

## Shopping for a Mortgage Loan and Lender

You're no sucker. You've done your homework. Shopped around, called several of those lenders in the Sunday paper rate guide, and received a slew of quotes and good faith estimates. So now, you pick the one that has the lowest cost or APR and live happily ever after.

That's the way it ought to work. But in reality the chances are that 35% of the quotes you received were not legitimate.

A recent survey in California found that 70% of borrowers indicated that the terms they received at closing on mortgage loans from sub-prime mortgage lenders differed significantly from the terms they had been promised at the time of application or at an earlier stage of the loan process.

Other mortgage industry surveys reveal that the "bait and switch" routine in mortgage lending occurs in more than 35% of conforming mortgage loan transactions (non-sub-prime).

How does the "bait and switch" routine work? Lenders provide rate quotes and cost estimates to a borrower at the time of application. The borrower relies on these quotes and applies for a mortgage loan with the lender offering the favorable quote. Later, on the day of closing or possibly only days before, the lender informs the borrower that the lender cannot honor the original quote. The lender's representative will provide a variety of reasons or excuses why they can't provide the promised terms (some which sound completely plausible) or in more flagrant cases of abuse will simply tell the borrower "tough luck". Sitting at the closing table with the moving van parked in the street the borrower will reluctantly accept the modified terms rather than risk a breach of contract or the embarrassment of not proceeding with closing.

What makes the problem even more confusing is that contrary to representations of those lenders that offer less favorable terms, there is a fairly wide gap between what is offered by competing mortgage lenders in terms of rate and costs for identical loan programs. On larger loan amounts the variance in fees at a particular rate might vary by as much as \$10,000.

There is no sure way of avoiding this trap, but there are a few rules that can be followed that will minimize the chance that you'll be a victim.

### Pick the Lender before the Loan

Before you begin obtaining quotes and cost estimates from lenders, do a little research to narrow down the list of available candidates. Before you pick the loan, pick the lenders. Here are a few tips that will reduce the chance of ending up with a "bad apple".

1. **Choose a local lender.** I always advise using mortgage lenders that are based in the state in which the subject property is located, or at a minimum have an office within the state. There are a variety of reasons, the least of which is that if something does go awry, you'll be able to seek legal recourse in the courts of your state. If you attempt to prosecute a claim against an out-of-state lender you'll encounter a number of obstacles. Out-of-state entities are often not governed by local licensing agencies and in some cases may not even be subject to a lawsuit in the state. There are ample Texas based lenders to choose from so my advice is to not take a chance with an out-of-state lender. (I've also found that these out-of-state guys provide very misleading information. Texas has very unique laws relating to real estate and mortgages. One example is the fact that Texas is the only state that does not use title policy forms promulgated by the American Land Title Association. In our review of out-of-state lender websites their estimates of third party closing costs were notoriously inaccurate.)

2. **Visit the state regulating agency website.** If you do decide to give an out-of-state lender a chance to provide a quote, verify that they are registered or licensed with the Texas Department of Savings and Mortgage Lending (the agency charged with regulating mortgage activities in Texas). If a lender is not listed on the agency's lender search page you'd best steer clear of that company. Here's a link to the agency's internet search page.
3. **Visit the BBB website.** Check the Better Business Bureau's list of company records to determine whether a company has had complaints filed with the BBB. You should access the local BBB website in the geographical region for the home office of the mortgage lender. In some cases the company is not listed. Steer clear of a company that's not listed on any BBB website. That means that they have not been in business for a sufficient period of time to be reliable. You should also avoid those companies that have had complaints filed with the BBB, even if they were resolved to the satisfaction of the customer. Do you really want to have to file a complaint to get a resolution to a problem with a lender? And keep in mind that for every complaint filed against a lender there are probably a dozen or more that go unreported. The safest course of action is to only deal with companies who have had no complaints filed with the BBB within the past three years. Here are some links to the BBB websites. Here's a link to our company's report with the Dallas BBB.
4. **Use lenders with online rate quotes.** To save time and resources it is my opinion that if you are going to use the internet as a tool for locating the best mortgage you should also limit yourself to those lenders that provide an online rate quote for your program. I would estimate that at least 75% of companies with an internet presence at a minimum provide online rate quotes for the most common loan programs (15 and 30 year fixed-rate loans). If a company does not post a rate and pricing it is usually because they are non-competitive on pricing. Others will attempt to get your contact information so that you can be "contacted by a loan consultant to provide a rate quote". It is my opinion that you should shy away from online websites that ask for contact information before providing you with an online quote. Many of these websites are merely portals seeking contact information or "leads" which are then sold to mortgage companies who will contact you with an annoying sales pitch. Those that are legitimate are attempting at any cost to get your contact information so that their loan "consultants" can contact you with an extremely polished sales pitch to downplay the importance of rates and pricing. The bottom line is that the vast majority of mortgage companies that have internet website post the pricing for their most popular programs. So why waste your time with a company that doesn't! Also, don't waste your time with companies that don't provide the relevant information in their online quotes. At a bare minimum the quote should provide the rate, the annual percentage rate (APR) and an indication of the total "lender" or "loan" fees (or "finance charges"). If you haven't already read my articles on How to Real a Good Faith Estimate and The APR Fallacy I suggest you do so before beginning the comparison of quotes from various lenders.

### Shopping for the Best Deal

Having culled through the available lenders and narrowed the list to a set of local favorites that provide online price quotes you must now attempt to choose the one that offers the best rate/pricing combination. If you're not familiar with the relationship between rate and discount points (and premium) you should take a minute to read my article on Rates, Points and Costs. You should also read the articles "Before Shopping for a Mortgage", "Understanding the Good Faith Estimate" and "The Fallacy of Having acquainted yourself with a general understanding of how mortgage rate pricing works and how to compare the cost estimates you will be provided by lenders you can proceed to compare the offers of various lenders.

1. **Don't compare apples to oranges.** The first rule in comparing quotes is to get quotes at identical interest rates (called "coupons" in the mortgage industry) from the list of available lenders. You can't compare one company's 6% quote to another company's 5.75% quote. Doing so is, quite simply, like comparing apples to oranges. If you want to get quotes at two or more different rates, then ask for multiple Good Faith Estimates from each lender.
2. **Communicate the details of your transaction.** Make sure you explain in detail your transaction to the loan representative with whom you're talking or corresponding. Pricing sometimes varies according to loan amount, loan-to-value ratio (LTV ratio), credit scores, occupancy types and other factors. A seasoned loan professional should, in fact, ask you all these questions prior to providing a quote. Unless the loan consultant has asked these types of questions you should be extremely wary as they are essential to providing an accurate quote. I would even suggest preparing a document that sets forth all of the details of your transaction that could affect pricing and then provide that to the lender as a basis for your quote. If you've taken the steps set forth in the article "Before you Shop for a Mortgage" then you'll have all the key elements required to get an accurate quote.
3. **Obtain a Good Faith Estimate.** Obtain a Good Faith Estimate of Costs ("GFE") from each lender for each rate ("coupon") that you are considering then group them by interest rate so that you are comparing the same rate for each lender. Any lender worth dealing with will provide a GFE with line numbers. Although the specific number and description of each item may vary from one GFE to another, they should all follow the following general criteria. If you're provided a GFE without line numbers I'd throw it in the trash and mark that lender off the list. Without the line numbers it is too easy for lenders to bury lender fees in with third party fees which can be misleading (which, unfortunately, some lenders do even on the numbered GFE's). As a precaution you should also warn lenders to provide GFE's that they should take care to include all lender fees in the "800" section of the GFE. The GFE should have the following characteristics.
  - a. The GFE should include an "800" section with line numbers ranging from 801 to 825 (although the total number of lines in the section may be well below 25). This section includes the lender or loan fees paid to mortgage brokers and lenders in connection with the transaction. The names of the items and the individual amounts of each item are irrelevant. Your only concern is to add these fees together to arrive at a cumulative "lender fees" total. One precaution ... Be aware that some lenders may not include the cost of the appraisal, credit report or an application fee in this section since these fees may be paid "prior" to closing and are typically not included as "finance charges" in determining the APR. Thus, if an appraisal fee, credit report fee or application fee is not shown in the "800" section of the GFE verify whether the lender charges the fee and ask the lender to include those charges on their GFE in the "800" section. Then use the amended GFE for your comparisons.
  - b. The "900" and "1000" section of the GFE includes pre-paid items and escrow/impound account deposits. Ignore these! They are nothing but estimates and not "costs" that should be considered in comparing pricing quotes.
  - c. The "1100" section is title fees over which the lender has little or no control (unless the settlement agent and title company are associated with the lender). With one exception they should not be considered when comparing pricing quotes. That one exception is "document preparation fees" in Texas that are usually listed in the "1100" section. Since attorneys are required to draft or review the deed of trust and other documents under Texas law, the fee paid to the attorney may be listed in the "1100" section since it is technically paid to a party other than the lender. However, these fees are typically controlled by the lender who chooses the attorney and the fees can vary in amount by

more than \$200 so it would probably make sense to include these “doc prep” fees in your rate quote comparison as if they were lender fees.

- d. The “1200” section of the GFE will include a “catch-all” location for other fees paid to third parties such as surveyors. Typically these fees need not be included in a comparison as they are not controlled by or paid to the lenders. Beware, however, that some lenders attempt to put fees in this section to exclude them from consideration when the GFE is being compared with competitors’ GFE’s.
  - e. Please note that the fees charged for a second lien mortgage closed simultaneously with the first lien mortgage may be shown for information purposes in this section. These fees should be considered separately when comparing rate quotes.
4. Once you’ve included all the proper items in the total of “lender fees” compare those fees for each lender at the same the interest rate and the quote with the least amount of lender fees is the best quote.

### **Play Two Hands**

In a perfect world you could take the results of your research and then proceed with the best quote knowing you’re getting the best deal. But as I am sure you are aware, we don’t live in a perfect world. As indicated in the opening section of this article consumer surveys indicate that more than a one-third (1/3<sup>rd</sup>) of consumers that participate in real estate transactions indicated that the terms they received at closing were not as favorable as the quote they received at the time of application. Participants in the subprime lending process experience this problem in more than 70% of the cases. Even though you’ve performed a fairly thorough analysis of the lenders you’re dealing with to determine that they are not among the mortgage bad boys, that is still no assurance that you won’t be the first on a list of disgruntled customers. Bear in mind that this phenomenon is not necessarily the result of an intention to misguide you. The price of a particular mortgage program at a particular rate is governed by a variety of transaction characteristics that involve “pricing adjustments” that drive up the points paid at a particular interest rate. For example, the cost (discount points) of an 80% LTV mortgage loan increases significantly if you are obtaining a simultaneously closed second lien that makes the combined LTV more than 90%. An experienced loan officer (or even one who makes an innocent mistake) may fail make the pricing adjustment associated with the higher CLTV when preparing your rate quote. In this event, the quote may be inaccurate as a result of negligence rather than any intentional deception on the part of the loan officer. Either way, your goal is to get the best deal and the fact that the mistake is unintentional will be of little comfort when only days before closing you’re informed of the mistake. But take heart ... There a few precautions you can take to avoid this problem. Here are a few suggestions.

- a. **Apply with more than one company.** You should apply with more than one company. Doing so will enable you to have options available further into the process in case something goes wrong with one of the lenders or their original quotes.
- b. **No need to pay pre-paid fees.** Concerned about paying an application fee in advance to more than one lender? Don’t! There are plenty of lenders who will process your application (including going out of pocket to obtain a credit report) at no charge. If a lender wants to charge you for making application, mark them off your list and move on to one who doesn’t.
- c. **Don’t worry about your credit score.** You’ve heard that excessive credit pulls can drive down your credit scores, right? In fact, the “inquiries” resulting from multiple credit pulls by lenders have only a nominal affect on your score in most cases, and for credit reports obtained by multiple mortgage lenders there is no adverse affect on your credit scores for

any reports obtained by within sixty days of the date on which the first report is obtained. In other words, if Mortgage Company A pulls a report on June 1<sup>st</sup> subsequent pulls by competing mortgage companies during the months of June and July will not adversely affect your scores. Click here for more information.

- d. **Get an unconditional loan approval before ordering an appraisal.** Don't pay any lender a fee for an appraisal until they have issued an unconditional loan approval (except for conditions relating to appraisal and title). In some transactions an appraisal will not be required. Many lenders can determine within minutes of receiving an application whether an appraisal is required and the type of report that is specified by the "automated underwriting system" that is used for that particular program. For information on this process see ...
- e. **Get your own an appraisal.** Most lenders can process your application without first obtaining an appraisal. In most cases (especially purchase transactions) the file can be fully validated and underwritten without the necessity of an appraisal. Again, if a lender requires you to use "their" appraiser or attempts to collect a fee as a condition to processing your application I would consider removing them from the list of candidates. I also recommend obtaining your own appraisal so that you can provide the appraisal report to several lenders. Ask one of the lenders you are planning to apply with to suggest the name of an appraiser that meets their qualifications. Many lenders have an "approved list" of appraisers so before employing an appraiser contact each of the lenders you are likely to be dealing with and verify that the appraiser you will employ is on their "approved list". Then contact the appraiser and strike a deal that includes the appraiser's agreement to provide the appraisal report to up to three lenders at no additional charge.
- f. **Locking the rate complicates the shopping process.** Since "locking" in a rate and price may (but not always) involves a contractual obligation by and to the lender the desire or need to "lock" can complicate the process of "playing two hands at once." A borrower should carefully consider the prudence of locking early in the loan application process. Many borrowers believe that they are must or should lock at the time of application. In fact, in most cases locking at the time of application is not the most prudent course of action. (For more on when to lock read the article "When is the best time to Lock?") At a very minimum the applicant should wait until he has been provided an approval letter that assures the applicant that he is approved for the mortgage. Most competent lenders with the most competitive prices will refuse to "lock" a loan until the borrower has submitted sufficient information to permit the lender to be assured of his qualification for the requested loan program. This is because "lock fallout" by loan originators is one of several factors that drives up the cost of pricing offered to a particular originator in the secondary (wholesale) mortgage market. This fact often complicates the process for comparing loan quotes among competing lenders since the refusal to lock at the time of application also enables "baiters" to hook the applicant without committing to the quoted price at the time of application. Nevertheless, during periods of rising interest rates the borrower will likely want to lock early in the application process after the initial approval letters (subject to appraisal and title) have been issued by one or all of the lenders. At that time the borrower should obtain updated rate quotes from the two or three lenders with which an application was submitted and should then use the procedure outlined in the preceding section for again comparing the GFE's.
- g. **Get a written rate lock agreement or commitment.** After reviewing the updated pricing quotes and evaluating other factors such as the lenders performance and competency through the initial stage of processing, the borrower must make a choice. Once the lender

is chosen it is imperative to obtain the precise terms of the lock and pricing in a written lock agreement or commitment letter signed by the lender and the borrower. The agreement should specify all the detail of the loan program including amortization type (fixed, ARM, etc.), the “caps” and “index” details for an adjustable rate mortgage, the occupancy type, and type of property securing the loan. It must also specifically indicate any points, origination fees, commitment fees or other lenders fees that will be paid to the borrower. If the borrower is to receive a credit from premium that should be delineated in the agreement as should the cost of waiving escrows if the borrower is permitted and desires to do so. Finally, the agreement should contain a provision that permits the borrower to proceed with another lender in the event that the lender who issues the lock commitment is unable or unwilling to comply with the terms of the commitment. On purchase transactions the agreement should also require the lender to provide closing instructions to the settlement agent at least five (5) business days prior to closing so that the settlement agent can prepare and deliver a settlement statement to you for your review. This will enable you to quickly proceed with “plan B” in the event that the settlement statement does not conform to the terms of the lock agreement.

- h. **Continue to process your application with at least one other lender.** Even though you’ve locked the rate and committed to proceeding with one lender, you should continue the process with a second lender. By doing so you are keeping the door open for an alternative way to proceed in the event that the first lender is unable or unwilling to deliver on their promises.

By committing to a reasonable amount of research and adhering strictly to the procedures I’ve outlined in this article you’ll likely not become one of the unpleasant statistics mentioned earlier in this article.

One final note, if you do have an unpleasant experience or feel that you were purposely defrauded report your complaint to the agency regulating mortgage lending in your jurisdiction (Texas Department of Savings and Mortgage Lending in Texas) and report complaints to the attorney general for your state and the Better Business Bureau in your area. Your actions will assist others in avoiding any problems you may have encountered.