RESEARCH PROPOSAL

TOPIC: Racial Profiling Of Hispanic Mortgage Borrowers And The Ensuing Foreclosure Problems

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LL300-Research Seminar

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Competencies:

L8- Can pose questions and use methods of formal inquiry to answer questions and solve problems.

L9- Can evaluate the role and impact of lending practices on a community.

I - THE PROBLEM AND ITS SETTING

A. Statement of the Topic to be Explored

The topic for this research proposal will be racial profiling of Hispanic mortgage borrowers and the ensuing foreclosure problems. I believe that in addition to the common issues and problems faced by most urban communities, lending policies and practices have created a new set of problems that have been explored in many studies throughout the country. However, I believe that researchers have overlooked Chicago's Hispanic communities, including the community where I live. Some researchers have shown that lenders have targeted minorities with specific loan products and that there is a "high overall percentages of subprime loans made to African-Americans and Hispanics" (Bradford viii). What that study shows, on a national level, is that minorities have been placed at a disadvantage by lending practices; however there is no mention of Chicago's Hispanic communities. My proposed study seeks to fill the informational void and proposes to provide information and data as to the extent of the damage caused by lending policies and tactics.

B. Statement of the Problem and Sub-problems within the Topic to be Addressed

An increase in foreclosures has been shown to have a negative impact on a community for a multitude of reasons. Foreclosed properties remain vacant for extended periods of time, which in turn negatively affect the community's property values and can also cause an increase in crime in the neighborhood (money.cnn.com 1). Furthermore, the foreclosed properties tend to become distressed due to the lack of ownership and this causes neighborhood blight. Since these findings shed light on the problem of foreclosures, race and lending practices on a national scale, then Chicago's Little Village neighborhood, which is predominantly Hispanic and is geographically bounded by

Western Avenue, Ogden Avenue, Kostner Avenue and I-55 (explorechicago.org), would have been the target of various mortgage lenders for subprime lending. Due to this targeting, the Hispanic Borrowers in the area would have suffered from higher than normal foreclosure rates and the subsequent problems.

C. Statement of the Question about the Problem that Research will Answer

I am proposing a study that will qualify and quantify how mortgage lenders targeted Hispanic borrowers in Chicago's Little Village Neighborhood for subprime loans and what effect these loans have had on the foreclosure rates for this community. Therefore I propose answering the following research question: Is there an increase in foreclosures in Chicago's Little Village neighborhood due to lenders racially profiling borrowers and targeting them for subprime loans?

D. Statement of the Hypothesis that the Research will Test

My research question is based on the following hypothesis: Lenders racially profiling borrowers causes an increase in foreclosures.

E. Delimitations

The research will not take into account borrowers who are not Hispanic nor borrowers who are not in zip code 60623.

F. Definition of Terms

Foreclosure

> A foreclosure happens when a borrower defaults on a mortgage loan and the lender resorts to taking ownership of the collateral for the loan (i.e. the home itself) by legal process. After a borrower defaults on a mortgage debt, the lender files a suit in court and obtains a motion that allows the lender to take possession

of the home used as collateral for a loan. After the foreclosure the bank will recuperate all or some of the money they lent out by selling the home to another party. The original borrowers that defaulted lose any money invested in the home prior to the foreclosure.

Lender

For the purposes of this study, a lender will be defined as a corporate entity that lends money to individuals in need of a home loan and uses a mortgage on real estate as security for said loan. It can be a full-service national or community bank (e.g. Bank of America or Washington Mutual) or a company that specializes only in mortgage loans (e.g. Long Beach Mortgage Company).

Racial profiling

The American Civil Liberties Union defines racial profiling as a “ discriminatory practice of targeting individuals (based) on the individual's race, ethnicity, religion or national origin”(aclu.org). For this study, racial profiling is what happens when mortgage lenders offer only certain products to potential borrowers based on the borrower’s race or language and disregard other qualifying mortgage products also due to the prospective borrower’s race or language.

G. Assumptions

The research I propose to carry out is of great importance since Hispanics will continue to desire to buy homes and will be in need of mortgage products. Accordingly, banks and mortgage companies will continue to lend to Hispanics and the lenders policies and practices will continue to affect neighborhoods.

II - LITERATURE REVIEW

A. Major Issues Explored by Scholars who have Researched This Topic and Problem

For many years banks, real estate agents and even the government were promoting the idea that owning a home was the culmination of the American dream. Most Americans were raised with the mentality that owning a home was a rite of passage into adulthood, their proverbial piece of the pie. The United States Department of Housing and Urban Development, or HUD for short, promoted this idea with their "American Dream Downpayment Initiative" which provided millions of dollars in assistance to qualifying families looking to buy a home (hud.gov). However, over the course of the last four years most Americans have witnessed the implosion of the housing market. While the media and the government report that "the sluggish housing market has picked up" (Davidson and Hansen 1) and that "reports point to an economy that is growing" ("New Data: Economy Improving with Government Aid" 1), few can argue that too many people are still suffering from the near-catastrophic loss of their money, equity and ultimately their homes.

In times past, home ownership was seen as an investment since real estate appreciated over time. The equity homeowners accumulated over time could have been cashed out and used as a retirement fund or for any other purpose. Real estate was usually sold for a profit and then most borrowers upgraded to newer or bigger properties. In 2005, *Time Magazine* published an article on the subject and the authors wrote "the stock market may be dragging, but home prices are soaring, fueling a national obsession with real estate" (Steptoe, et al 16). The authors were referring to the fact that even though the stock market was recovering from a slump, most Americans considered owning real estate a good investment opportunity. Unfortunately for most Americans, the boom became a bust towards the middle of the last decade.

While a lot of banks and mortgage companies don't admit that there is, or ever was, a problem with their lending practices, consumers have come to realize that the majority of lenders were part of what most would think is the ugly side of the mortgage industry: "predatory" also known as "subprime" lending. There is no clear-cut definition for "predatory" lending but the Office of the Federal Inspector General loosely defines predatory lending as lending that "involves imposing unfair and abusive loan terms on borrowers"(Rau 1). In other words, the loans offered by predatory lenders are not considered fair or proper by common mortgage industry standards. Rau further clarifies that "predatory loans" have the following attributes:

1. Abusive collection practices,
2. Balloon payments with unrealistic repayment terms,
3. Equity stripping associated with repeated refinancing, and
4. Excessive interest rates that may involve steering a borrower to a higher-cost loan.

To put it simply, predatory loans are loans that are provided with rates and terms that are more expensive than traditional loans and at the same time deemed bad for consumers because they can leave consumers with no equity in their homes.

During the course of performing a literature review for my proposal, for which I plan to research how predatory lending affects the foreclosure rates for the Hispanic community in Chicago (specifically zip code 60623), I became aware of several consistent themes in the journal articles, literature and books that I read. Consistent themes included the notions that predatory loans were more likely to occur in minority communities (Immergluck 115) and that the ensuing foreclosures affected the communities as a whole, not just on those individuals who's homes were foreclosed (Schuetz, Been and Ellen 309). Additionally, there is as increase in crime and a decrease in property values throughout the community due to foreclosures (Immergluck and Smith 856).

According to Immergluck, who is an Associate Professor at the School of City and Regional Planning at the Georgia Institute of Technology and a prolific author in matters of real estate and communities, predatory lending is more widespread in minority communities compared to white neighborhoods. Immergluck goes on to provide data that states that predatory loans in Black neighborhoods are two to three times more common than those in white neighborhoods (115). I did not find any specific reports or journal articles on how the Hispanic community in Chicago is affected by predatory lending and foreclosures.

An additional and important theme I noticed was that foreclosures affect more than just the borrower who is in default. Foreclosures also affect the neighborhood as whole because when a borrower defaults on their loan, the borrower is likely to neglect the home, as there is no longer a reason to maintain a property that the borrower might lose in the foreclosure process. Additionally, once the foreclosure takes place, the property is likely to sit vacant and boarded up, essentially becoming an eyesore to the community, until a new owner takes over (Schuetz, Been and Ellen 309).

One more common theme found in the literature is that areas with high foreclosure rates also tend to have lower property values. Foreclosed properties usually sell at a reduced price and this affects the values of most other properties in the area.

Property values for homes near foreclosed properties can be diminished by as much as eight percent (Lin, Rosenblatt and Yao 389).

An additional commonality in my readings was a conclusion by scholars that foreclosed properties cause neighborhood crime to increase for several reasons. When a property is foreclosed upon, it eventually becomes vacant at least until a new owner takes ownership; vacant properties have been shown to attract local criminals and vandals to the neighborhood. Additionally, high foreclosure rates contribute to higher crime since abandoned properties become public eyesores that are used to traffic drugs, house criminals and contribute to general mayhem in a neighborhood (Immergluck and Smith 856).

The most important theme that I noticed while reviewing relevant scholarly publications for my literature review was that predatory loans are more common in communities with minority borrowers, specifically African American borrowers. In a report prepared for the Federal Reserve Board of Governors, Calem, Gillen and Wachter wrote that minority borrowers in Chicago were 24% more likely to have subprime loan when compared to white borrowers (11).

Although the majority of the studies and articles I found concluded that subprime lending and the country's financial crisis were directly related, I did find a couple of reports that suggested otherwise. In an interview with *The Wall Street Journal* former Federal Reserve Chairman Ben Alan Greenspan states that subprime lending "was not a significant cause of the financial crisis" (Orol 1). Greenspan's opinion was not common throughout most of my readings but I thought it was important to note since the office of the United States Federal Reserve plays an important role in our country's housing market.

My research proposal confirms the need to investigate whether the Hispanic community in zip code 60623 was targeted for subprime lending and if, as a result, there is a higher rate of foreclosures in that neighborhood, which in turn negatively affects the community through an increase in crime and a reduction of property values.

B. Methodologies Used by Scholars to Research This Topic and Problem

For my research study I plan to use data collection methods that were previously used by other researchers who have completed studies similar to the one I am proposing. In this way my work will build upon, and be comparable to, the work of other scholars.

Many of the studies that I read during the course of my literature review for my proposal relied on Census data compiled by the United States government Census Bureau, as it appears to capture the necessary information for a study like the one I am proposing. The Census Bureau's mission is stated on their web site as "to serve as the leading source of quality data about the nation's people and economy" (uscensus.gov). In other words, the census bureau counts all individuals in the country and provides different data about these individuals, which will be useful for my research. In their study on the relationship between crime and real estate foreclosures, researchers Dan Immergluck and Geoff Smith utilized Census data along with Chicago Police data to "estimate a reduced form equation"(Immergluck and Smith, 856) which helped them relate foreclosures to neighborhood crime.

The research I encountered also relies on HMDA (pronounced Hum-Duh) data to gather information. HMDA stands for The United States Home Mortgage Disclosure act, which was enacted by the U.S. Congress in 1975 and requires all lenders to report public loan data to the United States Government. HMDA data covers home purchase and home improvement loans as well as refinancing of existing loans. The data contains information about all mortgage loan originations, including all loans that denied, incomplete or withdrawn (ffiec.gov). The lenders are required to report information such as:

- The type and amount of the loan made (i.e., Conventional, FHA or other);
- Whether a loan application was approved or denied;
- The property to which the loan relates to (i.e., the type of property and its location);
- The borrower's ethnicity, race, sex and income;
- Loan Pricing on loans that exceed thresholds set by the Federal Reserve Board (the threshold is an annual percentage rate (or APR) of three percentage points above the interest rate on Treasury securities of comparable maturity.

While it is evident that Census and HMDA data alone cannot test my hypothesis, I believe that data is necessary for my research. I strongly feel that combining the research methodology other researchers have successfully used, along with the additional methods I outlined above would yield the best answers to my research problem and ultimately test my hypothesis.

III – RESEARCH METHODOLOGY

The research study I am proposing plans to utilize the two most common data collection practices from the research as outlined in my literature review, and while neither of the two most common research methods can fully test my hypothesis, they can still help in arriving at an answer to the research question I have posed.

A. Data or Evidence to be Collected

As with previous studies of a similar nature, this study proposes to request quantitative data from The Federal Census Bureau along with quantitative HMDA data from the Federal Financial Institutions Examination Council. In addition, I will obtain qualitative data via surveys and interviews. The qualitative data will provide a snapshot of the borrower's financial situation at the time of the loan origination as well as a longitudinal view of the changes in said situation throughout the life of the loan.

1. Description of the Data

I plan to extract the following information from the census tract data for all residents of zip code 60623:

- Homeownership Status
- Race
- Property Type

In addition to Census Data, I propose to request quantitative HMDA data from the Federal Financial Institutions Examination Council and extract the following information:

- Loans with interest rates over 3% of prime rate at time of loan origination

While HMDA data will provide valuable information for my research, it regrettably will not suffice since "it is not possible to conclude from HMDA data alone whether a lender is complying with fair lending laws. The HMDA data does not include many potential determinants of loan pricing, such as the borrower's credit history, debt-to-income ratio, and the loan-to-value ratio" (federalreserve.gov). In other words, HMDA data alone cannot help determine if a lender is complying with the necessary regulations. Additionally, Danni Krasner, a Staff Attorney and Director of Educational Services at

Bankers Advisory, states that even though HMDA data is supposed "detect and ultimately curtail discriminatory practices" (Krasner 1) it is not always the case. Furthermore, Krasner states that "current reporting requirements do not include adequate information to deter and detect the full range of harmful and risky lending practices" (Krasner 1). Krasner means that HMDA data can provide some information with regards to lending practices but it cannot solely detect or eliminate discrimination practices or stop lenders from placing consumers in predatory mortgage loans.

The information gathered from the above two processes will be cross-referenced to provide the primary sample group for the proposed study and whose subjects will meet the following criteria:

- Reside in zip code 60623
- Are Homeowners
- Are Hispanic
- Own a single-family home
- Own a 2-unit home
- Occupy the subject property
- Have loans at an interest rate that is/was greater than 3% over prime at origination.

2. Where the Data are Located

The initial data will be requested from the United States Census Bureau and from the Federal Financial Institutions Examination Council and both of these agencies can provide the desired information via electronic delivery methods, such as email. The remainder of the data will be gathered from zip code 60623 based in the criteria defined above.

B. Techniques for Collection of Data

Data collection will be a three-part process. The first step in data collection will be to obtain Census tract data as described above. Secondly, the HMDA data will be requested and cross-referenced with the Census data to create the primary data sample. Once the primary data sample is created we can begin with the third portion of the process, which will be the fieldwork. We will mail contact cards to all subjects with the intent of being able to conduct a survey of these subjects. Depending on the initial response, the plan is to send out three mailings in order to attempt to reach as many subjects as possible. After the mailing process is complete all respondents will be scheduled for a survey interview via one of the following five methods:

- Face-to-Face Interview
- Email Survey Web Survey
- Web Survey
- Telephone Survey
- Fax Survey

C. Methods of Analysis

Once all the data is collected it will be statistically analyzed and cross-referenced for content.

1. How the Data will be Examined for its Meaning

The replies to the surveys will be mined for statistical data that can be used to determine if the borrowers were the targets of predatory loans. The primary information that will be utilized will be a snapshot of the borrowers interest rate at origination versus the prime rate at that time. Additionally, qualitative information will be compiled that will describe how the borrower's finances were affected after their mortgage closed and if their loan is in risk of foreclosure. Ancillary information that contributed to any mortgage default will be taken into account, such as unemployment, illness or other causes for default.

2. How the Data will be Presented

The final research report will be presented as a longitudinal study in an essay format and will contain the following elements that will help describe and aid in interpreting the statistical analysis:

- Area Map of Little Village
- Pie charts demonstrating percentages of prime versus subprime loans
- Pie charts showing loans in foreclosure versus loans performing as agreed
- Statistical charts showing rates per borrower category and comparing them to prime rates
- Chart showing timeframe between loan origination and foreclosure

Additionally, there will be a qualitative portion of the report that will provide interviews and observations of some of those borrowers affected by the problem and will serve to promote a better understanding of the problem as well as the subjects.

IV – OUTLINE OF THE FINAL REPORT

The final report from my study will be presented in the following manner:

V – EXPECTED OUTCOMES

The information and data that is obtained by the study can be utilized by local housing counselors, governmental entities and non-profit agencies to assist local homeowners who have been victims of race biased lending practices as well as to educate future potential borrowers so that they do not become victims of targeted subprime lending. In addition, lenders can use the data and information from the study to either create or improve lending policies at all corporate levels.

As stated previously, this study will fill a void in the research of lending practices and their effects on communities since there are very few, if any, studies that have focused solely on Chicago's Hispanic borrowers.

VI - WORKS CITED

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