# EXPERIENCES OF OLDER REFINANCE MORTGAGE LOAN BORROWERS: BROKER- AND LENDER-ORIGINATED LOANS

## INTRODUCTION

Historically, mortgages were originated and held primarily by financial institutions such as savings and loans, commercial banks, and insurance companies. Mortgage documents, underwriting criteria, credit requirements, and appraisals varied from institution to institution. With the development of the secondary mortgage market and the standardization of loans in the late 1970s, mortgage brokers began originating loans by serving as intermediaries between the borrower and the entity funding the loan (that is, lenders or wholesalers).[1]

The number of mortgage brokers grew at an average annual rate of 14 percent between 1991 and 1998.[2] In 2000, 30,000 mortgage brokerage companies, with an estimated 240,000 employees, accounted for 55 percent of all home loans originated in that year.[3]

Mortgage brokers provide retail lending services, including counseling borrowers on loan products, collecting application information, ordering required reports and documents, and otherwise gathering data required to complete the loan package and mortgage transaction.[4] Some mortgage brokers indicate that they work with a number of funding sources and are in a position to shop for the best loans for borrowers.[5]

However, a concern has been raised that mortgage brokers may focus more on the short-term profitability incurred at the origination of the loan rather than on the long-term performance of the loan since they are intermediaries who do not hold loans through maturity. For instance, the question of whether the compensation system for mortgage brokers inevitably results in higher interest rates or higher costs for borrowers has been widely debated, and the U.S. Department of Housing and Urban Development (HUD) has conducted three rule-makings over the past seven years regarding mortgage broker fees[6] to try to ensure that borrowers are not overcharged.

Aggressive "push marketing"[7] by some mortgage brokers has also raised a concern that many loans, particularly refinance loans,[8] are "sold, not sought."[9] In addition, mortgage brokers originate approximately half of all subprime mortgage loans,[10] which have been identified as the primary source of predatory lending practices.

According to Harvard's Joint Center for Housing, regulatory oversight has not kept pace with changes in the mortgage industry. A growing share of mortgage loans, including the vast majority of subprime loans, is not subject to federal Community Reinvestment Act (CRA) requirements,[11] and regulation of mortgage brokers as a profession generally occurs at the state level outside of the regulatory structure for mortgage lending. State oversight of mortgage brokers is a patchwork of laws and regulations. Some states have no licensure requirements, and more than two-thirds do not have examination requirements.[12] Practices of concern to regulators include multiple refinancing, excessive up-front fees (such as inappropriate points and closing costs), asset-based lending without regard to the borrower's ability to repay,

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[1] U.S. Department of Housing and Urban Development. *Regarding Lender Payments to Mortgage Brokers*, 1999. Retrieved June 12, 2002 from http://www.hud.gov/offices/hsg/sfh/res/resp0222.cfm
[2] Wholesale Access. *Mortgage Brokers 1998*, 1999.
[3] National Association of Mortgage Brokers. *Industry facts*, 2000. Retrieved June 12, 2002 from http://www.namb.org/consumers%5Cind_facts.htm
[4] *Federal Register* 67 (145) (July 29, 2002): 49, 140.
[5] Ibid.
[6] U.S. Department of Housing and Urban Development, 1999. *op. cit.*
[7] U.S. Senate Committee on Banking, Housing, and Urban Affairs, testimony of Thomas Miller, Iowa Attorney General, at a hearing on Predatory Mortgage Lending: The Problem, Impact, and Responses, July 26, 2001.
[8] K. Engel and P. McCoy. "A Tale of Three Markets: The Law and Economics of Predatory Lending." *Texas Law Review* 80 (6) (May 2002).
[9] Center for Community Change. *Risk or Race? Racial Disparities and the Subprime Refinance Market*, May 2002.
[10] U.S. Senate Committee on Banking, Housing, and Urban Affairs, testimony of Neill Fendly, National Association of Mortgage Brokers, at a hearing on Predatory Mortgage Lending: The Problem, Impact, and Responses, July 27, 2001.
[11] Joint Center for Housing Studies of Harvard University. *The State of the Nation's Housing 2002*.
[12] Four states do not require licensure (Alaska, Colorado, Montana, and Wyoming). AARP Public Policy Institute. *Mortgage Brokers: A Summary of State Laws,* Forthcoming.

overaggressive marketing, and targeting of groups such as minorities[13] and older persons.[14]

## METHODOLOGY

This data digest presents results from a national study[15] of 1,008 borrowers age 65 and older (hereafter referred to as older borrowers) who acquired prime or subprime refinance loans between January 1999 and December 2000. Borrowers were selected randomly from public mortgage records[16] and identified as having either prime or subprime loans.[17]

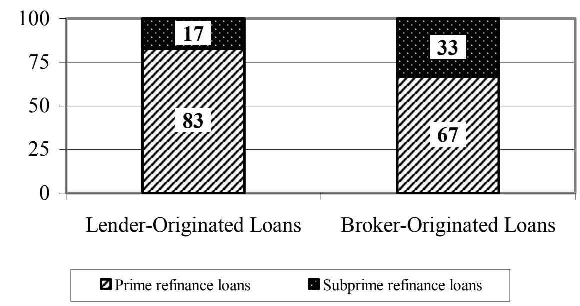
A telephone survey of these borrowers was conducted, and borrowers were asked an extensive array of questions, including whether they obtained their loan from a lender or broker. Statistical results for this report were weighted[18] to correct for the disproportionate sampling design and for any systematic non-response that could bias results to ensure sample estimates appropriately represented the national population of borrowers. Findings (other than prime or subprime status) reported in this data digest are self-reported data obtained from the telephone survey.

## FINDINGS

Nearly half (49 percent) of refinance loans among older borrowers were lender-originated loans, and 39 percent were broker-originated.[19]

**Refinance Loan Type: Prime and Subprime**
Broker-originated refinance loans (33 percent) were nearly twice as likely as lender-originated loans (17 percent) to be subprime loans (see Figure 1).

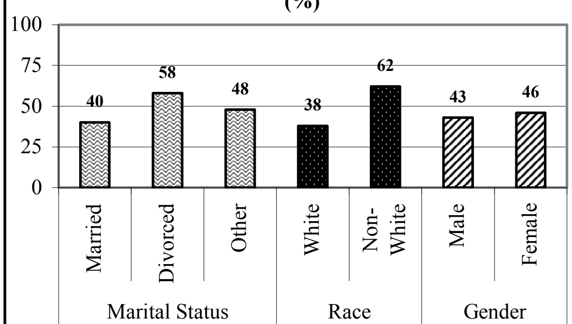
***Figure 1.*** **Lender- and Broker-Originated Refinance Loans: Prime and Subprime (%)**




*Source*. AARP Mortgage Borrower Survey, 2001 (N=1,008)

**Demographic Factors**
Broker-originated refinance loans were more prevalent than lender-originated loans among older refinance loan borrowers who were divorced, female, or non-white (see Figure 2).

***Figure 2.*** **Prevalence of Broker-Originated Loans Among Older Borrowers by Demographic Factors (%)**




*Source*. AARP Mortgage Borrower Survey, 2001

Marital Status. Older refinance loan borrowers who were divorced (58 percent) were more likely than married borrowers (40 percent) to have broker-originated loans.
Race. Broker-originated loans accounted for a larger share of loans among non-white borrowers: 64 percent of black borrowers and 66 percent of Asian or Pacific Islander borrowers had broker-originated loans, compared to 38 percent of white borrowers.
Gender. Older female borrowers (46 percent) were slightly more likely than older male borrowers (43 percent) to have broker-originated loans.

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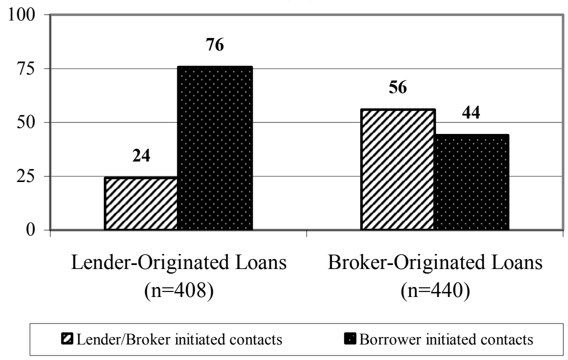
[13] Center for Community Change. Risk or Race? *Racial Disparities and the Subprime Refinance Market*, May 2002.
[14] N. Walters and S. Hermanson. *Subprime Mortgage Lending and Older Borrowers*. Washington DC: AARP Public Policy Institute (DD57), 2001.
[15] The national study, conducted by Market Facts for AARP's Public Policy Institute and the Federal Home Loan Mortgage Corporation, included 7,942 mortgage borrowers (purchase and refinance) at least 18 years of age.
[16] Loans were randomly selected from a list of first lien borrowers generated by DataQuick, a proprietary firm that collects and analyzes mortgage transaction data from county records.
[17] Using industry sources and information from HUD and the Federal Reserve Board, a list of approximately 50 lenders was created representing those institutions that primarily make subprime loans.
[18] Due to the disproportionate geographic distribution of the sample of mortgage borrowers, weighting of raw survey data was necessary. Weights by state were computed through a multistage procedure to compute national estimates of mortgage borrowers that match stratification control counts based on HMDA data to adjust for oversampling or undersampling of borrowers from particular states. This weighting procedure inflates the raw numbers of the survey participants to approximate the estimates of total population of mortgage borrowers represented in HMDA data.
[19] Borrowers also reported loans originated by home improvement contractors (1 percent), other (11 percent), and both lenders and brokers (1 percent).

**Search Behavior**
Older mortgage borrowers with broker-originated refinance loans reported more broker-initiated contact, more reliance on the broker to find the best loan, and a higher response to advertisements that guaranteed loan approvals.

Initiation of Contact. More than half of older borrowers (56 percent) with broker-originated loans reported that the brokers initiated the contact with them, while less than one-fourth (24 percent) of older borrowers with lender-originated loans reported the lender had done so (see Figure 3).

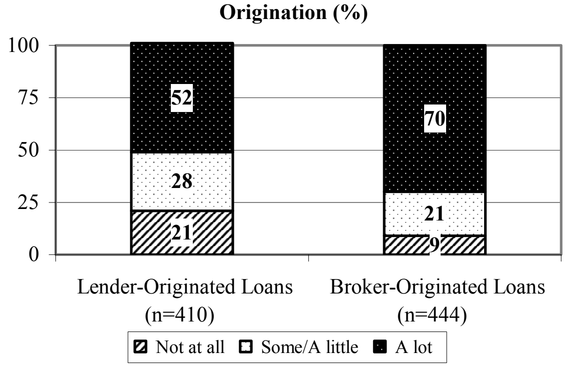
***Figure 3* . Initiation of Contacts by Loan Origination (%)**




*Note.* Due to rounding, the sum may not equal to 100%.
*Source*. AARP Mortgage Borrower Survey, 2001

Counted on Lenders or Brokers to Find the Best Mortgage. Seventy percent (70 percent) of older borrowers with broker-originated refinance loans reported that they relied "a lot" on their brokers to find the best mortgage for them, compared to only half (52 percent) of older borrowers with lender-originated loans (see Figure 4).

***Figure 4.* Reliance on Lenders or Brokers by Loan Origination (%)**




*Note.* Due to rounding, the sum may not equal to 100%.
*Source*. AARP Mortgage Borrower Survey, 2001

Responded to Advertisements. Forty percent (40 percent) of older borrowers with broker-originated loans reported that they responded to guaranteed loan advertisements at least "a little," compared to 31 percent of borrowers with lender-originated loans.

**Mortgage Terms**
Older borrowers with broker-originated refinance loans were more likely than borrowers with lender-originated loans to report that they had paid points for a mortgage and have loans with a prepayment penalty.

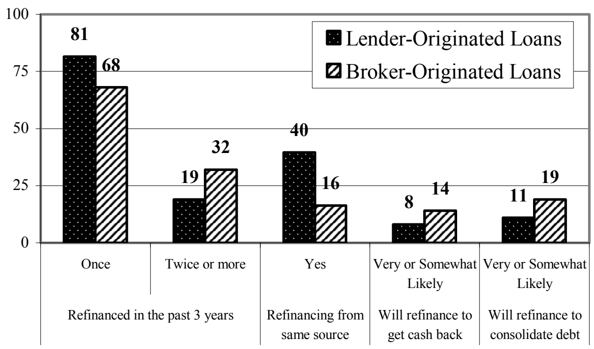
Paid Points for Mortgage. Older refinance loan borrowers with broker-originated loans (25 percent) were more likely to report that they paid points for a mortgage than borrowers with lender-originated loans (15 percent).
Prepayment Penalty. Older borrowers with broker-originated refinance loans (26 percent) were twice as likely as borrowers with lender-originated loans (12 percent) to report having a loan with a prepayment penalty.

**Mortgage Refinancing**
Older refinance loan borrowers with broker-originated loans were more likely than older borrowers with lender-originated loans to refinance frequently, less likely to go back to the same broker, and more likely to predict they will refinance.

Number of Times Refinanced in the Past Three Years. Approximately one-third (32 percent) of older borrowers with broker-originated refinance loans reported having refinanced two or more times in the past three years, compared to 19 percent of older borrowers with lender-originated loans.
Refinancing from the Same Lender or Broker. Among older borrowers with broker-originated loans, only 16 percent reported that they returned to the same broker to refinance, while 40 percent of older borrowers with lender-originated loans did so.
Will Refinance to Get Cash Back. Fourteen percent of older borrowers with broker-originated loans responded that they were either "somewhat" or "very" likely to refinance within the next 12 months to get cash back, compared to eight percent of older borrowers with lender-originated loans.
Will Refinance to Consolidate Debt. Almost twice as many older borrowers with broker-originated loans (19 percent) as borrowers with lender-

originated loans (11 percent) responded that they were "somewhat" or "very" likely to refinance within the next 12 months to consolidate debts.

*Figure 5.* **Differences in Refinancing Patterns Among Older Borrowers by Loan Origination (%)**




*Source*. AARP Mortgage Borrower Survey, 2001 (N=1,008)

**Borrower Perception of Mortgage Received**

Older borrowers with broker-originated loans were more likely than older borrowers with lender-originated loans to respond that the loans were not the best for them, the rates and terms were not fair, and they did not receive accurate and honest information from their brokers. Borrowers with broker-originated loans also reported that they obtained worse loans than they expected (see Figure 6).

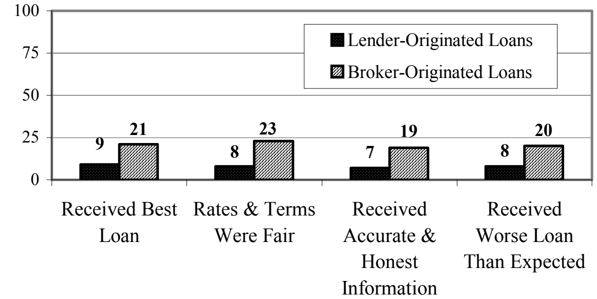
Received Loan that Was Best for Them. Twenty-one percent (21 percent) of older borrowers with broker-originated loans reported that they did not receive a loan that was best for them, compared to nine percent of older borrowers with lender-originated loans.

Mortgage Rates and Terms Were Fair. Older borrowers with broker-originated loans (23 percent) were nearly three times more likely than older borrowers with lender-originated loans (eight percent) to report that they did not feel the rates and terms of their mortgage were fair.

Received Accurate and Honest Information. Nineteen percent of older borrowers with broker-originated loans reported that they did not feel they had received accurate and honest information about their loans, compared to only seven percent of older borrowers with lender-originated loans.

Received Worse Mortgage than Expected. Twenty percent of older borrowers with broker-originated loans reported that they received loans worse than expected, compared to eight percent of borrowers with lender-originated loans.

*Figure 6.* **Older Refinance Loan Borrowers: Perceptions of Mortgage Received by Loan Origination (%)**




*Note*. Percentages shown reflect "Strongly disagree" or "somewhat disagree" responses except for "Received Worse Loan" ("yes" responses).
*Source*. AARP Mortgage Borrower Survey, 2001 (N=1,008)

**SUMMARY**

This study finds that borrowers with broker-originated loans were much more likely to report that they did not initiate the contact about the loan, and they relied more on the broker than borrowers with lender-originated loans. In addition, borrowers with broker-originated loans were more likely to report having received loans with less favorable terms such as prepayment penalties and points paid upfront than borrowers with lender-originated loans. Considering the high degree of reliance on mortgage brokers by older borrowers, especially among minority and female borrowers, in making important mortgage-related decisions, more research is needed to better understand how borrowers are affected by the ever-increasing diversity in lending products and retailers.

Furthermore, because home equity is a key component of wealth among older households, assuring that older mortgage refinance borrowers obtain appropriate loans, regardless of who originates them, is critical to ensuring the current and future financial security of millions of older Americans.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***AARP Public Policy Institute, January 2003***
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