Emerging industry fills void by making loans to minorities

Lending *from 1A*

A 2001 study by researchers at Freddie Mac, which buys traditional loans, found that 38 percent of borrowers in a national sample of loans from high-rate lenders potentially qualified for a lower rate. Other studies and industry statistics show a similar pattern.

Banks say they are trying to find those borrowers. They have spent millions on outreach. They have earmarked billions for lending programs focused on minority neighborhoods. They have relaxed their lending standards.

But the nation's 10 largest banking companies made only 5 percent of their home purchase loans to blacks last year, according to an Observer analysis. Wachovia made 8.8 percent of its loans to blacks. Bank of America made 6.2 percent.

The nation's population was 13 percent black in 2004.

"I think (banks) are doing better today than they were yesterday, and clearly they need to be doing better tomorrow," said John Dalton, president of the Housing Policy Council of the Financial Services Roundtable, which represents the largest banks and other financial companies.

At the same time, some banking companies have ventured into the high-rate market through subsidiaries that specialize in such loans.

Banks also profit from high-rate lending through investments and by serving as the bankers for high-rate companies.

Given this financial stake, some community advocates question how hard banks are trying to compete for customers in minority neighborhoods.

Peter Skillern, executive director of the nonprofit Community Reinvestment Association of North Carolina, asks banks at meetings: If you are competing, "Why is it that subprime lenders are eating your lunch in this market?"

The rise of a new industry

Charles Bradley quit his job in 1990 as president of a company that made music for theme parks to start a mortgage lending business in Charlotte.

Bradley, a certified public accountant with a background in real estate finance, believed the traditional lending industry was missing an opportunity.

Credit scoring programs were predicting with increasing accuracy the likelihood that people would repay loans. And the federal government had lifted its caps on interest rates, opening an era of loosened regulations on the sale of loans and other financial services.

Traditional lenders long have made loans to people they regarded as virtually certain to pay them back. Now companies could make loans to riskier borrowers and charge them higher interest rates. The new lenders still make money even if a larger share of their borrowers fail to repay their loans.

For the new borrowers, "it made home ownership possible whereas 15 years ago that would have been impossible," Bradley said.

His company, EquiFirst, became a pioneer in this new field of lending to "subprime" borrowers. Last year, EquiFirst loaned more than $5.4 billion.

The industry grew from $35 billion in lending in 1993 to $530 billion in 2004, according to a Federal Reserve Board estimate.

Its rise came with the emergence of independent mortgage brokers, who arrange two-thirds of all high-rate loans for a fee paid by the borrower. EquiFirst relies entirely on brokers to sell its loans.

These small businesses reach customers long ignored by banks – particularly, minority customers. Last year, EquiFirst made 21 percent of its loans to black borrowers.

"Does that not tell you that perhaps financial institutions are not servicing minorities in the way that they should?" asked Bradley, who left the company at the end of 2004.

Success raised the profile of the high-rate business. ACC Capital Holdings Corp., the nation's largest high-rate lender under the brand names Argent and Ameriquest, is an official sponsor of Major League Baseball and of the Rolling Stones concert tour.

At the same time, lawsuits about pricing practices have popped up.

Last month in a Securities and Exchange Commission filing, ACC said it had set aside $325 million for potential settlements with 30 states of charges it raised rates and fees without customer permission. The company has denied wrongdoing.

High-rate arms thrive

Four of the nation's largest banking companies have divided their home purchase lending: HSBC Holdings plc, National City Corp., Regions Financial Corp. and Washington Mutual Inc.

A larger, traditional arm continues to make market-rate, "prime" loans.

A smaller arm, often an acquired company, makes loans with higher interest rates.

Three of those lenders make most of their loans to blacks through their smaller, high-rate arm. National City declined to provide separate data for its First Franklin subsidiary.

■ EquiFirst was purchased by Alabama-based Regions in 1998. Regions made twice as many loans as EquiFirst last year. But EquiFirst made 1,872 loans to blacks, and Regions made 1,681.

■ Decision One, also based in Charlotte, is the high-rate arm of London-based HSBC. HSBC made about 1.75 times as many loans as Decision One in America last year. But Decision One made 3,456 loans to blacks and HSBC made 1,216.

■ Long Beach Mortgage is the high-rate arm of Seattle-based Washington Mutual. Washington Mutual made almost three times as many loans as Long Beach last year. But Long Beach made 4,910 loans to blacks, and Washington Mutual made 3,762.

All of the companies say race is not a factor in their lending decisions. HSBC said in a statement that its two lending arms are separate businesses that offer different products in different markets, and their lending cannot be compared.

Washington Mutual said it recognized the need to do more market-rate lending in minority neighborhoods. The company said it began in 2003 to open market-rate lending offices in urban areas in partnership with former NBA star Magic Johnson's development company.

"We're hiring folks from within that community to serve that community," said Greg Imm, Washington Mutual's fair lending executive. "We're having that group target and focus on underserved communities."

A customer who could qualify for a market-rate loan likely will get a more expensive loan from a high-rate lender. But high-rate lenders generally don't refer qualified customers to the market-rate arms of their parent companies.

EquiFirst, for example, says it considers Regions a separate business, and it has no obligation to lose customers by referring them.

"We don't do any type of comparison, no more than we would for some other firm," said Jeffrey Tennyson, the CEO of EquiFirst. The company notes that Regions also does not refer customers to EquiFirst.

Documents filed with the Securities and Exchange Commission in connection with the sale of 10,045 EquiFirst mortgage loans in 2004 show that 23 percent of the loans went to people with credit scores above 675, marking them as potential candidates for market-rate loans.

The company said many of those people could not have qualified for a market-rate loan for other reasons, such as a low proposed down payment.

Critics say it's unacceptable that customers can get a different rate simply because they applied to the high-rate arm of a bank.

"It shouldn't matter whether a borrower walks through the doors of a subprime affiliate or a prime affiliate of a lender; they should get the best loan that they qualify for," said Keith Ernst of the Durham-based Center for Responsible Lending.

Big banks reach to minorities

The prime arms of those lenders and other banks, such as Bank of America and Wachovia, have loosened some standards in recent years to win more customers, they say.

They increasingly work with people who don't have a history of borrowing money, an issue particularly common in Hispanic communities. Some mainstream lenders now accept a history of timely payments on utility bills, for example, as proof that a borrower is credit-worthy.

The big banks also spend millions on education to help people improve their financial profiles.

And they have turned to their greatest critics for help in reaching customers.

In 1995, Bruce Marks, chairman of the Boston-based Neighborhood Assistance Corp. of America, told then-Bank of America CEO Hugh McColl Jr. that all bankers were evil. McColl retorted that nonprofits wanted handouts without accountability.

But McColl agreed to work with Marks, and last year Bank of America committed an additional $6 billion to a NACA mortgage program. With the money, the nonprofit provides loans with no down payment, no fees and below-market interest rates.

Wachovia also works with hundreds of community groups in cities throughout the 15 states where the company has bank branches.

"They're a little closer to the customer, if you will," said Mike Rizer, community relations director for Wachovia. "It helps us reach out."

Both banks say they would like to reach more minority customers.

"Are we happy at 6 (percent of loans to blacks)? No," said Floyd Robinson, Bank of America's consumer real estate president. "We believe we're working hard to increase our share of loans to minorities."

A Wachovia spokeswoman said: "We are always committed to helping more people qualify for home loans at the best rates possible."

Community advocates, including Thompson of East St. Louis, said banks have a long way to go to close the disparities revealed by the new data on loan pricing.

Lenders who profit by operating the mainstream mortgage industry have an obligation to end racial disparities no matter their origin, Thompson said.

"I don't want to beat up on lenders. I just want them to close the gap," she said. "I don't care how they do it. I just want them to close the gap."

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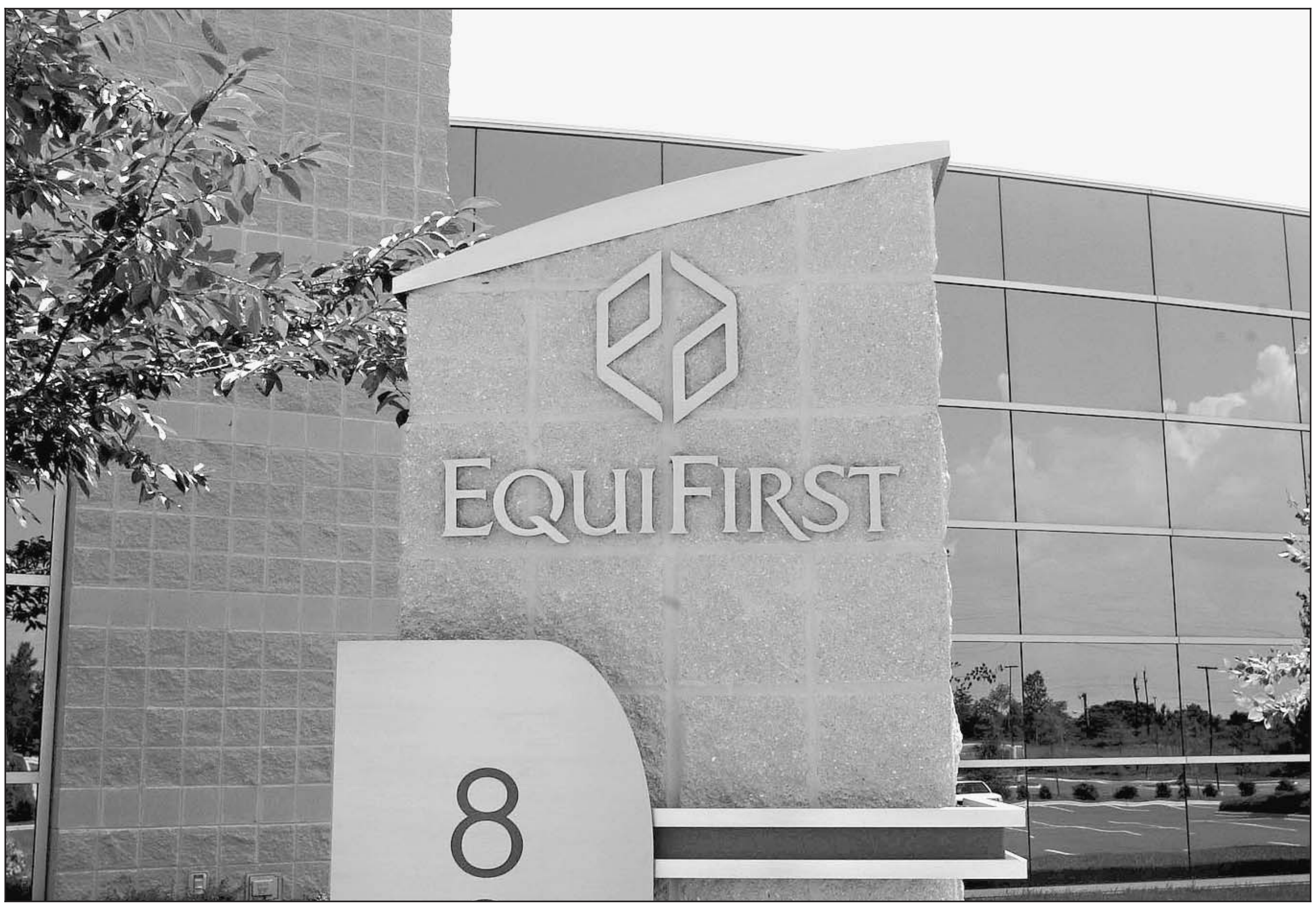

JUSTIN HINSHAW – SPECIAL TO THE OBSERVER

EquiFirst, formed in 1990 in Charlotte, was a pioneer in the field of lending to borrowers who don't get bank loans. The company now employs 1,200 people and fills three office buildings in southwest Charlotte (pictured here) and one in Phoenix.

High-Rate Lenders and Lending to Blacks

Mortgage lenders that make a large share of high-rate home purchase loans also tend to make a high share of loans to blacks. The result: Blacks get a lot of high-rate loans. Critics would like to see more loans to blacks, and fewer at a high rate.

High-rate loans	Lender	Black share of all loans
58.4%	ACC Capital	20.1%
31.6%	New Century	16.1%
30.5%	Regions	13.3%
16.5%	**HSBC**	8.4%
16.5%	General Motors	7.1%
12.8%	National City	11.0%
11.2%	Irwin Financial	10.2%
8.3%	AVERAGE	7.0%
8.2%	Countrywide	5.9%
5.2%	**Washington Mutual**	7.2%
4.7%	Flagstar	6.5%
3.6%	First Tenn.	5.3%
2.9%	PHH	6.1%
2.9%	BB&T	6.3%
2.7%	**Wells Fargo**	4.4%
2.1%	**Wachovia**	8.8%
2.0%	Ohio Savings	3.3%
1.9%	**US Bancorp.**	4.7%
1.8%	**SunTrust**	7.3%
1.4%	**JPMorgan Chase**	5.1%
1.3%	**Citigroup**	5.6%
1.2%	North Fork	5.3%
0.6%	**Citizens**	5.3%
0.2%	**Bank of America**	6.2%
0.1%	ABN AMRO	2.2%
0.0%	World Savings	4.9%

Bold-faced companies are among the 10 largest U.S. banking companies measured by assets.
High-rate loans carried an interest rate of about 8% or higher, according to a federal standard.

SOURCE: Observer analysis of lender data for 2004 home purchase loans in metro areas.

DAVID PUCKETT – STAFF

Two Lenders in One

Six of the nation's top market-rate home purchase lenders also own a subsidiary that makes many high-rate loans. Two of those companies, Countrywide Financial Corp. and National City Corp., declined to provide separate data for that subsidiary. The other four made most of their home purchase loans to blacks through their high-rate subsidiary.

Parent	Subsidiaries	Total loans	High rate	Loans to blacks
General Motors	■ GMAC	39,965	2.3%	1,780
	■ Homecomings	18,515	47.3%	2,389
HSBC	■ HSBC	35,279	0.7%	1,216
	■ Decision One	20,024	44.4%	3,456
Regions Financial	■ Regions and Union Planters	17,880	12.7%	1,681
	■ Equifirst	8,775	66.7%	1,872
Washington Mutual	■ Washington Mutual	88,776	0.1%	3,762
	■ Long Beach Mortgage	31,116	19.7%	4,910

SOURCE: Observer analysis of 2004 lender data

STAFF CHART

Charlotte Connection

Two of the more prolific high-rate lenders are based here.

EQUIFIRST

■ **Employees:** 1,212 (668 in Charlotte).
■ **CEO:** Jeffrey Tennyson.
■ **Background:** Founded in 1990 by Charles Bradley, a certified public accountant with a background in real estate finance. Acquired by Alabama-based Regions Financial Corp. in 1998.

HSBC MORTGAGE SERVICES
(includes Decision One Mortgage)

■ **Employees:** 3,000 (about 600 in Charlotte).
■ **Group executive:** J.C. Faulkner.
■ **Background:** Former First Union banker Faulkner founded Decision One in 1996. In 1999, the company was bought by Household International, which was acquired by London-based HSBC in 2003.

Bank Town:
Part of a Yearlong Series

This year, Observer banking reporters Rick Rothacker and Binyamin Appelbaum are examining the Charlotte banking industry's influence on communities and the economy.

Series Summary

SUNDAY: An Observer study found blacks are four times more likely than whites to receive high interest rates on home purchase loans. Even blacks with incomes above $100,000 a year received high rates more often than whites with incomes below $40,000.

Experts, studies and analysis point to three reasons blacks get fewer market-rate loans:

Discrimination can occur throughout the lending process.

Blacks on average have less wealth and more credit problems.

And blacks on average are less knowledgeable about the home-buying process.

Lenders say they don't consider race.

TODAY: Over the last decade, several million people bought homes with loans from a new mortgage lending industry. These companies offer loans that carry higher interest rates and cost on average tens of thousands of dollars in extra interest.

Community advocates and federal agencies say the success of these lenders stems in part from traditional lenders' failure to serve all Americans – particularly the black borrowers who take high-rate loans most frequently.

The banks say they are spending millions to find those borrowers. But the nation's 10 largest banking companies made only 5 percent of their home purchase loans to blacks last year, according to an Observer analysis.

COMING TUESDAY: How Congress and the lending industry can improve the loan process and help borrowers.