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Predatory Lending Practices: Beware of Loan Steering!

One of the biggest fears about buying a home for the first time is the possibility of succumbing to predatory lending practices due to a lack of knowledge about the industry. As unfortunate as it is, there are some lenders out there that will charge a borrower as much as possible instead of the rates and fees they really deserve. There have been studies conducted that show evidence of subprime (or bad credit) lenders creating high interest loans for clients who unknowingly could have qualified for low-rate prime loans. Mortgage finance company once estimated that almost half of all subprime borrowers could have received less expensive mortgage loans had they been better informed. The biggest problems areas seem to be low-income areas where the majority of home loan lenders are subprime dealers. People in these areas often do not realize that there are other lower-cost loan options available.

The scary truth for many of these first-time or low-income borrowers is that they will end up paying thousands more in interest on these costly loans they get “steered” into. For example, if you went to a unscrupulous subprime lender you might be charged as much as 4% more on your interest rate for your loan, even if your credit score is good. Let’s say you get a 9% rate on a $200,000 30-year fixed loan from a subprime lender. You will pay approximately $1600 a month and $380,000 total in interest over the course of the loan. If you had taken your business to a subprime lender, you may have gotten the same loan with an interest rate of only 6.5%. Your monthly payment would have only been around $1300 and you would have paid roughly $255,000 in total interest. That is savings of $125,000 in interest!

So what can you do to avoid being steered into a loan program that suits your lender’s desires but not your needs? The best prevention is getting the right information. Simply knowing the difference between subprime and prime lenders is key. Lenders are not legally required to give you the best terms available. You should be prepared to shop around and negotiate for the best terms. Do not just take whatever offer the first lender gives you. Next you should find out what your credit score is before you start shopping for a loan. You can get it for a fee online or by requesting it by mail from any of the three major credit reporting agencies: Experian, TransUnion, or Equifax. This way you will know what kind of terms and rates you can expect to be offered. A helpful resource is myFICO.com. It shows you what the average interest rates are for each credit score range. You can search by national average or by your state. For example, today the site says that a borrower with very poor credit (500-579) can expect to get a rate of 9.683% on a 30-year fixed mortgage. If you have excellent credit (760-850), the national average fro the same loan is 5.892%. Once you know your score and know the national or state averages on interest rates you can compare loan offers from different lenders. Once you find a lender offering the right rate, be sure that he or she is not giving you that low rate at the cost of higher closing fees. Be sure to get quotes from several mortgage lenders to make sure you are getting the very best deal available.

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