



## **Eliminate the “Exit Tax” on Subprime Loans: *Prepayment Penalties Prevent Qualified Homeowners from Getting Better Loans***

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Subprime loans typically include a prepayment penalty, an expensive fee for paying off a mortgage early, usually charged when a homeowner refinances. Only about 2% of prime loans include prepayment penalties, but these expensive fees come with about 70% of subprime loans.

### **What are some of the problems with prepayment penalties (PPs) on subprime mortgages?**

- Loans with PPs are much more likely to go into foreclosure than loans without PPs.<sup>11</sup>
- Families who can least afford these penalties are most likely to receive them. Borrowers in heavily minority neighborhoods face 35% higher odds of having a PP on their subprime mortgage compared to borrowers in predominantly white neighborhoods.
- PPs pose a no-win situation for cash-strapped families: either they remain trapped in a high-cost loan, or they must spend precious equity to pay the fee.
- PPs are linked to “yield-spread” premiums, or broker kickbacks.
- Home buyers often aren’t aware of the PP, and are typically pushed into a loan with one.

### **What is the typical cost of a prepayment penalty (PP)?**

- A typical PP penalty costs six months’ interest on the loan or approximately 3% of the principal loan amount—a significant amount of equity to lose. For a \$200,000 loan, a 3% prepayment penalty costs homeowners \$6,000.

### **What are the benefits of receiving a prepayment penalty?**

- CRL research shows there are NO benefits to families who get loans in the subprime market based on CRL research—on home purchases, interest rates were higher.<sup>2</sup>

### **Policymakers have recognized the need to curb abusive prepayment penalties.**

- Many states have already taken actions to severely limit or ban prepayment penalties.
- 12 states have a broad ban on prepayment penalties: Alabama, Alaska, Indiana, Iowa, Maine, Minnesota, New Jersey, New Mexico, North Carolina, Ohio, South Carolina, Vermont
- Prepayment penalty abuses factored into major public enforcement actions against subprime lenders Household and Ameriquest.

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**H.R. 3915 stands up for homeowners by eliminating prepayment penalties on subprime mortgages.  
Please support this bill, but stress that the bill can only work if it is strengthened, not weakened.**

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<sup>1</sup> See, e.g., *The Impact of Predatory Loan Terms on Subprime Foreclosures: The Special Case of Prepayment Penalties and Balloon Payments*, Center for Community Capitalism – University of North Carolina at Chapel Hill (January 25, 2005).

<sup>2</sup> <http://www.responsiblelending.org/issues/mortgage/reports/page.jsp?itemID=28012342>.