

# *Protecting Yourself from Bait-and-Switch Scams*

## **Explanation of Bait-and-Switch Mortgage Practices:**

You are “baited” by the promise of a mortgage at a rate and fees that seem (and are) too good to be true. Then you are “switched” at closing to a loan that is significantly worse than the one promised.

One of Jim Carrey’s shining moments is in the film “Liar Liar,” in which he plays an attorney who lies all the time. His son’s birthday wish is that his dad be unable to lie for just one day. He gets his wish.

During this very stressful, truth-filled day, our lovable liar (Carrey’s character) gets his car impounded. When he picks it up from the impound lot, it is badly scratched. He complains that the impounders damaged his car. The lot attendant insists that the scratch was already there.

He yells at the attendant “You, you liar!! You know what I’m to do about it?” Jim Carrey is unable to lie at that point, even to himself. So he tells the truth. “*Nothing*.... Because if I take you to small claims court, it’ll just drain 8 hours out of my life; and you probably won’t show up; and if I finally *got* the judgment, you’d just *stick* it to me anyway. So what I’m going to do is piss and moan like an impotent jerk, and then bend over and TAKE IT UP THE TAILPIPE!”

The attendant responds wryly, “You’ve been here before, haven’t you?”

The mortgage industry was very much like that impound lot before the new RESPA regulations took effect January 1, 2010. If someone cheated you, they would probably have gotten away with it. You could sue but, ultimately, if you signed the loan papers you would most likely

wind up “taking it up the tailpipe.” **Your best defense is to always to know enough about loans to protect yourself from being cheated in the first place.**

People innocently ask me all the time, “But, Holly, isn’t it illegal to give borrowers a different loan from the one they were promised?” **Yes, it is illegal and immoral.** It is also illegal and immoral for someone to break into your house and kill you. Unfortunately, no matter how good the police force is, people are still murdered. A great police force will catch the murderer, but that doesn’t bring the victim back to life. The best of all possible situations is to be able to protect yourself *and* have a great police force backing you up.




Regulations that took effect January 1, 2010, will go a long way toward protecting you from these unethical practices, and toward punishing lenders who try to get away with cheating you. However, no matter how well the government regulates, they can’t protect *everyone, all of the time.* **You need to know how to protect yourself.**

Fortunately, I am not alone in recognizing this issue. Federal regulators recently enacted a law requiring loan officers be licensed in lending, and that they have 20 hours of training in lending (including training in ethics). Some state laws require even more training. This new training will be required as of December 2010 for loan officers who are licensed, and 6 months sooner than that for those without a license.

This is a wonderful change to previous requirements. It always boggled my mind that I have a license to sell real estate, rather than a lender’s license. Most of the information I learned studying for my broker’s license has nothing whatsoever to do with becoming an excellent loan officer. Worse yet, there is a large amount of information that loan officers *should* know in order to support borrowers when they get a home loan, but is *not taught*. I haven’t seen any training, outside of the book you are holding in your hands, that teaches loan officers and borrowers how to calculate the potential risks and rewards inherent in adjustable rate loans. That information should be *standard training* for all loan officers. My hope is that it will be included in the curriculum required to get a lending license.

I am happy that regulators have caught on and now require greater training for loan officers. However, the buyer must always beware. In the chapter titled “Choosing a Lender,” I lay out the characteristics of excellent loan officers, and the questions you should ask about their training to determine those most committed to their craft.

### **In this Chapter, you will learn:**

-  The truth about mortgage ads: All that glitters is not gold!
-  How to spot the signs that your loan officer may not be honest.
-  How to scare off “bad guys” and insure you will get the loan you want.

## The Truth about Mortgages

- **There is no such thing as a “fire sale” or “going out of business sale” in the mortgage industry.**

All loans are either sold to investors, or kept in a bank's portfolio. All are designed to make a solid return on investment. Therefore, most will be in the same neighborhood regarding rates. Do not kid yourself. You can do well for yourself with knowledge about mortgages and an excellent loan officer, but normally you can't get a rate several percentage points below someone else with similar qualifications. If you think you can, you may soon become the victim of a con man, or an inexperienced loan officer. Some exceptions include:

1. In 2007, during the “Liquidity Crisis,” I was able to get jumbo loans for my clients 2% to 3% lower in rate than the loans sold on Wall Street because I went only to lenders who used their own money to fund loans, and who kept the loans in their portfolios. There may be a significant difference in rate between loans that are sold on the secondary market (saleable loans) and those that stay with the bank who offers you the loan (portfolio loans).
2. Another exception to the rule regards private banking. If you have significant assets with a bank and a private banking relationship, they are often willing to give you a mortgage at a rate that is well below the market rates. They want to keep *all of your business* with them to cement the valuable relationship they have with you.

- **It is impossible to “do it yourself” when getting a home loan.**

Many of us (myself included) like to save money by doing things for ourselves whenever possible, rather than hiring a professional. A common misconception when getting a home loan is that you can go online and get a lower home loan rate because you are “doing it yourself”. In fact, the *only* way to get a home loan is to work with a loan officer or salesman. **You cannot “do it yourself” with a mortgage, as you can with home repairs.** You save money best by working with a skilled loan officer who acts in your best interests.

- **The rates quoted in ads are often not real.**

Mortgage rates are like stock prices, they change at least once a day. You wouldn't dream of calling your stockbroker on Monday and demanding he get you a stock for the price he quoted last Thursday. Newspapers need the copy for an ad several days in advance of printing.

So it is highly unlikely that the rate you read in a newspaper ad will be the same rate offered when you call. Similarly, radio ads often obscure the truth.

➤ **APR tells some of the truth, but not all of it.**

I read an ad in the newspaper that offers quotes from several different banks and brokers. I found some lenders quoting rates that were realistic. Then there were the less-reputable lenders who quoted lower rates in the same ad, but buried the truth concerning their charges in the APR. There are myriad ways to “tweak” the APR to make the loan look better than it really is. Add to that the fact that the rates in many ads are meant to make the phone ring and are not actually available to most borrowers (if any), and you can see that trusting mortgage ads doesn’t make sense.

➤ **It is impossible to advertise rates that apply to more than a small portion of the population, if that.**

You may ask “Why would lenders quote rates they either cannot or will not honor?” The answer is that they want to lure in consumers who believe they are getting an interest rate that is significantly lower than loans offered by the competition. They are hoping you do not figure them out. If you *do figure out* that the loan you get is not the one you were promised, it may be too late to change lenders. They bait you with a promise they never intend to keep; and then switch you to a worse loan. Their game plan is that either you will not spot the switch or you will take the loan anyway because you feel powerless to do anything about it. The worst part is that the loan you could wind up with will most likely be significantly worse than one an honest lender would have provided for you. Con men are greedy by nature, and take advantage of people whenever possible.

There is another aspect to pricing a loan that you should know about. There are complicated pricing adjustments for many features of the loan, including FICO score, “loan to value” ratio, property type, transaction type, loan size, and many more. Because of all of these factors, it is literally impossible for anyone to publish a rate that will be correct for more than a small portion of the population. For instance, ads usually quote a rate with no pricing adjustments. Few people fall into the demographic to which that would apply. To give you a feel for just how complicated loan pricing is, below is a pricing grid for a “simple” Fannie Mae conforming loan.

Fannie Mae Expanded Streamline Refinance (doc #r5348)					FNMA Streamline Refinance (doc #5339)									
Use Fannie Mae 30Y/15Y and I-O 10/20 Pricing					Use Fannie Mae 30Y/15Y and I-O 10/20 Pricing									
Alt-A Adjustments					FD/SISA Adjustments									
LTV	660-679	680-699	700-719	720+	LTV 95.01-97% subtract 0.50 from price	<90%	<680	680-699	700-719	>720				
0-60	-1.500	-1.250	-1.250	-1.000	LTV 97.01-100% subtract 1.00 from price	90.01-95%	-1.000	-0.750	-0.500	-0.250				
60.01-70	-2.000	-1.750	-1.500	-1.250		95.01-97%	-1.250	-1.000	-0.750	-0.500				
70.01-80	-2.750	-2.500	-2.250	-1.750	<b>EA Adjustments</b>	97.01-100	-1.750	-1.500	-1.250	-1.000				
80.01-90	-3.000	-2.750	-2.500	-2.000	See EA FICO/LTV adjustments on pg. 2	<b>FH Streamline Refinance (doc #5343)</b>								
90.01-95	-3.000	-2.750	-2.500	-2.000		No adjustment - use Freddie Mac 30Y Fixed								
<b>State Tier Adjustments (exclude FN High Bal and FH Super Conf.)</b>														
Tier 1+	TX								Purpose	CO Refinance Price Adjustment Grid (FICO/LTV)				
<b>Tier 1</b>	FL, NY								>=740	<=60%	60.01-70%	70.01-75%	75.01-80%	80.01-85%
<b>Tier 2</b>	GA, MD, NC, NJ, OK, PA, TN								700-739	-0.125	-0.375	-0.375	-0.625	-0.750
<b>Tier 3</b>	AL, AR, AZ, CT, DE, ID, IN, IA, KS, KY, LA, MI, MS, MO, NE, NH, NM, ND, OH, RI, SC, SD, VA, VT, WA								680-699	-0.125	-0.875	-0.875	-1.500	-2.625
<b>Tier 4</b>	CA, CO, MA, ME, MT, NV, UT (CA no escrow waiver fee)								660-679	-0.375	-0.875	-0.875	-1.625	-2.625
<b>Tier 5</b>	IL, OR, WI (no escrow waiver fee)								640-659	-0.375	-1.375	-1.375	-2.375	-3.125
<b>Tier 6</b>	AK, DC, HI, MN, VI, WV, WY (MN no escrow waiver fee)								620-639	-0.375	-1.375	-1.375	-2.875	-3.125
									<620	-1.375	-2.375	-2.375	-2.875	-3.125
<b>Loan Size</b>														
		Tier 1+	Tier 1	Tier 2	Tier 3	Tier 4	Tier 5	Tier 6	RT Refinance subtract .125 from price					
\$30,000-\$49,999		-0.725	-0.750	-0.825	-0.875	-0.925	-1.000	-1.025	<b>Occupancy</b>					
\$50,000-\$74,999		-0.225	-0.250	-0.325	-0.375	-0.425	-0.500	-0.525	Investment property <=75% subtract 1.75 from price					
\$75,000-\$99,999		-0.100	-0.125	-0.200	-0.250	-0.300	-0.375	-0.400	Investment property 75.01-80% subtract 3.00 from price					
\$100,000-\$124,999		0.025	0.000	-0.075	-0.125	-0.175	-0.250	-0.275	Investment property <=75% subtract 1.50 (HomePath only)					
\$125,000-\$149,999		0.085	0.060	-0.015	-0.065	-0.115	-0.190	-0.215	Investment property 75.01-80% subtract 2.00 (HomePath only)					
\$150,000+		0.150	0.125	0.050	0.000	-0.050	-0.125	-0.150	Investment property 80.01-90% subtract 2.50 (HomePath only)					
\$175,000-\$224,999		0.190	0.165	0.090	0.040	-0.010	-0.085	-0.110	<b>Subordinate Financing</b>					
(CONV. 30Y, 15Y ONLY)									LTV	CLTV	FICO	Non I-O	I-O	
\$225,000+		0.225	0.200	0.125	0.075	0.025	-0.050	-0.075	65.01-80%	90.01-95%	<720	-0.50	-0.75	
(CONV. 30Y, 15Y ONLY)									65.01-80%	90.01-95%	>=720	-0.25	-0.50	
									75.01-80%	76.01-90%	<720	-0.25	-0.50	
									75.01-80%	76.01-90%	>=720	0.00	-0.25	
									80.01-90%	81.01-95%	<720	-1.00	-1.25	
									80.01-90%	81.01-95%	>=720	-0.50	-0.75	
									<b>Fannie Mae Cooperative (doc #5917)</b>					
									<b>FN/FH Int-Only 15/15 (doc #5327)</b>					
									subtract 0.50 from price - use Int-Only 10/20					
									<b>Freddie Mac Alt 95 (doc #5320)</b>					
									<b>FNMA Multiple Property (doc #5351)</b>					
									subtract 0.50 from price - use Freddie Mac					
									No adjustment - use Fannie Mae 30Y Fixed					
									<b>Fannie Mae HomePath (doc #5349)</b>					
									LTV 80.01-85% subtract 1.00 from price					
									LTV 90.01-95% subtract 2.50 from price					
									LTV 85.01-90% subtract 1.75 from price					
									LTV 95.01-97% subtract 3.625 from price					
									<b>FICO/LTV adjustments (excludes 10Y/15Y products)</b>					
		FICO	<=60%	60.01-70%	70.01-75%	75.01-80%	80.01-85%	85.01-95%	>95%				3-4 units subtract 1.5 from price	
		740+	+0.250	0.000	0.000	0.000	0.000	0.000	0.000				Condo or Co-op LTV >75% subtract 0.75 from price **	
		720-739	+0.250	0.000	0.000	-0.250	0.000	0.000	0.000				** (excludes 10Y/15Y products and FNMA Site Condos)	
		700-719	+0.250	-0.500	-0.500	-0.750	-0.500	-0.500	-0.500				<b>NY Transfer Tax</b>	
		680-699	0.000	-0.500	-1.000	-1.500	-1.000	-0.750	-0.500				subtract .25 from price (NY properties only)	
		660-679	0.000	-1.000	-2.000	-2.500	-2.250	-1.750	-1.250				<b>Temporary Buydown (30Y, 15Y Only)</b>	
		FN 640-659	-0.500	-1.250	-2.500	-3.000	-2.750	-2.250	-1.750				1-0 subtract 0.875 from price 2-1 subtract 2.75 from price	
		FH 640-659	-0.500	-1.250	-2.500	-2.750	-2.750	-2.250	N/A				<b>LTV (FNMA/FHLMC Interest-Only)</b>	
		FN 620-639	-0.500	-1.500	-3.000	-3.000	-3.000	-2.750	-2.500				<=90% LTV subtract 1.0 from price	
		FH 620-639	-0.500	-1.500	-2.750	-2.750	-2.750	-2.750	N/A				>90% LTV subtract 1.25 from price	
		FN <620 & No FICO	-0.500	-1.500	-3.000	-3.000	-3.000	-3.000	-3.000				<b>Loans Closing in the name of "Flagstar Bank"</b>	
		FH <620 & No FICO	-0.500	-1.500	-2.750	-2.750	-2.750	-2.750	N/A				subtract .05 from price	
		<b>Lender Paid Mortgage Insurance</b>									<b>Lock Fallout</b>			
		Only available through Radian, Genworth, RMIC and MGIC. Other MI company restrictions may apply.									Meets Expectations add .05 to price			
		Please check the product description for eligibility as not all price adjustments are effective for all products.									Needs Improvement subtract .10 from price			
		<b>Conforming Fixed</b>									<b>40 Year</b>			
		LTV	620-679	680-699	700+	Second Home subtract 0.60 from price				Contact Lock-Ins or use www.wholesale.flagstar.com				
		<=85.00	-1.550	-1.100	-0.990	Cash-Out Refinance subtract 0.80 from price								
		85.01-90	-2.650	-1.800	-1.400	Rate/Term Refinance subtract 0.40 from price								
		90.01-95	-4.200	-2.950	-2.400	Terms <=25Y add 0.35 to price								
<p>Bank will not fund nor purchase a High Cost Home Loan (as that term is defined in Sec. 32 of Reg. Z. or in applicable State or local predatory lending laws). Flagstar Bank is not privy to negotiations with individual borrowers. It is the responsibility of the broker/corr to discern the appropriateness of the loan program chosen with regard to the individual borrower's needs and circumstances. Please refer to our High Cost Home Loan Policy, Doc. 4612 for further information.</p> <p>Escrow waiver, separate fee of .25 charged, contact underwriter for details. Excludes CA, IL, MN, OR, WI and conforming products in NY</p> <p style="text-align:center"><b>RATES SUBJECT TO CHANGE AT ANY TIME WITHOUT NOTICE</b></p>														

Unless you are in the mortgage industry, this will probably look like Greek to you. So I will attempt to translate it into English. The area highlighted in yellow says that if: 1) you want cash out; 2) your FICO score is between 680 and 699; and, 3) the loan to value ratio is between 75.01% and 80%, you will have to pay 1.5 points more than if you were not getting cash out.

The green highlight says that if: 1) you have a condo or co-op; and, 2) the loan to value ratio is greater than 75%, you will pay 0.75 points more.

The blue area says that if: 1) the property is in one of the Tier 6 states; and, 2) your loan amount is between \$75,000 and \$99,999, you will pay 0.4 points more.

Add those three highlighted sections together and you will pay 2.65 points more than the advertised price.

That may *still* sound like Greek. But what it means to you—in real life—is that it is very unlikely that the *advertised* price will be *your* price, even if the loan officer is honest. **There are too many variables.** You can only know the rate and cost for your particular loan if the loan officer has all the information about you and your property that is necessary to give you an honest quote. Consequently, calling all over town for loan quotes, listening to radio ads and going online, is unlikely to yield you quotes that are real.

## Spotting the Signs of Dishonesty

We often have to learn how to spot dishonesty from the school of hard knocks. That being said, here are some clues to look for:

1. **The loan terms change mid-stream to less favorable terms for no good reason.** There are legitimate reasons for a lender to change the terms of your loan after the initial quote. Those reasons include:
  - a. Your credit score changes
  - b. Your income verification doesn't support the level of income you thought it would when you completed the loan application
  - c. You have less money in the bank than you initially represented to the lender
  - d. You lose your job
  - e. Your property value is different from the value you expected, or it changes due to new comparables ("Comparables" are similar properties that have sold in your area, or are listed for sale. More commonly called "comps", they affect the appraised value of your home)

If your credit, income level, assets, employment circumstances and property value are all unchanged from your initial application, and your lender has told you that your rate is locked, *and* he then switches you to less-favorable loan terms, run—don't walk—away from that lender!

2. **Your gut says something is wrong.** Our sub-conscious mind assimilates a lot of information that our conscious mind doesn't know we are processing. It is always a good idea to trust your instincts, even if you are not sure why you feel the way you do. Better safe than sorry.
3. **Your spouse, mom, dad, best friend, or anyone else you trust has doubts that you are in good hands.** These people love you and may have a perspective that you do not have. Do not let your ego dismiss their instincts and cause you to stubbornly move forward in spite of their discomfort. Please listen carefully to the counsel of people who care about you.
4. **The loan officer does not return your calls in a timely fashion.** This can be a sign that she is flakey. Do you really want to trust a flake with one of the biggest financial decisions of your life?

## How to Scare Off the “Bad Guys” Before They can Cause You Harm

Wolves like to pick off the least protected sheep in a flock. These are the “easy kills.” Why should wolves work hard for a kill when they can find easy ones? Make yourself a “hard kill.” The knowledge in this book about junk fees, points, and the differing loan types will already make you a harder “kill” than those who know little about loans. If you do not know the loan officer well, or he does not come highly recommended by a trusted source, you would do well to be extra vigilant.

## What Attracted Con Men to the Mortgage Industry?

Why does it seem that the mortgage industry has more corruption than many other industries? As I see it, there are two main reasons:

1. There is a lot of money involved in the mortgage industry. Corrupt people typically follow the money.
2. The barriers to entry into the industry were too low. Did you know that it was possible to sell used cars one day, and mortgages the next day, without any formal training in loans? As mentioned in the Introduction, recent regulations have corrected this problem to a large extent.

The first reason will not be a problem if we correct the second one. So, how can we increase the chances that a loan officer who helps you with your loan will be excellent? In my

experience, con men are not committed enough to the mortgage industry to get the training necessary to be excellent loan officers. The only excellence that interests them is excellence at cheating people and getting away with it.

Fortunately, I am not alone in recognizing this issue. Federal Regulators recently enacted a law that requires loan officers be licensed in lending, and that they have 20 hours of training in lending (including ethics!). Some State laws require more training. This will be required as of December 2010 for loan officers who are licensed, and 6 months sooner than that for those without a license.

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## Chapter Summary:

**Your best protection from unscrupulous lenders is to spot them early and scare them off.** However, knowing how loans and fees work is also critical to your success. The rest of this book teaches you what you *really need to know* about loans.