

HUD PROPOSES MAJOR RESPA OVERHAUL

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In 2004, when HUD withdrew its controversial July 29, 2002, proposal "Simplifying and Improving the Process of Obtaining Mortgages to Reduce Settlement Costs to Consumers," no one believed it was HUD's last word on the subject. After sending out several signals it was about to release a revised proposal, HUD dropped the other shoe in its March 14, 2008, "Proposed Rule To Simplify and Improve the Process of Obtaining Mortgages and Reduce Consumer Settlement Costs". The proposal would overhaul HUD's Regulation X implementing the Real Estate Settlement Procedures Act (24 CFR part 3500).

With articles throughout the popular press trumpeting customer claims that they didn't understand the mortgage deals they entered into, it's not surprising that HUD is moving aggressively to tighten up disclosure requirements on real estate loans. This article provides a very brief heads-up on the highlights of proposed changes to the regulation that implements RESPA. We've also broken out the new model forms that are being proposed so you can start to get an idea about what they would entail.

The comment deadline is May 13, 2008. Because the changes would be so substantial, HUD proposes to provide a one-year transition period following adoption of a final rule, during which compliance with the amended rule would be optional.

Purpose of Revisions

HUD's stated purpose for proposing the extensive revisions to the RESPA Reg is to reduce "unnecessarily high settlement costs" by taking steps to:

- Improve and standardize the Good Faith Estimate (GFE) form, to make it easier to use for shopping among settlement service providers;
- Ensure that page one of the GFE provides a clear summary of the loan terms and total settlement charges so that borrowers will be able to use the GFE to comparison shop among loan originators for a mortgage loan;
- Provide more accurate estimates of costs of settlement services shown on the GFE;
- Improve disclosure of yield spread premiums to help borrowers understand how they can affect their settlement charges;

- Facilitate comparison of the GFE and the HUD-1/HUD-1A Settlement Statements (HUD-1 settlement statement or HUD-1);
- Ensure that at settlement borrowers are made aware of final loan terms and settlement costs, by reading and providing a copy of a "closing script" to borrowers;
- Clarify HUD-1 instructions;
- Clarify HUD's current regulations concerning discounts; and
- Expressly state when RESPA permits certain pricing mechanisms that benefit consumers, including average cost pricing and discounts, including volume based discounts.

Problems with the Current GFE

HUD points to the following problems with the existing Good Faith Estimates:

- Because the GFE doesn't have to be given to the borrower until after he or she submits a full application to an originator, the borrower might be paying significant fees before receiving a GFE. This inhibits the possibility of shopping beyond the provider with whom the applicant first applies.
- The GFE requires a lender to provide a list of charges, but there's not a standard form for the list. This also makes it difficult to comparison shop because different originators may list different types of categories of charges or use different names for the charges, or both.
- The GFE currently doesn't have to include information on the terms of the loans, such as the rate, for comparison purposes.
- The GFE doesn't provide certain important explanatory information to the borrower including, for example, how the borrower can use the document to shop and compare loans.
- The GFE does not make clear the relationship between the closing costs and the interest rate on a loan.
- Because the suggested GFE format found in Appendix C to the current regulation provides a space for listing any other applicable services and charges beyond the 20 common ones in the form, it's led in many instances, to a proliferation of charges for separate "services" without any actual increase in the

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work performed by individual settlement service providers.

- It’s difficult for borrowers to know how much they’re paying or to compare because the GFE doesn’t currently clearly identify the total charges of major providers of settlement services, including lenders and brokers (loan originators), title agents and insurers (title charges), and other third party settlement service providers.
- Estimated costs on GFEs are frequently unreliable or incomplete, or both, and final charges at settlement often include significant increases in items that were estimated on the GFE, as well as additional surprise “junk fees,” which can add substantially to the consumer’s ultimate closing costs.

Proposed GFE Modifications

There would be separate definitions for a “GFE application” and a “mortgage application.” The GFE application would trigger the requirement to provide a GFE. The GFE application would include name, Social Security Number, property address, gross monthly income, borrower’s information on the house price or best estimate of the value of the property, and the amount of the mortgage loan sought. When that is submitted (either in writing or in computer-generated form), the applicant will be entitled to a GFE. The lender will have the option to accept an oral GFE application, but if it does so, it would be required to reduce the oral application to a written or electronic record.

When a borrower chooses to proceed with a particular loan originator, the loan originator may require that the borrower provide a “mortgage application” to begin final underwriting. The mortgage application would expand on the info provided in the GFE application.

To facilitate shopping and lower the cost burden of shopping on consumers and industry alike, the proposed rule would not require that all underwriting information be supplied at the GFE application stage, but borrowers must be protected against “bait and switch.” If a borrower qualifies based on the GFE application data, the borrower may not subsequently be rejected unless the originator determines that there is a change in the borrower’s eligibility based on final underwriting, as compared to information provided in the GFE application and credit information developed for such application prior to the time the borrower chooses the particular originator. In that case, the originator must document

the basis for any such determination and keep these records for no less than 3 years after settlement.

Where a borrower is rejected for a loan for which a GFE has been issued, and another loan product is available to the borrower, the loan originator must provide the borrower with a revised GFE. Where a borrower is rejected, the borrower must be notified within one business day and the applicable notice requirements satisfied.

There would be major changes in the content of the GFE, as shown in the proposed model form. The proposed new GFE form can be found online at http://www.bankersonline.com/lending/respa_rev_gfe_form.pdf. The proposed revised GFE instructions can also be found online at http://www.bankersonline.com/lending/respa_rev_gfe_instr.pdf.

That’s just the tip of the iceberg. The prefatory material published with the proposed regulation contains substantial detail about other flaws in the real estate settlement process, along with explanations for why the HUD-1 is being changed and why there are other new requirements being imposed. Check out what else is changing below.

HUD-1 Settlement Statement

The HUD-1 Settlement Statement would undergo substantial changes as well. As before, there is a version for a purchase transaction and a separate version for transactions without sellers. There is a category of information relating to Reserves Deposited with Lender that looks interesting, as well as many other alterations. Note that there is no complete set of HUD-1 instructions in the proposal. Just the portions of the instructions they propose to change are excerpted in the proposal located on line at http://www.bankersonline.com/lending/respa_hud1_instr_chng.pdf.

The proposed new HUD-1 form can be found at http://www.bankersonline.com/lending/respa_rev_hud1.pdf.

Closing Script

A script is to be used at closing to ensure the borrower receives all the necessary information. The closing script has an introduction, then covers eight other areas: loan description; interest rate; payment; late payment; prepayment penalty; balloon loan; closing costs; and acknowledgment. Not only do they specify what clauses are to be included in the closing script, they also require them to be provided in a particular order. The proposed Instructions to Closing Script Preparer,

showing the proposed clauses, typeface requirements and other details, can be found at http://www.bankersonline.com/lending/respa_closingscript_instr.pdf.

Examples of Completed Closing Scripts

In order to assist lenders in seeing precisely how the closing scripts should read, HUD has included six examples of completed closing scripts. The first example is for a fixed interest rate mortgage scenario. Example 2 is for an adjustable rate mortgage. The third example is for a loan with an adjustable interest rate that features an initial discounted interest rate. Example 4 illustrates a hybrid fixed rate adjustable rate mortgage. Example 5 is for a loan with a fixed interest rate and a balloon payment. The final example is also for a loan with a fixed interest rate and a balloon payment. Examples of closing scripts can be found at http://www.bankersonline.com/lending/respa_script_examples.pdf.

GFE & HUD-1/1A Charges Comparison Chart

The lender (or lender's agent) will be required to prepare a comparison chart of the actual charges from the GFE and HUD-1 or HUD-1A using the exact information and amounts from those forms. The comparison chart consists of three categories: Charges Cannot Increase, Charges Cannot Increase More Than 10%, and Charges Can Change, along with three columns: Good Faith Estimate, HUD-1/1A, and dollar amount increase. The sample chart from the proposal can be viewed at http://www.bankersonline.com/lending/respa_gfe_hud1_comp_chart.pdf.

Servicing Disclosures Statement

Changes to the servicing disclosure are also being contemplated and can be viewed at http://www.bankersonline.com/lending/respa_rev_servng_discl_stmt.pdf. In short, the disclosure has been shortened. The lender simply must choose between three servicing option notices:

- We may assign, sell, or transfer the servicing of your loan while the loan is outstanding. [or]
- We do not service mortgage loans of the type for which you applied. We intend to assign, sell, or transfer the servicing of your mortgage loan before the first payment is due. [or]
- The loan for which you have applied will be serviced at this financial institution and

we do not intend to sell, transfer, or assign the servicing of the loan.

Other Provisions

In addition to the proposed regulatory changes, HUD intends to ask Congress to modify RESPA to provide authority for HUD-imposed civil money penalties and other relief for specific RESPA violations involving GFE, HUD-1 and special information booklet disclosures, mortgage servicing, kickbacks and other "Section 8" concerns, title insurance and escrow accounts. HUD's "wish list" for Congress will also include changes to require actual delivery of HUD-1 settlement statements to borrowers three days before closing, and standardization of the statute of limitations on actions under RESPA.

Related Links:

- Proposed RESPA revisions (PDF format), March 14, 2008 Federal Register - <http://a257.g.akamaitech.net/7/257/2422/01jan20081800/edocket.access.gpo.gov/2008/pdf/08-1015.pdf> [Note: The file is very large. Click, then go get a cup of coffee while it loads.]
- Proposed RESPA revisions (Text format), March 14, 2008 Federal Register - <http://a257.g.akamaitech.net/7/257/2422/01jan20081800/edocket.access.gpo.gov/2008/08-1015.htm>
- Current version of HUD's Reg X - <http://www.bankersonline.com/regs/3500/3500.html>
- Federal Reserve Board's proposed Reg Z changes relating to mortgage lending - <http://www.federalreserve.gov/newsevents/press/bcreg/highlightsregz20071218.htm>

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THE COST OF RESPA REFORM

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HUD has provided several tables of estimated costs involved in complying with these new rules. The following recap of these costs may be of interest to you and senior management as you decide whether or not to submit a comment letter.

Compliance Costs of the Proposed Rule

These costs assume 12.5 million loans are done annually. The per loan cost estimate is that compliance with the new GFE disclosure rule will cost \$44.40 per loan. Compliance with the new HUD-1/1A disclosure rule will cost \$54.08 per loan.

As an industry, one-time costs involved in compliance for these two disclosures are estimated to be \$570,000,000. The recurring costs for compliance are estimated to be \$1,231,000,000.

One-Time Software Upgrade & Training Costs of the New GFE

The cost for the industry is estimated to be \$91,042,558. Mortgage brokers have the largest part of that cost estimated to be \$61,267,428 while credit unions have the lowest expense at \$2,569,710. Commercial banks costs are estimated to be \$11,647,288, with mortgage banks paying out \$10,308,241 and thrifts paying \$5,249,891.

One-Time Legal Consultation Costs on the New GFE

HUD recognizes that new costs will be paid as a result of the new rules. One-time legal expenses are estimated to be \$115,874,000 for the industry. These estimates are broken down by entity category as follows:

Mortgage Brokers	\$73,219,520
Commercial Banks	\$ 2,053,150
Mortgage Banks	\$ 1,551,500
Thrifts	\$ 974,750
Credit Unions	\$ 420,600

One-Time Training Costs on the New GFE

With any regulatory change there will be training costs you will have to pay. One-time training expenses are estimated to be \$193,591,648 for the industry. These estimates are broken down by entity category as follows:

Mortgage Brokers	\$134,522,236
Commercial Banks	\$ 22,653,771

Mortgage Banks	\$ 21,285,461
Thrifts	\$ 9,981,440
Credit Unions	\$ 5,148,741

Incremental Costs of Third Party Pricing Arrangements for the New GFE

It is estimated that the additional disclosures will take an estimated 10 to 20 minutes more per loan. Basing this time on 12.5 million loans annually at a rate of \$72 per hour, the industry cost will be \$300,000,000. These estimates are broken down by entity category as follows:

Mortgage Brokers	\$180,000,000
Commercial Banks	\$ 49,275,600
Mortgage Banks	\$ 37,236,000
Thrifts	\$ 23,394,000
Credit Unions	\$ 10,094,400

For the above industry costs, \$970,508,206 represents a one-time expense to be paid to comply. Recurring costs will amount to \$1,531,000,000 annually.

EDITOR'S NOTE: Both articles on the proposed RESPA Reform initiatives were reprinted with the express permission of BankersOnLine and first appeared on www.bankersonline.com on March 14, 2008. BankersOnline has become one of the banking industry's premier sources of information and is a joint effort by Glia Group, Inc. and the Bankers Information Network.

Both articles were authored by the BankersOnLine team led by MaryBeth Guard, Executive Editor and Principal of BankersOnLine.com. Mary Beth Guard spent many years as a banking lawyer, serving as general counsel for the Oklahoma Banking Department and the Oklahoma Bankers Association. She is nationally known as a banking speaker and author.

LEARN MORE ABOUT THE RESPA PROPOSAL

Join BOL Gurus Mary Beth Guard and Jack Holzknicht for a comprehensive analysis of this significant new proposal for a webinar. The live webinar will be April 25, 2008 from 1:30 to 3:30 p.m. Central Time but participants are given the option of the LIVE Webinar, Webinar_CD-ROM or CD-ROM. Registration information can be found online at: https://www.bollearningconnect.com/eventreg/LC_respa0408_register.php