



July 18, 2005

New Research: Homebuyer "Preapproval" Letters Often Virtually Worthless

A new national research study confirms what many Realtors know only too well: "Preapproval" and "prequalification" letters presented by would-be buyers of homes often are faulty and cause problems later in the transaction.

Over half of all realty agents interviewed for a statistically-representative national poll said faulty lender or mortgage broker preapprovals are a major reason why sales transactions break down before closing.

The agents identified Internet-based lenders' preapprovals as the worst: fully 39 percent of their letters are "invalid" -- issued without any direct evaluation of the buyers' credit reports, income or assets. Roughly one out of three of all preapprovals issued by mortgage brokers also are based on the borrower's word, not on confirmed facts. One out of every five preapprovals issued by national lenders are in the same category.

The new study, conducted by Washington DC-based market research firm Campbell Communications and sponsored by the lending trade newsletter Inside Mortgage Finance, polled 1,717 realty agents around the country.

Tom Popik, a principal at Geosegment Systems Corp., designer of the statistical sample, said faulty or outright bogus preapprovals have been a growing issue for Realtors. In many markets, agents won't entertain offers from bidders who don't have some form of preapproval letter to demonstrate their financial capacity to afford and finance the house they want to buy.

Yet with growing numbers of mortgage customers using subprime and "alternative" mortgage financing, a rising number of preapproval letters are based on little more than "stated income," stated assets, and little or no check of credit files, said Popik.

When such bidders later apply for a mortgage, they often don't qualify for the rate or program or loan amount they need to swing the deal. At that point, said Popik, the sales transaction may jump off the tracks, with the buyer left searching for financing and the seller sitting with an unsold house that's been off the market for weeks.

John Marcell Jr., the incoming president of the California Association of Mortgage Brokers and an active Realtor, says preapprovals based on unconfirmed information "are totally useless." Functioning as a realty broker within his firm, Compass Realty of Upland, CA., Marcell says he never accepts a bidder's preapproval letter unless it contains guarantees from the issuing lender or loan officer that the information was indeed verified.

Otherwise, he said, "we go to the mortgage broker and say, look, we've got to see the W-2s, we've got to see the bank statements," and some indication of credit standing.

In today's hot markets, "we just don't have the time to waste looking at preapprovals based on thin air," said Marcell.

What should be in a preapproval: It needs to be explicit about what information has been checked and evaluated -- credit, employment, cash on hand, etc -- and what has not. And it must be explicit about whether the borrower has been preapproved to close on a mortgage in a specified maximum amount at a specified interest rate, subject only to an appraisal.

Anything less than that should be suspect.

Written by Kenneth R. Harney

Copyright © 2005 [Realty Times](#). All Rights Reserved.