The years leading up to the recent foreclosure crisis\textsuperscript{111} saw an avalanche of predatory mortgage lending. The predatory market can be seen as a subset of the subprime market.\textsuperscript{112} In the predatory market, price may have more to do with gouging than with risk.\textsuperscript{113} There is no single definition for predatory lending, and due to the lack of publicly reported data on this market, it is difficult to quantify the number of predatory loans or the percentage of the subprime market that they represent. One researcher estimated that 22.3\% of properties in Philadelphia had at least one of three indicators of predatory lending.\textsuperscript{114} Similarly, in Montgomery County, Ohio, an independent study of a random sample of mortgage loans revealed that 64\% of subprime mortgages in foreclosure had predatory features.\textsuperscript{115}

Unsurprisingly, because of the higher costs and other unfair terms of predatory and other subprime mortgages, the rate at which loans went into foreclosure was significantly higher in the subprime market than in the prime market. During the second quarter of 2009, the height of the foreclosure crisis, 26.5\% of subprime mortgage loans were seriously delinquent, meaning they were more than ninety days delinquent or in foreclosure. This stands in stark contrast to the rate for prime loans: 5.44\% during the same period.\textsuperscript{116} Nationally, from 1998 to 2007, the percentage of seriously delinquent prime loans remained constant at less than 2\% while the percentage of seriously delinquent subprime loans ranged from about 4\% to 13\%.\textsuperscript{117}

A significant factor contributing to default and foreclosure risk was the increased marketing of unregulated loan products (often called “nontraditional,” “alternative,” or “exotic” loans), especially between 2004 and 2007. Such products included interest-only loans, payment-option adjustable rate mortgages, and hybrid adjustable rate mortgages, such as “2-28s” and “3-27s.”\textsuperscript{118} On the one hand, abuses in this area were just another form of lending without regard to ability to repay. On the other hand, these products represented a specific and hazardous path to foreclosure.

From 2004 to 2007, these nontraditional mortgage products—especially interest-only loans—moved from a marginal role in the mortgage market to a place of dominance.\textsuperscript{119} In the secondary market, 23.5\% of all securitized subprime loan originations in 2005 were interest-only loans.\textsuperscript{120} Almost three-quarters of securitized subprime mortgages originated in 2004 and 2005 were 2/28 and 3/27 hybrid adjustable rate loans.\textsuperscript{121} These were sometimes called “exploding ARMs” because of what would happen to the payments required after the low initial teaser rate readjusted upward after the first two or three years.\textsuperscript{122}

The fact that this occurred in an environment of low interest rates raises serious questions about how and why consumers received these products. Interest-only and hybrid adjustable rate loans may be suitable for households expecting significant increases in income, for those with fluctuations in income that enable the borrower to pay down principal during certain periods, or for investors seeking to maximize cash flow. But subprime borrowers generally did not fit any of these criteria. Many were on fixed incomes, and those with fluctuating incomes did not see substantial upswings in incoming funds. Accordingly, these loans could only have been made to such borrowers if the lender dispensed with underwriting that analyzed whether the borrower could afford the loan beyond the initial payments, if then.

Because many nontraditional mortgage products, and adjustable rate mortgages in general, were made without adequate underwriting, they presented major risks to consumers and to the economy. The widespread and inappropriate origination of nontraditional mortgages ultimately led to huge increases in defaults and foreclosures, devastating individual consumers, their families, and their communities.\textsuperscript{123}

Footnotes

\textsuperscript{111} See § 1.2.5 [1], infra.

\textsuperscript{112} Prime loans could be predatory, though the likelihood is much smaller in that market.


Note that the definitions of predatory lending varied between the Dayton and Philadelphia studies.


Thirty percent of purchase loans were interest-only as of March 2006. Loan Performance, Interest-Only, Neg AM and Investor Activity for Purchase Loans, The Mkt. Pulse 3 (Mar. 2006 data).


123 [123] See, e.g., Debbie Gruenstein Bocian, Wei Li & Carolina Reid, Ctr. for Responsible Lending, Lost Ground, 2011: Disparities in Mortgage Lending and Foreclosures [6] 17 (Nov. 2011), available at www.responsiblelending.org (as of February 2011, of the hybrid or option ARM mortgage loans originated between 2004 and 2008, 12.8% had been foreclosed upon and 11.7% were seriously delinquent; noting that these loans represented 25.4% of all mortgage loans originated and 56.7% of all mortgage loan foreclosed).
1.2.4 The Rise of Predatory Lending

Links
[1] https://library.nclc.org/nclc/link/ML.01.02.05
[3] https://library.nclc.org/nclc/link/ML.06.02.06.01