Effective interest rate charged for the loan.

You should understand these terms and receive them *in writing* from the lender or mortgage broker when you apply for the loan. Make sure that the terms of the final loan documents are the same as those you were given when you applied for the loan.

The loan terms can vary depending upon the lender. Some consumers talk to several mortgage brokers or lenders to shop for the best available loan terms. Study the various offers presented to you and ask questions if one lender is offering you a loan with significantly different terms than another lender.

When you apply for a mortgage loan, you should receive a “Good Faith Estimate of Settlement Costs” from the lender. This form outlines the costs you will be required to pay at or before the time the loan is closed.

PREDATORY LENDING PRACTICES

Borrowers may be victimized by something known as predatory or abusive lending practices. Whether your history of paying your bills is good or bad, you must watch out for the following abusive practices.

HIGH PRESSURE SALES TACTICS

Predatory lenders and predatory mortgage brokers often use appealing sales lines along with aggressive marketing tactics. Many times offers of extra cash, lower payments or eliminating credit card debt are used to sell loans with high interest rates and fees. What they may not tell you is that they are combining all of your debt into a longer term loan secured by your home. You may end up paying more money over a longer period of time. Also, if you are unable to make the loan payments, you may lose your home. Many predatory lenders and predatory

mortgage brokers deliberately steer unsuspecting borrowers into loans with higher interest rates than the borrower would otherwise qualify for and away from more affordable options. Be careful of lenders or mortgage brokers that advertise one loan plan, but direct you to another plan.

BAIT AND SWITCH

Bait and switch occurs when a lender or mortgage broker changes the terms of the mortgage loan just before you are scheduled to receive the loan (the loan “closing”). The borrower is then given the choice of accepting the changed terms or rejecting the loan. Always obtain a copy of the final loan documents and disclosures at least one day before the closing to compare the terms of the final loan documents to the terms contained in the “Good Faith Estimate of Settlement Costs” you received earlier. Be careful of lenders or mortgage brokers that advertise low rates as bait to get you to apply only to change the loan terms later on.

FEE PACKING

Fee packing occurs when the lender or mortgage broker adds additional services or goods to the mortgage loan transaction without your knowledge or consent prior to the closing. For example, the lender may add credit insurance or other products to the loan package you are receiving and add the cost of these items to the loan balance. You are then forced to buy the additional goods or services, or delay the loan closing.

EQUITY STRIPPING

Equity stripping may occur when you are refinancing your existing home. If you agree to include the cost of refinancing as part of the loan, rather than paying these costs with your own money, you are “stripping” away the “equity” or “free and clear” ownership you have in your home. With a refinance you always have a choice of paying closing costs from available cash, or financing these costs by adding them to the loan amount. Adding the loan costs to the loan amount not only reduces your equity, it also increases the cost of the loan because you are paying interest on the money borrowed to pay these costs.

LOAN FLIPPING

Loan flipping may occur when a lender or mortgage broker contacts you and encourages repeated refinancings of your existing loan. Make sure that a refinance provides a benefit to you when comparing the terms of a new loan to the terms of your existing loan including the costs of the new loan. Loan flipping may also lead to equity stripping.

REFINANCING SPECIAL MORTGAGES

Some borrowers already have special subsidized mortgages that contain terms favorable to them, such as Michigan State Housing Development Authority (MSHDA) loans and Habitat for Humanity loans. Be especially careful when refinancing one of these loans to make sure that a refinance provides a benefit to you when comparing the terms of a new loan to the terms of your existing loan including the costs of the new loan.

ENCOURAGEMENT OF DEFAULT

Be especially careful if a lender or mortgage broker encourages you not to make payments on your existing loan before you refinance your loan with them. This could lower your credit score and cause you to pay more for your refinance loan and may increase the interest rate on your credit card debt or other future loans.

POTENTIAL PREDATORY LENDING PRACTICES

Other loan terms, conditions and features may, under certain circumstances, be considered predatory, abusive, unfair or deceptive. The practices may, however, provide you with a benefit under other circumstances. Please carefully evaluate the benefit to you of the following practices:

OFFER OF ONLY SINGLE PREMIUM INSURANCE

Single premium credit insurance is insurance to repay your loan upon your death. This insurance product may cost more than traditional life insurance. In addition, you pay a single premium up front, in full at closing. If, however, the amount of the premium is added to your loan balance, then you also must pay additional interest. Credit insurance should be offered with a choice of premium payment options.