



Anti-Predatory Lending Ordinances

A City Practice Brief

February 2008

Sub-prime, or high cost, mortgage loans are a major factor in the increasing rate of non-tax related foreclosures, and a large percentage of recent foreclosures are the direct result of predatory lending practices. A high rate of foreclosure creates financial distress for cities as they deal with the loss of property taxes in conjunction with increases in costs for other municipal services, such as abandoned property maintenance, safety and security.

Sub-prime loans are defined by the federal Home Ownership and Equity Protection Act (HOEPA) as a loan with excessive points, fees, and APR above the yield on US Treasury securities. It is important to note that not all sub-prime loans can be defined as predatory. Legitimate sub-prime lenders address sub-par credit consumers without misrepresenting the terms of the mortgage loans. Predatory sub-prime loans are identified as those which use tactics such as aggressive and deceptive marketing, ignoring the borrower's ability to pay, financing excessive fees into the loan, charging higher interest rates than a borrower's credit allows, and home improvement scams.

States and cities have used the HOEPA standard, in combination with other deceptive lending practices, as a basis for modifying their own definitions of predatory loans. And most states and local governments have laws to protect consumers against fraud and unfair and deceptive acts and practices (UDAP laws), and civil rights laws which might be used to curb predatory lending practices. Many city anti-predatory ordinances are preempted by state law, and most have been challenged in court by the American Financial Services Association.

The following examples typify how cities are defining predatory loans, and the measures they are actively taking to discourage predatory lenders from entrapping low income families and wreaking havoc in working class neighborhoods. For more examples, visit the City Practices database on the NLC website or contact the NLC Municipal Reference Service at (202) 626-3130 or mrs@nlc.org.

City: **Chicago, Illinois**

Population: 2,896,000

For more information, contact: City Hall, (312) 744-4000

The City of Chicago passed the nation's first local Anti-Predatory Lending Initiative (Ordinance SO2000-2145) in August 2001, with the strategy of placing predatory lending within the context that addresses the three main phases of foreclosure: preventing abusive lending practices, assisting at-risk homeowners, and expanding the rehabilitation of vacant homes. The ordinance discourages predatory lending by (1) prohibiting predatory lenders from doing business in, or with, the city, and (2) places a larger cost on foreclosure by making the lending institution responsible for the upkeep of the foreclosed properties they acquire.

Chicago defines a high-cost, predatory loan as one with an interest rate 5% above the US Treasury and points or fees that exceed 6% of the loan amount. It further defines a predatory loan as one made under circumstances that are abusive, including fraudulent, high pressure, or misleading marketing tactics; excessive fees or interest rates; financing excessive fees into the

loan; prepayment penalties; short-term balloon payments; loan flipping; negative amortization; and lending without regard to a borrower's ability to repay. A predatory lender is defined as an institution that has made 25 such loans within the previous year, or whose predatory loans make up 5 percent of its portfolio.

The Chicago, Illinois ordinance became effective November 2001, and has not been challenged in court.

City: **Los Angeles, California**

Population: 3,694,820

For more information, contact: City Hall, (213) 485-2121

The city of Los Angeles passed an Anti-Predatory Lending Ordinance (#01-1476) in November 2002 which states that predatory lending is a municipal affair and a matter of unique local interest and declaring the ordinance to be within Los Angeles' home rule powers and police powers of the city. The ordinance specifically targets High-Cost Refinance Home Loans, defined as a loan in which proceeds are not used to finance the purchase of secured real property, and that meets either (a) the APR of the loan exceeds by more than 6 percentage points the yield on Treasury securities or the points and fees exceed 4 percentage points of the total loan amount.

Prohibitions on high-cost refinance home loans include: no lending without home loan counseling; a reasonable belief in a borrower's ability to repay loan; making a loan without net borrower benefit; prepayment penalties; financing of credit insurance; no lending without disclosure to the borrower of credit scores and appraisals; failing to report loan repayment to credit agencies; no mandatory arbitration clause without full disclosure; and no violations of state or federal laws.

Penalties to lenders may include actual damages sustained by borrower, costs and attorneys fees; injunctions against lenders from collecting under any home loans in violation; injunctions against foreclosures or other lender actions; statutory damages to the borrower of points, fees plus 10% of the total loan amount; and punitive damages.

The Los Angeles ordinance was passed November 2002, and as of February 2008 is currently held up by an American Financial Services Association lawsuit.

City: **Oakland, California**

Population: 399,484

For more information, contact: City Hall, (510) 238-3141

The Oakland City Council passed an Anti-Predatory Lending Ordinance (#12361) in October 2001 that prohibits abusive lending terms and practices for home mortgage loans. The ordinance requires borrowers to receive independent loan counseling prior to closing a high-cost home loan. The ordinance regulates a number of predatory lending practices including loan flipping, steering borrowers into high-cost home loans that charge high interest rates or points and fees, prepayment penalties, financing of single-premium credit insurance, encouraging consumers to default on existing loans in order to refinance into a new loan, and making loans regardless of the borrower's ability to repay.

Further protections apply to high-cost loans, which Oakland defines as loans with an APR 3 points above the Fannie Mae standard (5 points above Fannie Mae for second mortgages) or points and fees in excess of 5 percent of the loan amount. For these loans points or fees over 5 percent cannot be financed into the loan, prepayment penalties are prohibited, the borrower's ability to prepay must be considered, the borrower must receive tangible benefit, no refinancing of special low rate mortgages, and no call provisions or interest rate changes upon default.

Penalties to the ordinance include reimbursement plus damages for the borrower, plus a fine of \$500-\$50,000 per violation.

Trial court upheld Ordinance 12361 under a lawsuit from the American Financial Services Association in June 2002. As of February 2008, the decision is still on appeal in District Court.

City: **Philadelphia, Pennsylvania**

Population: 1,517,550

For more information, contact: City Hall, (215) 686-1776

Philadelphia passed one of the most stringent anti-predatory lending ordinances in 2001 (Chapter 9-2400). The ordinance prohibited predatory lenders, or high-cost lenders, from doing business with the city. Financial institutions were required to certify that neither they, nor their affiliates, were predatory or high-cost lenders, defined as one whose predatory loans over the previous year comprised 5 percent of its portfolio or who made at least 10 predatory loans, whichever was less.

“Predatory loans” were defined as loans with an APR exceeding 4.5 percent of the Treasury rate and contained prohibited features such as: fraud, financed credit insurance, points and fees in excess of 4% of the loan, prepayment penalties, certain balloon payment structures, negative amortization, loan flipping, mandatory arbitration, or disregard for the borrowers ability to pay. “High-cost loans” were defined as loans with an APR exceeding 6.5 points (8 points for second lien loans) or total points and fees financed into the loan equaling or exceeding 4 percent. The ordinance also required counseling for borrowers and required contractors to give borrowers written warnings against mortgaging their house in return for a home improvement loan.

The ordinance required all lenders to file disclosures with the city outlining the annual percentage rate and points charged on each loan. Violators were subject to fines of \$100-\$300 per day, the loss of city contracts and business privilege licenses, and the loss of government housing funds. The ordinance also required the city pension fund to divest of holdings of companies that engaged in predatory lending.

The Philadelphia ordinance was passed in April 2001, but preempted by state law in June 2001.

City: **Washington, D.C.**

Population: 572,059

For more information, contact: City Hall, (202) 478-9200

The Home Loan Protection Act of 2002 protects Washington D.C. city residents from predatory lenders by imposing restrictions and prohibited practices on sub-prime, or high cost, mortgage loans. The City defines a sub-prime loan as one with an APR 6 points higher than Treasury securities and points and fees in excess of 5% of the loan amount and stipulates that such loans cannot include: prepayment penalties, balloon payments within 7 years, call provisions based on lender’s discretion, negative amortizations, payments made from loan proceeds, and aggressive, mandatory arbitration clauses. In addition, lenders cannot steer borrowers to a loan product which is more expensive than the borrower qualifies for, lenders must provide a “Red Flag Warning Disclosure” statement three days before closing the loan, and lenders must submit a copy of the loan package to the mayor’s office within 14 days of closing. Lenders must also notify borrowers of their right to obtain counseling regarding the mortgage loan. Violations of the Home Loan Protection Act incur penalties including reformation of the loan to correct or remove the unfair term, actual damage reimbursement to the borrower, injunctive relief, attorney fees and costs, and statutory damages.

The Home Loan Protection Act of 2002 was passed in March 2002 and remains active.

State Mini-HOEPA Laws

Since 1999, states began enacting statutes patterned directly on the federal Home Ownership and Equity Protection Act. As of January 2007, twenty-eight states and the District of Columbia had enacted their own mini-HOEPA laws. Fourteen additional states augmented older loan regulation laws with parts of HOEPA.

As a result, by January 2007 only seven states – Arizona, Delaware, Montana, North Dakota, Oregon, South Dakota and Washington – had no mini-HOEPA statutes or any other laws or regulations in effect restricting prepayment penalties, balloon payment clauses, or mandatory arbitration clauses for residential mortgages.

Just as state law preempts some city anti-predatory loan ordinances, federal law can preempt portions of state laws. City officials should contact their state municipal league for more information on state and federal lending regulations.

Anti-Predatory Loan Resources for Lawmakers

Association of Community Organizations for Reform Now

739 8th Street SE, Washington, DC 20003

202-547-2500 ▪ www.acorn.org

ACORN's online presence includes tips and tools for lawmakers to oppose federal and state preemption of local anti-predatory loan legislation.

Center for Responsible Lending

302 West Main Street, Durham, North Carolina

(919) 313-8500 ▪ www.responsiblelending.org

The Center for Responsible Lending website contains online resources which list anti-predatory loan ordinances by state and locality and includes updates on federal and state legislative action.

National Community Reinvestment Coalition

727 15th Street, Suite 900, Washington, DC 20005

(202) 628-8866 ▪ www.ncrc.org

NCRC provides an anti-predatory loan toolkit which offers lawmakers a complete guide to crafting and proposing state and local laws to curb unsavory lending practices, including model anti-predatory loan legislation.

This Brief was developed by Larry Foxman, City Program Resources Coordinator.

City Practices Briefs contain examples from NLC's City Practices database, available at www.nlc.org.

Series editors: Bruce Calvin and Larry Foxman. For more information contact the NLC Municipal Reference Service at (202) 626-3130 or email mrs@nlc.org.
